

International **Comparative** Legal Guides



Practical cross-border insights into project finance

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1 Overview

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

PPP/PFI Projects. The 1999 Act on Promotion of Private Finance Initiative (the PFI Act) introduced the contemporary private finance initiative (PFI) regime into Japan. Many availability-based accommodation projects have since been implemented (e.g., schools, hospitals, school catering service facilities and libraries). Subsequently, the PFI Act was amended in 2011 to introduce a concession scheme, pursuant to which a concessionaire may collect a commission, toll, fee or other consideration for the use by the general public of the infrastructure operated by the concessionaire. Airports and certain other facilities such as water facilities, bus terminals, stadiums/indoor sports facilities and hydropower plants have been or are being planned to be privatised under concession schemes.

In addition, each of the Port and Harbour Act and the Urban Park Act provide for a public-private partnership (PPP) regime applicable to specific public property.

Renewable Energy Projects. Since the feed-in tariff (FIT) was introduced in Japan in 2012, there have been many FIT projects. As a result of the amendment to the FIT regime effective as of April 2022, however, the vast majority of renewable energy project categories were no longer granted FIT approval; instead, these project categories were granted feed-in premium (FIP) approvals. Under the FIP regime, project companies can receive prescribed premiums from the government to supplement their revenue. Also, unlike FIT projects where grid-operating utilities are legally required to purchase all electricity generated by the plant (subject to curtailment) at a fixed price and term, project companies sell their generated electricity on the power market or to retailers via bilateral power purchase agreements and therefore are exposed to market risk to the extent they sell it on the market. Both sponsors and lenders are exploring ways to adapt project finance to renewable energy projects in the post-FIT era.

In light of concerted efforts by the Japanese government to promote renewable energy in pursuit of a carbon-neutral society by 2050, and due to the numerous opportunities afforded by Japan's island geography, offshore wind projects have attracted an increasing share of market attention. The 2019 Act on Promoting the Utilisation of Sea Areas for the Development of Marine Renewable Energy Power Generation Facilities established a new regime under which the government designates sea areas suitable for offshore wind projects, and selects a project developer through a tender process, with such developer being

granted the right to use the designated sea area for up to 30 years. Following the first such tender process under this Act, the outcome of which was announced in December 2021, it is expected that similar tender processes will be held for other sea areas currently subject to government feasibility studies.

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

Beginning with the privatisation of Kansai International Airport and Osaka International Airport via a 44-year concession using approximately JPY200 billion of project finance, there have been a number of project financings for the airport privatisation projects under the PFI Act, and most of the country's key airports have been privatised. The national government issued a new guideline in January 2023 for further use of this PFI Act concession scheme for the redevelopment of stadiums and sports arenas.

In the renewable energy sector, starting with a preceding project in a harbour area, project financings to offshore wind projects are becoming a trend as noted in question 1.1 above.

2 Security

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

Under Japanese law, legal requirements for creating and perfecting security interests differ among types of assets, and a single security that purports to cover the debtor's assets in general is not permitted under Japanese law. However, the Financial Services Agency of Japan has announced its intention to legislate a so-called "business growth security" (*jigyō seicho tampo*), which would enable companies to provide security over their business as a whole. It is expected that such a security could be utilised for project finance. Few details have been determined, however, and this plan will need several years to get through the legislative process.

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

Mortgages are used to create a security interest over real property. In addition, a factory mortgage (*kojo teito*) or a factory foundation

mortgage (*kojo zaidan teito*) under the Factory Mortgage Act can be used for an entire plant (including a power plant). Mortgages, factory mortgages and factory foundation mortgages must be registered with the public registry to be perfected.

Machinery and equipment at such a plant may be treated as movables (as independent of the land on which the plant is located) or as having become part of the plant or the land. If they are considered movables, collateral assignment can be used as a means to subject them to a security interest. If, on the other hand a factory mortgage or a factory foundation mortgage is created, machinery and equipment would be covered thereby. If machinery and equipment are considered to have become part of the land, they will be covered by a mortgage that is created over such land. Collateral assignment of movables are in most cases perfected through registration with the public registry.

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

This arrangement is often seen in secured transactions.

Either a pledge or a collateral assignment is used to create a security interest over receivables. For both such security interests, while the security is created over receivables by way of an agreement between the chargor and the chargee (without involving the debtor), that security is not to be perfected against the debtor until the debtor is notified of, or acknowledges, the creation of such security, and is not perfected against the other third parties until such notification or acknowledgment is made on a date-certifying instrument (typically, date-certifying posting mail or document with a date-certifying stamp affixed by a notary public) or the security is registered at the legal bureau.

When that arrangement is made, the security is perfected through the registration, and creation of the security is not notified to the debtor until the security is enforced.

Once a pledge is created or a collateral assignment is made over receivables, the chargor loses its power to collect those receivables. However, it is common practice that such power is granted back to the chargor until certain credit events (e.g., events of default) occur.

In enforcing the security, the chargee notifies the debtor of the creation of the security and also terminates the chargor's power to collect the receivables. By doing so, the chargee becomes able to collect the receivables from the debtor directly and the debtor is no longer permitted to pay the receivables to the chargor.

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

A pledge or a collateral assignment can be used for creating a security interest in claims regarding bank accounts, subject to consent of the depository bank, and is perfected by notification to or consent by (in each case with a certified date) such depository bank. With respect to savings accounts, despite widespread use of pledges and collateral assignments, there is a certain degree of legal uncertainty with respect to the validity of the security interests created thereby.

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

Project companies are typically either *kabushiki kaisha* or *godo kaisha*, both of which entity types are formed in Japan. The

shares in a *kabushiki kaisha* can be issued in certificated form, while the membership interest in a *godo kaisha* cannot be in certificated form. Pledges over shares or membership interest are perfected as follows:

- a pledge created over a share in a *kabushiki kaisha* for which share certificates are issued is perfected upon delivery of the share certificate representing such share to the pledgee;
- a pledge created over a share in a *kabushiki kaisha* for which share certificates are not issued is perfected upon the company recording the pledge in its shareholder ledger in response to the joint request by the pledgor and the pledgee;
- a pledge created over a share in a listed company is perfected upon the pledge being recorded in the share transfer recording system administered by the Japan Securities Depository Centre, Incorporated (JASDEC) in response to the joint request by the pledgor and the pledgee; and
- a pledge created over a membership interest in a *godo kaisha* is perfected in the same manner as a pledge over receivables and, in practice, is perfected by obtaining the company's (i.e., the *godo kaisha's*) written acknowledgment accompanied by a date-certifying stamp of a notary public.

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

A registration tax (*torokumenkyo zei*) is imposed on the registration of a security interest. For mortgages over real estate, the rate is 0.4% of the registered face value of the secured obligations (0.25% in the case of a factory foundation mortgage). Occasionally, provisional registration (*kari toki*) of a mortgage is used in order to save registration tax, provided that the borrower is obliged to convert provisional registration to a definitive registration (*hon toki*) upon the occurrence of a specified credit event. Once provisional registration is made on a mortgage, the priority of the mortgage is secured; however, it must be converted to definitive registration to implement in-court foreclosure under the mortgage. The registration tax for provisional registration is JPY1,000 per registration. Registration tax of a pledge or collateral assignment of movables or claims is JPY7,500 per registration.

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

With respect to registration tax, please see question 2.6 above. The fee for obtaining a date-certifying stamp from a notary public is nominal. Creating and perfecting a security interest usually does not involve a significant amount of time as registration is considered to have been made when the registration is applied for. With respect to factory foundation mortgages, while such mortgages are useful in that the entire plant is covered by a single security interest, the creation of a factory foundation mortgage must be preceded by establishment of a factory foundation. If a factory foundation consists of movables in addition to real estate, then a public notice must be made for the list of such movables, and the factory foundation cannot be established until certain period of time (one month to three months) elapses without any objections from interested persons.

To avoid such waiting period, in many cases a factory foundation is established with real property only, with security over movables provided by way of collateral assignment; the public notice is then made for the list of such movables. When the waiting period elapses without any objections, such movables are incorporated into the factory foundation.

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

Generally, no regulatory or similar consent is required. If, however, a project receives subsidies from the central government or a regional government, consent of the relevant governmental authority is required for creating a security interest over assets that are procured with the subsidies (Act on Regulation of Execution of Budget Pertaining to Subsidies, etc.).

3 Security Trustee

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

The concept of trust is recognised in Japan. For practical reasons, however, security trusts are not commonly used in project finance or other syndicated lending transactions in Japan.

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

Parallel debt is sometimes discussed as an alternative solution to the security trust arrangement, but it is not accepted by the market to date. There are some academics that question the legality and enforceability of parallel debt due to its constructive nature. Under the established practice, security is granted to each of the lenders individually.

4 Enforcement of Security

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

See question 5.1 for the impact of insolvency proceedings. In order to alleviate risks associated with insolvency proceedings, lenders typically require that the relevant project documents include a set of provisions which purport to prevent the project company from commencing insolvency proceedings.

Regarding mortgages created in PFI projects over Concession Interests (*kokeyoshisetsuto uniken*) (i.e., specified rights and interests in infrastructure assets granted to a concessionaire in relation to a

concession scheme project under the PFI Act), since any transfer of Concession Interests is subject to the consent of the grantor thereof, unlike other mortgages, enforcing a mortgage over Concession Interests requires the consent of such grantor.

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

In Japanese judicial proceedings, Japanese citizens and foreigners are afforded equal treatment, and there are no substantive restrictions on a foreign lender's ability to enforce its rights under a loan or security agreement. As the official language in Japanese courts is Japanese, however, all the documents to be filed with the Japanese court must also be in Japanese or be accompanied by a Japanese translation. With respect to foreclosure on the shares in a project company in Japan, see section 6 below.

5 Bankruptcy and Restructuring Proceedings

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

In corporate reorganisation (*kaisha kousei*) proceedings, secured creditors are not permitted to enforce their security outside the proceedings. This differentiates corporate reorganisation proceedings from other insolvency proceedings, namely bankruptcy (*hasan*), civil rehabilitation (*minjisaisei*) and special liquidation (*tokubetsu seisan*) proceedings where secured creditors can enforce their security outside the proceedings and recover their loans from the enforcement proceeds of the collateral. The amount of secured loans and the terms of secured loans to secured creditors in a corporate reorganisation proceeding are modified in accordance with the reorganisation plan. Project finance lenders preferring bankruptcy remoteness therefore require the project company to be a *godo kaisha*, because corporate reorganisation proceedings are only available against a *kabushiki kaisha*.

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

The priority of security interests is typically determined by the order of perfection. Thus any given security interest is subordinate to a security interest prior in order of perfection. Tax debt, however, has equal priority with secured debt, and the order of priority between a security interest and tax obligation is determined by the order of perfection of the security interest and statutory due date of the tax debt (*boutei non kigen*).

Securities granted by the debtor to secure existing claims by a debtor that is already experiencing financial difficulty may be avoided in bankruptcy (*hasan*), civil rehabilitation (*minjisaisei*) and corporate reorganisation (*tokubetsu seisan*) proceedings.

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

No private entities are excluded from insolvency proceedings in Japan, although special liquidation proceedings and corporate reorganisation proceedings are only available to *kabushiki*

kaisha. Governments and local municipalities are considered to be immune to insolvency proceedings.

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

In general, in order to petition for attachment, an unsecured creditor must first obtain a title of obligation (*saimu meigi*), which is typically a final and conclusive judgment rendered by a court, while a secured creditor may petition for attachment without a title of obligation. It is typical, however, that the secured parties and security provider agree in a security agreement that the security can be enforced out of courts, i.e., a right of the secured creditor (i) to sell the property and apply proceeds from the sale to repayment of the secured obligation, or (ii) to acquire the property at the value it appraises and apply such value to repayment of the secured obligation.

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

An out-of-court restructuring is possible. While it can be implemented by the lawyers individually hired by the debtor, there are a number of organisations and procedural rules to facilitate such private restructuring. The restructuring under such informal processes requires consent of all the lenders and other creditors, unlike in formal insolvency proceedings. Although there are no precedents in the project finance field, Turnaround ADR pursuant to the Act on Promotion of Use of Alternative Dispute Resolution may be an option. Turnaround ADR is a forum to discuss and agree to rescheduling of financial debt. Some of the merits of using Turnaround ADR would be: (i) financial institutions are able to expense debt written off during the Turnaround ADR for accounting and tax purposes; and (ii) as commencement of Turnaround ADR is not publicly announced, it is more likely that the value of the business will not be impaired by reputational damage.

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

Generally, a director owes the duty of good manager *vis-à-vis* the company formed as a *kabushiki kaisha*, subject to the business judgment rule. If, however, such a director acts in bad faith or with gross negligence in performing his or her duties, he or she would be also liable to creditors of the company or other third party for their losses under the Companies Act. Thus, for example, a director of a company that continues to trade with knowing that there is no reasonable possibility that the company will be recovered would be liable if the company enters into an insolvency proceeding.

6 Foreign Investment and Ownership Restrictions

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

Under the Foreign Exchange and Foreign Trade Act (the FEFTA), in general, the following categories of non-Japanese investors are required to file an *ex post facto* notification to the Bank of Japan:

- investors who have acquired a share in an unlisted company or 1% of shares in a listed company; or
- investors who have provided finance of JPY100 million or more by way of extending a loan or subscribing for a bond with a term of one year or more to a company, which has resulted in 50% or more of such company's outstanding debt with a term of one year or more being owed to them.

Where, however, the subject company conducts business in a Designated Industry (which is divided into (i) "Core Industry", being an industry that is closely connected to national security and/or fundamental infrastructure such as manufacturing firearms, aircraft or spacecraft, or is related to electricity, telecommunications, oil or gas, and (ii) "Non-Core Industry", being an industry other than a Core Industry that is still considered important from a national security perspective, pertains to fundamental infrastructure, such as broadcasting, or relates to biological products, or marine or air transportation), subject to certain exceptions, foreign investor may not make an investment in such subject company unless they make a prior notification and the specified waiting period expires; such period is generally 30 days, which could be shortened to five business days or extended up to five months. If the government determines during the waiting period that the investment may undermine national security, public order or public safety, or adversely affect the national economy, it may issue a warning to change the terms of the investment, or cancel it.

In addition to the general restriction under the FIFTA, certain industry specific restrictions might apply depending on the business to invest in, such as broadcasting or air transport businesses under the relevant laws.

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

No, there are not.

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

There is no specific statute to compulsorily nationalise a project company. However, the Constitution of Japan provides that private property may be taken for public use upon just compensation therefor. On this constitutional basis, the Expropriation of Land Act permits the expropriation of land for public interest undertakings, such as the establishment of roads, railroad facilities, water supply or sewage facilities, or electric facilities for electricity transmission. Such takings require the approval of a governmental committee and compensation of losses. No exception to the foregoing exists for any particular form of investment.

7 Government Approvals/Restrictions

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

The Agency for Natural Resources of the Energy of Ministry of Economy, Trade and Industry have authority over the renewable energy sector, although other agencies or departments may be relevant for the purposes of governmental licence, approval, permission or the like. For an offshore wind power project, for instance, the licensing authority of the exclusive use of general sea areas is the Ministry of Land, Infrastructure, Transport and Tourism (MLIT).

Governmental bodies having authority over PPP/PFI projects differ depending on the governmental functions for which such PPP/PFI is adopted. For instance, the Civil Aviation Bureau of MLIT mainly has authority over airport privatisation projects.

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

Generally, no formal requirement exists for a financing or project document to be valid and enforceable. However, certain types of fixed term land or building lease agreement needs to be executed in the form of a notarised document (*kousei shosho*).

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

As a general matter, there is no licence requirement for land ownership in Japan. This is also the case for foreign entities.

Under the Mining Act, minerals or other natural resources, such as natural gas and crude oil, may not be extracted without a licence, and such licences are not granted to non-Japanese persons or corporations.

Certain other regulations may apply. For instance, the transportation of petroleum through a pipeline requires permission under the Petroleum Pipeline Business Act.

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

Mining and mining area taxes, as well as application and registration fees, apply to mining businesses. The export of natural resources is not restricted under the FEFTA (see, question 10.1).

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

Foreign currency exchange business does not require any licence, although certain reporting and know-your-customer confirmation and notification requirements are applicable under the FEFTA and related laws.

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

Under the FEFTA, *ex post facto* notification to the Bank of Japan is usually required for any cross-border payment of more than JPY30 million, unless such payment is made in connection with the international trade of goods.

Dividends and interest payable to a foreign recipient are generally subject to a withholding tax of 20.42% (but see question 17.2 for potential treaty benefits).

Under the thin-capitalisation rules or earning stripping rules, the payer of interest may not be permitted to fully deduct interest expenses for Japanese corporate tax purposes.

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

There is no restriction as to maintaining onshore foreign currency accounts and/or offshore accounts under Japanese law. However, ownership of an asset located outside Japan worth more than JPY50 million in total at the year-end necessitates filing a reporting form with the tax authority.

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

Under the Companies Act, a *kabushiki kaisha* can distribute dividends by the approval of a general meeting of shareholders only (i) if its net assets exceed JPY 3,000,000, and (ii) from and to the extent of its distributable amount for each fiscal year as calculated in accordance with the formula stipulated under the Companies Act and related governmental order. There is a similar restriction on dividend distributions by a *godo kaisha*, although distribution by a company with net assets less than JPY 3,000,000 is permitted and the calculation formula is different in several points from that for a *kabushiki kaisha*. Any distribution in excess of these limits would be subject to certain recovery mechanisms and possible criminal charges.

See question 7.6 for the FEFTA *ex post facto* notification and tax treatment where the parent is an offshore entity.

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

The Environmental Impact Assessment Act (the EIA Act) may apply to the development of certain types of projects the size of which exceeds a certain threshold. For those projects, the EIA Act requires that the project company prepare a planning document, conduct a public hearing, implement planned research, projection and evaluation, prepare an environmental impact statement and otherwise follow requisite procedures. It is a time-consuming process, and because the completion of such process is in many cases a prerequisite to certain further governmental approval process, such as the issuance of a forest development permit under the Forest Act, it substantially impacts the project development schedule. Solar, wind and other power plant projects with a size exceeding a certain threshold (for solar projects, 40,000kW of output capacity, or 30,000kW for some regional governments; for wind projects, 50,000kW, or 37,500kW for some regional governments) are subject to the EIA Act.

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

No, there is not.

8 Foreign Insurance

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

In general, foreign insurance companies are not permitted to

provide insurance to Japanese residents for property located in Japan or vessels or aircraft registered in Japan, unless they open a branch office in Japan and obtain a licence under the Insurance Business Act, with certain exceptions.

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

There are no restrictions on foreign creditors receiving proceeds from insurance policies over project assets.

9 Foreign Employee Restrictions

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

Whether an individual can be employed in Japan depends on his or her residential status in general. In addition to the application of general labour laws, businesses hiring foreign employees must notify the Minister of Health, Labour and Welfare of the names, residential status and other matters of such employees upon commencement and termination of employment, and must make an effort to take measures to adapt such foreign employees to the job, as well as support them in their search for re-employment after leaving the job under the Act on Comprehensively Advancing Labor Measures, and Stabilizing the Employment of Workers, and Enriching Workers' Vocational Lives.

10 Equipment Import Restrictions

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

Under Japanese import restriction laws, only certain limited categories of items are subject to general import restrictions, such as arms, weapons and nuclear-related items. Project equipment or equipment used by construction contractors is not typically subject to such restrictions, although a case-by-case confirmation is necessary. Goods imported into Japan are generally subject to import consumption tax (i.e. Japanese VAT). Custom duties may also apply, depending on the types of goods to be imported.

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

The applicable rate of custom duties varies depending on various factors, such as types of imported goods and exporting country, and a case-by-case analysis is necessary.

11 Force Majeure

11.1 Are force majeure exclusions available and enforceable?

The concept of *force majeure* is generally recognised. The Civil Code provides that an obligor may not raise the defence of *force majeure* with respect to failure to pay monetary debts. What constitutes *force majeure* is not, however, stipulated by legislation. It would be prudent therefore for project parties to agree on the terms of *force majeure* provisions on a project-by-project basis.

12 Corrupt Practices

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

Under the Penal Code, a public official accepting a bribe in connection with his or her duties may be punished by imprisonment for up to five or seven years, depending on the situation. If a public official consequently acts illegally or refrains from acting in the exercise of his or her duty, he or she may be imprisoned for between one and 20 years. A person giving a bribe may be punished by imprisonment for up to three years, or a fine up to JPY2,500,000. In addition, bribery of foreign public officials is also prohibited under the Unfair Competition Prevention Act. Violations may result in imprisonment for up to five years, a fine up to JPY5,000,000, or both.

Commercial bribery is prohibited under the Companies Act and may in principle be subject to prosecution, although in practice such prosecutions are rarely seen. A director or certain other senior corporate officer accepting property benefits in connection with such person's duties in response to an improper request may be punished by imprisonment for up to five years or a fine up to JPY5,000,000. Any person giving such benefits is punished by imprisonment for up to three years or a fine up to JPY3,000,000. Bribery in connection with exercising of certain shareholder rights, creditor or bondholder under the Companies Act is also criminalised (imprisonment for up to five years or a fine up to JPY5,000,000). Certain senior corporate officers and employees giving property benefits on the account of a *kabushiki kaisha* in exchange for the exercise of certain shareholder rights may be subject to imprisonment for up to three years or a fine up to JPY3,000,000.

13 Applicable Law

13.1 What law typically governs project agreements?

Project agreements are typically governed by Japanese law. A PFI/PPP agreement or concession agreement with the Japanese government, a local municipality or a state-owned entity is always governed by Japanese law. Fuel supply agreements with foreign suppliers in power projects (e.g., conventional power projects and biomass projects), however, are sometimes governed by foreign law, such as English law or New York law.

13.2 What law typically governs financing agreements?

Financing agreements are always governed by Japanese law, with the exception that security agreements on collateral located outside Japan would typically be governed by the laws of the jurisdiction where such collateral is located.

13.3 What matters are typically governed by domestic law?

As described in questions 13.1 and 13.2, project agreements and financing agreements are governed by Japanese law, with a few exceptions.

14 Jurisdiction and Waiver of Immunity

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

Under the Act on General Rules for Application of Laws, parties to a contract may choose the jurisdiction governing the contract, and the courts of Japan generally uphold the choice of foreign law provision in a contract. However, if it is found that the application of a foreign law chosen would lead to a consequence that is detrimental to the public order of Japan, a Japanese court will refuse to apply the chosen foreign law and apply Japanese law instead. Furthermore, Japanese laws and regulations covering certain areas – e.g., antitrust, foreign exchange, labour, usury and real estate leasing – are considered mandatory, and will therefore apply regardless of any choice of foreign law.

The Code of Civil Procedure provides that the parties to a contract may choose a court in a foreign country as the agreed venue of dispute resolution, and the courts of Japan generally recognise a contractual choice of foreign court. However, a choice of foreign court will not be upheld if a Japanese court decides that such court in a foreign country does not have the requisite jurisdictional capacity.

A waiver of immunity of foreign states is binding and enforceable under the Act on the Civil Jurisdiction of Japan with respect to Foreign States.

15 International Arbitration

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

An agreement to submit disputes to an international arbitration is honoured in Japanese court procedures. An arbitral award (irrespective of whether or not the place of arbitration is in Japan) has the same effect as a final and binding judgment under the Arbitration Act. Where the venue of arbitration is in Japan, however, a party may file a petition with the court to set aside an arbitral award based on stipulated grounds such as certain procedural deficiencies or public policy concerns.

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

As Japan is a contracting state of the New York Convention, an arbitral award would be recognised by the courts of Japan and may be enforced without retrial as to the merits of the decision, in accordance with, and subject to, the New York Convention and the Arbitration Act.

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

Under the Arbitration Act, an arbitration agreement is effective only when the subject thereof is a civil dispute (excluding disputes of divorce or dissolution of adoptive relation) which can be settled between the parties. In this context, whether certain types of dispute, such as a dispute concerning patent validity, breach of anti-monopoly law, or legality of administrative actions, can be settled or not may be a difficult question depending on the substance of each such dispute. It is specifically provided in this Act, however, that (i) an arbitration

agreement for a future individual labour dispute is invalid, and (ii) a consumer can generally cancel an arbitration agreement with a business operator.

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

No, there are not.

16 Change of Law / Political Risk

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

No such demand has been seen in the Japanese project finance market. It is common, however, for project finance lenders to enter into a direct agreement with the local or national government implementing a PFI project, pursuant to which the governmental authority sets out its consent to the lenders' security, and agrees to mutual cooperation in a critical situation such as default of the project company.

17 Tax

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

See question 7.6 for applicable withholding tax on interest on loans provided by foreign lenders. The proceeds of a claim under a guarantee or security payable to a foreign person will also be subject to withholding tax of 20.42%, if and to the extent the interest on the underlying loans is classified as Japan sourced income (but see question 17.2 for potential treaty benefits).

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

Withholding tax on dividends and interest (including proceeds of a claim under a guarantee or security) may be reduced or exempt if Japan has a treaty with the country where the foreign recipient is resident, subject to satisfaction of the applicable conditions to enjoy treaty benefits. Certain agreements executed for project finance (such as loan agreements) will be subject to stamp duties.

Japan has numerous incentives available for foreign investments generally, but not specifically targeting project financing. METI and the Japan External Trade Organization publish a list of programs or other information concerning these incentives on their websites.

18 Other Matters

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

No, there are none.

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

In addition to the relevant corporate law requirements for the issuance of such capital market instruments (e.g., a *kabushiki kaisha* must follow the procedures stipulated in the Companies Act such as board meeting approval for bond issuance), typical capital market instruments such as bonds are categorised as securities (*yuka shoken*) under the Financial Instruments and Exchange Act. Accordingly, solicitations for newly issued securities may be subject to certain licensing and disclosure requirements. Where a public offering is not intended, financing is generally structured to utilise certain exemptions to disclosure requirement, such as limiting the investors to certain Qualified Institutional Investors as defined in the Act and related regulations. To date, however, it is not common to use such capital market instruments for project financing in Japan.

19 Islamic Finance

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

Islamic finance is not commonly used in project financing in Japan. Although a careful regulatory and broader legal analysis

would be required due to the absence of an established market standard, a theoretical possibility might be an *Istina'a* financing structure among an EPC contractor, a project company and Islamic financial institutions through which agreed EPC contract price would be financed.

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

In general, *Shari'ah* law is not considered governing law for the purpose of Japanese conflict of law rules. There is no relevant court precedent in Japan.

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

No, subject to the applicable interest rate cap (15% to 20% *per annum* depending on the loan amount) under the Interest Rate Restriction Act.



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