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Asia Pacific Guide to Lending and Taking Security

TRANSACTIONAL POWERHOUSE

Leading and closing complex deals – every day

Welcome to the third edition of our Asia Pacific Guide to Lending and Taking Security

The Asia Pacific Guide to Lending and Taking Security was originally published in 2017 and last updated in 2021. We have once again revised and updated the guide to ensure it remains current and relevant to the Asia Pacific lending market. It contains questions and answers that are important to lenders in the region when considering whether to lend, what security can be taken to protect their investment and what happens if things go wrong. It also includes a section on working digitally. This section covers the electronic execution of documents, verification of the signature of a person witnessing a document, perfecting security without a wet ink signature, and any legal restrictions to the electronic execution of financing documents.

The guide covers 13 jurisdictions in the region: Australia, Cambodia, Mainland China, the Hong Kong SAR, India, Indonesia, Japan, Malaysia, the Philippines, Singapore, Thailand, Taiwan and Vietnam.

This guide is a result of combined efforts from lawyers across major cities and financial centers in Asia Pacific. We hope you will find this guide useful and we would be very happy to help you to navigate these and any other markets you are operating in or looking to go into.

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Foreword from our Financial Institutions Global Chair

2023 proved to be challenging for some businesses to obtain access to financing or to refinance existing debt and for lenders to lend to certain businesses. A number of factors gave rise to this situation, such as rapid and substantial rises in interest rates and a slowdown in economic growth with some markets looking at a downturn. This was all set against a backdrop of stubbornly high inflation driven by resurgent demand since the end of the COVID-19 pandemic, together with energy and commodity pressures exacerbated by both Russia's invasion of Ukraine and, more recently, the escalating conflict in the Middle East. Additionally, the effects of last spring's banking crisis remained with us in the tightening of rates and collateral requirements. Banking supervisors are reviewing their prudential supervision of regional and global systematically important banks to identify lessons learned, and this is likely to make capital more expensive still.

In 2024 we expect to see considerable activity around "amend and extend" refinancing, as well as inquiries from borrowers over covenant relief. Nonetheless, good-quality credit propositions remain as new products are continuing to emerge, such as asset-backed lending with businesses borrowing against receivables rather than future project revenues. Alternative lenders are increasing their share of the market, providing some healthy competition for traditional lenders and increasing funding options for borrowers operating in the tightening market, as less regulation means they can underwrite higher leverage ratios and transact faster.

The importance of environmental, social and governance (ESG) factors carries on rising, as shown by the rapid growth in sustainability-linked loans, green loans and social loans. The region and, in particular, Japan are leading the way globally through the adoption of transition finance products and initiatives that look to support high-emission businesses in hard-to-abate sectors seeking to reduce their greenhouse gas emissions under a long-term strategy to align with carbon net zero — take a look at our recent Transition Finance Briefing for more information. The challenge, for lenders and borrowers alike, from ESG is to manage the risks of greenwashing — for example, over the credibility of KPIs — that can lead to reputational damage, regulatory investigations and associated litigation. To help mitigate such risks, the International Sustainability Standards Board recently published common baseline standards to disclose climate-related risks and opportunities. There is much lenders and businesses can do to prepare themselves for and mitigate climate-related litigation — in this regard, see our briefing on Preparedness for Climate-Related Litigation in the Financial Sector.

Technical innovation also merits a mention. Artificial intelligence (AI) and generative AI have captured the attention of all financial market participants with their potential to facilitate due diligence, preparation of reports and other internal underwriting tasks, thereby increasing efficiencies and cutting costs. A further area of interest is the potential use of crypto-assets as collateral to secure lending. While the market is naturally and understandably cautious in its approach to this asset class, internationally, the courts are recognizing crypto as a valid form of property right. The coming year should be as interesting as it is challenging.

My colleagues and I hope that you find this guide helpful and informative.

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AUSTRALIA

Australia

When considering whether to lend

1. Is it necessary or advisable for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in this jurisdiction: (a) by reason only of its execution, delivery or performance of the finance documents; or (b) to enable it to enforce its rights under the finance documents?

Execution, delivery or performance of the finance documents

A lender, arranger, facility agent or security agent would be subject to regulatory regimes or licensing requirements where it is:

- Carrying on "banking business" in Australia under the Banking Act 1959 (Cth) ("**Banking Act**"). A person who carries on banking business in Australia must be authorized by the Australian Prudential Regulation Authority (APRA) to be an authorized deposit-taking institution (ADI). However, an entity that merely lends to companies in Australia and does not take deposits will not be deemed to be carrying on banking business and will not require approval by APRA to be an ADI or be regulated by the Banking Act.
- Carrying on a "financial services business" in Australia. An entity that carries on a financial services business in Australia must hold an Australian financial services license (AFSL) under Chapter 7 of the Corporations Act 2001 (Cth) ("**Corporations Act**"). However, credit facilities are generally excluded from the definition of "financial product" under the Corporations Act and the provision of a credit facility only to an Australian company will not trigger regulation by the Australian Securities & Investments Commission (ASIC) as a financial services business. However, the entry into related exchange contracts and derivative transactions may trigger regulation under the Corporations Act.

In addition, under Section 66 of the Banking Act ("**Section 66**"), an entity is prohibited from assuming or using certain restricted terms in Australia, including "bank," "banker" and "banking" (in any language) in relation to its financial business unless the APRA has granted permission otherwise. It is an offense with a civil penalty for each breach of Section 66. Therefore, a lender, arranger, facility agent or security agent that is a bank, or is related to a bank (and certain other types of financial institutions) must not breach Section 66 by assuming or using the word "bank," "banker" or "banking" (even in its corporate name) when dealing with an Australian counterpart.

In an open letter to foreign banks, the APRA has provided guidance that it would not consider a foreign bank to be in breach of Section 66 if all of the following conditions have been satisfied:

- The foreign bank does not maintain an office or permanent staff in Australia, including staff employed by an entity within the banking group that conducts non-banking business on its behalf in Australia.
- The foreign bank does not solicit business from retail customers in Australia.
- All business contracts and arrangements are clearly transacted and booked offshore.
- The foreign bank does not engage in advertising or allow bank staff to physically solicit business in Australia.
- Where offshore staff of the foreign bank meet with clients and potential clients in Australia, it is for the limited purpose of arranging or executing documentation in relation to the business of those clients.

If all five conditions above have been satisfied, the APRA is also of the view that the foreign bank will not be in breach of Section 66 where it lends from offshore and uses restricted words such as "bank" to register a security interest over property in Australia, including on the Personal Property Securities Register (PPSR) established under the Personal Property Securities Act 2009 (Cth).

Please refer to the answer to question 11 of the "When lending to borrowers" section for information in relation to consumer credit regulation that may be applicable for consumer lending to individuals.

Enforcement of rights under the finance documents

Foreign investments in Australian entities, businesses and land are regulated by the Foreign Acquisitions and Takeovers Act 1975 (Cth) (FATA), the Foreign Acquisitions and Takeovers Fees Imposition Act 2015 (Cth), the Foreign Acquisitions and Takeovers Regulation 2015 (Cth) ("**Regulations**") and Australia's Foreign Investment Policy ("**Policy**").

The Australian Foreign Investment Review Board (FIRB) administers the FATA, the Regulations and the Policy. It also assists the Australian treasurer to make decisions on foreign investment proposals submitted for examination and approval.

Approval may be required under the FATA if a "foreign person" or "foreign government investor" is involved in an acquisition of an entity, business or land in Australia. However, there are exemptions in the situations set out below.

Foreign persons whose ordinary business includes the lending of money: moneylending exemption

A foreign person whose ordinary business includes the lending of money is exempted from the requirement to obtain the approval of the FIRB to take or enforce security over shares or other assets or over an interest in land, provided the interest is held solely by way of security for the purposes of a "moneylending agreement" (the "**moneylending exemption**"). A "moneylending agreement" is:

- An agreement entered into in good faith, on ordinary commercial terms and in the ordinary course of carrying on a business (a "**moneylending business**") of lending money or otherwise providing financial accommodation, except an agreement dealing with any matter unrelated to the carrying on of that business; and
- For a person carrying on a moneylending business, or a subsidiary or holding entity of a person carrying on a moneylending business, an agreement to acquire an interest arising from a moneylending agreement (within the meaning of the above paragraph).

The moneylending exemption covers connected parties to reflect modern lending and debt trading practices. This includes any subsidiary or holding entity, a person who is in a position to determine the investments or policy of the lender, a security trustee, a receiver, or a receiver and manager appointed by a lender or another connected party.

Where the interest is in residential land or where the interest is acquired by a foreign government investor (as defined in the FATA and Regulations) by way of enforcement of a security, additional requirements must be met for the foreign person to benefit from the moneylending exemption. These are described below.

From 1 January 2021, the moneylending exemption will not apply to acquisitions upon enforcement of a security in national security land (which includes defense premises or land belonging to or relating to a national intelligence agency of the Commonwealth Government) or national security businesses (which includes a business carried on in Australia with respect to critical infrastructure, network telecommunications and national defense information and technology), unless a receiver or receiver and manager have been appointed to manage the process.

Taking and enforcing security over residential land

Where a foreign lender (other than a foreign government investor) takes security over, or acquires an interest by way of enforcement in, residential land, the moneylending exemption only applies where:

- The lender (or its holding entity) is an ADI; or
- The lender (or its holding entity) is otherwise licensed (in Australia or elsewhere) as a financial institution and either has at least 100 holders of securities in it or is listed on a stock exchange (in Australia or elsewhere).

Foreign government investor lenders

For an interest acquired by a foreign government investor by way of enforcement of a security, the moneylending exemption only applies in the following cases:

- Where the foreign government investor is an ADI or a subsidiary of an ADI, it may acquire and hold an interest over shares, assets or land through enforcement of its security without FIRB approval for 12 months only. FIRB approval will be required for a foreign government investor to hold its interest in the shares, assets or land after the 12-month period, unless it is making a genuine attempt to dispose of the interest.
- Where the foreign government investor is not an ADI or a subsidiary of an ADI, that entity may acquire and hold an interest through enforcement of its security without FIRB approval for six months only. Similarly, FIRB approval will be required for the lender to hold its interest after the six-month period unless it is otherwise making a genuine attempt to dispose of the interest.

2. Will any lender, arranger, facility agent or security agent be deemed to be resident, domiciled, carrying on business or subject to tax by reason only of the execution, delivery, performance or enforcement of the finance documents?

A lender, arranger, facility agent or security agent may be deemed to be carrying on business in Australia depending on the circumstances in each particular case. While lending to an Australian company on a one-off or very limited basis will, in most cases, probably not qualify as carrying on business in Australia, repeated lending and a course of dealing will most likely constitute carrying on business, which could trigger tax and/or other regulatory consequences. A foreign company that carries on business in Australia must be registered with the ASIC under the Corporations Act and comply with various disclosure and other requirements imposed on registered foreign companies under the Corporations Act.

In addition, there are events or circumstances that may result in a foreign lender, arranger, facility agent or security agent being taken to have a permanent establishment in Australia. Please contact our Australian tax group if you would like to receive further information in relation to the tax consequences.

No state or territory in Australia charges ad valorem stamp duty on loan and security documents — see also the answer to question 12 of the "If taking security" section.

The sale of secured property following enforcement can give rise to a liability for the security holder to pay goods and services tax (GST) on the sale, at the rate of 10% and liability for stamp duty if the sale of the property sold attracts duty, at normal conveyance rates. Land and goods will normally attract stamp duty. Stamp duty is charged on a state-by-state basis and, in most jurisdictions, is approximately 5% of the value of the property sold.

3. Are there any regulatory reporting requirements that lenders must observe in connection with those transactions?

Yes. In addition to reporting requirements applicable to an ADI under the Banking Act and an AFSL holder under the Corporations Act, a lender, arranger, facility agent or security agent may be subject to regulatory reporting requirements in the following instances:

- If it is carrying on business in Australia and, if so, it must be registered with the ASIC under the Corporations Act.
- If it is a "registrable corporation" under the Financial Sector (Collection of Data) Act 2001 (Cth) ("**FSCOD Act**"). A foreign corporation or a trading or financial corporation formed within Australia that engages in the provision of finance in the course of carrying on business in Australia is a "registrable corporation" if any of the following applies:

- Its assets in Australia that consist of (outstanding) debts due (being debts resulting from transactions entered into in the course of providing finance) at any time exceed AUD 50 million or more. Examples of transactions entered into in the course of providing finance include lending money (with or without security), carrying out activities that directly or indirectly result in the funding or originating of loans or other financing, acquiring debts due to another person, and purchasing bills of exchange or promissory notes (Section 32 of the FSCOD Act).
- The principal amounts of loans or other financing initiated (in the recently completed financial year) are AUD 50 million or more.

Registrable corporations must be registered with the APRA within 60 days, but they will not be subject to actual supervision by the APRA. They are subject to certain disclosure and reporting requirements.

The regulatory reporting requirements under the Corporations Act and/or FSCOD Act may apply to an entity as long as the above tests have been met, regardless of whether the entity is an ADI or an AFSL holder.

4. Is it necessary to establish a place of business in your jurisdiction in order to enforce any provision of the finance documents?

No.

5. Is a foreign bank/financial institution permitted to approach local entities for business?

No. A foreign bank that is not licensed as a bank in Australia must not engage in advertising or allow its staff to physically solicit business in Australia. This is one of the conditions set out by the APRA that is discussed in the answer to question 1 of this section. If the foreign bank fails to adhere to the five conditions set out by the APRA (as set out in the answer to question 1 of this section), the APRA may consider it to be in breach of Section 66.

If a financial institution is not a bank (and does not include the word bank in its name), there are circumstances in which it can approach Australian entities for business from offshore. There is currently* an exemption for approaching wholesale clients wholly from offshore. There are also exemptions in relation to offering particular financial products (for example, derivatives or foreign exchange contracts) to professional investors (a subset of wholesale clients).

* This exemption is set to expire on 31 March 2024.

When lending to borrowers

1. Are there any restrictions in relation to the type of borrower who may borrow foreign currency or in relation to the term of foreign currency and/or the amount of foreign currency borrowed by local entities?

No, there are no restrictions of this type. However, the borrower should take into consideration the Australian thin capitalization rules — see the answer to question 6 of this section.

2. Are there any restrictions on the rate of interest or default interest that may be charged?

In principle, there are no restrictions of this type in the case of corporate borrowers (in contrast with individuals, who are protected by statutory usury provisions, and individuals and small businesses, who may be protected by unfair contract terms legislation). The interest or default interest is governed by the contractual arrangements between the parties and by common law. However, there may be circumstances in which the default interest may be considered an unenforceable penalty.

3. Are there any restrictions on particular lenders or classes of lender entering into credit transactions with borrowers?

Yes, certain restrictions apply in relation to lending in Australia.

Please refer to the answer to question 1 of the "When considering whether to lend" section for information in relation to when various regulatory regimes or licensing requirements apply.

Please refer to the answer to question 2 of the "When considering whether to lend" section for information in relation to when a lender may be required to be registered with the ASIC under the Corporations Act as it is carrying on business in Australia.

Please refer to the answer to question 3 of the "When considering whether to lend" section for information in relation to when a lender is a "registrable corporation" under the Financial Sector (Collection of Data) Act 2001 (Cth) and is required to be registered with the APRA.

Please refer to the answer to question 11 of this section for information in relation to consumer credit regulation.

Please also note that under the Foreign Acquisitions and Takeovers Act 1975 (Cth), certain lenders may have to obtain the prior approval of the Australian FIRB when taking or enforcing security over Australian land or assets. Certain exemptions apply, such as the moneylending exemption referred to in the answer to question 1 of the "When considering whether to lend" section. Please refer to that answer for more information in relation to the moneylending exemption.

4. Are there any exchange controls that will apply to payments to be made in foreign currencies or to foreign lenders?

No.

5. Is there any requirement to deduct or withhold tax from any amounts to be paid or repaid to a lender (whether domestic or foreign)? If so, at what rate must tax be deducted and from what kinds of payment?

Repayments of the principal of loans are not subject to taxation in Australia. However, interest withholding tax, at the rate of 10%, is payable on interest paid to a foreign resident lender not carrying on business through an Australian permanent establishment by an Australian resident borrower not operating through an offshore permanent establishment or a nonresident borrower carrying on business through an Australian permanent establishment. Certain exemptions and rate reductions apply, such as debts that qualify under the public offer test and situations where interest is paid to a foreign resident financial institution that qualifies for an Australian double tax treaty benefit.

6. Are there any "thin capitalization" or other rules that may limit the extent to which interest payments may be deducted for tax purposes?

The Australian thin capitalization rules may limit debt deductions for entities that are geared in excess of certain thresholds. Under the rules, debt deductions will be denied to the extent a taxpayer's debt level exceeds the "maximum allowable debt" threshold. Please contact our Australian tax group if you would like to receive more information in relation to the thin capitalization rules.

7. Are there any registration, notarization, translation or reporting requirements in relation to the loan documents?

No — see the answer to question 11 of the "If taking security" section for the requirements in relation to security documents.

8. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to the loan documents? If yes, what are the amounts and when are they payable?

No — see the answer to question 13 of the "If taking security" section for the requirements in relation to security documents.

9. Does the law recognize the subordination of the debt that a debtor owes to one creditor to that which the debtor owes to another creditor? If yes, how is this usually effected?

Yes. The Corporations Act accepts subordination to which the subordinated creditor agrees. This is usually effected by contractual subordination, including intercreditor arrangements.

10. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors (e.g., the claims of employees and tax authorities or the claims of creditors under particular kinds of instrument)? If yes, what classes of creditors are preferred?

All unsecured creditors rank equally, except for certain classes of claims that have priority. These classes include the following:

- Costs and fees incurred by a liquidator or administrator.
- Employees' (excluding directors and their relatives) unpaid wages, superannuation, leave entitlements, etc. — for more information, please refer to the answer to question 1 of the "If things go wrong" section under the sub-heading "Winding up".

11. Are there any consumer protection or similar laws that apply if credit is made available to individuals or other classes of debtor? If yes, what laws are applicable?

Yes, the Australian Consumer Law (ACL) is the national law in relation to fair trading and consumer protection. The full text of the ACL is set out in Schedule 2 of the Competition and Consumer Act 2010 (Cth). The protections in the ACL are generally reflected in similar provisions in the Australian Securities and Investments Commission Act 2001 (Cth) ("**ASIC Act**") so that financial products and services are treated in the same way.

The ACL and the ASIC Act apply if the debtor is a "consumer" or a "small business" (both of which are defined terms).

The National Credit Code and the National Consumer Credit Protection Act 2009 (Cth) ("**National Credit Act**") apply if, when the credit contract is entered into or (in the case of pre-contractual obligations) is proposed to be entered into, the following all apply:

- The debtor is a natural person or a strata corporation (a defined term).
- The credit is provided or intended to be provided wholly or predominantly for personal, domestic or household purposes or to purchase, renovate or improve residential property for investment purposes or to refinance credit that has been provided wholly or predominantly to purchase, renovate or improve residential property for investment purposes.
- A charge is or may be made for providing the credit.
- The credit provider provides the credit in the course of the business of providing credit carried on in Australia or as part of, or incidentally to, any other business of the credit provider carried on in Australia.

Similar to the extended jurisdiction in respect of financial services, offshore conduct that is intended to induce people in Australia is considered to be carried out in Australia and subject to this regime. This is stated by the Australian legislature to be intended to capture credit providers who do not have a physical presence in Australia but may use the internet or intermediaries to offer consumer credit products to persons in Australia.

However, unlike the financial services regime, there is no clear exemption for activities with no solicitation by the provider. Therefore, where a loan request is made to an offshore lender, there is a risk that the resultant provision of credit is still a credit activity that is carried out in Australia.

This is consistent with ASIC guidance that even if only one of the borrowers is in Australia, the loan and the lending business is considered to be carried out in Australia.

The National Credit Act imposes a credit licensing regime and responsible lending obligations.

12. Are there any prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of: (a) its own shares or those of any affiliated company; or (b) assets owned by it or any affiliated company?

Yes, there are restrictions on a company giving financial assistance to a third party to acquire its shares or its holding company's shares, except where giving the financial assistance does not materially prejudice the interests of the company or its shareholders, the company's ability to pay its creditors, or where the assistance is approved by the shareholders under what is called a "whitewash" procedure, or the assistance is exempted. The "whitewash" procedure generally involves the following:

- Having the shareholders of the company approve the details of the financial assistance; and
- Filing certain notices with the ASIC.

Financial assistance cannot be given until at least 14 days after the lodgment with the ASIC of the notice informing it of the intention to give financial assistance. This means that financial assistance can typically only be given after an acquisition has been completed.

There are, however, no equivalent prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of assets owned by it or any affiliated company.

If taking security

1. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's secured creditors?

No, in the case of a real property mortgage or a security interest in the company's noncirculating assets under the Personal Property Securities Act 2009 (Cth) (PPSA), provided that the security interest was duly perfected. A secured creditor's floating charge (see the answer to question 3 of this section) or security interest attached to circulating assets, however, would rank behind certain employee claims (such as unpaid wages, superannuation payments, etc.) and administrator's fees and expenses.

2. May security given by a company rank in a specified order so as to secure liabilities owed to different creditors of the company in that order and, if that is not possible, is it viable for parties to enter into a contractual arrangement for the purposes of moderating this order?

Yes, secured creditors may agree that their respective securities rank in any order.

3. Does this jurisdiction recognise the concept of floating security or similar equivalent (i.e., security over a changing pool of assets that the company giving the security is free to buy, sell and generally deal with)?

Yes. Floating charges and security interests attached to circulating assets are referred to as circulating security interests in the PPSA.

4. If so, are there any practical reasons why floating security is difficult to take, maintain or enforce?

No. However, please note that claims under a floating security rank behind certain employee claims and administrator's fees and expenses, as mentioned in the answer to question 1 of this section.

5. May security be granted to a trustee to be held on trust for the lenders from time to time, in such a way that a change of lenders does not require new security to be taken?

Yes.

6. If not, are there any techniques that can be used to achieve substantially the same effect (e.g., parallel debt structures)?

Not applicable.

7. If an agent holds security for the lenders rather than a trustee, is it necessary to take new security on a change of lenders? If no, why not? If yes, are there ways to structure the transaction to avoid such a requirement?

Although the concept of agency is recognized in Australia, a trustee usually holds the security.

8. Under the laws of this jurisdiction, is there any class of asset over which it is difficult or impossible to grant effective and perfected security, or in relation to which any security granted will be of limited effect?

Generally, no. However, and as mentioned in the answer to question 1 of this section, a secured creditor's floating charge or security interest attached to circulating assets would rank behind certain employee claims and administrator's fees and expenses.

9. Under the laws of this jurisdiction, are there any restrictions on offshore lenders taking security over any class of asset?

Generally, there are no such restrictions specific to offshore lenders. However, offshore lenders must comply with the FATA and FIRB requirements described in question 1 of the "When considering whether to lend" section.

10. Must a company receive a corporate benefit in return for giving a guarantee or security? In particular, are there restrictions on the grant of upstream and cross-stream guarantees and security? If yes, briefly what is the effect of these laws?

Yes. The enforceability of a guarantee or security may be affected by certain laws in Australia that require the guarantee to benefit the guarantor (known as "corporate benefit") or certain laws relating to creditors' rights and the giving of a financial benefit to a related party of a public company, which requires approval from shareholders. Companies should also observe financial assistance rules in Australia, as described in the answer to question 12 of the "When lending to borrowers" section. Apart from the above, unless there is a specific restriction contained in the constitution of the guarantor or the grantor of the security, there would not be other restrictions.

11. What type of security interests does your jurisdiction recognise, e.g., pledge, charge, mortgage, hypothecation? In relation to each type of security interest, please state the formalities required to create and perfect that security.

Types of security interest

Security over land in Australia is granted under a real property mortgage. In relation to other types of tangible and intangible personal property, the PPSA has introduced a new concept of a "security interest" that not only covers pre-existing forms of security interests, such as fixed charges, floating charges, pledges and liens but also extends to any interest in personal property provided for by a transaction that, in substance, secures payment

or performance of an obligation. This new concept of security interest includes an interest in personal property provided by a range of transactions that were previously not treated as security arrangements in Australia if the transaction, in substance, secures payment or performance of an obligation, such as flawed asset arrangements, retention of title arrangements and leases of goods.

Formalities

Generally, a real property mortgage must be registered in the relevant land register. Each Australian state and territory has its own land titles office that administers the land register in relation to that place. To be registered, the mortgage must be validly executed and sufficiently identify the land that is the subject of the mortgage, the debt secured by the mortgage and the interest in the land that is to be mortgaged. Various other local formalities for registration in each state or territory must also be complied with, including in relation to registration forms, execution requirements and requirements regarding relevant title certificates.

The formal requirements that apply to security over personal property are less prescriptive. Under the PPSA, the creation of an effective security interest in personal property generally requires the security interest to have "attached," be "enforceable against third parties" and be "perfected".

Attachment

"Attachment" occurs when:

- The grantor has sufficient rights in the collateral or power to transfer rights in the collateral to the secured party; and
- Value is provided for the security interest or the grantor carries out an act by which the security interest arises.

This requirement is usually satisfied by the provision of a loan or other financial accommodation in return for the granting of the security interest or by the grantor signing a security agreement.

Enforceability against third parties

Being "enforceable against third parties" is a further step required by the PPSA and is satisfied when attachment has occurred and one of the following is satisfied:

- The secured party has "possession" of the collateral.
- The secured party has perfected the security interest by "control" of the collateral (which applies in relation to certain forms of personal property such as shares and certain bank accounts).
- The grantor has signed a security agreement that describes the collateral.

Perfection

"Perfection" is the final formal requirement and occurs when the security interest is attached to the collateral, the security is enforceable against a third party and any of the following applies:

- The secured party has "possession" of the collateral;
- The secured party has "control" of the collateral (which only applies in relation to certain forms of personal property such as shares and certain bank accounts); or
- A registration on the PPSR in favor of the secured party is effective with respect to the collateral (see the answer to question 12 of this section below).

12. Are there any registration, translation or notarization requirements in relation to security, guarantees, subordination or intercreditor documents?

Yes, there are registration requirements in relation to security in Australia.

For security over land, while it is not mandatory to register a mortgage if the mortgage is not registered, it will not have the benefit of registration and may be defeated by subsequent holders of legal interests in the land (including holders of subsequent mortgages). There is no prescribed time limit within which the registration of a mortgage must occur. However, until registration occurs, the secured party does not have the benefit of registration.

In relation to personal property, while registration is not mandatory, it is the most common method of perfection under the PPSA. The priority of unperfected security interests over personal property is generally deferred to perfected security interests and will generally vest in the grantor if the grantor becomes insolvent (i.e., it will not be enforceable against a liquidator or administrator of the grantor). For Australian companies and foreign companies doing business in Australia, the registration in respect of the security interest must generally occur within 20 business days of the creation of the security interest.

There are no registration requirements for guarantees and subordination or intercreditor agreements in Australia.

There are no translation or notarization requirements for security, guarantees and subordination or intercreditor agreements in Australia.

13. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in respect of security, guarantees, subordination or intercreditor documents? If yes, what are the amounts and when are they payable?

No state or territory in Australia charges ad valorem stamp duty on these documents. However, where the document contains a declaration of trust over cash receivables, such as the amount of a loan repayment, certain fixed duties may apply. Fees of a nominal amount are payable on the registration of security with the PPSR (see the answer to question 12 of this section).

If things go wrong

1. Please provide a brief description of the insolvency regime. In particular what rights and duties do unsecured and secured lenders have on the insolvency of a debtor? Are there any other matters of concern?

Australia has a number of formal corporate insolvency processes, as set out below:

- Voluntary administration
- A deed of company arrangement
- Restructuring and a restructuring plan
- Provisional liquidation
- Liquidation/winding up
- Receivership
- A scheme of arrangement

These processes may operate sequentially, concurrently or as alternatives.

Voluntary administration

The voluntary administration regime in the Corporations Act is the most widely used formal corporate insolvency mechanism. A voluntary administration may be commenced by any of the following:

- The directors of a company resolve that, in their opinion, the company is, or is likely to become, insolvent and that an administrator should be appointed.
- A liquidator or provisional liquidator if they think that the company is insolvent or likely to become insolvent.
- A secured creditor is entitled to enforce a security interest over the whole or substantially the whole of the company's assets.

Administrators' fees and expenses and employee entitlements ordinarily take priority over assets subject to a circulating security interest in external administration.

The administrator's right of indemnity out of the property of the company (for debts or liabilities incurred by the administrator and for the administrator's remuneration) takes priority over:

- Unsecured debts of the company; and
- Any debts secured by any circulating security interest (such as cash, receivables and inventory).

The administration usually ends after creditors resolve at the second meeting of creditors to:

- End the administration and return control of the company back to its directors.
- Enter into a deed of company arrangement if one has been proposed; or
- Have the company wound up.

Therefore, the voluntary administration process is very much creditor controlled.

Deed of company arrangement

A deed of company arrangement (DOCA) is a very flexible restructuring agreement between a company and its creditors. The terms of a DOCA are, in essence, limited only by the imagination of the draftsperson, and may allow the debtor company to:

- Trade on, whether under the control of its directors, deed administrators or receivers appointed by a secured creditor; or
- Provide for the sale of assets, for the sale or issue of equity or for creditors' claims to be transferred to a creditors' trust or another entity in a corporate group.

A DOCA will provide for the contribution to a fund for the distribution of dividends to creditors in return for a release of creditors' claims against the company.

A DOCA must give employee entitlements, such as wages, statutory priority to which the employees would be entitled in a winding up out of assets of the company, unless the employee creditors vote to modify this priority.

Significantly, a DOCA may bind secured creditors of a debtor company, even if they vote against or abstain from voting on the resolution to enter into the DOCA, but a DOCA leaves secured creditors free to deal with their security outside the DOCA.

Restructuring - restructuring plan

The new process of "restructuring" was introduced to the Corporations Act from the start of 2021.

The process has many similarities to voluntary administration, but unlike that process, it is a debtor-in-possession regime. The process is initiated by the directors, who appoint a restructuring practitioner to have oversight of the restructuring. To be eligible, companies must have liabilities of less than AUD 1 million (including contingent and future liabilities) and must not have used the process within the preceding seven years.

Like an administration, the restructuring practitioner's fees and expenses ordinarily take priority over assets subject to a circulating security interest.

The restructuring practitioner's right of indemnity out of the property of the company (for debts or liabilities incurred by the restructuring practitioner and for the restructuring practitioner's remuneration) takes priority over the:

- Unsecured debts of the company; and
- Any debts secured by any circulating security interest (such as cash, receivables and inventory).

The company develops a restructuring plan that is put to creditors. The "restructuring" phase will ordinarily end following a vote by creditors about this plan. The vote takes place without a formal meeting. There are two possible outcomes of the vote: either the restructuring plan is adopted (in which case it will become binding) or it is rejected by the creditors.

The intent of the restructuring plan is to create a fund that is used to pay creditors in return for compromising their claims against the company. The restructuring plan:

- Will identify what property of the company will be dealt with under the plan and its anticipated value, how it will be dealt with and, if sales are proposed, how they will take place; and
- Must provide that all admissible debts and claims rank equally.

As the restructuring plan cannot be proposed unless all outstanding employee entitlements have been paid, and as future employee entitlements are excluded from its operation, employee entitlements are given no specific priority in the plan itself.

A secured creditor is only bound by the restructuring plan:

- To the extent that the value of the assets that are the subject of its security is less than its debt (and then to the extent of its unsecured claim); and
- Otherwise, only to the extent that the secured creditor consents to be bound by the plan.

Provisional liquidation

The Federal Court of Australia or the Supreme Courts of the states and territories of Australia may appoint a provisional liquidator to the company. The court may appoint a provisional liquidator if a valid winding up application has been made and it is reasonably likely that a winding up order will be made. A provisional liquidator's primary duty is to preserve the status quo to ensure the least possible harm to all parties and to enable the court to decide, after further examination, whether the company should be wound up.

Winding up

A winding up (or liquidation) on insolvency is a terminal procedure intended to realize a company's assets and distribute the assets among its creditors.

A court-ordered or compulsory winding up can only be effected by an order of the Federal Court of Australia or the Supreme Courts of the states and territories of Australia.

A creditors' voluntary winding up usually commences either:

- Pursuant to a special resolution of the company's members in circumstances where there is no declaration of solvency made by the directors of the company; and
- By resolution of creditors at a second meeting of creditors of a company in voluntary administration.

In a winding up, all unsecured creditors with debts or claims against the company are entitled to participate in seeking payment of a dividend from the available assets if the circumstances giving rise to their debt or claim arose before the "relevant date." The relevant date is usually the date on which the winding up order was made or the date of the appointment of the administrator in a preceding voluntary administration.

Claims are submitted to the liquidator pursuant to a statutory proof of debt procedure.

Secured creditors are generally entitled to enforce their security interest during the liquidation. However, a secured creditor's claim to assets subject to a circulating security interest (usually cash, receivables, inventory and similar assets) may be subordinated to specified employee claims such as wages, superannuation, and leave and redundancy entitlements, where the property of the company is insufficient to meet payment of those employee claims.

The following specified priority debts and claims will take priority over the claims of unsecured creditors:

- Expenses incurred by an administrator or liquidator to preserve and realize the property of the company.
- The costs and expenses of obtaining any order for liquidation.
- Priority employee entitlements.

Receivership

A secured creditor may appoint its own receiver "over the top" of the administrator — generally, provided it does so within 13 business days of the appointment of the administrator. The court may also appoint a receiver in exceptional circumstances. If the secured creditor appoints a receiver, the receiver assumes effective control of some or all of the company's assets (depending on the terms of the charge or security) with a view to realizing enough of the charged assets to repay the debt owed to the secured creditor. Concurrent receiverships and administrations are common.

While secured creditors are subject to a moratorium, the administrator is not at liberty to deal with the assets that are the subject of secured creditors' rights without the secured creditors' consent, leave of the court or unless it is in the ordinary course of business.

A receiver has no direct role in relation to the unsecured creditors of the company.

Schemes of arrangement

A scheme of arrangement is a mechanism that may be used by a solvent or insolvent company to reach an agreement or compromise with its creditors or members, or both. Schemes of arrangement are, however, less commonly used as a restructuring process, due to the time and cost associated with their implementation.

2. Is it possible to obtain a moratorium before insolvency?

As a general proposition, no. Australia has introduced a "safe harbor" regime that protects directors from personal liability for insolvent trading. The regime does not provide any moratorium for claims against the company itself.

A discussion of the moratoria that arise after the commencement of formal insolvency processes is set out below.

Voluntary administration

The voluntary administration procedure imposes a statutory moratorium in respect of claims and proceedings against the company during the period of the voluntary administration.

Subject to a few limited exceptions, unless consent of the administrator or the court is first obtained, the following will apply during the period of the voluntary administration:

- Creditors will be prohibited from taking any action against the company to recover debts, enforce security interests or have the company wound up.
- Owners or lessors of property that is being used by the company (including landlords and retention of title suppliers) will be prohibited from seizing or reclaiming their property.

There is also a general prohibition on the transfer of shares of a company in administration and a moratorium on the enforcement of guarantees given by directors, their spouses or relatives.

The statutory moratoria ceases once the company proceeds to liquidation or a DOCA, although other moratorium provisions will then apply.

Receivership

There is no moratorium or stay in relation to the enforcement of claims against a debtor company where it is only in receivership. However, where a receivership is concurrent with an administration, the receiver will effectively have the benefit of the statutory moratorium applicable in the administration.

Deed of company arrangement

The Corporations Act specifies certain minimum requirements of a DOCA, including the nature and duration of any moratorium period.

Restructuring - Restructuring plan

The restructuring process attracts similar moratoria for claims against the company as the voluntary administration process.

Creditors bound by the restructuring plan cannot apply or proceed with an application to wind up the company or begin or proceed with court proceedings or enforcement of court orders, where to do so would rely on a debt compromised by the plan.

Winding up

In a winding up, there is a statutory stay of proceedings against the company and a prohibition on enforcement (by unsecured creditors) against the property of the company other than with the consent of the liquidator or leave of the court. Unsecured claims against the company should generally be pursued under the proof of debt procedure.

Dealings with the property of the company after a winding up other than by the liquidator are void.

Prohibition on use of *ipso facto* clauses

There is a statutory moratorium on the enforcement of ipso facto clauses in pre-insolvency contracts entered into on and from 1 July 2018 to enable the proper facilitation of some of the insolvency processes identified above. This stay does not apply to variations to or novations of contracts where the original contract was entered into prior to 1 July 2018, but only where such variation or novation is made before 1 July 2023. From 1 July 2023, these carve-outs for varied or novated contracts will cease to apply.

An ipso facto clause is a clause in a contract that permits the other contracting party to either terminate or modify the operation of the contract due to an insolvency event occurring.

A contracting party is restricted from enforcing such a right while the insolvent party is undergoing a voluntary administration process, a restructuring, a receivership over all or substantially all the assets of the company, or a scheme of arrangement undertaken by reason of the company's insolvency. Therefore, the other contracting party will not be entitled to rely on the ipso facto clause to terminate the contract or modify or accelerate any payments under the terms of the contract in reliance on the insolvency event.

Importantly for lenders, there are various exclusions to the operation of the restriction. A significant exclusion is for lenders in respect of rights to enforce security agreements with obligors (but note the discussion below in question 4, dealing further with the enforcement of security agreements in a formal insolvency context). There are numerous other exemptions to the stay. In the event that a restriction imposed on the enforcement of an ipso facto clause is relevant to you, we recommend that you take specific advice in relation to those exemptions relevant to your circumstances.

3. When a company is the subject of a formal insolvency procedure, can the company's pre-insolvency transactions be set aside?

Yes, in certain circumstances. There is a range of actions that become available to a liquidator when a company is wound up, which can involve challenges to pre-insolvency transactions.

Liquidators have broad powers to investigate the affairs of the company, including compulsory powers to compel the assistance of directors and officers as well as the production of books and records and to require the attendance of persons before a court to face examination.

Liquidators may also have various causes of action available to them to recover assets or undo certain transactions, including recovering preferential payments, unwinding uncommercial transactions and setting aside unfair loans and unreasonable director-related transactions. Financing transactions are not immune from those causes of action as set out below.

Unfair preferences

A liquidator may recover, as an unfair preference, payments made to, or benefits received by, a creditor of the company in respect of an unsecured debt owed by the company within a period of six months prior to the deemed commencement of the winding-up, if:

- That unsecured creditor was preferred over other unsecured creditors; and
- The payment or benefit was received at a time when the company was insolvent or the company became insolvent as a result of making that payment or giving that benefit.

There are various defenses to an unfair preference claim, including that the payment(s) were received in good faith or that a "running account" existed between the creditor and the debtor.

A grant of security for a previously unsecured debt may constitute an unfair preference that can be avoided by a liquidator under this cause of action.

Rights to recover unfair preferences may be more restricted where the company has undergone a liquidation using the simplified liquidation regime. Such a regime is only available for companies with liabilities of less than AUD 1 million.

Uncommercial transactions

An uncommercial transaction of the company entered into within two years prior to the deemed commencement of the liquidation is voidable on the application of the liquidator if it was entered into, or given effect to, at a time when the company was insolvent or if the company became insolvent as a result of it entering into the transaction.

Whether a transaction is "uncommercial" is assessed by reference to, among other factors, the benefits and detriment to the company and to other parties entering into the transaction. There are various defenses to an uncommercial transaction claim.

Certain financing transactions may be capable of being attacked as uncommercial transactions, for example, the granting of security for previously unsecured debts or the granting of guarantees for the indebtedness of third parties.

4. When can a lender enforce its security? Can security be enforced out of court following an event of default (or other contractual trigger event), or is a court order required? Are there any restrictions that apply before a lender may enforce its security?

As a general proposition, a secured lender will be free to enforce its security at any time following an event of default by a debtor on the terms of the relevant security instrument and without a court order. However, a secured lender may need to obtain a court order permitting the enforcement of its security where, for example, there is some defect or ambiguity in the security instrument. In relation to security over real estate and certain

other types of assets, various notice requirements may also apply before enforcement action may be taken (or a sale of the secured property effected).

The other restriction is that if a voluntary administrator is appointed to a debtor or a restructuring is commenced, then the secured lender, if it has security over the whole, or substantially the whole, of the property of the debtor, has 13 business days from the appointment of the voluntary administrator or the commencement of a restructuring to elect to appoint a receiver.

Depending on the nature of the security, for example, if the security is a possessory security interest, further restrictions on enforcement rights during an administration or restructuring may apply.

5. Do any limitation periods apply in relation to bringing an action to enforce security?

Yes. However, as Australia is a federation of states and territories, each of which may have its own peculiar laws concerning the limitation of actions for suing on securities and in respect of interests in land, the relevant time limits will turn on the facts. Expert assistance should be sought in relation to particular enforcement scenarios.

6. Is there any particular way in which secured assets must be liquidated on enforcement (e.g., by auction or court sale)?

No, but as a general proposition, mortgagees and receivers are under a duty, when exercising a power of sale of secured property, to take all reasonable care to obtain either of the following:

- Not less than market value for the property if, when it is sold, it has a market value; or
- The best price reasonably obtainable if it does not have a market value.

To best protect themselves from liability, mortgagees and receivers will typically obtain independent valuations of secured assets prior to attempting to sell those assets and will then often engage in a public sale process or campaign to generate interest in the asset, for example, by public auction, tender or expressions of interest.

7. Are there any particular legal or practical difficulties or delays in enforcing security?

Where the relevant security instruments are immediately enforceable in accordance with their terms, the enforcement and sale of the security property can be straightforward and completed relatively quickly.

However, that process can be complicated or delayed in any number of ways where third parties seek to intervene, for example, where competing interests are claimed in land or where a challenge to the relevant power of sale is commenced.

The possibility of a voluntary administration or restructuring moratorium (discussed in the answer to question 2 of this section) must also be kept in mind.

8. In relation to enforcement, are there any specific requirements to be borne in mind if the lender is a foreign entity?

Issues may arise for a foreign entity that is the mortgagee of land and wishes to acquire the relevant secured property (if it is real property) (rather than exercising a power of sale to a third party) in the event of a default by the mortgagor. In that case, the mortgagee may first need to obtain approval from the FIRB before completing the acquisition. Similar considerations may also apply if the security is over shares in an Australian listed company.

For more information regarding the enforcement of security by a foreign entity, please see the answer to question 1 of the "When considering whether to lend" section.

Separately, the insolvency process may be complicated if a debtor company has assets in multiple jurisdictions or where there are concurrent foreign and local proceedings regarding the debtor company. However, the UNCITRAL Model Law on Cross Border Insolvency has been adopted in Australia in the Cross-Border Insolvency Act 2008 (Cth), which may be invoked by the application for "recognition of a foreign proceeding." The process that flows is designed to facilitate multijurisdictional insolvencies and can be a useful tool in these scenarios.

9. Is there any reason why you think that arbitration rather than litigation might be advantageous in resolving disputes under the finance documents, and if so, why? Please outline the relative merits of arbitration and litigation, including the ease of enforcement of foreign judgments and foreign awards from different jurisdictions. Is it possible to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit?

The key advantage of arbitration is the availability of arbitral awards being enforced in over 150 countries that are parties to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. This means that an award made in one state that is party to the New York Convention can be enforced by the courts of any other state party (e.g., where the award debtor has assets) as a judgment of the court. There are limited grounds (relating to procedural issues and public policy) on which a court can refuse to enforce an award.

Foreign judgments can generally be enforced in countries and from countries where reciprocal arrangements have been established if there are no reciprocal arrangements, parties seeking to enforce a foreign judgment in Australia will need to rely on common law principles.

Other advantages of arbitration include that an award is final and binding and cannot be appealed. It can only be challenged on limited procedural grounds or public policy. Litigation generally permits appeals (either by right or by leave) that may involve one or more layers of appeal and involve additional time, cost and complexity. However, the right to appeal in litigation may also be considered an advantage, depending on the circumstances of the case.

In addition, arbitration proceedings in most places (including Australia) are confidential unless the parties expressly agree otherwise. Litigation is generally conducted in public, with the decision also being made available to the public.

Other advantages of litigation include the certainty of the procedure of the courts and costs and efficiency. Compared with other jurisdictions, Australian courts are known to finalize matters promptly and efficiently. The courts also have the power to join additional parties to proceedings (provided they are subject to the court's jurisdiction). With arbitration, the powers of the tribunal are more limited to those powers given by the parties in the arbitration agreement or by the arbitral rules or the law that applies. For example, they cannot join parties unless the parties have consented to arbitration.

A hybrid enforcement clause that allows for the election by one party to pursue claims through litigation or arbitration is enforceable in Australia.

10. Are asymmetrical jurisdiction clauses enforceable? (By this we mean clauses that allow the lenders, but not the borrowers, to make certain choices in relation to choice of jurisdiction and how to litigate. These types of clauses allow the lenders, but not the borrowers, to commence proceedings in any court they choose, but restrict the borrowers to commencing proceedings in one jurisdiction only. This may also allow the lenders, but not the borrowers, to choose whether to litigate the finance documents before a court or to submit to arbitration in relation to them, but restrict the borrowers to either litigation or arbitration, as specified in the agreement).

It is common for an option clause (where one party may choose arbitration over litigation or vice versa) to be included in finance documents. These clauses have not yet been tested in the Australian courts but they have been enforced by the English courts. The definition of an "arbitration agreement" under the International Arbitration Act 1974 (Cth) would appear to be broad enough to cover these option clauses. There is nothing in the Act or the general law that would prevent a party from agreeing to this type of option clause.

Asymmetrical jurisdiction clauses that purport to restrict the right of one party to commence proceedings in one jurisdiction but permit the other party to commence proceedings in any jurisdiction have not been considered in the Australian courts. It is likely that, if faced with this type of clause, an Australian court would resolve the issue of whether it had jurisdiction by reference to the common law principle of forum non conveniens.

Working digitally

1. Is it possible for documents to be executed electronically (whether by the manual insertion of a digital signature or the use of an e-signing platform) under the laws of this jurisdiction? If so, is this limited to only particular types of finance documents?

The electronic execution of documents may be permitted in Australia, depending on the following:

- The type of document, that is, whether the document is an agreement or a deed.
- If the document is to be signed by a natural person or a corporation.

Execution by natural persons

Generally speaking, agreements can be signed electronically by natural persons. However, certain types of agreements must be signed in wet ink (such as mortgage documents to be lodged with the relevant land registry) unless electronic execution is expressly permitted in the relevant legislation or by the relevant authority. See the answer to question 3 of this section for further details.

In respect of deeds, the electronic execution of deeds has historically been problematic due to the long-standing common law requirement for deeds to be written on parchment or paper and, therefore, requiring wet ink signatures. However, the electronic execution of deeds by natural persons is now allowed in the following jurisdictions:

- New South Wales (NSW) under the Conveyancing Act 1919 (NSW).
- Queensland under the Property Law Act 1974 (Qld) pursuant to amendments passed by the Justice and Other Legislation Amendment Act 2021 (Qld) — except for powers of attorney by individuals in deeds and general powers of attorney, which must be a physical document and witnessed (subject to limited exceptions).
- Victoria under the Electronic Transactions (Victoria) Act 2000 (Vic) pursuant to amendments passed by the Justice Legislation Amendment (System Enhancements and Other Matters) Act 2021 (Vic).

No other Australian states have enacted measures concerning the electronic execution of deeds by natural persons.

Execution by corporations

Corporations registered under the Corporations Act can sign documents electronically by its authorized agent under Section 126 of the Corporations Act or by its directors and company secretaries under Section 127 of the Corporations Act.

However, if a corporation signs by an authorized agent, the other parties to the contract may not rely on the assumption in Section 129(5) of the Corporations Act, which provides that a person may assume that a document has been duly executed by a company if it is executed in accordance with Section 127(1) of the Corporations Act.

Under Section 127(1) of the Corporations Act, a corporation may execute a document without a common seal if the document is signed by any of the following:

- Two directors of the company;
- A director and a company secretary of the company; or
- For a proprietary company that has a sole director who is also the sole company secretary — that director

Electronic execution and split execution under Section 127(1) of the Corporations Act is allowed pursuant to amendments to the Corporations Act passed in the Corporations Amendment (Meetings and Documents) Act 2022 (Cth), which came into force on 22 February 2022.

The latest amendments to the Corporations Act under the Treasury Laws Amendment (*Modernising Business Communications and Other Measures*) *Act 2023* (Cth) closed several existing gaps, confirming that any document

required or permitted to be signed under the Corporations Act can now be signed physically or electronically. In addition, electronic signing is expressly allowed for other documents that require a signature such as directors' annual reports and declarations and creditors' statutory demands.

Split execution by directors: Section 110A of the Corporations Act permits directors to sign a copy or counterpart of a document (including a deed) by wet ink or electronically without the need for that copy or counterpart to include the signature of the other company officer signing the document. Each director must sign a complete copy of the document.

Electronic signature by directors: For electronic execution of a document (including a deed) to be effective, the following conditions must be met:

- A method of signing is used to identify the person in the electronic signature and to indicate the person's intention to sign a copy or counterpart of the document. Platforms such as DocuSign would appear to satisfy this requirement.
- The copy or counterpart includes the entire contents of the document.
- The method used to sign electronically is "as reliable as appropriate for the purpose for which the information was recorded, in light of all the circumstances, including any relevant agreement" or is proven, in fact, to have identified the signatory and the signatory's intention in respect of the contents of the document, by itself or together with further evidence.

In practice, when a company is executing a document under Section 127 of the Corporations Act, directors can sign electronically, provided that the method used identifies the signatory and indicates their intention. This can be done in one of two ways:

- By applying an electronic or digital signature through an application such as Adobe Sign or DocuSign, which would appear to be valid under the act without further evidence, as these applications use authentication technology to verify the signer's identity.
- By applying an "e-signature," for example by "copy and pasting" an image of the signature into a document. This method would require further evidence of the signatory's identity and intention (for example, through a confirmatory email) given the risk that the e-signature could be applied without the signatory's consent.

2. Where the witnessing of a signing is contemplated, is it possible for the witness to verify the signature over a live video call?

Regarding corporations, witnessing the affixation of a common seal can be done remotely under Section 127(2A) of the Corporations Act. Witnessing a signing is not otherwise required under the Corporations Act and depends on the laws of the relevant State.

Remote witnessing is now available in NSW, Queensland and Victoria:

- In NSW, the Electronic Transactions Act 2000 (NSW) allows for remote witnessing by live audio-visual link, subject to procedural requirements.
- In Queensland, the Property Law Act 1974 (Qld) and the Powers of Attorney Act 1998 (Qld) permit deeds and general powers of attorney for corporations to be executed electronically without a witness. Witnessing of the signing of affidavits and statutory declarations may also be done by audio-visual link, subject to procedural requirements.
- In Victoria, the Electronic Transactions (Victoria) Act 2000 (Vic) permits witnessing to occur via audio-visual link for most documents (including deeds), subject to procedural requirements. With the exception of testamentary instruments and power of attorney documents, the witness does not need to be physically located in Victoria. All of the witnessing requirements must be satisfied on the same day.

In other Australian jurisdictions, specific legislation allowing for the remote witnessing of documents typically used in financing transactions does not currently exist or has expired (in the case of temporary COVID-19 measures).

3. Is it possible to register/perfect security electronically without wet ink signatures?

Real property

With the exception of NSW, Victoria and South Australia, wet ink signatures are ordinarily required for a real property mortgage to be validly executed and thereafter registered in the relevant land register.

In particular, in Queensland, wet ink signatures are still ordinarily required for the execution of mortgage documents that are intended to then be delivered to the land register for registration. However, mortgages lodged electronically in accordance with the Electronic Conveyancing National Law (Queensland) are permitted to be electronically signed.

Personal property

Security over personal property governed under the PPSA may be perfected by "possession", "control" or registration on the PPSR (see the answers to questions 10 and 11 of the "If taking security" section for more details). The process of registering a security interest on the PPSR is completed online and no further signatures from the grantor or secured party will be required to complete the process. However, it will be necessary to examine if the underlying security agreement has been executed validly in accordance with the formalities described in the answer to question 1 of this section.

4. Are there any other legal restrictions that may prevent the parties from executing a finance transaction electronically?

There are no other restrictions apart from those above. As discussed, only some of the COVID-19 emergency measures put in place during the pandemic have been permanently adopted under statute and the specific formalities will depend on the jurisdiction under which the documents are signed.

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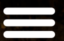
CAMBODIA



Cambodia

When considering whether to lend

1. **Is it necessary or advisable for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in this jurisdiction: (a) by reason only of its execution, delivery or performance of the finance documents; or (b) to enable it to enforce its rights under the finance documents?**

   Currently, there is a law that requires a person providing loans on a regular basis to apply for a banking license from the central bank. This requirement is applicable to both local and offshore lenders. However, in practice, we are unaware of any circumstance where the regulator enforces this rule on offshore lenders. The rule does not apply to the arranger, facility agent or security agent.

   Please note that our responses are prepared in the context of cross-border lending by an offshore lender to customers in Cambodia.

2. **Will any lender, arranger, facility agent or security agent be deemed to be resident, domiciled, carrying on business or subject to tax by reason only of the execution, delivery, performance or enforcement of the finance documents?**

   There is a risk of a lender, arranger, facility agent or security agent being deemed to be carrying on business in Cambodia due to the execution, delivery, performance or enforcement of the finance documents because of the broad definition of "business" under the Law on Taxation dated 16 May 2023 ("**Law on Taxation**"). The legal meaning of "business" is "economic activity with the aim of deriving income." The term "economic activity" is defined broadly under the Law on Taxation as the regular, continuous or from time-to-time activity of a person, whether or not for profit, in relation to the supply of or with the intent to supply goods or services to another person for the purpose of obtaining a benefit. However, there is no legal definition of "benefit." Entering into finance documents in a commercial situation should always involve a benefit and would, therefore, technically fall within the definition of "economic activity." Notwithstanding this, the risk is low in our view because we have never seen the execution, delivery, performance or enforcement of finance documents being deemed "economic activity." However, if a lender, arranger, facility agent or security agent is deemed to be performing an economic activity, it must register with the Cambodian tax authority within 15 days following the commencement of those activities. In this case, there is also a risk that the entity will also be deemed to have a permanent establishment (PE) in Cambodia. The Cambodian tax authority decides on this matter on a case-by-case basis.

   If an entity is deemed to have a PE, any income generated from a Cambodian source will be subject to a 20% tax on that income (known as corporate income tax in other countries). However, even if, in some cases, a PE is deemed to exist, to our knowledge and to date, the Cambodian tax authority has never enforced the tax income laws. It currently relies entirely on the withholding tax mechanism (for example, payment of interest to a non-resident taxpayer is subject to withholding tax at the rate of 14%). However, the approach of the Cambodian tax authority may change. Therefore, it would be prudent to obtain current advice before proceeding.

3. **Are there any regulatory reporting requirements that lenders must observe in connection with those transactions?**

   No.

4. **Is it necessary to establish a place of business in your jurisdiction in order to enforce any provision of the finance documents?**

   No.

5. **Is a foreign bank/financial institution permitted to approach local entities for business?**

   No, as banks are usually required to have a license first.

When lending to borrowers

1. **Are there any restrictions in relation to the type of borrower who may borrow foreign currency or in relation to the term of foreign currency and/or the amount of foreign currency borrowed by local entities?**

   No.

2. **Are there any restrictions on the rate of interest or default interest that may be charged?**

   Yes. Under the Civil Code 2007 ("**Civil Code**"), the interest rate for a loan may be fixed by a contract, but the Ministry of Justice may set a maximum interest rate within the range of 10% to 30% per annum ("**MOJ Rate**"). The current MOJ Rate is 18% per annum. The rate fixed by a contract may not be higher than the MOJ Rate. However, it is unclear whether the MOJ Rate applies to an offshore lender that is a bank or financial institution.

   If the contract indicates that interest is payable but fails to specify the rate, 5% will apply.

   In relation to default interest, the Ministry of Justice has fixed a ceiling rate. Currently, the ceiling rate is 27% per annum of the principal amount of the loan.

3. **Are there any restrictions on particular lenders or classes of lender entering into credit transactions with borrowers?**

   No.

4. **Are there any exchange controls that will apply to payments to be made in foreign currencies or to foreign lenders?**

   There is no restriction on foreign exchange operations, provided that loan disbursements and repayments are made through an authorized intermediary (i.e., a Cambodian-licensed bank). However, the National Bank of Cambodia may impose temporary restrictions on foreign exchange operations during times of foreign exchange crises.

5. **Is there any requirement to deduct or withhold tax from any amounts to be paid or repaid to a lender (whether domestic or foreign)? If so, at what rate must tax be deducted and from what kinds of payment?**

   Payment to non-resident lender

   A resident taxpayer making payments of interest or other types of payments, such as fees (except payment on goods and the repayment of a loan), to a non-resident lender, must withhold and pay withholding tax at a flat rate of 14% of the amount of the payment.

   Cambodia has double taxation agreements, which have an effect on implementation, with some countries such as the Hong Kong Special Administrative Region, the Republic of China, Singapore, Thailand, Vietnam, Indonesia, Brunei, the Macao Special Administrative Region, the Republic of Korea and Malaysia. Therefore, if a non-resident lender is from any of these countries, the 14% rate could be reduced to 10% if the legal condition is met.

Payment to resident lender

For an interest payment, the interest payment by a resident borrower to a resident lender is subject to withholding tax at the rate of 15%, but it is exempted if the resident lender is a domestic bank and if it is a repayment loan.

For service-related payments, the withholding rate would be 15%, but it is exempted in the following circumstances:

- Payment of service to a tax-registered lender and supported by a valid value-added tax (VAT) invoice.
- Payment of service with an amount less than KHR 50,000 (approximately USD 12.50), regardless of whether there is a proper VAT invoice or not.

6. Are there any "thin capitalization" or other rules that may limit the extent to which interest payments may be deducted for tax purposes?

The deductible interest expense for one taxable year must not exceed 50% of the net non-interest profit combined with the interest income. In cases where the total interest expense exceeds the amount allowed to be deducted for one taxable year, the interest expense will be carried forward successively to the following tax years until the fifth tax year. On a separate but related note, for a related party's loan, the borrowing rate must follow the arm's length principle under the Cambodian transfer pricing rule. Otherwise, it would be subject to reassessment.

7. Are there any registration, notarization, translation or reporting requirements in relation to the loan documents?

No. However, for tax purposes, the borrower must file the loan agreement with the Cambodian tax authority within 30 days after the relevant transaction date. Otherwise, there is a risk that the tax authority may reassess the loan as a taxable profit for the borrower. However, under current practice, the risk is low. In addition, late filing of the loan agreement will result in penalties.

8. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to the loan documents? If yes, what are the amounts and when are they payable?

No.

9. Does the law recognize the subordination of the debt that a debtor owes to one creditor to that which the debtor owes to another creditor? If yes, how is this usually effected?

There is no specific law governing a subordination arrangement. The general rules of the contract are applicable.

Two principal methods are used to document these types of arrangements, usually in the form of a tripartite agreement between the senior lender, the junior lender and the debtor. The two methods are as follows:

- The contingent debt method, by which the junior lender's right to have its debt repaid is contingent on the senior lender's debt having been repaid first
- The turnover method, by which the junior lender agrees to pay the senior lender (and/or to hold the proceeds on behalf of the senior lender) any amounts paid by the debtor to the junior lender, until the senior lender has been repaid.

10. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors (e.g., the claims of employees and tax authorities or the claims of creditors under particular kinds of instrument)? If yes, what classes of creditors are preferred?

Under the Law on Insolvency 2007 ("**Insolvency Law**"), the classes of unsecured and unsubordinated claims against a debtor that would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors are as follows:

- Employees' wages, provisional administrator remuneration, administrative fees and court fees
- Outstanding state taxes
- Other admissible unsecured claims, i.e., general unsecured claims exceeding the secured claims that are not satisfied as secured claims

However, please note that the Insolvency Law does not apply to claims against debtors that are covered by the Law on Banking and Financial Institutions 1999 ("**Law on Banking and Financial Institutions**"), the Law on Insurance 2014 ("**Law on Insurance**") and the Law on Non-Government Securities 2007 ("**Law on Non-Government Securities**"), unless provided for in those laws. The Law on Banking and Financial Institutions contains specific ranking provisions for claims against banks, microfinance institutions and other financial institutions stated in that statute. The Law on Insurance contains specific ranking provisions for claims against insurance companies or other entities stated in that statute. The insolvency regime for entities covered by the Law on Non-Government Securities such as securities dealers, securities underwriters, securities brokers, investment advisers or other entities stated in that statute is governed by 2018 Sub-Decree No. 24 on Rehabilitation and Liquidation in Securities Sector.

11. Are there any consumer protection or similar laws that apply if credit is made available to individuals or other classes of debtor? If yes, what laws are applicable?

Yes, if credit is made to a consumer for personal, domestic or household purposes, the 2019 Law on Consumer Protection applies to protect such borrowers' rights and interests.

12. Are there any prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of: (a) its own shares or those of any affiliated company; or (b) assets owned by it or any affiliated company?

No.

If taking security

1. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's secured creditors?

Under the Insolvency Law, claims for employees' wages, provisional administrator remuneration, administrative fees and court fees rank above the claims of the debtor's secured creditors.

If the debtor is a legal entity covered under the Law on Banking and Financial Institutions, the following claims rank above those of the debtor's secured creditors:

- Fees or other charges for the provisional administration and for the liquidation, either voluntary or by order of the court
- Taxes and fees due to the National Treasury
- Salaries owed to staff for a period of up to three months preceding the date of the liquidator's appointment.

If the debtor is a legal entity covered under the Law on Insurance, the following claims rank above those of the debtor's secured creditors:

- Remuneration and other expenses related to the provisional administration and liquidation
- Claims by insurance claimants
- Claims by insurance policyholders
- Employees' wages, administrative fees, court fees and other court levies

If the debtor is a legal entity covered under the Law on Non-Government Securities, the following claims rank above those of the debtor's secured creditors:

- Remuneration and other expenses related to the provisional administration and liquidation
- Employee salary, administrative fees, court fees and other court levies.

2. May security given by a company rank in a specified order so as to secure liabilities owed to different creditors of the company in that order and, if that is not possible, is it viable for parties to enter into a contractual arrangement for the purposes of moderating this order?

Yes. Generally, security interests over the same collateral take priority according to the order in which they are filed or are otherwise perfected. However, secured creditors may agree to vary or forego the usual order of priority.

3. Does this jurisdiction recognise the concept of floating security or similar equivalent (i.e., security over a changing pool of assets that the company giving the security is free to buy, sell and generally deal with)?

Yes, a security package over a changing pool of movable property is possible in Cambodia.

4. If so, are there any practical reasons why floating security is difficult to take, maintain or enforce?

While there is no restriction under Cambodian law, the concept has never been tested with a Cambodian court.

5. May security be granted to a trustee to be held on trust for the lenders from time to time, in such a way that a change of lenders does not require new security to be taken?

The law is silent on this matter. However, it is now becoming a trend for a security interest to be created in favor of a trustee.

6. If not, are there any techniques that can be used to achieve substantially the same effect (e.g., parallel debt structures)?

Not applicable.

However, in a syndicated loan transaction, an Asia Pacific Loan Market Association-style security agent structure (i.e., where the security agent holds the security on behalf of the original lenders and any assignees that become lenders of record) is commonly used to achieve substantially the same effect as a trust. See also the answer to question 7 of this section

7. If an agent holds security for the lenders rather than a trustee, is it necessary to take new security on a change of lenders? If no, why not? If yes, are there ways to structure the transaction to avoid such a requirement?

No, taking new security on a change of lenders is unnecessary. It is possible for security to be given to and to be enforceable by a person such as a security agent as security for debts owed to other persons such as the syndicated lenders.

The security agent may hold a security interest on behalf of the lenders under the concept of a "mandate" under the Civil Code. The term "mandate" refers to a contract by which one party ("**mandator**") grants to another party ("**mandatary**") the power to administer business on behalf of the mandator. Moreover, under the Law on Secured Transactions 2007 (LST), the term "secured party" includes a lender, seller or other person in whose favor a security interest is created under a security agreement. Therefore, a security agent may hold a valid security interest on behalf of the syndicate of lenders whether it is a lender or not. The security remains the same without the need to make any changes to the registration when there is a change in the pool of lenders in the syndicate.

However, this structure has never been tested in a Cambodian court.

8. Under the laws of this jurisdiction, is there any class of asset over which it is difficult or impossible to grant effective and perfected security, or in relation to which any security granted will be of limited effect?

Security interests in Cambodia can be created under either the Civil Code or the LST

Under Cambodian law, there are two fundamental types of security: real security and personal security. Real security creates security interests over "real" rights, i.e., the right to control an object that may be directly asserted against any person. Personal security includes a guarantee and a joint obligation.

Civil Code

Under the Civil Code, only an object or right that is transferable can be the object of a real security right. The object of a real security right under the Civil Code includes movable property, immovable property, a perpetual lease, a usufruct of immovable property, and contractual and other claims.

LST

Under the LST, collateral may be goods or movable things of any nature. The collateral may be in existence or may arise in the future and may be located anywhere, within or outside Cambodia. The LST classifies movable collateral into various categories but generally, it can be divided into the following two broad categories:

- Tangible collateral
- Intangible collateral

Tangible collateral consists of "goods," defined as all things that are movable when a security interest attaches, and this broad classification can be further subdivided into five specific categories:

- Consumer goods
- Inventory
- Farm products
- Equipment
- Fixtures

Intangible collateral may consist of the following:

- Secured sale contracts, defined as records that create a monetary obligation and a security interest in or a lease of goods
- Documents of title or receipt, e.g., bills of lading, dock warrants and warehouse receipts
- Instruments, including negotiable instruments, share certificates or any other instrument in writing that evidence a right to the payment of money, is not itself a security agreement or lease and is of a type that is, in the ordinary course of business, transferred by delivery with any necessary endorsement or assignment
- Accounts, which are defined as any right to payment for goods sold or leased or for services rendered that are not evidenced by an instrument or secured sales contract
- Other intangibles, including any movable thing or right other than goods, accounts, secured sales contracts, documents, instruments and money

It may be difficult or impossible to grant effective and perfected security over any class of asset that is not in the above classifications, or security over it may be of limited effect.

9. Under the laws of this jurisdiction, are there any restrictions on offshore lenders taking security over any class of asset?

No.

10. Must a company receive a corporate benefit in return for giving a guarantee or security? In particular, are there restrictions on the grant of upstream and cross-stream guarantees and security? If yes, briefly what is the effect of these laws?

No.

11. What type of security interests does your jurisdiction recognise, e.g., pledge, charge, mortgage, hypothecation? In relation to each type of security interest, please state the formalities required to create and perfect that security.

Types of security interest

As noted above, security interests in Cambodia can be created under either the Civil Code or the LST.

Under the Civil Code, there are five types of real security rights, as follows:

- Rights of retention, where a person possessing a thing belonging to another has a claim arising in relation to that thing and may retain the thing until the claim is satisfied.
- Statutory liens, where a creditor is granted a preferential right to secure payment, either from a specified property or from the assets of the debtor in general, in preference to the claims of other creditors.
- Pledge over movable property, immovable property or contractual and other claims.
- Hypothecation over ownership rights, perpetual leases and usufruct of immovable property.
- Transfer as security, where a debtor transfers ownership of a specified movable item to the creditor for the purposes of securing an obligation.

Security may be taken under the LST in respect of any transaction where its effect is to secure an obligation with collateral, including by way of pledge, transfer of title, consignment or assignment. The law applies to these transactions regardless of the form or terminology used in the agreement and regardless of whether the ownership right is held by the secured party or the debtor.

Perfection of security interests

No mandatory form, notarization or registration is required for the security agreement to be effective between the parties. However, to be effective against third parties (i.e., to perfect the security), the formalities set out below apply.

Under the Civil Code

Pledge of movable property:

- Continuous possession of the pledged object is required.

Pledge of immovable property:

- Continuous possession of the pledged object, and notarization and registration of the pledge agreement in the land registry are required.

Pledge of rights and claims:

- The third-party obligor must be given notice or provide an acknowledgment. Further, to assert against a third party other than the obligor, this notice or acknowledgment must be in an instrument bearing a fixed date.

Hypothecation:

- Notarization and registration of the hypothec agreement in the land registry are required.
- If the hypothec agreement is made in any language other than Khmer, a Khmer translation is required for the purpose of registration.

Transfer as security:

- Possession of the object transferred is required.

Under the LST

Three means of perfection are available under the LST, as set out below.

Filing: Filing a notice in relation to a secured transaction at a filing office is the most common way to perfect a security interest. In general, by filing a notice, a secured party has all the rights of the holder of a perfected security interest for as long as the notice is effective.

Possession: Possession of the collateral by the secured party is another means of perfecting a security interest if the collateral comprises goods, instruments, documents, certificated securities or secured sales contracts.

Automatic perfection on attachment: A security interest in consumer goods is automatically perfected when it attaches to the consumer goods (i.e., goods used primarily for personal, family or household purposes) without the need for filing a notice or possession by the secured party. When a security interest is created, it becomes enforceable between the debtor and the creditor, and it is said to have "attached."

12. Are there any registration, translation or notarization requirements in relation to security, guarantees, subordination or intercreditor documents?

In relation to security documents, see the answer to "Perfection of security interests" in question 11 of this section.

In relation to guarantees, subordination or intercreditor documents, there are no registration, translation or notarization requirements.

Registration and notarization fees payable for perfecting a security interest under the Civil Code vary from case to case, while the fee for filing a notice of a secured interest under the LST is KHR 40,000 (approximately USD 10) per filing.

13. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in respect of security, guarantees, subordination or intercreditor documents? If yes, what are the amounts and when are they payable?

No, except as noted in the answer to question 12 of this section.

If things go wrong

1. Please provide a brief description of the insolvency regime. In particular what rights and duties do unsecured and secured lenders have on the insolvency of a debtor? Are there any other matters of concern?

The structure of the insolvency regime under the Insolvency Law follows what is frequently termed the "unitary" approach.

The opening of insolvency proceedings under the Insolvency Law sets off an initial period of an objective assessment of the debtor's financial condition. The creditors determine whether the debtor will be rehabilitated or liquidated at the opening creditors' meeting, which must be held within 30 to 60 days of the opening of the insolvency proceedings. The proceedings will then be directed toward either a rehabilitation of the debtor through the implementation of a plan of compromise or a liquidation.

Under the Insolvency Law, creditors are decision-makers in a number of key areas. For example, during liquidation proceedings, creditors are given the authority to dismiss the liquidator, to approve the temporary continuation of the business by the liquidator and to approve a private sale. In rehabilitation proceedings, they have the authority

to dismiss the administrator and to propose and approve a rehabilitation plan. They may also request or recommend action from the court, including recommending that the rehabilitation proceedings be converted into a liquidation.

However, the Insolvency Law does not apply to debtors covered under the Law on Banking and Financial Institutions, the Law on Insurance and the Law on Non-Government Securities. The insolvency of banks, microfinance institutions and other financial institutions specified in the Law on Banking and Financial Institutions is covered by the Law on Banking and Financial Institutions. The Law on Insurance covers the insolvency of insurance companies, such as life insurers, general insurers, micro-insurance companies, and reinsurance companies. The insolvency regime for entities covered by the Law on Non-Government Securities (for example, securities dealers, securities underwriters, securities brokers and investment advisers) is governed by the 2018 Sub-Decree No. 24 on Rehabilitation and Liquidation in the Securities Sector.

2. Is it possible to obtain a moratorium before insolvency?

No.

3. When a company is the subject of a formal insolvency procedure, can the company's pre-insolvency transactions be set aside?

Yes, on a complaint by the administrator and on a hearing of the other party to a transaction, the court may avoid the following transactions:

- A transaction entered into by the debtor with the intent to defraud creditors by placing the debtor's assets beyond the reach of creditors that may seek to recover claims owed by the debtor
- A transaction effected within three years prior to the opening of insolvency proceedings for which no consideration was received by the debtor, except for ordinary transactions in favor of the debtor's spouse or relatives of direct descent or ascent
- A transaction effected within one year prior to the opening of insolvency proceedings in which the value of the debtor's obligation considerably exceeded the value of the other party's obligation
- A transaction effected within one year prior to the opening of insolvency proceedings in which the debtor discharged a debt that was not due or provided new or additional security for a debt and in which the other party to the transaction is a related person
- A transaction effected within six months prior to the opening of insolvency proceedings in which the debtor discharged a debt that was not due or provided new or additional security for a debt
- A transaction effected within one year prior to the opening of insolvency proceedings in which the debtor discharged a debt that was not due, provided new security or granted a security right for the repayment of certain shareholder loans or similar claims

Where a transaction is avoided, any money paid, property transferred or proceeds from the sale of the transferred property will be recovered and included in the estate of the debtor.

4. When can a lender enforce its security? Can security be enforced out of court following an event of default (or other contractual trigger event), or is a court order required? Are there any restrictions that apply before a lender may enforce its security?

If the security is created under the Civil Code, generally, the holder of a real security right may enforce it in accordance with procedures established under the Civil Procedure Code. However, summary enforcement is available for a pledge and a transfer as security.

For a security interest over movable property that is created and perfected in accordance with the LST, the secured party, on a default (which the parties are free to define as they choose), has the right to take possession or control of the collateral even if the security agreement is silent about possession or control. The secured party may only take possession or control of collateral without legal proceedings if the debtor has agreed to this in writing after default. The debtor is not permitted to agree to this in advance in the security agreement.

5. Do any limitation periods apply in relation to bringing an action to enforce security?

The extinctive prescription period for claims is five years, commencing on the date that the claim is capable of being exercised. "Extinctive prescription" is a term meaning the extinction of a claim based on a secured party's failure to exercise a claim within a certain period.

6. Is there any particular way in which secured assets must be liquidated on enforcement (e.g., by auction or court sale)?

Under the Civil Code, a real security right may be enforced in accordance with procedures laid down by the Civil Code, i.e., compulsory sale, summary enforcement for a pledge over movable property or, in the case of a transfer as security, conversion to cash or conclusive transfer of ownership.

Under the LST, a secured party (the disposing secured party) may dispose of the collateral. Disposal may be by sale, lease, license or another method. A disposing secured party might sell the collateral in parts or as a whole, or it might dispose of some at one time and some at other times. Disposal of the collateral may be arranged in a public forum or privately. If the disposal is public, the disposing secured party may buy the collateral. The debtor is entitled to reasonable notice of the disposal, provided that notice is practicable under the circumstances. The debtor may waive its right to receive notice. If another secured party with interest in the same collateral notifies the disposing secured party of its interest, the disposing secured party must give notice to the other secured party in advance of the disposition.

7. Are there any particular legal or practical difficulties or delays in enforcing security?

Yes. Notwithstanding the enforcement provisions in various laws, in practice, enforcing security through court proceedings remains a major challenge for secured parties in Cambodia, especially in relation to security over movable property.

8. In relation to enforcement, are there any specific requirements to be borne in mind if the lender is a foreign entity?

No. However, as a foreign entity is not permitted to own land in Cambodia, it is worth noting that the foreign entity may not bid for nor purchase the land collateral when the land collateral is being liquidated on enforcement.

9. Is there any reason why you think that arbitration rather than litigation might be advantageous in resolving disputes under the finance documents, and if so, why? Please outline the relative merits of arbitration and litigation, including the ease of enforcement of foreign judgments and foreign awards from different jurisdictions. Is it possible to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit?

When comparing arbitration and litigation as a forum to resolve disputes under the finance documents, there are three major points to be aware of.

First, arbitration in general, can be advantageous when compared to litigation in a number of ways, mainly due to the freedom of the parties to determine their own procedure to govern the proceedings. The parties may determine the qualifications and appointment procedure of the arbitral tribunal, the language of the proceedings, the privacy and confidentiality of the proceedings and the governing laws and rules for conducting the proceedings. Arbitral awards are also final and binding. They cannot be appealed. However, they can be set aside or not recognized for enforcement based on limited legal grounds under Cambodian law. Litigation, on the other hand, may not afford any of these advantages.

Second, in comparison to court judgments, arbitral awards are more widely recognized and enforced internationally. Subject to limited exceptions, foreign arbitral awards are generally recognized and enforceable by Cambodian courts since Cambodia is a member of the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards ("**New York Convention**"). That would also mean that arbitral awards issued in Cambodia are generally recognized and enforceable in countries that are members of the New York

Convention. On the other hand, foreign judgments are generally unenforceable in Cambodia unless the country in which the foreign judgments are made has a bilateral agreement with Cambodia to reciprocally recognize and enforce judgments of each other's courts. So far, Cambodia only has such a bilateral agreement with Vietnam. That should also mean that Cambodian court judgments may not be recognized and enforceable in other jurisdictions, subject to their local laws. Arbitration would, therefore, likely be more advantageous against a party that has assets in multiple jurisdictions.

Third, one potential risk for using arbitration to resolve disputes under the finance documents is the question of whether disputes under security documents are capable of being resolved by arbitration or whether enforcing arbitral awards against secured property would violate Cambodia's public policy. Resolving disputes under security documents by arbitration might affect the rights of third parties that have interests in the secured property but are not parties to the arbitration agreement. Nonetheless, to date and our knowledge, this question has never been tested in Cambodian courts.

With regard to hybrid enforcement provisions, while Cambodian law does not expressly prohibit this type of provision, to date and to our knowledge, their legality has not yet been tested in Cambodian courts.

10. **Are asymmetrical jurisdiction clauses enforceable? (By this we mean clauses that allow the lenders, but not the borrowers, to make certain choices in relation to choice of jurisdiction and how to litigate. These types of clauses allow the lenders, but not the borrowers, to commence proceedings in any court they choose, but restrict the borrowers to commencing proceedings in one jurisdiction only. This may also allow the lenders, but not the borrowers, to choose whether to litigate the finance documents before a court or to submit to arbitration in relation to them, but restrict the borrowers to either litigation or arbitration, as specified in the agreement).**

    While Cambodian law does not expressly prohibit this type of arbitration clause, there is a possibility that asymmetrical arbitration clauses may be considered invalid if they can be shown to be contrary to Cambodian public policy. Arbitral awards issued from this clause might run the risk of being unenforceable on the grounds of invalidity of the arbitration agreement or violation of Cambodia's public policy. Nonetheless, to date and to our knowledge, this concept has never been tested in Cambodian courts.

Working digitally

1. **Is it possible for documents to be executed electronically (whether by the manual insertion of a digital signature or the use of an e-signing platform) under the laws of this jurisdiction? If so, is this limited to only particular types of finance documents?**

    Yes, generally, documents can be executed electronically, except for powers of attorney, wills and succession-related documents, and documents for the sale or transfer or that otherwise dispose of immovable property.

    Please note that the Law on Electronic Commerce dated 2 November 2019 ("**E-Commerce Law**") defines "electronic signature" as a signature created by electronic means used to identify the signatory and includes digital signatures, biometric signatures and other signatures. Valid electronic signature ("**E-Signature**") should have the following criteria:

    - It is possible to identify the person or reflect the approval of such person for the information or records contained in electronic communication.
    - It is reliable and consistent with characteristics, purposes and circumstances whereby such electronic communication is made or communicated.

In addition to the E-Signature discussed under the E-Commerce Law, Sub-Decree No. 246 on Digital Signatures dated 29 December 2017 ("**Sub-Decree No.246**") sets out further criteria for digital signatures ("**Digital Signature**"), as follows:

- Verification of the digital signatory's identity correctly and specifically
- Verification of the authenticity of the electronic message
- Verification of the time and date of the signing of the Digital Signature
- Other criteria as determined by the Ministry of Post and Telecommunications (MPTC)

Once the above criteria are fulfilled, the Digital Signature owner shall obtain a digital signature certificate from the certificate authority ("**Certificate Authority**"), which will be established under a separate regulation of the MPTC.

Although the E-Commerce Law and the Sub-Decree No. 246 discussed the above specification and criteria for both E-Signatures and Digital Signatures, in practice, the use of E-Signature and Digital Signature remains unclear. To further implement the usage of the E-Signature and Digital Signature, the MPTC and relevant ministry are currently working on (i) the draft regulation on the form, procedure and registration requirement of Digital Signature and (ii) the guideline/regulation for the Certificate Authority to issue a digital signature certificate to the user. This ambiguity also applies to the implementation and effect of the E-Signatures registered and effective in jurisdictions other than Cambodia.

2. Where the witnessing of a signing is contemplated, is it possible for the witness to verify the signature over a live video call?

There is no law on the issue. It is unclear to what extent a Cambodian court would admit such witnessing as evidence in court.

3. Is it possible to register/perfect security electronically without wet ink signatures?

Yes, except for security over immovable property.

4. Are there any other legal restrictions that may prevent the parties from executing a finance transaction electronically?

No, except for security over immovable property. However, it is generally recommended that finance documents are executed with wet ink signatures.

This chapter on Cambodia was prepared by BUN Youdy, KIM Daraboth and ROATH Sovannarith with BUN and Associates, a Cambodian law firm.

MAINLAND CHINA

Mainland China

When considering whether to lend

1. **Is it necessary or advisable for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in this jurisdiction: (a) by reason only of its execution, delivery or performance of the finance documents; or (b) to enable it to enforce its rights under the finance documents?**

   No.

2. **Will any lender, arranger, facility agent or security agent be deemed to be resident, domiciled, carrying on business or subject to tax by reason only of the execution, delivery, performance or enforcement of the finance documents?**

   No, although interest and fees payable to the offshore lender, arranger, facility agent or security agent are subject to PRC withholding tax and VAT.

3. **Are there any regulatory reporting requirements that lenders must observe in connection with those transactions?**

   No.

4. **Is it necessary to establish a place of business in your jurisdiction in order to enforce any provision of the finance documents?**

   Generally, it is not necessary to establish a place of business in the PRC to enforce any loan or security documents.

5. **Is a foreign bank/financial institution permitted to approach local entities for business?**

   Yes, as long as communications with local entities are limited to the underlying loan transaction.

When lending to borrowers

1. **Are there any restrictions in relation to the type of borrower who may borrow foreign currency or in relation to the term of foreign currency and/or the amount of foreign currency borrowed by local entities?**

   2017 Regime

   On 12 January 2017, the People's Bank of China (PBOC), the central bank of the PRC, further revised the macroprudential administrative regime ("**2017 Regime**") in relation to inbound financing on a nationwide basis, which came into effect on the same date.

   An entity incorporated in the PRC (whether a PRC domestic enterprise or a foreign-invested enterprise (FIE), i.e., a company that is not wholly owned by PRC nationals or entities) may obtain inbound financing from offshore lenders without any prior approval from the PBOC or the State Administration of Foreign Exchange (SAFE), the PRC exchange control authority.

Under the 2017 Regime, a borrower may obtain inbound financing provided that the "outstanding" may not exceed the "ceiling".

"Outstanding" means, in respect of the borrower, the sum of the amount drawn but not yet repaid under each of its inbound financings (loans, trade finance, certain contingent liabilities, etc.) with risks pertaining to the tenor, type and exchange rate of each inbound financing taken into account.

"Ceiling" means the maximum amount of "outstanding" permitted under the 2017 Regime, which is calculated based on the borrower's net asset value (if the borrower is not a financial institution), or tier one capital (if the borrower is a banking financial institution) or paid-up capital plus capital reserve (if the borrower is a nonbanking financial institution) multiplied by the leverage ratio and the macroprudential adjustment multiplier, each as determined by the PBOC.

The PBOC may adjust the relevant multipliers and calculation methods from time to time, either generally or with respect to a particular enterprise or industry.

Under the 2017 Regime, where the borrower is not a financial institution, the borrower should perform the following:

- File its inbound financing with the SAFE capital account information system no later than three working days before the drawdown.
- Update its inbound financing and other relevant data (such as details of the offshore lender, tenor of the loan, amount of the loan, interest rate and its net assets value) with the SAFE on an annual basis.

For any change to its audited net assets value or certain terms of the financing agreement (such as an offshore creditor, the tenor of the loan, amount and interest rate), the borrower should promptly update the SAFE.

Foreign Debt Regime

If the borrower is a FIE, it may elect to continue to follow the rules applicable to the existing foreign debt regime by relying on the borrowing gap available (in the case of a FIE borrower) in calculating the amount of foreign debt that it may incur ("**Foreign Debt Regime**") or the 2017 Regime.

Under the Foreign Debt Regime, the borrower must effect a "foreign debt registration" with the local branch/ sub-branch of the SAFE. As long as the borrower has registered its foreign debts with the SAFE and the aggregate amount of its foreign debts does not exceed its so-called borrowing gap, it may freely borrow from non-Chinese lenders.

NDRC registration

The borrower must obtain a Certificate of Approval and Registration (in Chinese, 审核登记证明) from the National Development and Reform Commission (NDRC) before incurring any foreign debt with a tenor of over one year.

Local regulations

Different local regulations apply to some specific regions, such as the free trade zones. This guide does not cover the different regulatory registration, filing or reporting requirements under those local regulations.

2. Are there any restrictions on the rate of interest or default interest that may be charged?

There is no regulatory restriction on the interest rate or default interest rate that may be charged on foreign debt. However, the interest rate is part of the information required for SAFE registration. The SAFE can refuse to register a loan if the interest rate is not deemed acceptable. Usually, the interest rate will be acceptable to the SAFE if it is in line with the market interest rate (e.g., by reference to SOFR, Term SOFR or any other replacement benchmark rate commonly adopted in the market in the case of a USD foreign loan).

3. Are there any restrictions on particular lenders or classes of lender entering into credit transactions with borrowers?

No, there is no regulatory restriction of this type. A foreign lender may be a foreign financial institution, a company (whether or not it is a related company of the borrower) or a foreign citizen.

4. Are there any exchange controls that will apply to payments to be made in foreign currencies or to foreign lenders?

Please refer to the answer to question 1 of this section.

2017 Regime

The borrower should use the loan proceeds for its manufacturing and business operations.

Foreign Debt Regime

After the completion of foreign debt registration with the SAFE, the borrower must open a designated foreign debt account with a bank in the PRC, which will be used to receive the loan proceeds. The loan proceeds must be remitted into the foreign debt account. They may only be used for the borrower's operation within its scope of business, i.e., the specific scope of business that is recorded in its business license.

NDRC requirements

For foreign debt with a tenor over one year, the loan proceeds may only be used for purposes recorded on the Certificate of Approval and Registration (in Chinese, 审核登记证明) issued by the NDRC. In particular, the use of such foreign debt shall not:

- Violate any PRC laws and regulations;
- Threaten or be detrimental to the national interests, economy, information and data security of the PRC;
- Contravene the goal of the PRC's macroeconomic regulation and control;
- Contravene the PRC's development, planning and industrial policies;
- Increase local government's hidden debts; or
- Be used for speculative purposes or (except for banking/financial institutions) be lent to others (other than any circumstance which has been stated in the application materials and approved by the NDRC).

5. Is there any requirement to deduct or withhold tax from any amounts to be paid or repaid to a lender (whether domestic or foreign)? If so, at what rate must tax be deducted and from what kinds of payment?

A foreign company without any presence in the PRC but receives profits, interest, rent, royalties or other income from sources in the PRC is subject to withholding tax on that income. The withholding tax rate is 10%, unless the foreign company is from a jurisdiction with which China has entered into a tax treaty that allows a preferential rate.

6. Are there any "thin capitalization" or other rules that may limit the extent to which interest payments may be deducted for tax purposes?

According to the PRCs thin capitalization rules, interest for debts in excess of the prescribed debt-to-equity ratio (i.e., 5:1 for financial enterprises and 2:1 for other enterprises) is not deductible unless the borrower is able to prove that borrowings from a related lender are on arm's length terms or that the actual tax burden of the domestic borrower is no higher than its domestic related lender.

In this answer, reference to "thin capitalization" is not a reference to a company's borrowing capacity (in the PRC, the expression is sometimes used in that context).

7. Are there any registration, notarization, translation or reporting requirements in relation to the loan documents?

Other than the cross-border financing filing and foreign debt registration with the SAFE or the NDRC, there are no other registration, reporting or notarization requirements in relation to the loan agreement. Further, the loan agreement and other relevant transaction documents will need to be translated if such documents are to be submitted to a PRC court in legal proceedings. Please refer to the answers to question 8 of the "If things go wrong" section.

However, there are governmental approval and registration requirements in relation to certain security documents. Please refer to the answers to questions 11 and 12 of the "If taking security" section.

8. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to the loan documents? If yes, what are the amounts and when are they payable?

Stamp duty is levied on categories of dutiable documents that have legal effect in the PRC and that are "protected under PRC law." The categories of dutiable documents are exhaustive so that any document that does not fall within these categories is not subject to stamp duty in the PRC.

For dutiable documents, stamp duty is due on the execution of the documents if the documents are executed in the PRC. However, if a document is executed outside the PRC but is used in the PRC, stamp duty will be payable.

A loan agreement is subject to stamp duty. Each party to the loan agreement must pay stamp duty at the rate of 0.005% of the principal amount (e.g., 5,000 out of 100 million). However, there is debate on whether it is the foreign party's obligation to pay the stamp duty in the case of a foreign debt agreement. The issue is whether the stamp duty applies to a foreign lender. Failure to pay the required stamp duty will trigger sanctions by the tax authority (such as a penalty), but it will not affect the validity, legality or enforceability of the agreement itself and it will not prevent the admission of the loan agreement as evidence in court.

Effective from 1 May 2016, VAT at the rate of 6% is charged on income derived by a foreign entity for providing a service in the PRC.

There are no other documentary, registration or other similar taxes, duties or fees chargeable in respect of a loan agreement.

Foreign debt registration with the SAFE and the NDRC is free of charge.

For security documents, please refer to the answers to questions 11 and 12 of the "If taking security" section.

9. Does the law recognize the subordination of the debt that a debtor owes to one creditor to that which the debtor owes to another creditor? If yes, how is this usually effected?

PRC law recognizes the concept of subordination. Subordination is usually effected by way of a contractual arrangement among the senior creditor, the subordinated creditor and the debtor.

10. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors (e.g., the claims of employees and tax authorities or the claims of creditors under particular kinds of instrument)? If yes, what classes of creditors are preferred?

The PRC Enterprise Bankruptcy Law sets out a hierarchy of debts to determine payment priority. The following claims rank above those of general (or "common") unsecured and unsubordinated creditors, and they must be paid in the following descending order of priority:

- Bankruptcy expenses
- Common interest debts incurred for the benefit of the creditors
- Employee claims including unpaid salaries, medical and disability subsidies, basic old age and medical insurance premiums, and compensation in accordance with PRC law
- Social insurance premiums and outstanding tax

If the property available for distribution in the bankruptcy is insufficient to discharge all of the debts within a particular rank of debts, the discharge of the debts within that rank will be effected on a pro rata basis.

11. Are there any consumer protection or similar laws that apply if credit is made available to individuals or other classes of debtor? If yes, what laws are applicable?

Currently, PRC nationals are not allowed to borrow money from outside the PRC. The PRC consumer protection regime is therefore not relevant.

12. Are there any prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of: (a) its own shares or those of any affiliated company; or (b) assets owned by it or any affiliated company?

There is no concept of "financial assistance" in the PRC and therefore, there is no particular prohibition on a PRC company providing security or giving a guarantee to a third party. Nevertheless, the PRC Company Law contains a general restriction on PRC companies providing security on behalf of its shareholders or de facto controllers. Where a PRC company provides security to secure the liabilities of any of its shareholders or a person who actually controls the PRC company, the security must be approved by its shareholders. Approval must be in the form of a shareholders' resolution passed by the shareholders with more than half of the voting rights of all the shareholders present at the relevant shareholders' meeting. Shareholders whose debts are being secured by the company and any shareholders controlled by the de facto controller are not entitled to vote.

If taking security

1. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's secured creditors?

No. Secured creditors generally have priority to the extent of the value of their security, but any portion of the debt not covered by the value of the security is treated as an unsecured claim.

2. May security given by a company rank in a specified order so as to secure liabilities owed to different creditors of the company in that order and, if that is not possible, is it viable for parties to enter into a contractual arrangement for the purposes of moderating this order?

For certain types of security, such as a mortgage, it is permissible for a security provider to create securities in favor of different creditors over the same assets. The PRC Civil Code contains general provisions in terms of priority among different creditors in relation to securities created over the same assets. For example:

- If there is more than one mortgage over the same asset (with a mortgage taking effect on registration with the relevant governmental authority), the priority is determined based on the sequence of registration.
- If there is a mortgage and a pledge over the same asset, a registered mortgage has priority over a pledge but a pledge has priority over an unregistered mortgage.

However, in practice, except for mortgages over real property, having more than one mortgage over the same asset does not often occur in banking transactions.

3. Does this jurisdiction recognise the concept of floating security or similar equivalent (i.e., security over a changing pool of assets that the company giving the security is free to buy, sell and generally deal with)?

The PRC Civil Code recognizes the concept of a floating mortgage. This is usually created over assets such as equipment, raw materials, semi-finished products and finished products.

4. If so, are there any practical reasons why floating security is difficult to take, maintain or enforce?

A floating mortgage will take effect when the mortgage contract takes effect, but it will not be upheld against bona fide third parties unless it is registered with the PBOC. Due to the floating nature of the underlying assets, a floating mortgage is not common in banking transactions.

5. May security be granted to a trustee to be held on trust for the lenders from time to time, in such a way that a change of lenders does not require new security to be taken?

Yes, although for domestic syndicated loan transactions, as only licensed trust companies may carry on trust business but cannot be a party to a syndicated loan transaction, a security agent (rather than a security trustee), which is one of the lending banks, is used.

6. If not, are there any techniques that can be used to achieve substantially the same effect (e.g., parallel debt structures)?

Not applicable.

7. If an agent holds security for the lenders rather than a trustee, is it necessary to take new security on a change of lenders? If no, why not? If yes, are there ways to structure the transaction to avoid such a requirement?

No. If the security is held by a security agent, it is not necessary to take new security (or amend the security agreement or update the security registration with government authorities) if there is a change of lenders.

8. Under the laws of this jurisdiction, is there any class of asset over which it is difficult or impossible to grant effective and perfected security, or in relation to which any security granted will be of limited effect?

Under the PRC Civil Code, a mortgage or a pledge cannot be created over the following assets:

- Land title (with a few exceptions, land title belongs to the state; therefore, the land title cannot be mortgaged or pledged and, instead, the land use right can be mortgaged).
- A land use right in relation to collectively owned land (which refers to some land in rural areas).
- Educational facilities, hospital facilities and other public service facilities.
- Assets whose title or use right is unclear or in dispute.
- Assets that are subject to attachment.
- Assets that are not allowed to be mortgaged or pledged by law (as may be prohibited by national and local laws and regulations).

9. Under the laws of this jurisdiction, are there any restrictions on offshore lenders taking security over any class of asset?

There are no such restrictions.

10. Must a company receive a corporate benefit in return for giving a guarantee or security? In particular, are there restrictions on the grant of upstream and cross-stream guarantees and security? If yes, briefly what is the effect of these laws?

There is no concept of "corporate benefit" under PRC law; therefore, there is no prohibition on a PRC company providing security or a guarantee to a third party.

11. What type of security interests does your jurisdiction recognise, e.g., pledge, charge, mortgage, hypothecation? In relation to each type of security interest, please state the formalities required to create and perfect that security.

Types of typical security

The PRC Civil Code recognizes the following types of typical security:[1]

Guarantee

It is not necessary to complete any regulatory formalities to create and perfect a guarantee.

Mortgage

A mortgage can be created over real property and movable assets.

For a mortgage over real property (including real property with construction in progress), the mortgage will take effect on its registration with the local authority (usually the local real estate registration authority).

For a mortgage over movable assets (such as equipment, vehicles and aircraft), the mortgage will take effect when the mortgage contract takes effect, but it will not be upheld against bona fide third parties unless it is registered with the relevant authority. See the answer to question 4 of this section in relation to a floating mortgage.

Pledge

A pledge can be created over movable assets and certain rights (such as stocks, equity interest and accounts receivable). For a pledge over movable assets, the pledge will take effect when the pledged asset is delivered to the pledgee. For a pledge over rights, the pledge will take effect when the following occur:

- The certificate evidencing that right (such as a certificate of time deposit) is delivered to the pledgee; and
- The pledge is registered with the relevant authority.

Deposit

A cash deposit takes effect when the deposit is delivered to the beneficiary.

Lien

It is not necessary to complete any regulatory formalities to create and perfect a lien.

General

Administrative practices and requirements in different provinces, cities, districts and counties may vary. It is therefore advisable to check with the relevant local authorities before taking security.

For further details on the registration requirements, see the answer to question 12 of this section.

1 Apart from the types of typical PRC law security listed, the PRC Civil Code also recognizes the "non-standard security" interest contemplated by "non-typical security contracts." Such contracts are contracts that do not take the form of a guarantee, mortgage or pledge but would nevertheless serve a security function according to their respective terms. Currently, security by transfer of ownership, retention of title, financial leasing and factoring arrangements would generally fall within the scope of such "non-standard security." The overall legal judicial practice regarding such "non-standard security contracts" has not yet been well established. It is expected to evolve given that the PRC Civil Code is still fairly new legislation and it is not yet common for creditors to take "non-standard security" in the market. Hence, we have only focused on the types of typical security in our responses that are most popular among offshore lender banks.

12. Are there any registration, translation or notarization requirements in relation to security, guarantees, subordination or intercreditor documents?

Jurisdiction of companies involved

There are some particular requirements, depending on whether the security relates to a PRC company or a foreign entity.

For a pledge over an equity interest in a PRC company, the pledge must be recorded in the company's share register and registered with the local counterpart of the State Administration for Market Regulation.

If the beneficiary of the security is a foreign entity, the exchange control regulations on cross-border security may be relevant. In particular, if:

- Both the primary obligor and the creditor (i.e., the beneficiary of the security) are foreign parties; and
- The security provider (references to "security provider" include reference to guarantors as well) is a PRC party,

the security provider (references to "security provider" include reference to guarantors as well) must effect cross-border security registration with the State Administration of Foreign Exchange. The registration is not a condition that affects the validity of the security but without registration, it will be difficult for the security provider to remit the enforcement proceeds out of the PRC when the security is enforced.

Additional requirements in some localities

In some localities, there are additional administrative requirements. For example, for a mortgage over real property, if the mortgagor or mortgagee is a foreign entity, the mortgage contract and the foreign entity's corporate documents may need to be notarized and legalized[2] or apostilled[3] before they are permitted to be submitted to the local authorities.

Subordination and intercreditor documents

There are no registration or notarization requirements in relation to subordination or intercreditor documents.

13. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in respect of security, guarantees, subordination or intercreditor documents? If yes, what are the amounts and when are they payable?

No stamp duty is payable in relation to securities (including guarantees), subordination or intercreditor documents.

In most cases, the registration of securities is free of charge, except that local authorities may charge a fee for the registration of a mortgage over real property. Local practice should therefore be checked at an early stage.

2 Applicable to documents issued in a non-contracting state of Hague Convention Abolishing the Requirement of Legalization.

3 Applicable to documents issued in a contracting state of Hague Convention Abolishing the Requirement of Legalization.

If things go wrong

1. Please provide a brief description of the insolvency regime. In particular what rights and duties do unsecured and secured lenders have on the insolvency of a debtor? Are there any other matters of concern?

Bankruptcy Law

The PRC Enterprise Bankruptcy Law ("**Bankruptcy Law**") came into effect on 1 June 2007.

The Bankruptcy Law introduced the following key concepts:

- Voluntary and involuntary bankruptcy
- An independent administrator
- The involvement of creditors in the administration of the bankruptcy
- Restructuring and settlement
- Extraterritoriality, allowing property outside the PRC and certain foreign proceedings to fall within the regime
- Voidable transactions
- Ratable distribution

Grounds for bankruptcy

An enterprise qualifies for bankruptcy, restructuring or settlement under the Bankruptcy Law if one of the following occurs:

- The enterprise is not able to meet its obligations to repay its debts, and its assets are less than its liabilities.
- The enterprise is knowingly incapable of paying its debts.

Application to court

Bankruptcy proceedings are commenced in the people's court in the location in which the enterprise is domiciled. Either the debtor or its creditors can initiate it. If the debtor is a financial institution, the relevant regulatory authorities under the State Council file the court application.

Appointment of an administrator

On acceptance of the bankruptcy application, the court appoints a bankruptcy administrator. The bankruptcy administrator may be a member of a recognized legal, accounting or specialist bankruptcy firm, or they may otherwise possess the relevant professional expertise and qualifications.

The administrator reports to the people's court and the creditors' meeting, and the creditors' committee supervise them. The creditors' meeting can replace the administrator or seek their removal if they fail to perform their duties in a lawful and impartial manner or if the creditors' meeting decides that there are circumstances that prevent them from performing their duties competently.

Creditors' meetings

The Bankruptcy Law involves creditors in the bankruptcy process through creditors' meetings and the creditors' committee.

A creditor that has submitted a claim in bankruptcy is entitled to attend and vote at the creditors' meeting. The exception is that secured creditors cannot vote on the adoption of a settlement plan or a distribution plan of the debtor's assets unless they have waived their right to priority. Generally, a resolution of the creditors' meeting is passed by a simple majority of the creditors with voting rights that are present at the meeting and that represent 50% or more of the value of the debtor's unsecured debt.

The creditors' meeting may establish a creditors' committee that comprises creditor representatives elected by the creditors' meeting, and it must include an employee representative of the debtor or a representative of its trade union. The creditors' committee is responsible for supervising the management, disposal and distribution of the debtor's property, proposing the convening of creditors' meetings and any other duties that are delegated to the creditors' committee by the creditors' meeting.

Priority and ranking of debts

The Bankruptcy Law sets out a hierarchy of debts to determine payment priority. Payment must be made in the following descending order of priority:

- Bankruptcy expenses
- Common interest debts incurred for the benefit of creditors
- Employee claims including unpaid salaries, medical and disability subsidies, basic old age and medical insurance premiums, and compensation in accordance with PRC law (such as compensation payable due to the early termination of an employment contract)
- Social insurance premiums and outstanding tax
- General or "common" unsecured claims

If the property available for distribution in the bankruptcy is insufficient to satisfy the discharge of all of the debts within a particular rank of debts, the distribution within that rank will be effected on a pro rata basis.

Secured creditors generally have priority to the extent of the value of their secured property, and any shortfall is treated as an unsecured claim.

Restructuring and settlement

The Bankruptcy Law also provides a formal process by which to restructure or rehabilitate viable businesses. Although the court may have accepted a bankruptcy application, the Bankruptcy Law allows a debtor or its creditors, prior to an enterprise being declared bankrupt, to apply to the court for the restructuring or reorganization of its business. The legislation also allows a debtor to apply for a compromise or settlement of its debts with its creditors.

2. Is it possible to obtain a moratorium before insolvency?

A moratorium is imposed on the debtor's assets upon the acceptance of the bankruptcy application by the court. Upon the acceptance of the bankruptcy application, all preservation measures (such as court attachments) against the debtor's property are lifted and all enforcement actions are suspended. Civil actions or arbitration procedures that have commenced against the debtor but that are not completed are stayed. Any repayment of debts to a creditor during this period is deemed invalid.

3. When a company is the subject of a formal insolvency procedure, can the company's pre-insolvency transactions be set aside?

The administrator can petition the people's court to revoke the following types of transactions entered into within one year preceding the court's acceptance of the bankruptcy application:

- Transfers of property for no consideration
- Transactions carried out at markedly unreasonable prices
- Provision of security for unsecured debts
- Premature settlement of undue debts
- Renouncement of creditors' claims

The administrator can also recover debts that have been repaid to individual creditors within six months prior to the acceptance of the bankruptcy petition, except where the debtor has benefited from the repayment.

Transactions that conceal or transfer assets for the purpose of avoiding liabilities, fabricating debts or acknowledging a fictitious debt would be deemed invalid under the Bankruptcy Law.

4. When can a lender enforce its security? Can security be enforced out of court following an event of default (or other contractual trigger event), or is a court order required? Are there any restrictions that apply before a lender may enforce its security?

Assets subject to security do not fall within the scope of bankruptcy assets. Secured creditors may exercise their security rights from the date the court approves the settlement that is part of the bankruptcy proceedings.

5. Do any limitation periods apply in relation to bringing an action to enforce security?

Yes, the statutory time limit in relation to the action is three years, subject to suspension and discontinuation provided by law. Calculation of the three-year period may be paused or restarted under certain circumstances. The beneficiary of the security should take legal action against the security provider within the time limit in relation to the action of the primary debt. Usually, the beneficiary of the security takes legal action against the primary obligor and security provider concurrently.

6. Is there any particular way in which secured assets must be liquidated on enforcement (e.g., by auction or court sale)?

No.

7. Are there any particular legal or practical difficulties or delays in enforcing security?

Without the cooperation of the debtor or security provider, the beneficiary will need to go through court proceedings to enforce the security.

If the debtor and the security provider fail to honor the court judgment or arbitral award after the beneficiary of the security obtains a favorable judgment or arbitral award, the creditor can apply to the court for the enforcement of the judgment or arbitral award. Typically, the court disposes of the assets by way of a public auction organized by the court. The court may request the beneficiary of the security to provide information (such as bank account details and the location of the assets) in relation to the relevant assets. This may add certain difficulties or prolong the process in relation to the enforcement, as it will take additional time for the beneficiary to collect the relevant information (which may not always be available).

8. In relation to enforcement, are there any specific requirements to be borne in mind if the lender is a foreign entity?

There are several specific requirements, as set out below.

Engaging PRC counsel

Procedurally, for a foreign lender to take legal action before a PRC court, it must engage a qualified PRC law firm. The power of attorney of the lender from outside the PRC for engaging the PRC law firm must be notarized and legalized[4] or apostilled[5] in the lender's home jurisdiction.

4 Applicable to documents issued in a non-contracting state of Hague Convention Abolishing the Requirement of Legalization.

5 Applicable to documents issued in a contracting state of Hague Convention Abolishing the Requirement of Legalization.

Language version

Court proceedings in the PRC are conducted in Chinese. Therefore, where a transaction document is prepared in English or another foreign language, a Chinese translation must be prepared and submitted to the court. Usually the people's court will require the translation to be prepared or reviewed by a third-party translation firm designated by or acceptable to the court.

Governing law

Generally, parties to a contract with a "foreign element" are allowed to choose either PRC law or foreign law as the governing law of the contract, unless otherwise provided under PRC law.

Loan documents and security documents entered into by a foreign lender are considered contracts with a "foreign element." The foreign lender may (but it is not obliged to) choose PRC law or foreign law to govern its loan and security documents to be entered into with PRC clients, except under certain PRC laws. A mortgage over property located in the PRC and any pledge over rights (such as an equity pledge, a pledge over receivables, a pledge over securities and negotiable instruments) created in the PRC must be governed by PRC law.

If the parties to a transaction document choose to have it governed by foreign law, the PRC court may still apply PRC law during the court proceedings in relation to the transaction document if it determines the following:

- The parties have not provided or proved the relevant contents of the foreign law to the court.
- The parties chose the foreign law to evade mandatory PRC law requirements.
- The choice of the foreign law violates the social and public interests of the PRC.

Recognition and enforcement of a foreign court judgment

Under the PRC Civil Procedures Law, a foreign party seeking the recognition and enforcement of a foreign court judgment in the PRC court may perform one of the following:

- Make a direct application for the recognition and enforcement of that judgment to a relevant PRC court.
- Ask a foreign court to submit a request to the PRC court for the recognition and enforcement under the judicial assistance procedure.

The PRC court will only recognize and enforce a foreign judgment when both the PRC and the country where the judgment in respect of which enforcement is sought have concluded or acceded to a bilateral or international judicial assistance treaty regarding the mutual recognition and enforcement of commercial judgments, or where reciprocity can be demonstrated.

If there is no international judicial assistance treaty regarding the recognition and enforcement of commercial judgments between the PRC and the relevant country, in practice, the PRC court would only consider an application if the foreign applicant is able to prove the existence of reciprocity, i.e., that the courts of the foreign jurisdiction would enforce and have previously enforced a judgment of a PRC court. Although proof of reciprocity by the foreign plaintiff is not specifically stated in the PRC Civil Procedures Law, as a matter of practice, it appears to be a requirement of the PRC courts.

Therefore, in the PRC, it would be difficult to enforce a judgment given by a foreign court unless the PRC has concluded or acceded to a judicial assistance treaty regarding the enforcement of a commercial judgment with that foreign jurisdiction.

Recognition and enforcement of a foreign arbitral award

The PRC acceded to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards ("**New York Convention**") on 22 April 1987. The party seeking the recognition and enforcement of a foreign arbitral award in a PRC court may make a direct application to a competent PRC court within two years after the award is made. Under the notice published by the Supreme People's Court on implementing the New York Convention, the PRC court may reject the application for the recognition and enforcement of foreign awards on the following grounds, as set forth in Article V of the New York Convention:

- A party to the arbitration agreement ("**Arbitration Agreement**"), under the laws applicable to it, had no capacity to enter into the Arbitration Agreement, or the Arbitration Agreement was indeed invalid under the law to which the parties are subject or, in the case where there is no express governing law of the Arbitration Agreement, the Arbitration Agreement was indeed invalid under the law of the place where the arbitration award was made.
- The party against whom the application is filed was not given proper notice of the appointment of the arbitrator or was otherwise unable to present its case.
- The award deals with any dispute not contemplated by or not falling within the terms of the Arbitration Agreement or the award contains decisions on matters beyond the scope of the submission to arbitration. However, if the award contains decisions on matters submitted to arbitration that can be separated from those not submitted, the part of the award that contains decisions on matters submitted to arbitration will be enforced.
- The composition of the arbitral tribunal or the arbitral procedures was not in accordance with the agreement of the Arbitration Agreement or, failing that agreement, with the law of the place where the arbitration took place.
- The award has not become binding on the parties, or it has been annulled or its enforcement has been suspended by the court or in accordance with the law of the place where arbitration took place.
- The PRC court decides that the dispute is incapable of being settled by arbitration under the laws of the PRC.
- The PRC court holds that the enforcement of the arbitration award in the PRC would be contrary to the public interests of the PRC.

For foreign arbitral awards made in a territory that is not a member of the New York Convention, the recognition and enforcement of those awards will be reviewed in light of bilateral agreements between that jurisdiction and the PRC (if any) or in light of the principle of reciprocity.

9. Is there any reason why you think that arbitration rather than litigation might be advantageous in resolving disputes under the finance documents, and if so, why? Please outline the relative merits of arbitration and litigation, including the ease of enforcement of foreign judgments and foreign awards from different jurisdictions. Is it possible to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit?

In practice, in the PRC market, for most banking transaction documents (even those of foreign banks' subsidiary banks or branches in the PRC), the parties choose to have their disputes resolved by the court rather than use arbitration.

One important advantage of having a dispute resolved by the court is that if a party is not satisfied with the results of the court's judgment at the first hearing, it may appeal to a higher court for a second (and final) hearing. In arbitration, there is no second hearing. As mentioned, the enforcement of an arbitral award needs to go through the court.

In light of the above, we do not consider there to be a strong advantage in using arbitration rather than court litigation to resolve disputes under the finance documents.

Finally, the effect of a hybrid enforcement provision that provides for an option for the lenders to choose between arbitration and litigation depends on the governing law of such enforcement provision. From a PRC law perspective, a jurisdiction clause that allows for a choice between court proceedings and arbitration is invalid. Therefore, PRC courts will not recognize the effect of a hybrid enforcement provision if the parties have chosen PRC law as the governing law or the PRC courts have otherwise decided to apply PRC law to determine the effect of such provision.[6]

However, there is one exception to such rule in judicial practice: If a party has submitted the dispute to the selected arbitration institution based on a hybrid enforcement provision and the opposing party does not object to it before the commencement of the first hearing of the arbitration tribunal, then the arbitration tribunal will proceed with arbitration even if the jurisdiction clause is a hybrid one. Meanwhile, a hybrid enforcement provision will generally be acceptable to the PRC courts if the parties have expressly chosen a foreign law that recognizes the effect of such provision as the governing law of such provision.

10. **Are asymmetrical jurisdiction clauses enforceable? (By this we mean clauses that allow the lenders, but not the borrowers, to make certain choices in relation to choice of jurisdiction and how to litigate. These types of clauses allow the lenders, but not the borrowers, to commence proceedings in any court they choose, but restrict the borrowers to commencing proceedings in one jurisdiction only. This may also allow the lenders, but not the borrowers, to choose whether to litigate the finance documents before a court or to submit to arbitration in relation to them, but restrict the borrowers to either litigation or arbitration, as specified in the agreement).**

    It is not prohibited by law to document that the lenders, but not the borrowers, may commence proceedings in any court they choose but restrict the borrowers to commence proceedings in one jurisdiction only.

    However, under PRC law, the parties must select in the loan agreement either court litigation or arbitration to resolve the disputes.

Working digitally

1. **Is it possible for documents to be executed electronically (whether by the manual insertion of a digital signature or the use of an e-signing platform) under the laws of this jurisdiction? If so, is this limited to only particular types of finance documents?**

    In general, electronically signed finance documents are legally valid and enforceable in the PRC, provided that the electronic signatures satisfy all of the following conditions and are therefore deemed reliable electronic signatures under PRC law:

    - The electronic data that is used to generate the electronic signature is exclusively owned by the signing party at the time of execution.
    - The electronic data that is used to generate the electronic signature is exclusively controlled by the signing party at the time of execution.
    - Any alteration to the electronic signature after signing can be detected.
    - Any alteration to the contents and form of any electronic data can be detected after signing.

6 This would usually happen if: (i) the parties have not expressly selected a governing law for the hybrid enforcement provision but have chosen a PRC arbitration institution or the PRC as the place of arbitration; or (ii) the parties have not expressly selected a governing law for the hybrid enforcement provision and have not expressly agreed on the arbitration institution or place of arbitration, but the dispute has a PRC nexus (for example, one of the parties is a PRC resident or the contract is signed within the territory of the PRC).

However, finance documents may not be executed using electronic signatures in certain scenarios as they are subject to specific form requirements. For example, for finance documents that must be registered with the relevant authorities (e.g., in the case of the registration of an equity pledge or mortgage of real property), the relevant authorities usually only accept wet ink signatures and/or company chops for registration purposes.

2. **Where the witnessing of a signing is contemplated, is it possible for the witness to verify the signature over a live video call?**

   Witnessing is not mandatory for signing of finance documents under PRC law. Nevertheless, where witnessing is required pursuant to the stipulation of the underlying finance document, the witness will usually attend the signing process in person.

3. **Is it possible to register/perfect security electronically without wet ink signatures?**

   It depends on the type of security contemplated by the undertaking finance documents. For mortgage over real property, an equity pledge and other types of security that require the physical submission of the registration application with the relevant authorities, the relevant authorities usually only accept wet ink signatures. For certain types of security that either do not require registration or can be registered or perfected through online registration with the relevant authorities (e.g., mortgage of movable assets, pledge over receivables, etc.), the security can be registered and/or perfected electronically without requiring wet ink signatures.

4. **Are there any other legal restrictions that may prevent the parties from executing a finance transaction electronically?**

   There are no additional restrictions other than those stated in our responses to questions 1 and 3 of this section.

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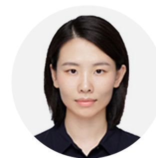

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HONG KONG SAR

Hong Kong SAR

When considering whether to lend

1. Is it necessary or advisable for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in this jurisdiction: (a) by reason only of its execution, delivery or performance of the finance documents; or (b) to enable it to enforce its rights under the finance documents?

A lender, arranger, facility agent or security agent ("**Finance Party**") that is a party to any loan or security arrangements with a company located in Hong Kong is generally not subject to any licensing requirements provided it is an "authorized institution" (AI) under the Banking Ordinance (BO). There are three types of AI, namely, licensed banks, restricted license banks and deposit-taking companies.

If a Finance Party is not an AI, but intends to lend money in Hong Kong (e.g., whether to a Hong Kong company or other legal person, or if the loan is advanced in Hong Kong), then the Money Lenders Ordinance (MLO) imposes licensing and other compliance requirements that may apply to a non-AI lender. The MLO requires any lender (other than an AI) that is in the business of making loans in Hong Kong (or who advertises, announces or holds themselves out as doing so) to obtain a money lenders' license and to comply with various requirements relating to the making of loans.

Exemptions from the MLO licensing requirements and most of the MLO compliance requirements (other than in relation to restrictions on charging excessive interest rates) are available, namely, in respect of "exempted persons" and "exempted loans" (as specified in Schedule 1 of the MLO).

Exempted persons include banks incorporated or established outside Hong Kong that are considered by the Hong Kong Monetary Authority (HKMA) (pursuant to a declaration to be obtained from the HKMA on a case-by-case basis) to be subject to prudential supervision by a recognized banking supervisory authority.

Exempted loans include, amongst other, loans made to any of the following persons:

- A company where the loan is secured by a mortgage, charge, lien or other encumbrance that is registered under the Companies Ordinance (CO).
- A company that has a paid-up share capital of not less than HKD 1,000,000 (or an equivalent amount in any other approved currency which is freely convertible into Hong Kong dollars).
- A company the shares or debentures of which are listed on a recognized stock market (or any subsidiary of that company).

Securities margin financing-related activities may be regulated separately by, or require compliance with, Guidelines, Codes or Rules published or overseen by the Securities and Futures Commission (SFC). This may include (except in the case of an AI lender for which an exemption may be available) a requirement for licensing by the SFC.

2. Will any lender, arranger, facility agent or security agent be deemed to be resident, domiciled, carrying on business or subject to tax by reason only of the execution, delivery, performance or enforcement of the finance documents?

Carrying on business

The execution, delivery and enforcement of loan or security documents in Hong Kong do not, of themselves, usually lead to the conclusion that a Finance Party is carrying on business in Hong Kong, nor would those acts generally

result in a Finance Party being deemed to be resident or domiciled in Hong Kong. However, the performance by a Finance Party of its obligations under a loan or security document in Hong Kong might suggest that the relevant person is carrying on business in Hong Kong. For example, where the facility agent function is carried out through an office or branch in Hong Kong or the loan is arranged through employees operating in Hong Kong.

Residence

Residence is usually determined in the first instance by the place of incorporation. However, a company may be resident in a particular place, even though it is not incorporated there, if its central management and control is exercised there. As the tax system in Hong Kong does not adopt a residence basis of taxation, residence is generally not relevant in the context of determining a company's tax liability in Hong Kong.

Domicile

Domicile is not relevant for tax purposes in Hong Kong.

Tax

Hong Kong profits tax is territorial in nature and only profits which have, or which are deemed to have, a Hong Kong source are subject to profits tax. To be liable to profits tax:

- A person must carry on a trade, profession or business in Hong Kong
- The person must derive profits from that trade, profession or business, other than profits arising from the sale of capital assets
- Those profits must arise in, or be derived from, Hong Kong

Whether interest or fees arise from the carrying on of a business in Hong Kong will be a question of fact to be determined based on all the circumstances in each case. If operations of substance relating to a transaction are carried out in Hong Kong, the relevant person would be regarded as carrying on business in Hong Kong.

The Hong Kong Inland Revenue Department and the Hong Kong courts have tended to the view that the threshold test for whether a person is carrying on business in Hong Kong is low. Ultimately, whether this is the case is a question of fact, and it is necessary to take into consideration all the activities of the Finance Party.

If in doubt, it is possible to obtain an advance ruling from the Hong Kong Inland Revenue Department (IRD) in relation to a specific arrangement or transaction. The ruling granted is only binding on the taxpayer applicant in relation to that particular transaction for the specified period provided the facts set out in the ruling are complete and remain correct. The IRD has a standard timeframe of up to six weeks (as noted in the Departmental Interpretation and Practice Notes No. 31 Advance Rulings as revised in April 2020) for processing any advance ruling application provided that all relevant information has been furnished. This timeframe can be extended for another six weeks if additional information is required. However, in more complex cases, a longer review period may be required by the IRD. The advance ruling mechanism is not available for stamp duty issues.

3. Are there any regulatory reporting requirements that lenders must observe in connection with those transactions?

To comply with the BO, if an institution is an AI (see the answer to question 1 of this section), it is generally required to submit periodic reports to the HKMA, including periodic reporting in relation to its assets, provisions and capital adequacy.

In addition, if a Finance Party carries on business in Hong Kong (see the answer to question 2 of this section), it must generally file annual profits tax returns that disclose specified information about the business. The financial accounts and a number of supporting documents must accompany the returns. The IRD can request any person to provide further information relevant for administering tax law. The IRD regularly uses this power to request further information and documents from taxpayers to assist it with its tax assessment.

4. **Is it necessary to establish a place of business in your jurisdiction in order to enforce any provision of the finance documents?**

   No. Please also refer to the answer to question 1 of this section in respect of the applicable licensing requirements.

5. **Is a foreign bank/financial institution permitted to approach local entities for business?**

   A foreign bank or financial institution that is an AI or a licensed money lender or that can avail itself of an exemption from the MLO may approach local entities for lending business. Please also refer to the answer to question 1 of this section in respect of the applicable licensing requirements, which also apply to foreign banks and financial institutions. In addition, approaching local entities for business may support the view that a foreign bank or financial institution carries on business in Hong Kong (please refer to our discussion in the answer to question 2 of this section).

   In the case of a Hong Kong-incorporated AI, various lending restrictions may apply. For example, the BO provides for connected party lending limits (e.g., advances to directors and their relatives, certain controllers of the AI and employees who handle credit approvals for an AI and those employees' relatives), as well as large exposure limits (i.e., limits on the financial exposure of an AI to any single counterparty or any group of related counterparties).

   Foreign banks and financial institutions that establish, with HKMA approval, a local representative office in Hong Kong are generally subject to strict restrictions in relation to the activities that their local representative office may conduct. These restrictions are generally imposed by way of conditions that the HKMA includes in its approval letter. Representative offices are generally prohibited from carrying out anything other than limited marketing, liaison or representational activities.

When lending to borrowers

1. **Are there any restrictions in relation to the type of borrower who may borrow foreign currency or in relation to the term of foreign currency and/or the amount of foreign currency borrowed by local entities?**

   No.

2. **Are there any restrictions on the rate of interest or default interest that may be charged?**

   The MLO regulates the charging of excessive rates of interest by any person (other than an AI), whether or not that person is a money lender and regardless of whether an exemption from the MLO applies. Under the MLO, an effective annual interest rate in excess of 48% is illegal. In addition, an effective annual interest rate that exceeds 36% but does not exceed 48% is presumed to be extortionate and a Hong Kong court may reopen the underlying transaction.

   Under the MLO, an agreement that provides, directly or indirectly, for the payment of compound interest to a money lender is illegal. Similarly, an agreement that provides for the payment of interest to a money lender at a default rate is illegal, except for simple interest on the principal amount of the amount in default at the same rate at which interest is charged on the principal amount that is not in default.

   Although the MLO does not (and, therefore, the restrictions referred to above do not) apply to an AI, the Code of Banking Practice (a nonstatutory code that the HKMA expects all AIs to comply with) recommends that AIs also observe the MLO interest rate and default interest restrictions in relation to their dealings with customers who are individuals. However, there are no particular statutory restrictions on excessive interest rates or default interest in relation to loans by AIs to customers that are not individuals (e.g., Hong Kong companies). In any case, a provision in a loan agreement requiring any person to make any extra or increased payment as a result of a breach or a default (for example, a default interest provision) would be unenforceable if a Hong Kong court considered it a penalty.

3. Are there any restrictions on particular lenders or classes of lender entering into credit transactions with borrowers?

No, subject to the comments in the answer to question 1 of the "When considering whether to lend" section in relation to the licensing requirements for lenders.

4. Are there any exchange controls that will apply to payments to be made in foreign currencies or to foreign lenders?

No.

5. Is there any requirement to deduct or withhold tax from any amounts to be paid or repaid to a lender (whether domestic or foreign)? If so, at what rate must tax be deducted and from what kinds of payment?

No.

6. Are there any "thin capitalization" or other rules that may limit the extent to which interest payments may be deducted for tax purposes?

Hong Kong does not have a thin capitalization regime.

Generally, interest expenditure is deductible for tax purposes where it is incurred in the production of assessable profits. However, because certain types of interest income are exempt from tax in Hong Kong, there are specific situations in which deduction on interest may be limited to remove asymmetry that can arise where interest is deductible to the payer but is not assessable in the hands of the recipient. Broadly, these restrictions are concerned with situations where:

- The interest payment is secured or guaranteed by a deposit that is made by the borrower (or its associate) to certain persons and the interest income on the deposit is not taxable in Hong Kong
- The interest arises from an arrangement under which the interest payable is paid, directly or through an interposed person, back to the borrower (or a person connected or associated with the borrower) that is not assessed (or is chargeable at a reduced tax rate under certain tax concessions) on the interest income paid back

Failure to comply with these tests does not necessarily disallow deduction of the interest expense in its entirety. The restriction on interest deduction is confined to the portion of the interest relating to the portion of the loan, debenture or debt instrument that failed the tests and in respect of the time in which the failure persisted.

7. Are there any registration, notarization, translation or reporting requirements in relation to the loan documents?

No, provided that the loan documents do not contain any provisions creating registrable security. (See also the answer to question 1 of the section "When considering whether to lend" in relation to reporting requirements, as well as question 12 of the section "If taking security" in relation to security documents).

8. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to the loan documents? If yes, what are the amounts and when are they payable?

No, provided that they do not contain any provisions creating registrable security. (See the answer to question 12 of the "If taking security" section in relation to security documents).

9. Does the law recognize the subordination of the debt that a debtor owes to one creditor to that which the debtor owes to another creditor? If yes, how is this usually effected?

It is possible to provide contractually for the subordination of the debt a debtor owes to one creditor (the subordinated creditor) to that which the debtor owes to another creditor (the senior creditor). This is usually effected by the debtor and the senior and subordinated creditors entering into a subordination deed

(or, alternatively, an intercreditor deed, which usually sets out more detailed priority and intercreditor arrangements between the senior and junior creditors).

Under a typical contractual subordination, the senior and subordinated creditors agree that the subordinated creditor will not exercise its rights in respect of the relevant debt until the senior creditor has been paid in full.

Case law has confirmed the validity of contractual subordination arrangements in which a creditor agrees to waive, postpone or subordinate its debt to the debts of other creditors both before and on insolvency. However, any arrangement that interferes with the rights of other creditors might be called into question on the liquidation of the company.

10. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors (e.g., the claims of employees and tax authorities or the claims of creditors under particular kinds of instrument)? If yes, what classes of creditors are preferred?

Certain classes of unsecured creditors are preferred by statute. These include certain debts due to employees (e.g., wages and salaries up to a specified amount) and the government (e.g., taxes and duties). In the case of the liquidation or winding-up of a Hong Kong company, the expenses of the winding-up (including the liquidator's remuneration) have priority over all other debts (preferential or otherwise) and any charge on goods distrained may also take priority over the rights of unsecured creditors. In addition, statutory insolvency set-off (see the answer to question 1 of the section "If things go wrong") may effectively confer priority on an unsecured creditor.

A lender to a Hong Kong entity should also be aware of the Partnership Ordinance. According to the Partnership Ordinance, where a loan is made at an interest rate that varies with the borrower's profits or where repayment is made by way of a share of the borrower's profits, the lender may be subordinated to the borrower's other creditors and, in certain cases, this arrangement may result in the lender being held to be a partner of the borrower unless it is clear from a consideration of all the relevant facts and the finance documents that the lender is not intended to be considered to be a partner of the borrower.

11. Are there any consumer protection or similar laws that apply if credit is made available to individuals or other classes of debtor? If yes, what laws are applicable?

Apart from the BO, the MLO and the Code of Banking Practice (a nonstatutory code that the HKMA expects all AIs to comply with) provide general principles and guidelines that an AI should observe in dealings with individual customers, including in making available loans or other facilities and in taking the benefit of guarantees or security. Where a licensed money lender is a member of the Licensed Money Lenders Association (LMLA), the nonstatutory LMLA Code of Practice provides similar guidance.

In addition, various general consumer protection ordinances may provide additional protections in the context of a lending relationship with a bank or financial institution (and, in particular, where the counterparty is a consumer and where it is dealing with the bank or financial institution in the ordinary course of business), such as the following:

- The Control of Exemption Clauses Ordinance limits the effect and extent of exemption and the limitation of liability clauses if they are not considered reasonable.
- The Unconscionable Contracts Ordinance provides that certain contractual terms are not enforceable if they have an unconscionable effect.
- The Supply of Services (Implied Terms) Ordinance provides certain terms in the contractual relationship that suppliers of services, including lenders, must observe (e.g., an implied term to use reasonable care and skill).
- The Trade Descriptions Ordinance outlines that it is an offense to use false trade descriptions or to provide false, misleading or incomplete information (this ordinance does not apply to AIs).
- The Personal Data (Privacy) Ordinance provides statutory privacy protections for individuals.

12. **Are there any prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of: (a) its own shares or those of any affiliated company; or (b) assets owned by it or any affiliated company?**

Under the CO, there are certain prohibitions on a company, private or public, incorporated in Hong Kong providing financial assistance in connection with the acquisition of shares in itself or its parent company.

The CO prohibits a company ("**Target**") from giving financial assistance directly or indirectly for the purpose of acquiring shares in itself or its holding company or for the purpose of reducing or discharging liabilities so incurred. Financial assistance includes assistance given by way of guarantee, security, indemnity, loan, novation or other similar agreement, gift or any other assistance by which the company's net assets are reduced to a material extent.

This only applies to financial assistance given by the Target or by any of its subsidiaries. Therefore, the prohibition does not apply where the assistance is given by a parent in respect of an acquisition of its subsidiary's shares or by a subsidiary to assist in the acquisition of its sister subsidiary's shares. Moreover, the prohibition applies only to financial assistance given by a Hong Kong subsidiary for the acquisition of its own shares or shares in its Hong Kong holding company. It does not restrict a Hong Kong subsidiary from giving financial assistance for the purpose of acquiring shares in its offshore-incorporated holding company.

The restrictions above apply to financial assistance given before or at the same time as the acquisition and to reduce or discharge a liability incurred for the purpose of (i.e., after) the acquisition.

There are some exceptions to the prohibition, including where the giving of financial assistance is authorized in accordance with the so-called whitewash procedure.

If taking security

1. **Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's secured creditors?**

Secured creditors generally stand outside the order of priority of payments because they are entitled to be paid from the proceeds of their security. The exception is a creditor secured by a floating charge (discussed in the answer to question 3 of this section). Creditors secured by a floating charge rank below preferential creditors (e.g., employees and the government).

2. **May security given by a company rank in a specified order so as to secure liabilities owed to different creditors of the company in that order and, if that is not possible, is it viable for parties to enter into a contractual arrangement for the purposes of moderating this order?**

Yes, it is possible to contractually provide for a specified order of priority among different creditors. This is usually effected by the creditors and the debtor entering into a subordination agreement or an intercreditor deed.

3. **Does this jurisdiction recognise the concept of floating security or similar equivalent (i.e., security over a changing pool of assets that the company giving the security is free to buy, sell and generally deal with)?**

Yes. A floating charge allows the chargor to continue to deal with the charged assets in its ordinary course of business until the charge "crystallizes" into a fixed charge over the assets in existence at the point of crystallization, usually on a specified crystallization event.

4. If so, are there any practical reasons why floating security is difficult to take, maintain or enforce?

There are certain issues that a security holder needs to be aware of when taking a floating charge as security. On the insolvency of the chargor, the security granted by a floating charge ranks behind all fixed charges and behind the rights of certain preferential creditors (see the answer to question 1 of this section). On a winding-up of the chargor, a floating charge that was created within 12 months, or, in the case of a charge that was created in favor of a person connected to the chargor, within two years, of the commencement of the winding-up is invalid except to the extent of new consideration from the chargee, if any, unless it is shown that the chargor was solvent immediately after the creation of the floating charge.

However, contractual protections can be included in security documents to control and to mitigate against these types of risks, including the ability to automatically crystallize a floating charge into a fixed charge immediately on the occurrence of certain events (e.g., where insolvency proceedings against the chargor have commenced or where the lender considers that the assets subject to the floating charge may be in danger of being seized or otherwise be in jeopardy). On crystallization, a floating charge becomes a fixed charge and ranks as a fixed charge. This means that it would rank behind an earlier fixed charge but it would have priority over subsequent fixed charges and floating charges.

5. May security be granted to a trustee to be held on trust for the lenders from time to time, in such a way that a change of lenders does not require new security to be taken?

Yes.

6. If not, are there any techniques that can be used to achieve substantially the same effect (e.g., parallel debt structures)?

Not applicable.

7. If an agent holds security for the lenders rather than a trustee, is it necessary to take new security on a change of lenders? If no, why not? If yes, are there ways to structure the transaction to avoid such a requirement?

In Hong Kong secured lending transactions, the security agent usually acts as a trustee for the lenders, although the security agent may not necessarily be given the title of "trustee." If the security agent acts as an agent and not as a trustee, it would be necessary to consider the terms of the security agent's appointment and the agency provisions in the transaction documents to determine whether new security would be required on a change of lenders. Therefore, the simplest and most practical approach is for the security agent to always act as a trustee in relation to the security.

8. Under the laws of this jurisdiction, is there any class of asset over which it is difficult or impossible to grant effective and perfected security, or in relation to which any security granted will be of limited effect?

Security may be conferred over most assets that are likely to be of interest to lenders as security for a financing transaction. However, lenders should note the following:

- Future assets (i.e., those not in existence at the time of entering into the security document) may only be made the subject of equitable security, such as a charge, and not legal security, such as a legal mortgage. In practice, the distinction is unlikely to be significant.
- For a charge to be fixed (rather than floating), it is advisable for a lender to ensure that it exercises actual control over the charged assets so that the chargor is not permitted to freely deal with the assets as though they were not subject to the fixed charge. Otherwise, the security may be recharacterized as a floating charge. In practice, it is often difficult to take a fixed charge over inventory or trade receivables if they are trading assets of the chargor because the taking of a fixed charge is likely to be strongly resisted by a chargor.

- Where security is taken over contractual rights, the underlying contract giving rise to the assigned rights must be examined to ensure that those contractual rights can be made the subject of security. Prohibitions on the assignment of those rights will invalidate any purported security over them. In addition, rights under contracts that are "personal" to the contracting parties (e.g., an employment contract) are not assignable.
- In some cases, the involvement of a third party may be required before effective security can be granted. For example, it may be necessary to obtain a waiver or consent to the creation of the security from a contract counterparty.
- In the case of land in Hong Kong, it is necessary to consider the land grant conditions to determine whether the grant of security over land is permitted or subject to any restrictions. The land grant conditions may prohibit the creation of security over the land (even where security is granted to finance the land acquisition cost) or may otherwise limit the persons to whom security may be granted. In addition, the land grant conditions in respect of certain Hong Kong real property may contain restrictions on alienation that require, for example, specific consents to be obtained from the Hong Kong government or a government-linked entity prior to security being created in favor of a lender. In those cases, the consent may limit the maximum amount that may be secured by the relevant security.
- In the case of shares in a Hong Kong company, it is necessary to consider whether the articles of association of the company impose any restrictions on the grant of security over, or on the transfer of, those shares. The effectiveness of the security or a lender's rights to enforce that security may be compromised if the restrictions in relation to the transfer contained in the articles of association are not first altered or disapplied, or if any required consents are not obtained.
- As a matter of public policy, generally, it is not possible to assign (by way of security) a bare right to sue or litigate.

9. Under the laws of this jurisdiction, are there any restrictions on offshore lenders taking security over any class of asset?

No, but see the responses to question 8 of this section (which would apply equally to an offshore lender wishing to take security).

10. Must a company receive a corporate benefit in return for giving a guarantee or security? In particular, are there restrictions on the grant of upstream and cross-stream guarantees and security? If yes, briefly what is the effect of these laws?

Directors of a Hong Kong company have a common law duty to act in the best interests of the company and to exercise powers and to take actions that benefit the company commercially. The Companies Registry of Hong Kong ("**Companies Registry**") has issued nonstatutory guidelines that outline general principles for directors in the performance of their functions that embody the requirement for directors to act in the best interests of the company.

When considering whether a company should provide a guarantee or security, the directors must therefore consider whether any commercial benefit will accrue to the company from the provision of that guarantee or security.

Generally, Hong Kong law does not recognize the concept of a group benefit. When a parent company gives a guarantee or grants security in respect of a subsidiary's obligations, the commercial benefit to the parent can be clearly established. However, when a subsidiary company gives a guarantee or grants security in respect of its parent's obligations or the obligations of another subsidiary of its parent (i.e., a "sister" company), it is often more difficult to establish what the commercial benefit is to the subsidiary.

Whether a company derives a commercial benefit from providing a guarantee or security is a factual matter for consideration in each particular case however, practical steps can be taken to reduce the risk of commercial benefit arguments being successfully raised by the most likely objectors (the company's shareholders and creditors). Assuming a guarantee or security is proposed to be granted by a solvent company, two key steps are obtaining

the unanimous approval of the company's shareholders to the giving of the guarantee or the granting of the security and obtaining a statement from the company's directors that the company will not be unable to pay its debts as a result of the giving of the guarantee or the granting of the security. This will also protect the guarantee or security from being subsequently challenged as unenforceable on the basis that, for example, the directors used the powers conferred on them for an improper purpose or for a purpose not authorized by the company's articles of association (i.e., not in the best interests of the company), provided that the lender/chargee does not have actual knowledge of that impropriety.

Lastly, there are general presumptions in law that allow parties to presume that the transactions undertaken by a Hong Kong company are not ultra vires acts.

11. What type of security interests does your jurisdiction recognise, e.g., pledge, charge, mortgage, hypothecation? In relation to each type of security interest, please state the formalities required to create and perfect that security.

Types of security interests

The types of security interests typically used in financing transactions in Hong Kong include:

- For shares, a legal or equitable mortgage or an equitable charge.
- For real property, a legal charge.
- For other immovable assets: a fixed charge over specific assets.
- For movable assets: a chattel mortgage, a floating charge, or a pledge - note that under Hong Kong law, a "pledge" is a "possessory security" and can only be created over movable assets, but not over immovable assets or intangible assets.
- For bank accounts, book debts and contractual rights (such as rights to insurance and rights to trade receivables), an equitable or legal assignment, or a charge.
- Generally, a floating charge over all or certain classes of assets.

Formalities

Security over specified assets of a company incorporated in Hong Kong or a company registered under the CO as a "non-Hong Kong company" must be registered with the Companies Registry within one month of the creation of the relevant security. Otherwise, the security will not be enforceable against any liquidator or creditor of the security provider.

In addition, in the case of a legal charge over real property or any other security document affecting land, the security interest must also be registered within one month of its creation with the Land Registry of Hong Kong ("**Land Registry**") to preserve its priority.

The registration of certain assets with other registries may also be necessary or advisable. See the answer to question 12 of this section for the registration requirements.

To perfect an assignment of debts and contractual rights, written notice of the assignment must be provided to the debtor or counterparty. For some classes of an asset (e.g., shares and other securities), it is common for lenders or security agents to hold in their possession and control any documents of title (e.g., title deeds), blank transfer forms and other ancillary documents (e.g., signed but undated resignation letters of the directors) to assist with the enforcement of the security and prevent unauthorized dealings by the chargor.

Security interests over real property must generally be made by way of deed and it is common for security over other kinds of assets to be made by deed.

12. Are there any registration, translation or notarization requirements in relation to security, guarantees, subordination or intercreditor documents?

If a document creates registrable security, it must be filed with the Companies Registry within one month of the date of its execution (and together with a certified translation, if the security document is not in Chinese or English). This registration requirement only applies to security created by companies incorporated in Hong Kong and any foreign company that is registered as a non-Hong Kong company (as referred to in the answer to question 11 of this section).

Where a foreign company (not a non-Hong Kong company) enters into a security document and the secured property is situated in Hong Kong, and the company subsequently becomes registered as a non-Hong Kong company under the CO, the registration of the security with the Companies Registry is required within one month of the date of the foreign company's registration as a non-Hong Kong company.

As mentioned in the answer to question 11 of this section, a legal charge over real property or any other security document affecting land must also be registered within one month of its creation with the Land Registry (and if the security document is not in Chinese or English, together with a Chinese or English translation to enable the Land Registry to determine whether the relevant registration requirements have been complied with).

Apart from the registration requirements referred to above, there may be different registration requirements in respect of certain types of assets (e.g., vessels and intellectual property) and in relation to different types of security providers (e.g., individuals).

There are no notarization requirements in relation to security, guarantee, subordination or intercreditor documents.

13. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in respect of security, guarantees, subordination or intercreditor documents? If yes, what are the amounts and when are they payable?

A registration fee of HKD 340 must be paid to the Companies Registry on the submission for the registration of each security document.

A registration fee of HKD 450 must be paid to the Land Registry on the submission for the registration of each security document (or HKD 230 if the amount or value of the consideration or value of the property or interest affected is less than HKD 750,000).

Other than the registration requirements and fees set out above and in the answer to question 12 of this section, no stamp duty or similar taxes or charges are payable in respect of security documents. However, in respect of a mortgage of shares in a Hong Kong company, nominal stamp duty of HKD 5 is payable on the execution of an instrument of transfer signed "in blank" (which lenders normally require). The execution enables the shares to be registered in the name of the lender (or its nominee) by converting an equitable share mortgage into a legal share mortgage. Stamp duty at a rate of 0.26% of the value of shares being transferred will be payable on the enforcement of the security. After the execution of an agreement for the transfer of shares, the parties should submit the relevant documents for stamping, if that agreement is executed in Hong Kong, within two days of signing; if it is executed outside Hong Kong, within 30 days of signing.

If things go wrong

1. Please provide a brief description of the insolvency regime. In particular what rights and duties do unsecured and secured lenders have on the insolvency of a debtor? Are there any other matters of concern?

Insolvency regime

There are three types of liquidation in Hong Kong: a members' voluntary liquidation, a creditors' voluntary liquidation and a compulsory liquidation.

A members' voluntary liquidation can be commenced only where the company is solvent. The directors must sign a certificate of solvency stating their opinion that the company will be able to pay its debts in full within a period not exceeding 12 months from the commencement of the winding-up. Then, the shareholders pass a special resolution to place the company into voluntary liquidation.

A creditors' voluntary liquidation occurs where the shareholders pass a special resolution to place the company into voluntary liquidation and where the directors have not signed a certificate of solvency. The resolution is usually passed on the basis that the company cannot continue its business because of its liabilities. A creditors' meeting is also required.

A compulsory liquidation occurs where a company is wound up by an order of the court. A company may be wound up by the court on a number of grounds, most often in an insolvency situation because it is unable to pay its debts. There is also a broad discretionary power under which the court can order a company to be wound up where it is just and equitable to do so. The application submitted to the court to wind up a company may be made by a creditor, a shareholder or the company itself. This is done by way of a winding-up petition.

Unsecured creditors

An unsecured creditor must prove its debts in a liquidation by submitting a proof of debt form to the liquidator.

After the liquidator has received all the proof of debt forms from the creditors, the liquidator will assess each of the claims and decide whether to admit each proof. If the liquidator considers a claim unenforceable, the liquidator can reject the claim and put the onus of proving the debt back on the creditor.

Assuming that there are sufficient assets available to enable the liquidator to make a distribution to the creditors of the company, the liquidator must make a distribution in accordance with the order prescribed by legislation. Generally, the order of distribution is as follows:

- Secured creditors — assets of the company under security will be realized to pay off secured creditors first, with any excess proceeds distributed according to the subsequent priority below.
- Expenses of the liquidation, including liquidator's fees.
- Preferential payments (usually employees' wages and statutory debts due to the government).
- Floating charge holders.
- General unsecured creditors.
- Members/shareholders of the company.

If there are insufficient assets to be distributed to pay a class of creditors in full, the general principle of pari passu distribution (i.e., all creditors of the same class rank equally in a winding-up) applies.

Statutory insolvency set-off applies to unsecured debts. Where before the company goes into liquidation there have been mutual credits, mutual debts or other mutual dealings between the company and any creditor of the company proving or claiming in the liquidation, an account must be taken of what is due from each party to the other and the sums due from one party are set off against the sums due from the other; only the balance can be proved in the liquidation. Statutory insolvency set-off is mandatory in a liquidation and it cannot be contracted out of.

Secured creditors

A secured creditor (e.g., a creditor holding a mortgage, charge or lien) is entitled to enforce its security despite the making of a winding-up order. It can rely on its security and need not prove in the liquidation if the security is worth the same as, or more than, the debt owed.

If the creditor is undersecured, it can realize the security and prove for any balance or waive the security and prove for the entire debt.

Guidelines issued by the HKMA and the Hong Kong Association of Banks

The HKMA and the Hong Kong Association of Banks have issued nonstatutory guidelines as in relation to how institutions should deal with borrowing customers in financial difficulties where the borrower is dealing with multiple banks. Banks are encouraged to opt first for a workout (a private contractual arrangement to assist a company in financial difficulty).

2. Is it possible to obtain a moratorium before insolvency?

There is no formal moratorium available to an insolvent company on the presentation of a winding-up petition. However, in practice, the period between the presentation of a winding-up petition and the creation of a winding up-order provides a moratorium period (otherwise unavailable under the current legislative regime) in which to conduct restructuring negotiations. The reason for this is that once a winding-up petition is presented, the insolvent company (and any creditor and person obliged to contribute to the assets of the company) can apply to the court for a stay of proceedings.

Once a winding-up order has been made or a provisional liquidator appointed, no action or proceeding can commence or continue except by leave of the court.

In 2020, the Hong Kong government announced its intention to introduce the Companies (Corporate Rescue) Bill ("**Bill**") in the Legislative Council at a date to be confirmed. The Bill was aimed at introducing a statutory corporate rescue procedure in Hong Kong, which would involve the appointment of an independent professional third party (a certified public accountant or solicitor) as a provisional supervisor of a company in financial difficulty. The provisional supervisor would displace the directors and management of the company and act as its agent during the period of provisional supervision (proposed to be set at 45 business days), during which the company would continue to operate as a going concern. There would be a moratorium on civil proceedings and actions against the company and its property during this period. As a protective measure for secured creditors, one of the proposed requirements to commence provisional supervision was that a person holding charges on the whole or substantially the whole of the company's properties (the major secured creditor) would not object to the provisional supervision within a specified period upon being notified of the provisional supervision. However, as of the date on which this guide has been published, the Bill had not yet been tabled in the Legislative Council.

It remains to be seen whether and, if so, in which form the Bill will be enacted and take effect.

3. When a company is the subject of a formal insolvency procedure, can the company's pre-insolvency transactions be set aside?

Pre-insolvency transactions

Yes. In all forms of liquidation, a liquidator has the power to investigate the affairs of a company and seek redress from the court if it considers that assets belonging to the company have been dissipated. Some examples of possible areas that liquidators may investigate are set out below.

Unfair preference

A liquidator may challenge any creditor that received a payment from the company and may have been preferred against other creditors within six months of the commencement of the liquidation. The six-month period is extended to two years in the case of payments to a person connected with the company, which is broadly defined.

Disposition of property with the intent to defraud creditors

A disposition of property with the intent to defraud creditors is voidable at the behest of the person prejudiced by the disposition, except if the property has been disposed of for valuable consideration and in good faith to any person who has not been notified, at the time of the disposition, of the intent to defraud creditors.

Transactions at an undervalue

A court may set aside a transaction at an undervalue entered into within five years before the commencement of the liquidation. A transaction at an undervalue includes transactions that result in the company receiving consideration that is significantly less than the value provided by the company.

Disposition after the commencement of a compulsory liquidation

A disposition after the commencement of a compulsory liquidation is void and the recipients of these funds or assets must return them to the liquidator unless a validation order has been made by the court. A validation order is an order by which the court ratifies the relevant disposition of property.

Fraudulent trading

Where the business is carried on with the intent to defraud creditors or for any other fraudulent purpose, the persons who were knowingly parties to the carrying on of the business may be personally liable for the debts of the company.

Misfeasance

Where directors have breached their duties to the company or have misapplied or retained property of the company for their personal benefit, they may be ordered to repay or restore the money or property, or pay compensation to the company.

Insolvent trading

While fraudulent trading is prohibited, no legislation in Hong Kong prohibits insolvent trading or the incurring of a debt by a company at a time when it is unable to pay its debts as they fall due, although the liquidators may bring an action against the directors for the breach of their duties. The Hong Kong government is considering implementing provisions in relation to insolvent trading.

4. When can a lender enforce its security? Can security be enforced out of court following an event of default (or other contractual trigger event), or is a court order required? Are there any restrictions that apply before a lender may enforce its security?

Theoretically, a lender can enforce its security at any time; the precise time depends on the terms of the security document or other agreement between the lender and the borrower (e.g., as soon as the borrower is in default). However, the lender should give the debtor sufficient time to enable it to effect payment before enforcing the security.

Generally, there is no requirement to obtain a court order to enforce security. However, in respect of a mortgage over real property, a lender can bring a "mortgagee action" to obtain a court order for the payment of monies secured by the mortgage and for possession of the mortgaged property, among other things. Alternatively, a lender can enforce a mortgage by virtue of express or implied powers under the mortgage or powers implied into the mortgage by the Conveyancing and Property Ordinance.

Note that foreclosure of a mortgage (i.e., extinguishing a mortgagor's right to redeem (recover) the mortgaged asset on repayment of the secured debt) is only possible with a court order.

5. Do any limitation periods apply in relation to bringing an action to enforce security?

An action in simple debt is normally governed by the six-year limitation period for actions in contract and tort as stipulated by the Limitation Ordinance. The limitation period begins from the date on which the cause of action first accrues.

The Limitation Ordinance also provides that no action is permitted to be brought to recover any principal sum of money secured by a mortgage or other charge on property, or to recover proceeds of the sale of land, after the expiration of 12 years from the date when the right to receive the money accrued.

6. Is there any particular way in which secured assets must be liquidated on enforcement (e.g., by auction or court sale)?

There are no specific legal requirements on how secured assets must be liquidated on enforcement. Some relevant steps, however, in relation to the enforcement of security over real property, shares and movable assets are set out below.

Real property

A mortgagee must comply with its duties on the sale of the asset by acting in good faith and taking reasonable steps to obtain a proper price for the mortgaged property. Practically, this is usually done by way of an auction.

Foreclosure, which results in the lender becoming the absolute owner of the charged property, requires a court order.

Shares

Security over shares can generally be enforced without a court order. Depending on the terms of the security document, a lender usually has the right to sell the shares and exercise all the voting rights attached to the shares.

Movable assets

Movable assets secured by way of a fixed or floating charge are often realized by appointing a receiver to take physical possession of the assets and sell them. Usually the document creating the charge sets out the method of enforcement.

7. Are there any particular legal or practical difficulties or delays in enforcing security?

A debtor may resist the lender's attempt to enforce security, often by disputing the debt itself or by questioning the validity of the document creating the security. This often causes delays in enforcing the security.

8. In relation to enforcement, are there any specific requirements to be borne in mind if the lender is a foreign entity?

If a foreign entity that neither resides nor carries on business in Hong Kong brings proceedings to enforce security, the defendant may apply for security for costs of the action to be paid in court. The amount to be paid is generally an estimate of the defendant's costs in defending the action brought by the foreign entity. The court has discretion in relation to whether to grant this type of order, having regard to all the circumstances, including the plaintiff's prospects of success. However, security for costs is usually not required if the foreign entity has substantial property of a fixed and permanent nature within Hong Kong.

9. Is there any reason why you think that arbitration rather than litigation might be advantageous in resolving disputes under the finance documents, and if so, why? Please outline the relative merits of arbitration and litigation, including the ease of enforcement of foreign judgments and foreign awards from different jurisdictions. Is it possible to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit?

Confidentiality

Arbitration proceedings are typically private and confidential. By contrast, court proceedings are open to the public and the judgments are public documents. Parties normally opt for arbitration if the dispute is commercially sensitive.

Procedural matters

The arbitral tribunal can conduct the arbitration in the manner that is most efficient and expeditious without being bound by local court procedural rules. A common example is that the rules of evidence are not generally applicable in arbitrations.

Court hearings are governed by a fixed set of procedural rules. This may offer certainty to the parties over the more flexible but uncertain procedures in arbitration and, in some cases, can reduce delay in the proceedings.

Summary procedure

Under Hong Kong court rules, there is a summary judgment procedure for obtaining judgment in cases where there is no dispute about the facts. While institutional arbitration rules commonly used in Hong Kong allow an arbitral tribunal to decide points of law or fact in an early determination procedure, a summary judgment is not available in arbitration. As disputes under finance documents usually do not involve complex factual issues, the lack of a summary judgment procedure could increase time and costs in an otherwise straightforward case.

Enforceability

An arbitral award rendered in Hong Kong can be enforced in over 170 party states to the New York Convention on Recognition and Enforcement of Foreign Arbitral Awards, including most of the major business centers, as well as in Mainland China.

A foreign court judgment is enforceable by way of registration or under the common law if certain requirements are fulfilled. If the judgment is entered in Mainland China, the judgment may be enforced under the relevant Hong Kong Ordinance implementing the applicable Hong Kong/Mainland China arrangement on reciprocal recognition and enforcement of judgments. The existing arrangement under the Mainland Judgments (Reciprocal Enforcement) Ordinance (Cap. 597) ("**Old MJREO**") will be replaced effective 29 January 2024 by the new Mainland Judgments in Civil and Commercial Matters (Reciprocal Enforcement) Ordinance (Cap. 645) ("**New MJREO**"). However, the Old MJREO will continue to apply in certain cases even after the New MJREO has taken effect.

Appeals

Unlike litigation, there is generally no right of appeal in arbitration, unless the parties expressly agree on a right of appeal. Even in those circumstances, the right of appeal is limited.

Costs

While arbitrations require parties to pay the costs of the arbitral institution and arbitral tribunal whereas there is no or minimal costs in using the public court facilities in litigation, the cost difference between arbitration and litigation (in terms of legal fees) is usually not significant.

Hybrid enforcement

It is possible to adopt dispute resolution provisions that allow lenders to opt for either arbitration or litigation as they see fit.

10. Are asymmetrical jurisdiction clauses enforceable? (By this we mean clauses that allow the lenders, but not the borrowers, to make certain choices in relation to choice of jurisdiction and how to litigate. These types of clauses allow the lenders, but not the borrowers, to commence proceedings in any court they choose, but restrict the borrowers to commencing proceedings in one jurisdiction only. This may also allow the lenders, but not the borrowers, to choose whether to litigate the finance documents before a court or to submit to arbitration in relation to them, but restrict the borrowers to either litigation or arbitration, as specified in the agreement).

Hong Kong courts generally give effect to the contractual agreement of the parties, save in exceptional circumstances.

There is one case where a Hong Kong court held that a clause that gave only one of the parties the right to refer a dispute to arbitration was within the meaning of an "arbitration agreement" of Article 8(1) of the UNCITRAL Model Law (*China Merchants Heavy Industry Co Ltd v. JGC Corp* [2001] 3 HKC 580). More recent authorities further support the proposition that Hong Kong courts accept asymmetrical clauses.

While an asymmetrical jurisdiction clause is likely to be enforceable in Hong Kong, there may be additional considerations when the party with the option to choose the jurisdiction (i.e., usually the lender) wants to enforce a judgment in Mainland China through the Old MJREO, where the underlying contract contains an asymmetrical jurisdiction clause. Under the Old MJREO, to enforce the Hong Kong judgment Mainland China, the Hong Kong court needs to have exclusive jurisdiction, as agreed by the parties to the underlying contract. In *Industrial and Commercial Bank of China* (Asia) *Limited v. Wisdom Top International Limited* [2020] HKCFI 322 (which was followed in *TransAsia Private Capital Ltd v. Cheng Yu* [2022] HKCFI 1295), the Hong Kong court held that an asymmetrical jurisdiction clause is not an exclusive jurisdiction clause and so a judgment based on such contract would not be enforceable in Mainland China under the Old MJREO.[1]

Working digitally

1. Is it possible for documents to be executed electronically (whether by the manual insertion of a digital signature or the use of an e-signing platform) under the laws of this jurisdiction? If so, is this limited to only particular types of finance documents?

Yes, it is generally possible for documents to be executed electronically under the laws of Hong Kong, subject to certain restrictions under the Electronic Transactions Ordinance (ETO).

Schedule 1 to the ETO sets out certain categories of documents to which the relevant provisions of the ETO do not apply, for example, they require wet ink signatures or physical execution. Primarily relevant in the context of secured lending are documents creating, executing, varying or revoking an express trust or a power of attorney (including documents containing such trust/power of attorney provisions), Hong Kong land-related security documents and contracts assigning or otherwise disposing of an interest in immovable property in Hong Kong.

Charges created by companies that are registrable under the CO would generally also require physical execution. Security over particular types of assets (such as intellectual property, aircraft, vessels, etc.) may be subject to registrations with specialized registries. Whether the relevant security document can be executed electronically will depend on the specific registration requirements applicable in each case.

Special registration requirements apply for certain charges granted by individuals, which may require the security document to be executed in a physical written form.

In transactions involving government entities, a signature requirement under the law can only be satisfied by a "digital signature" supported by a recognized digital certificate issued by a certification authority recognized under the ETO. This requirement does not apply to transactions with parties that are not government entities.

2. Where the witnessing of a signing is contemplated, is it possible for the witness to verify the signature over a live video call?

Pending further clarification by legislation and case law, generally, it is prudent to assume that a witness must be physically present.

1 However, as indicated in the response to question 9 (under "Enforcement"), the New MJREO will take effect on 29 January 2024, in order to implement the new arrangement entered into by Hong Kong and Mainland China (the "Arrangement on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters between the Courts of the Mainland and of the Hong Kong SAR" of 18 January 2019 ("**2019 Arrangement**")). Under the 2019 Arrangement, the requirement that the judgment needs to be from a court with exclusive jurisdiction is abolished.

3. **Is it possible to register/perfect security electronically without wet ink signatures?**

   It is possible to submit documents relating to charges and the release of charges to the Companies Registry for registration in an electronic form (and to sign the relevant Companies Registry form without wet ink signatures), provided that, among other things, appropriate user accounts are opened with, and the relevant passwords or digital certificates are "registered" with, the Companies Registry's e-Registry. However, normally, it is not feasible to electronically submit the registrable security document itself to the Companies Registry (e.g., because they typically include a power of attorney and other provisions that cannot be executed electronically by virtue of Schedule 1 to the ETO). Please see the Companies Registry's website for more guidance.

4. **Are there any other legal restrictions that may prevent the parties from executing a finance transaction electronically?**

   No.

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INDIA

India

Background

India has an exchange control regime. The inflow and outflow of foreign currency is regulated by the Foreign Exchange Management Act, 1999 and the rules and regulations framed under it. All loans and credit facilities made available by a foreign lender to an Indian borrower are governed by that act. An external commercial borrowing (ECB) is a commercial loan raised by an eligible resident entity from a recognized nonresident entity. An ECB is required to conform to several parameters, including amount, minimum average maturity, end use and all-in-cost ceilings.

The framework in relation to ECBs is contained in the "Master Direction on External Commercial Borrowings, Trade Credits and Structured Obligations" dated 26 March 2019, as amended ("**ECB Guidelines**"), issued by the Reserve Bank of India (RBI).

Under the ECB Guidelines, ECBs can be made available either in a foreign currency or in Indian rupees.

When considering whether to lend

1. Is it necessary or advisable for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in this jurisdiction: (a) by reason only of its execution, delivery or performance of the finance documents; or (b) to enable it to enforce its rights under the finance documents?

No. However, depending on the nature of the security created to secure the ECB, an offshore security agent would need to have a digital signature to file certain forms with the Registrar of Companies (ROC) or have a dematerialized account with a depository in India. If it does not have either of these, it may be necessary to appoint a security trustee in India.

2. Will any lender, arranger, facility agent or security agent be deemed to be resident, domiciled, carrying on business or subject to tax by reason only of the execution, delivery, performance or enforcement of the finance documents?

No.

3. Are there any regulatory reporting requirements that lenders must observe in connection with those transactions?

Depending on the nature of the security created in relation to the ECB, the lender or the security agent may be required to sign certain forms with the ROC, make certain filings with the Central Registry of Securitization Asset Reconstruction and Security Interest (CERSAI) or assist with the registration of the security documents with the relevant land registry. Further, if a pledge or any other encumbrance is created over shares of a listed company, it may need to be disclosed by the lender or the security agent to the relevant stock exchange in accordance with the regulations issued by the Securities and Exchange Board of India (SEBI).

4. Is it necessary to establish a place of business in your jurisdiction in order to enforce any provision of the finance documents?

No.

5. Is a foreign bank/financial institution permitted to approach local entities for business?

A lender that is eligible to provide an ECB may approach Indian borrowers in relation to ECBs.

When lending to borrowers

1. Are there any restrictions in relation to the type of borrower who may borrow foreign currency or in relation to the term of foreign currency and/or the amount of foreign currency borrowed by local entities?

Yes. The ECB Guidelines (see "Background") prescribe the categories of entities to which an ECB can be made available and also limit the amounts that the entities may borrow without the RBI's approval.

Entities to which ECBs may be made available

A foreign currency-denominated ECB may be made available to all entities eligible to receive foreign direct investment in India, port trusts, units in a special economic zone, the Small Industries Development Bank of India and the Export Import Bank of India.

An ECB denominated in Indian rupees may be made available to all entities eligible to borrow foreign currency ECBs as well as to registered entities engaged in microfinance activities, entities that are registered not-for-profit companies, registered societies/trusts/cooperatives and nongovernmental organizations.

Term of ECBs

Generally, an ECB must have a minimum average maturity of three years. However, depending on the end use of an ECB, the ECB Guidelines prescribe the following minimum average maturities:

- ECB raised by manufacturing companies up to USD 50 million or its equivalent per financial year: 1 year.
- ECB raised from a foreign equity holder for working capital purposes, general corporate purposes or for repayment of Indian rupee loans: 5 years.
- ECB raised for working capital purposes or general corporate purposes or on-lending by nonbanking financial companies (NBFCs) for working capital purposes or general corporate purposes: 10 years.
- ECB raised for repayment of Indian rupee loans availed domestically for capital expenditure or on-lending by NBFCs for the same purpose: 7 years.
- ECB raised for repayment of Indian rupee loans availed of domestically for purposes other than capital expenditure or on-lending by NBFCs for the same purpose: 10 years.

Limits on the amount of ECBs

Eligible borrowers are permitted to borrow up to USD 750 million or the equivalent by way of ECBs each financial year. Any borrowings exceeding the above amounts require the RBI's prior approval.

2. Are there any restrictions on the rate of interest or default interest that may be charged?

The ECB Guidelines prescribe an all-in-cost ceiling of 500 basis points above the benchmark rates for foreign currency ECBs. For ECBs in Indian rupees, the ECB Guidelines prescribe an all-in-cost ceiling of 450 basis points above the benchmark rates. The benchmark rate in the case of foreign currency ECBs refers to any widely accepted interbank rate or alternative reference rate of six-month tenor applicable to the currency of borrowing, e.g., EURIBOR for euros. The benchmark rate in the case of Indian rupee-denominated ECBs is the prevailing yield of the government of India securities of the corresponding maturity. The "all-in cost" includes rate of interest, other fees, expenses, charges, guarantee fees and export credit agency charges, whether paid in foreign currency or Indian rupees, but will not include commitment fees and withholding tax payable in Indian rupees.

Default interest must not exceed 2% above the rate of interest agreed under the facility agreement. Any payment of default interest over and above that rate may require the RBI's prior approval.

3. Are there any restrictions on particular lenders or classes of lender entering into credit transactions with borrowers?

ECBs can only be extended by a lender that is a resident of any one of the following:

- A country that is a member of the Financial Action Task Force (FATF) or a member of an FATF-style regional body; and should not be a country identified in the FATFs public statement as a jurisdiction that has strategic anti-money laundering or combating the financing of terrorism deficiencies to which countermeasures apply, or a jurisdiction that has not made sufficient progress in addressing the deficiencies or has not committed to an action plan developed with the FATF to address the deficiencies.
- A country whose securities market regulator is a signatory to the Multilateral Memorandum of Understanding of the International Organization of Securities Commission's (IOSCO) Multilateral Memorandum of Understanding (Appendix A Signatories) or a signatory to a bilateral memorandum of understanding with the SEBI for information-sharing arrangements.

Further, the following are also recognized lenders under the ECB Guidelines:

- Multilateral and regional financial institutions of which India is a member.
- Individuals provided they are foreign equity holders.
- Individuals provided they are subscribing to bonds or debentures listed offshore.
- Foreign branches or subsidiaries of Indian banks (only for foreign currency-denominated ECBs).

4. Are there any exchange controls that will apply to payments to be made in foreign currencies or to foreign lenders?

Yes, see "Background." Further, the ECB Guidelines contain restrictions in relation to the following:

- The amount of ECBs that can be raised (see the answer to question 1 of this section).
- The amount of interest and fees that can be paid on ECBs (see the answer to question 2 of this section).
- The assets that can be provided as security for an ECB (see "Regulatory approvals" in the answer to question 10 of the "If taking security" section).
- The prepayment of ECBs (any proposed prepayment that does not comply with the stipulated minimum average maturity, as mentioned in the answer to question 1 of this section, requires the RBI's prior approval).
- Indemnity payments by an Indian borrower to a person resident outside India (these require the RBI's prior approval).

5. Is there any requirement to deduct or withhold tax from any amounts to be paid or repaid to a lender (whether domestic or foreign)? If so, at what rate must tax be deducted and from what kinds of payment?

Withholding tax is payable on payments of interest in relation to ECBs by Indian borrowers to foreign lenders. Currently, the rate is 5% where the loan agreement in relation to the ECB is entered into before 1 July 2023 subject to the satisfaction of certain conditions notified by the government of India. For interest payments by an Indian company on money borrowed or debt incurred in foreign currency on or after 1 July 2023, the rate is 20% plus surcharge and cess, while in other cases, a 40% rate plus surcharge and cess would apply. This is subject to the availability of tax treaty benefits and compliance with the requisite conditions for availing such benefits.

6. Are there any "thin capitalization" or other rules that may limit the extent to which interest payments may be deducted for tax purposes?

The thin capitalization provisions impose limitations on the deduction of excess interest incurred by way of interest or payments of a similar nature by an Indian company or a permanent establishment of a foreign company ("PE") to its nonresident associated enterprise in respect of debt borrowed. Excess interest is an interest amount exceeding 30% of the earnings before interest, taxes, depreciation and amortization (EBITDA) of the Indian company or PE.

These rules are only applicable where the interest, or payments of a similar nature, amount exceeds Indian rupees 10 million. Further, the interest expense that is disallowed against income will be allowed to be carried forward and allowed as a deduction against profits and gains of any business or profession carried on for up to eight assessment years, subject to the limits mentioned.

The thin capitalization rules are also applicable in instances of interest payments to third-party lenders that provide a loan on the basis of an associated enterprise, either providing an explicit or implicit guarantee to such third-party lender or depositing a corresponding amount with such lender.

Thin capitalization provisions are not applicable to Indian companies and PEs engaged in the banking or insurance business or notified NBFCs. These provisions are also not applicable with respect to interest paid in respect of a debt issued by a lender that is a PE of a nonresident that is engaged in the business of banking (for example, where the lender is the branch of a foreign bank in India).

7. Are there any registration, notarization, translation or reporting requirements in relation to the loan documents?

A facility agreement is not required to be registered or notarized with any authority. However, the details of the ECB are required to be reported to the RBI through the authorized dealer category-I bank in the form prescribed under the ECB Guidelines. The said report has to be made in English.

No specific translation requirements apply if the documents are in English.

See the answer to question 11 of the "If taking security" section for the requirements in relation to security documents.

8. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to the loan documents? If yes, what are the amounts and when are they payable?

There are no taxes, duties, fees or other charges payable to any governmental authority or the RBI for using foreign currency loans.

However, stamp duty must be paid on credit agreements, guarantee deeds and security documents. The stamp duty payable on the documents varies from state to state. Usually, it is the obligation of the borrower, guarantor or security provider (as the case may be) to pay the stamp duty.

Stamp duty is paid prior to, or at the time of, execution of a document in India. Payment of stamp duty is often a determinative factor in choosing the location for the execution of documents. However, if a document is stamped in one Indian state but the original or a copy of it is brought into another Indian state that levies a higher stamp duty, differential stamp duty may be payable in the other state, depending on the nature of the document and the stamp duty laws in that state.

If a document is executed outside India, under Indian law, no stamp duty is payable on or before its execution. However, if the document or a copy of it is received in India, stamp duty may be payable on it, depending on the Indian state where the document is received and the nature of the document.

See the answer to question 11 of the "If taking security" section for the requirements in relation to fees payable in relation to security documents.

9. **Does the law recognize the subordination of the debt that a debtor owes to one creditor to that which the debtor owes to another creditor? If yes, how is this usually effected?**

   Yes. Contractual subordination, by which lenders agree among themselves how the payment of debts will be prioritized, is the usual way of achieving this. It is usually documented in a subordination deed or an intercreditor agreement.

10. **Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors (e.g., the claims of employees and tax authorities or the claims of creditors under particular kinds of instrument)? If yes, what classes of creditors are preferred?**

    See the answer to question 1 of the "If things go wrong" section.

11. **Are there any consumer protection or similar laws that apply if credit is made available to individuals or other classes of debtor? If yes, what laws are applicable?**

    Individuals are not eligible to borrow ECBs and, therefore, consumer protection laws are not relevant to loans made under the ECB Guidelines.

12. **Are there any prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of: (a) its own shares or those of any affiliated company; or (b) assets owned by it or any affiliated company?**

    Under the Companies Act, 2013, a public company is not permitted to provide, whether directly or indirectly and whether by means of a loan, guarantee, the provision of security or otherwise, any financial assistance for the purpose of, or in connection with, a purchase or subscription made or to be made by any person of, or for any shares in, the company or its holding company. However, this rule does not apply to private companies.

    Further, under the ECB Guidelines, ECBs cannot be used for acquisition of shares other than acquisition of shares in an overseas entity in accordance with the guidelines issued by the RBI.

If taking security

1. **Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's secured creditors?**

   See the answer to question 1 of the "If things go wrong" section, where the priority waterfall for distribution if liquidation proceeds is discussed.

2. **May security given by a company rank in a specified order so as to secure liabilities owed to different creditors of the company in that order and, if that is not possible, is it viable for parties to enter into a contractual arrangement for the purposes of moderating this order?**

   Yes. An agreement between the borrower and the secured creditors prescribes the order of ranking. The lenders can also enter into an intercreditor agreement for moderating the order of priority of common security.

3. **Does this jurisdiction recognise the concept of floating security or similar equivalent (i.e., security over a changing pool of assets that the company giving the security is free to buy, sell and generally deal with)?**

   Yes. Indian law recognizes the concept of a floating charge. A floating charge may be created over movable assets, receivables and current assets.

4. If so, are there any practical reasons why floating security is difficult to take, maintain or enforce?

If appropriate safeguards and monitoring mechanisms are implemented in the finance documents, it is not difficult to maintain and enforce a floating charge over movable assets.

5. May security be granted to a trustee to be held on trust for the lenders from time to time, in such a way that a change of lenders does not require new security to be taken?

Yes. These arrangements are possible as Indian law recognizes the concept of a trust. The relevant legislation is the Indian Trusts Act, 1882.

6. If not, are there any techniques that can be used to achieve substantially the same effect (e.g., parallel debt structures)?

Not applicable.

7. If an agent holds security for the lenders rather than a trustee, is it necessary to take new security on a change of lenders? If no, why not? If yes, are there ways to structure the transaction to avoid such a requirement?

Although the concept of agency is recognized in India, security is usually held by a trustee to avoid any difficulties regarding creation of security pursuant to a change of lenders.

8. Under the laws of this jurisdiction, is there any class of asset over which it is difficult or impossible to grant effective and perfected security, or in relation to which any security granted will be of limited effect?

The security created over assets of a project for which a concession is granted by the government (i.e., because the government owns the relevant land or has commissioned the project) may be subject to governmental approvals and terms and conditions imposed by the relevant governmental authority.

9. Under the laws of this jurisdiction, are there any restrictions on offshore lenders taking security over any class of asset?

The ECB Guidelines permit an ECB to be secured by immovable assets, movable assets and financial securities of an Indian company subject to obtaining the no-objection certificate of the authorized dealer bank in India. However, if any such asset constitutes a cross-border asset (such as shares of an overseas company), additional conditions may apply.

10. Must a company receive a corporate benefit in return for giving a guarantee or security? In particular, are there restrictions on the grant of upstream and cross-stream guarantees and security? If yes, briefly what is the effect of these laws?

The Indian Contract Act, 1872 provides that anything done for the benefit of the principal debtor is sufficient consideration for the guarantor or provider of security. However, the guarantor or security provider must be empowered under its constitutional documents to enter into a guarantee or grant security (as the case may be).

Where a third-party Indian company provides the guarantee or security, shareholders' approval of that company (by way of a special resolution) is required if certain prescribed thresholds (in terms of paid-up capital and free reserves) are exceeded. However, the approval is not required if the guarantee or security is provided in respect of financing made available to its wholly owned subsidiary company or joint venture company.

Please note that under the Companies Act, a company ("lending company") cannot grant a loan, provide security or extend a guarantee to, or on behalf of, any other company that has common directors with the lending company if certain conditions are met, unless the loan, guarantee or security has been approved by the lending company's shareholders and such loan is used for the principal business activities of the borrower. This is subject to certain exceptions, such as the following:

- Any guarantee given or security provided by a holding company in respect of a loan made to its wholly owned subsidiary if that loan is used by the wholly owned subsidiary for its principal business activities.
- Any guarantee given or security provided by a holding company in respect of a loan made by any bank or financial institution to its subsidiary company if that loan is used by the subsidiary for its principal business activities.

If the lending company, in the ordinary course of its business, provides loans, guarantees or security for the due repayment of a loan and, in respect of that loan, interest is charged at a rate no less than the rate of the prevailing yield of 1 year, 3 years, 5 years or 10 years government security closest to the tenor of the loan.

11. What type of security interests does your jurisdiction recognise, e.g., pledge, charge, mortgage, hypothecation? In relation to each type of security interest, please state the formalities required to create and perfect that security.

Modes of security creation

Immovable property

Security over immovable property, such as land and buildings, is taken in the form of a mortgage. The Transfer of Property Act, 1882 ("**TOP Act**") primarily governs the creation of mortgages. The most common forms of mortgage are an English mortgage (a registered mortgage), a simple mortgage (a registered mortgage) and an equitable mortgage (a mortgage created by depositing the title deeds with the lender or security trustee).

Under the TOP Act, a mortgage (other than an equitable mortgage) for repayment of money exceeding Indian rupees 100 must be created by way of a registered instrument. The instrument must be signed by the mortgagor, attested by two witnesses and registered with the land registry where the mortgaged immovable property is situated.

In the case of an equitable mortgage, the mortgagor or its authorized representative deposits the title deeds in relation to the immovable property with the lender or security trustee and provides a declaration, at the time of the deposit, that records that the title deeds were deposited by that person with the lender or security trustee with the intention of creating a mortgage. The lender or security trustee records the deposit of title deeds by way of a memorandum of entry.

Shares and other securities

Security over shares and other securities is typically created by way of a pledge. There is no prescribed form under Indian law for the creation of a pledge of shares. However, a pledge agreement or deed is usually entered into between the pledgor and the pledgee to create and record the pledge. The pledgor also usually issues a separate power of attorney to the pledgee that allows the pledgee to deal with the pledged shares/securities in case of an event of default and take other actions on behalf of the pledgor.

Movable property

Movable property, such as cash deposits, bank accounts, receivables, plant and machinery and stock, is usually secured by way of hypothecation. Under Indian law, hypothecation generally means a charge over any movable property, existing or future, created by a borrower in favor of a creditor without the delivery of possession of the movable property to that creditor. The charge created by way of hypothecation may be a fixed charge over identifiable assets or fixed assets and is usually a floating charge over current assets and stock-in-trade.

The security provider executes a deed of hypothecation in favor of the lender or security trustee. The deed of hypothecation is usually a standalone document and covers all terms and conditions, powers and provisions to safeguard the interests of the lender/creditor. The security provider also usually issues a separate power of attorney to the lender or security trustee that allows the lender or security trustee to deal with the hypothecated assets in case of an event of default and take other actions on behalf of the security provider.

Corporate authorizations

If the security provider is a corporate entity, its constitutional documents must permit the creation of a mortgage over its immovable property. If the security provider is a company, it may need to obtain board and shareholder resolutions to approve the creation of the security, which must be in accordance with the requirements of the Companies Act.

Perfection requirements

In India, the perfection of a security occurs through registration. The type of security and the type of property determine where a security must be registered. While some securities do not require registration, others must be registered at more than one registry.

Registration under the Indian Registration Act, 1908

Any mortgage of immovable property, other than an equitable mortgage created by way of deposit of title deeds of the mortgaged property, must be registered in accordance with the Indian Registration Act, 1908 ("**Registration Act**") within four months of the execution of the mortgage deed. All Indian states require this type of mortgage to be registered. If the mortgage is not registered, it is invalid. However, where the mortgage is an equitable mortgage of immovable property created by way of deposit of title deeds of the mortgaged property, the document recording the deposit of title deeds is only required to be registered under the Registration Act in some Indian states.

No registration is required for any instrument creating any title or interest in, or right to, movable property under the Registration Act. Deeds of hypothecation and share pledge agreements are not required to be registered under the Registration Act.

Registration with CERSAI

A mortgage (by way of deposit of title deeds or otherwise), hypothecation (of plant and machinery, stocks, a debt (including book debt or receivables) and a security interest (in intangible assets, i.e., know-how, a patent, copyright, a trademark, a license, a franchise or any other business or commercial right of a similar nature, or on an under-construction residential or commercial building or its part by an agreement or instrument other than by mortgage) are also registered with CERSAI. This registration must be done by the lender or the security trustee with CERSAI.

Filing with the ROC

A mortgage, lien, charge, pledge, hypothecation or any other security interest created by an Indian company over its assets located in India or abroad must be registered with the relevant ROC within 30 days from the creation of the security interest. The ROC issues a certificate of charge. A charge created by an Indian company will not be taken into account by the liquidator or any creditor of the company unless it is registered with the ROC and a certificate of registration of the charge is issued by the ROC. The security provider company is also required to maintain a register of charges recording the details of the charge.

Intellectual property, ships and aircraft

Security over intellectual property, ships and aircraft must also be registered with the relevant government authority.

Registration and filing fees

Registration and filing fees vary according to the type of security and are payable at the time of registration. Some Indian states have a fixed registration fee, while others have a percentage-based fee. The amount of the registration fee for registering a mortgage of land with the land registry depends on the Indian state in which the property is located.

Registration fees for registering security documents with the ROC are nominal.

Regulatory approvals

Approvals from tax authorities

Creating a charge over certain types of assets (land, buildings, machinery, plant, shares, securities and fixed deposits in banks), to the extent to which those assets do not form part of the stock-in-trade of the taxpayer's business, may also need the income tax authorities' permission. If any proceedings are pending against the security provider under the Income Tax Act, 1961 where the amount of tax or other sum payable or likely to be payable exceeds Indian rupees 5,000, any mortgage or charge over assets of that type that are valued at more than Indian rupees 10,000 would be held to be void to the extent of any claims of the income tax authorities arising out of those proceedings. Further, as per the provisions of the Central Goods and Services Act, 2017 ("CGST Act"), if a company creates a charge over its assets after amounts under the CGST Act are due from such company and with an intention to defraud the government revenue, such charge will be void against any claim in respect of any tax or any other sum payable by the company. It is therefore, advisable for a lender to require that the security provider obtains the permission of the assessing officer under the Income Tax Act, 1961 and the proper officer under the CGST Act before creating any mortgage or charge in the lender's or security trustee's favor. However, this may delay the completion of the financing, as obtaining permissions from the income tax authorities and authorities under the CGST Act may be time-consuming.

Consents of the authorized dealers for ECBs

In the case of ECBs, the RBI has permitted authorized dealers (i.e., banks in India that have been given special licenses to deal with foreign exchange) to grant permission in relation to the creation of security over movable property, immovable property and financial securities in accordance with the ECB Guidelines.

Other formalities

Immovable property

As a matter of practice, a title search is conducted in relation to immovable property to ensure that the mortgagor is the legal owner and entitled to mortgage the property and to check whether any prior charge or mortgage exists over the property. The title search is conducted at the land registries in whose jurisdiction the immovable property is situated. Note that an equitable mortgage does not appear in the land registry's records unless registered with the relevant land registry. Therefore, it is advisable to also initiate a search with the ROC to check whether any equitable mortgage has been registered there.

Movable property such as bank accounts and contracts

In the case of a hypothecation over bank accounts or contracts, notices should be issued to the banks or the counterparties to the contracts informing them of the charge created. Often the bank will be the chargee and therefore know about the hypothecation. If the bank is not the chargee, however, and the notice is not issued, the chargee may find that the money in the relevant bank account is withdrawn and the charge is worthless.

Shares or other securities

Where the shares are in dematerialized form, certain forms have to be filed with the depository participant to mark a pledge over these shares in the shareholder's beneficial account.

12. Are there any registration, translation or notarization requirements in relation to security, guarantees, subordination or intercreditor documents?

In relation to registration requirements for security documents, please see the answer to question 11 of this section. Guarantees, subordination deeds and intercreditor documents are not required to be registered under Indian law.

There are no specific translation requirements that apply if the documents are in English.

13. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in respect of security, guarantees, subordination or intercreditor documents? If yes, what are the amounts and when are they payable?

Please see the answer to question 8 of the "When lending to borrowers" section.

If things go wrong

1. Please provide a brief description of the insolvency regime. In particular what rights and duties do unsecured and secured lenders have on the insolvency of a debtor? Are there any other matters of concern?

The insolvency regime for a company is governed by the Insolvency and Bankruptcy Code, 2016 ("**Code**"). The insolvency resolution process of corporate persons (CIRP) is governed by Part II (Corporate Insolvency Resolution Process) of the Code and the regulations made under it. The adjudicating authority in relation to any matters relating to the CIRP of a corporate person is the National Company Law Tribunal (NCLT). No civil court or any other authority has jurisdiction in relation to insolvency matters of companies. Under the Code, prepackage insolvency resolution is currently only permitted with respect to companies classified as micro, small and medium enterprises.

Insolvency resolution process

Commencement of process

The CIRP of a corporate person under Part II of the Code can be commenced when a corporate debtor has committed a default in relation to the payment of a debt of at least Indian rupees 10 million owed to a financial creditor or an operational creditor. Part II is applicable to companies (except for financial service providers) and limited liability partnerships.

To commence a CIRP, an application must be filed before the NCLT in the form prescribed, informing the NCLT of the details of the default and suggesting an insolvency resolution professional.

The Code prescribes a 14-day timeline for the NCLT to admit or reject the application (although this has been interpreted to be recommended and not mandatory). The CIRP commences from the date of admission of the application by the NCLT ("**Insolvency Commencement Date**").

Under the Code, a public announcement must be made by the insolvency resolution professional at the time of the commencement of the CIRP in relation to the company. The public announcement, among other things, is required to notify the last date for the submission of claims by all the creditors of the company.

The CIRP is to be completed within 180 days from the Insolvency Commencement Date. The above time period may be extended by the NCLT for a period of 90 days if an application to do so is made by an insolvency professional (acting pursuant to a resolution of a committee of creditors passed by a vote of 66% of the voting shares). Further, the Code prescribes that in any event, the CIRP must be completed within a period of 330 days from the Insolvency Commencement Date, including any extension of the period of the corporate insolvency resolution process granted and the time taken in legal proceedings in relation to such resolution process. However, this time period has been extended by the courts and tribunals on a case-by-case basis.

Moratorium

The Code prescribes that from the Insolvency Commencement Date until the completion of the CIRP or the passing of a liquidation order (whichever is earlier), a moratorium will be imposed in relation to the company as follows:

- No suits or proceedings are permitted to be instituted against the company.
- No security is permitted to be enforced.
- The company is not permitted to transfer or encumber any of its assets.

Interim resolution professional

An interim resolution professional must be appointed by the NCLT on the Insolvency Commencement Date. That resolution professional must be registered with an insolvency professional agency under the Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016 and be an independent party in relation to the company. From the date of appointment of the interim resolution professional, the management of the company's affairs will vest with the interim resolution professional.

The insolvency resolution professional is vested with the power to collate claims against the corporate debtor and, on the basis of claims received, constitute a committee of creditors. The form and manner, including the relevant documents that are required to be submitted by a financial creditor, operational creditor or a worker/employee in relation to their respective claims, must be in accordance with the applicable regulations. Please note that, in relation to any debt in foreign currency, such debt will be valued in Indian rupees at the reference rate published on the RBI's website on the Insolvency Commencement Date.

Creditors' committee

The insolvency resolution professional identifies the financial creditors and constitutes a creditors' committee. Operational creditors above a certain threshold are permitted to attend committee meetings but have no voting power. Depending on the item to be decided on, the creditors' committee can approve matters by a 51%, 66% or a 90% majority vote (depending on the type of matter). Decisions of the creditors' committee are binding on the corporate debtor and all its creditors.

The creditors' committee considers proposals for the revival of the debtor and must decide whether to proceed with a revival plan or liquidation within 180 days (subject to extensions as mentioned above). Any interested party may submit a revival proposal but it must provide for the payment of operational debts to the extent of the higher of the amounts that the operational creditors would have received had the company been liquidated and the amounts that the operational creditors would have received had the proceeds of the resolution plan been distributed as per the prescribed liquidation waterfall. Further, a plan must also provide for financial creditors who did not vote in favor of the plan to be paid a minimum of the amounts that they would have received had the company been liquidated.

If the resolution plan meets the requirements of the Code, the resolution professional will submit it to the creditors' committee for its consideration. Once a resolution plan is approved by the creditors' committee (by a 66% majority), the resolution plan will be submitted to the NCLT for its approval. A resolution plan approved by the NCLT is binding on all stakeholders, including employees, creditors, joint venture partners, members, partners of the corporate debtor and governmental authorities.

Liquidation

Under the Code, liquidation may be initiated against the corporate debtor in the following scenarios:

- A 66% majority of the creditors' committee resolves to liquidate the corporate debtor at any time during the CIRP.
- The creditors' committee does not approve a resolution plan within 180 days (or within the extended time periods as mentioned above).
- The NCLT rejects the resolution plan submitted to it on technical grounds.
- The corporate debtor contravenes the NCLT-approved resolution plan and an affected person makes an application to the NCLT to liquidate the corporate debtor.

In the case of liquidation, the priority waterfall for distribution of liquidation proceeds, prescribed under the Code, is as follows:

- The costs of the insolvency resolution (including any interim finance) and liquidation.
- Secured creditors (that are not enforcing their security outside the liquidation) together with worker dues for the preceding 24 months, on an equal basis.
- Wages and any unpaid dues owed to employees other than workers for the 12-month period preceding the liquidation commencement date.
- Financial debts owed to unsecured creditors.
- Amounts payable to the central and state governments for the preceding 24 months, and unrealized dues of secured creditors outside the liquidation on an equal basis.
- Any remaining debts and dues.
- Preference shareholders, if any.
- Equity shareholders or partners, as the case may be.

On liquidation, a secured creditor may choose to realize its security and receive proceeds from the sale of the secured assets as first priority. If the secured creditor enforces its claims outside the liquidation, it must contribute any excess proceeds to the liquidation trust. Further, in the case of any shortfall in recovery, the secured creditors will be junior to the unsecured creditors to the extent of the shortfall.

2. Is it possible to obtain a moratorium before insolvency?

Code

See the "Moratorium" paragraph in the answer to question 1 of this section in relation to the moratorium under the Code.

Prudential Framework for Resolution of Stressed Assets

The RBI issued the Reserve Bank of India (Prudential Framework for Resolution of Stressed Assets) Directions, 2019 ("**RBI Prudential Framework**") dated 7 June 2019. The RBI Prudential Framework applies to banks and financial institutions, as well as large nonbanking financing companies, and also requires asset reconstruction companies to adhere to the relevant resolution framework. The RBI Prudential Framework does not apply to foreign ECB lenders as they would not fall under the above category. However, such ECB lenders may voluntarily agree to participate in the resolution process and be bound by it (if the lenders that are bound by such a framework are agreeable).

Under the RBI Prudential Framework, upon the occurrence of a default (i.e., a day-one nonpayment) the lenders have to decide a resolution strategy within a review period of 30 days. A timeline of 180 days after the end of the review period is provided under the RBI Prudential Framework for preparing and implementing the resolution plan. Additional provisioning norms apply after 180 days.

To implement the resolution strategy, during the review period the lenders are required to sign an intercreditor agreement (ICA) to provide for basic rules for the finalization and implementation of the resolution plan. A resolution plan has to be agreed to by 75% of the creditors by value and 60% by number for it to be binding on all the creditors, and an ICA has to be entered into by the creditors for them to be bound. The resolution plan may, among other things, provide for a one-time settlement of the debt, a restructuring of the debt, a moratorium on principal and interest payments and/or conversion of some of the debt into equity/other instruments. It may also provide for a change of ownership. Further, resolution plans should provide for payment no less than the liquidation value (i.e., the estimated realizable value of the relevant borrower's assets, if such borrower were to be liquidated on the date of commencement of the review period) due to the dissenting lenders.

A resolution plan under the RBI Prudential Framework is not binding on creditors that do not sign the ICA. It is not mandatory for foreign ECB lenders to sign the ICA. However, if foreign ECB lenders sign the ICA, their dues will be paid or restructured per the resolution plan.

Please note that the ICA provides for a standstill period of 180 days within which no security can be enforced against the company, nor can an insolvency resolution process be commenced by the lenders that are signatories to the ICA.

State-specific legislation

Special state-specific legislation such as the Maharashtra Relief Undertakings (Special Provisions) Act, 1958 (applicable to Maharashtra), the Rajasthan Relief Undertakings (Special Provisions) Act, 1961 and the Karnataka Relief Undertakings (Special Provisions) Act, 1977 can also provide a veil of protection to debtor companies from claims by creditors on express notification by the debtor company as a relief undertaking by the respective state government.

3. When a company is the subject of a formal insolvency procedure, can the company's pre-insolvency transactions be set aside?

Preferences

If the liquidator or the insolvency resolution professional is of the view that the corporate debtor has given a preference to any person, they may apply to the NCLT to seek a declaration that any preferences that occurred at the relevant time are void and that their effect be reversed.

Under the Code, a corporate debtor is deemed to have given a preference if the following conditions are met:

- There is a transfer of property or an interest in the property of the corporate debtor for the benefit of a creditor or a surety or a guarantor for or on account of an antecedent financial debt or operational debt or other liabilities owed by the corporate debtor.
- That transfer has the effect of putting the creditor or a surety or a guarantor in a better position than it would have been in had the distribution of assets been made in accordance with the Code.

However, a preference does not include the following transfers:

- A transfer made in the ordinary course of the business or financial affairs of the corporate debtor or the transferee.
- Any transfer creating a security interest in property acquired by the corporate debtor to the extent that the following conditions are met:
    - The security interest secures new value and was given at the time of, or after, the signing of a security agreement that contains a description of that property as a security interest and was used by the corporate debtor to acquire that property.
    - The transfer was registered with an information utility (i.e., a depository of financial information registered with the Insolvency and Bankruptcy Board of India pursuant to the Code) on or before 30 days after the corporate debtor receives possession of that property.

"Relevant time" means:

- The period of two years preceding the Insolvency Commencement Date in relation to a related party (other than by reason only of being an employee).
- The period of one year preceding the Insolvency Commencement Date in relation to any other person.

Undervalued transactions

Additionally, the Code provides that the liquidator or the appointed insolvency resolution professional may make an application to the NCLT to seek a declaration that any undervalued transactions are void and that their effect be reversed. An undervalued transaction is a transaction that is not in the debtor's ordinary course of business and one where the corporate debtor does either of the following:

- Makes a gift to a person; or
- Enters into a transaction with a person that involves the transfer of assets by the debtor for consideration that is significantly less than the consideration provided by the corporate debtor at the time of acquisition of those assets.

An undervalued transaction may be declared to be void and be reversed if made with a related party within a period of two years preceding the Insolvency Commencement Date or with any other person within a period of 1 year preceding the Insolvency Commencement Date.

Separately, the Code provides that the NCLT must make an order restoring the position as it existed before the transaction and protecting the interests of persons who are victims of the transactions if the corporate debtor has deliberately entered into an undervalued transaction to do either of the following:

- Keep the debtor's assets beyond the reach of any person who is entitled to make a claim against the debtor.; or
- Adversely affect the interests of such a person in relation to the claim.

However, any order of this type will:

- Not affect any interest in property that was acquired from a person other than the corporate debtor and was acquired in good faith, for value and without notice of the relevant circumstances, or affect any interest deriving from such an interest; and
- Not require a person who received a benefit from the transaction in good faith, for value and without notice of the relevant circumstances, to pay any sum unless they were a party to the transaction.

Extortionate credit transactions

Further, the Code also provides the liquidator or the insolvency resolution professional with the power to make an application for the avoidance of any extortionate credit transaction entered into by a corporate debtor within a period of two years preceding the Insolvency Commencement Date. Under the regulations under the Code, a transaction is considered an extortionate credit transaction where one of the following conditions is met:

- The terms require the corporate debtor to make exorbitant payments in respect of the credit provided; or
- The terms are unconscionable under the principles of law relating to contracts.

4. When can a lender enforce its security? Can security be enforced out of court following an event of default (or other contractual trigger event), or is a court order required? Are there any restrictions that apply before a lender may enforce its security?

The terms and conditions of the security documents govern enforcement of security. Generally, a lender may enforce its security on the occurrence of an event of default. The process to be followed for enforcing the security is briefly set out below. (See the answer to question 11 of the "If taking security" section for the different types of security interest referred to below).

Except in the case of an equitable mortgage, a court order is generally not required for the enforcement of security. However, if the security provider objects to, or disputes, the enforcement and makes an application to the court, the dispute must be resolved through a court process.

Immovable property

If the mortgage is an English mortgage, the mortgagee has the power to sell the mortgaged property without the court's intervention, subject to certain notification requirements. Where the mortgage is an equitable mortgage, the mortgagor must apply to the court for a decree to sell the mortgaged property to recover the debt.

Movable property

The rights and remedies of a hypothecatee (that is a foreign lender or a security trustee for a foreign lender) are entirely regulated by the terms of the deed of hypothecation between the hypothecator and hypothecatee. A deed of hypothecation can be enforced by either compelling the delivery of the movable property or by selling or obtaining a decree for sale of the movable property if that is stipulated in the deed of hypothecation. If the deed does not specify the manner in which the hypothecated property may be dealt with, the remedy open to the creditor would be to obtain a money decree declaring its lien on the property and the right to sell that property.

Pledge over shares

A pledgee may enforce a pledge and sell the pledged shares by giving reasonable notice of enforcement to the pledgor. The pledgee does not need to obtain a court order to sell the pledged shares. If the pledged shares are held in physical form, the pledgee must submit to the company whose shares are being pledged the executed share transfer forms held by the pledgee. The company will then need to approve the transfer of shares in the name of the lender or third-party transferee at its board meeting. If the company refuses to approve the transfer of shares, the lender or third-party transferee will need to approach the competent courts and tribunals to challenge the refusal.

5. Do any limitation periods apply in relation to bringing an action to enforce security?

Any proceeding in court for the enforcement of security must be brought within the relevant limitation period. For example, a suit ordering the sale of the mortgaged property must be brought within 12 years from the date on which the money sued for becomes due, and a suit ordering a sale of charged or pledged property must be brought within three years from the date that the cause of action arises.

6. Is there any particular way in which secured assets must be liquidated on enforcement (e.g., by auction or court sale)?

No. The process is governed entirely by the terms of the security documents. However, please note the following stipulations under the ECB Guidelines (see under "Background") in relation to enforcement of security over relevant assets:

- In the case of the invocation of a pledge, any transfer of financial securities must be in accordance with the extant foreign direct investment policy, including provisions relating to sectoral cap and pricing, as applicable in accordance with the Foreign Exchange Management Act, 1999 and rules and regulations framed under it.
- In the event of the enforcement of a mortgage, immovable assets must only be sold to a person resident in India and the sale proceeds must be repatriated to liquidate the outstanding ECB.
- Charged movable assets may be taken out of India by a lender to the extent of the lender's claim, subject to obtaining permission from domestic lender(s), if any.

7. Are there any particular legal or practical difficulties or delays in enforcing security?

If the security provider contests enforcement action in relation to the security (which generally is the case), the enforcement process is time-consuming. It could take several years to obtain a judgment in India. The timeline depends on the facts and the relief sought, as well as the backlog of cases at the time of enforcement. However, it may be possible to obtain interim relief in a shorter time frame.

8. In relation to enforcement, are there any specific requirements to be borne in mind if the lender is a foreign entity?

Yes. The RBI's prior approval may be required to repatriate to an offshore lender from India any amounts recovered on enforcement of a judgment of a court that is not an Indian court.

9. Is there any reason why you think that arbitration rather than litigation might be advantageous in resolving disputes under the finance documents, and if so, why? Please outline the relative merits of arbitration and litigation, including the ease of enforcement of foreign judgments and foreign awards from different jurisdictions. Is it possible to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit?

It is not very common for a loan agreement between an Indian borrower and a foreign lender to select arbitration as the dispute resolution mechanism as it may be quicker to obtain a judgment in a foreign court rather than to appoint (after the dispute) an arbitral tribunal and have the dispute heard by arbitration.

Any judgment that is a money decree obtained from a superior court of any reciprocating territory notified under the Code of Civil Procedure, 1908 of India will be recognized and enforced by the courts in India, subject to certain statutory provisions, without re-examining the issues. The UK and Singapore have been declared reciprocating territories, and certain courts in those jurisdictions have been declared superior courts for the purposes of the Code of Civil Procedure.

India is a signatory to the New York Convention for the Enforcement of Foreign Arbitral Awards, 1958. Awards handed down by an arbitral tribunal whose seat is in a country that is a signatory to the New York Convention will be enforced in India as a "foreign award" under Part II of the Arbitration and Conciliation Act, 1996, without the need for any retrial and the award will be deemed to be a decree of an Indian court. However, there are certain grounds for objection to the enforcement of a foreign award governed by the New York Convention. These include the following:

- The parties to the arbitration agreement were, under the law applicable to them, under some incapacity, or the agreement is not valid under the law to which the parties have subjected it or under the law of the country where the award was made.
- The party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitral proceedings or was otherwise unable to present its case.
- The award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration.
- The composition of the arbitral authority or the arbitral procedure was not in accordance with the parties' agreement, or, failing such agreement, was not in accordance with the law of the country where the arbitration took place.
- The award has not yet become binding on the parties or has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made.
- The subject matter of the dispute is not arbitrable under the law of India.
- The enforcement of the award would be contrary to Indian public policy.

However, even if the arbitration takes place at a venue outside India, the parties are entitled to obtain interim relief in Indian courts against the Indian entity while the arbitration proceedings are still pending.

Under Indian law, there must be a clear intention and obligation under the contract to arbitrate. If an option is given to one party to arbitrate or litigate, Indian courts have, to date, largely held that there is no clear obligation to arbitrate on both the parties. While there are arguments to suggest that a hybrid enforcement provision does not mean that there is a lack of intention and obligation, the possibility of an Indian court ruling that such an arbitration or litigation provision is invalid and, therefore, the award or judgment is not enforceable cannot be ruled out.

10. **Are asymmetrical jurisdiction clauses enforceable? (By this we mean clauses that allow the lenders, but not the borrowers, to make certain choices in relation to choice of jurisdiction and how to litigate. These types of clauses allow the lenders, but not the borrowers, to commence proceedings in any court they choose, but restrict the borrowers to commencing proceedings in one jurisdiction only. This may also allow the lenders, but not the borrowers, to choose whether to litigate the finance documents before a court or to submit to arbitration in relation to them, but restrict the borrowers to either litigation or arbitration, as specified in the agreement).**

Yes, asymmetrical jurisdiction clauses are generally recognized by Indian courts.

Working digitally

1. **Is it possible for documents to be executed electronically (whether by the manual insertion of a digital signature or the use of an e-signing platform) under the laws of this jurisdiction? If so, is this limited to only particular types of finance documents?**

The validity of an electronically signed contract is recognized in India as long as such a contract satisfies the essential elements of a valid contract, including offer and acceptance, presence of a lawful consideration and lawful object, free consent of the parties, competency of the parties to contract, intention of the parties to create a legal relationship, the certainty and possibility of performance as intended, etc. The conclusion of electronically signed contracts on the satisfaction of these essential elements of a contract has also been recognized by Indian courts.

The Information Technology Act, 2000 ("**IT Act**") recognizes electronically signed contracts and provides that where a contract is expressed in electronic form or by means of an electronic record, such contract will not be deemed to be unenforceable solely on the ground that such electronic form or means was used for the purpose. The IT Act also provides for the type of signatures that can be used for the authentication of electronic records, namely (i) digital signatures and (ii) electronic signatures. Digital signatures issued by licensed certifying authorities (CA) are reliable and are legally valid in a court of law as per the IT Act, as they employ private and public keys that are unique to the subscriber and constitute a functioning key pair for authentication of a document.

While legal recognition has been provided to electronically signed contracts, as per the IT Act, the following documents cannot be signed electronically:

- A negotiable instrument (other than a check, demand promissory note or a bill of exchange issued in favor of or endorsed by an entity regulated by the RBI and other prescribed authorities) as defined in Section 13 of the Negotiable Instruments Act, 1881.
- A power of attorney as defined in Section 1A of the Powers of Attorney Act, 1882 (except when such power of attorney empowers an entity regulated by the RBI, SEBI or other prescribed authorities to act on behalf of them).
- A trust as defined in Section 3 of the Indian Trusts Act, 1882.
- A will as defined in Clause (h) of Section 2 of the Indian Succession Act, 1952, including any other testamentary disposition called by whatever name.

2. Where the witnessing of a signing is contemplated, is it possible for the witness to verify the signature over a live video call?

Documents that are mandatorily required to be witnessed cannot be witnessed over live video calls.

3. Is it possible to register/perfect security electronically without wet ink signatures?

Security over movable assets may be registered and perfected without wet ink signatures. However, security over immovable assets where registration with a land registry is mandatory would need to be executed by wet ink for the purposes of the registration process.

4. Are there any other legal restrictions that may prevent the parties from executing a finance transaction electronically?

Please refer to our response to question 1 of this section.

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INDONESIA

Indonesia

When considering whether to lend

1. **Is it necessary or advisable for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in this jurisdiction: (a) by reason only of its execution, delivery or performance of the finance documents; or (b) to enable it to enforce its rights under the finance documents?**

   No. It is not necessary for an offshore lender, arranger, facility agent or security agent to be licensed, qualified or entitled to do business in the Republic of Indonesia because of its execution, delivery or performance of the Asia Pacific Loan Market Association facility agreement (or other facility agreement), fee letters, Indonesian law security documents, intercreditor agreement, account management agreement and subordination agreement ("**Finance Documents**") or to exercise or enforce any of its rights under the Finance Documents in the Republic of Indonesia.

2. **Will any lender, arranger, facility agent or security agent be deemed to be resident, domiciled, carrying on business or subject to tax by reason only of the execution, delivery, performance or enforcement of the finance documents?**

   No. An offshore lender, arranger, facility agent or security agent is not deemed to be resident, domiciled or carrying on business in Indonesia by reason only of the negotiation, preparation, execution, delivery, performance or enforcement of or receipt of any payment under the Finance Documents if the offshore lender, arranger, facility agent or security agent is not deemed to have a presence in Indonesia (e.g., no presence of their employees for more than the time test under the Indonesian Income Tax Law, which is 60 days within a 12-month period).

3. **Are there any regulatory reporting requirements that lenders must observe in connection with those transactions?**

   No. Lenders are not required to do any reporting. However, Indonesian borrowers receiving offshore loans from foreign lenders are subject to periodic reporting of offshore loans to Bank Indonesia (Indonesia's central bank) and the Ministry of Finance of the Republic of Indonesia.

4. **Is it necessary to establish a place of business in your jurisdiction in order to enforce any provision of the finance documents?**

   Generally, it is not necessary for offshore entities to establish a place of business in the jurisdiction of the Republic of Indonesia to enforce any provision of the Finance Documents.

5. **Is a foreign bank/financial institution permitted to approach local entities for business?**

   Assuming that the business is involved in lending activities, a foreign bank/financial institution is generally permitted to approach local entities for business. If the business is related to offering hedging or structured products, there are certain restrictions or prohibitions (e.g., requiring approval from Bank Indonesia) on offering the products to local entities.

When lending to borrowers

1. Are there any restrictions in relation to the type of borrower who may borrow foreign currency or in relation to the term of foreign currency and/or the amount of foreign currency borrowed by local entities?

To the best of our knowledge, Indonesian borrowers are not restricted from borrowing in foreign currency. However, there are restrictions on the use of foreign currency in Indonesia (international financing transactions are exempted) and on the type of borrower that may borrow from foreign lenders.

Approval from the Minister of Finance

The ministries, regional governments and regional-government-owned entities are prohibited from receiving offshore loans.

Generally, Indonesian state-owned entities may only receive offshore loans if the offshore loan does not require a guarantee or collateral from the government of Indonesia, including Bank Indonesia or other state-owned banks, for the repayment, and if it will not give rise to any obligation from the government of Indonesia because of the acceptance of the offshore loan. However, there could be exceptions as may be determined by the government of Indonesia.

Indonesian state-owned entities and regional-government-owned entities are prohibited from providing security or acting as guarantors for the repayment of offshore loans received by state-owned entities, regional-government-owned entities or private companies.

The Minister of Finance must approve the offshore loan granted to a state-owned entity after hearing opinions from the Minister of the National Planning Agency, the Governor of Bank Indonesia and the Director General of Budget Financing and Risk Management.

Specific approval for certain industries

Specific approval is required for certain industries. In the banking industry, for example, a bank intending to obtain a long-term offshore loan (i.e., a loan having a tenor of more than one year) is required to obtain approval from Bank Indonesia. The application for approval must be submitted at least one month prior to receiving the offshore loan. Mining companies must also obtain approvals from the Minister of Energy and Mineral Resources before obtaining loans.

Local entities

There are no restrictions in relation to the term or the period and/or amount of foreign currency loans borrowed by local entities in Indonesia.

2. Are there any restrictions on the rate of interest or default interest that may be charged?

There are no restrictions on the rate of interest or default interest that may be charged. However, in two cases over approximately the past 20 years, the court decided to modify the agreed interest rate. The court did not provide any specific reasoning but in both cases, the court mentioned that the interest rate needed to be modified to be in accordance with the average interest rate applicable to state-owned banks and, in the earlier case, the court made several references to "justice".

As Indonesia is a civil law jurisdiction, court decisions do not create precedent in Indonesia. Court decisions are only final and binding on the parties to the case.

For Indonesian tax purposes, if the lender and borrower are related parties, the interest rate used must be the market rate.

3. Are there any restrictions on particular lenders or classes of lender entering into credit transactions with borrowers?

No, there are no such restrictions.

4. Are there any exchange controls that will apply to payments to be made in foreign currencies or to foreign lenders?

The purchase and sale of foreign currency between banks and their customers is subject to the following requirements:

- The exchange of rupiah into foreign currency without an underlying transaction is limited to USD 100,000 or its equivalent for a cash transaction per month per customer in the foreign exchange market.
- A customer's purchase of foreign currency without an underlying transaction is limited to USD 100,000 or its equivalent for a derivative exchange rate forward transaction per month in the foreign exchange market.
- A customer's sale of foreign currency without an underlying transaction is limited to USD 5 million or its equivalent for a derivative exchange rate forward transaction per transaction in the foreign exchange market.
- A customer's purchase of foreign currency without an underlying transaction is limited to USD 100,000 or its equivalent for a non-forward derivative exchange rate transaction per month in the foreign exchange market.
- A customer's sale of foreign currency without an underlying transaction is limited to USD 1 million or its equivalent for a non-forward derivative exchange rate transaction per transaction in the foreign exchange market.

Any purchase or sale of foreign currency above these limits must be supported by an underlying transaction. The maximum amount of foreign currency that can be purchased is equal to the value of the underlying transaction.

Rupiah transactions

Bank Indonesia has issued regulations on transactions in the foreign exchange market, as well as a policy on the use of rupiah in international activities ("**BI Forex Regulations**"). The BI Forex Regulations stipulate certain restrictions in respect of transfer overseas of rupiah, which include that onshore banks are prohibited from transferring rupiah overseas. However, Bank Indonesia provides an exemption to carry rupiah, and use rupiah offshore for the purpose of international activities that will be further stipulated in an implementing regulation to be issued by Bank Indonesia.

Onshore banks may transfer rupiah to an onshore account of a non-resident or to an onshore account jointly owned by a resident and a non-resident, provided the following conditions are met:

- The nominal value does not exceed the equivalent of USD 1 million per transaction, or such transfer is made between rupiah accounts owned by the same non-resident.
- If the value exceeds USD 1 million per transaction, the recipient bank of such transfer must ensure that the non-resident has an Underlying Transaction.

An "Underlying Transaction" is defined as an activity underlying the purchase or sale of foreign currency against rupiah, which includes the following:

- Activities in the current account, such as export, import and income transfer (primary and secondary).
- Activities in the financial account, such as foreign direct investment and portfolio investment.
- Activities in the capital account, such as capital transfer.
- Loans or financing from onshore banks to a resident for the purpose of investment and trade.
- Trading of domestic goods and services.
- Other underlying transactions stipulated by Bank Indonesia.

5. Is there any requirement to deduct or withhold tax from any amounts to be paid or repaid to a lender (whether domestic or foreign)? If so, at what rate must tax be deducted and from what kinds of payment?

The borrower is required by the laws of the Republic of Indonesia to withhold tax at a rate of 15% if the lender is an Indonesian tax resident and is not a bank in Indonesia; or 20% or the reduced withholding tax rate under the relevant tax treaty if the lender is a non-Indonesian tax resident from any payment of interest and any other payment of a similar nature in relation to loan documents.

6. Are there any "thin capitalization" or other rules that may limit the extent to which interest payments may be deducted for tax purposes?

The Minister of Finance issued Regulation Number 169/PMK.010/2015 on the Determination of the Debt-to-Equity Ratio (DER) for Companies to Calculate Income Tax ("**Regulation 169**"). Regulation 169 stipulates that the maximum permissible DER for income tax purposes is 4 to 1.

Regulation 169 is only applicable to corporate taxpayers whose capital consists of shares. Generally, however, there are six types of corporate taxpayers whose capital consists of shares that are not subject to this regulation, i.e., corporate taxpayers engaging in the following:

- The banking sector
- The financial institutions sector
- The insurance and reinsurance sector
- The oil and gas sector, which is based on production-sharing contracts, contracts of work or other mining cooperative agreements that do not set out a DER requirement
- Business activities where the income is subject to final income tax
- The infrastructure sector

If corporate taxpayers that are not exempted from Regulation 169 cannot meet the requirements under Regulation 169, their deductible borrowing costs will be limited to an amount that is in line with the 4 to 1 DER.

Regulation 169 also requires taxpayers that have foreign loans from private parties to report the amount of the loan to the Director General of Tax. If the taxpayers do not report the loan, the borrowing costs related to the loan cannot be deducted for tax purposes. The procedure to report the loan will be regulated further in a regulation that will be issued by the Director General of Tax.

7. Are there any registration, notarization, translation or reporting requirements in relation to the loan documents?

Registration and notarization

There are no registration or notarization requirements in respect of the loan documents, except as follows:

- Fiducia security must be made in notarial deed form and in the Indonesian language, and it must be registered with the relevant fiducia registration office through the fiducia registration online system (which can only be accessed by a notary).
- A hak tanggungan (a security right over a land right) must be made in a Pejabat Pembuat Akta Tanah (PPAT) (land deed official) deed form and in the Indonesian language, and it must be registered with the relevant land office. The registration of a hak tanggungan can be done through an online system.
- A hypothec over a vessel must be made in a grosse deed form and in the Indonesian language, and it must be registered with the relevant ship registration and recording official (Pejabat Pendaftar dan Pencatat Balik Nama Kapal).

- A security over warehouse receipts must be made in an agreement and should be registered with the Warehouse Registration and Management Center (Pusat Registrasi dan Pengelola Gudang). The registration is submitted to the Monitoring Body (Badan Pengawas) in a form that is determined by the Monitoring Body.

Further information about fiducia security, hak tanggungan, hypothec and security over warehouse receipts is set out in the answer to question 10 of the "If taking security" section.

Translation

On 9 July 2009, the government of Indonesia enacted Law No. 24 of 2009 on National Flag, Language, Emblem and National Anthem dated 9 July 2009 ("**Law 24**"). Law 24 requires implementing regulations to be issued within two years after 9 July 2009. On 1 March 2010, the president of Indonesia issued Presidential Regulation No. 16 of 2010 on the Use of Indonesian Language in Official Presidential and/or Vice Presidential as well as other State Officer Speeches ("**PR 16**"). On 30 September 2019, the president of Indonesia issued Presidential Regulation No. 63 of 2019 on the Use of Indonesian Language ("**PR 63**"), which was only made public on 9 October 2019. PR 63 basically revokes PR 16 and further stipulates the use of Indonesian language.

Article 31.1 of Law 24 and Article 26.1 of PR 63 require the use of Indonesian language in memoranda of understanding and agreements involving state institutions (lembaga negara), Indonesian government authorities (instansi pemerintah Republik Indonesia), Indonesian private institutions (lembaga swasta Indonesia) or Indonesian individuals (perseorangan warga negara Indonesia). The elucidation of Article 31 of Law 24 states that an agreement in this context includes international agreements made within the framework of public international law.

The applicability of Law 24 and PR 63 would affect the execution of the loan documents by Indonesian individuals or Indonesian private institutions with offshore parties. Article 31.1 of Law 24 and its elucidation and Article 26.1 of PR 63 are not particularly clear on whether: (a) the term "Indonesian private institutions" includes Indonesian companies or Indonesian branches of foreign companies; and (b) the term "agreements" includes private commercial agreements.

Article 31.2 of Law 24 and Article 26.2 of PR 63 further state that if the memoranda of understanding or agreements involve foreign parties, the national language of those foreign parties and/or the English language can also be used. Please note that the elucidation of Article 31.2 states that if an agreement is executed in multiple languages, (i.e., Indonesian language, the national language of the foreign party and/or English), each version will be equally authentic. Law 24 and PR 63 seem to also imply that the use of other language(s) in an agreement can only be done in agreements involving foreign parties, although Law 24 and PR 63 do not explain the form of the involvement being referred to.

Article 26.3 of PR 63 stipulates that the national language of those foreign parties and/or the English language are or is used as an equivalent or translation of the Indonesian language version to reconcile the understanding of the agreement with the foreign parties. This seems to imply that the Indonesian language version would need to exist first before the national language of those foreign parties and/or the English language versions exist because the non-Indonesian language version is a mere "equivalent" or "translation," and therefore the logical consequence would be that at the very least both versions or a bilingual form will need to be signed at the same time.

Article 26.4 of PR 63 further stipulates that if there is the national language of the foreign parties and/or the English language version, parties to an agreement may contractually choose the governing language of the agreement, which shall prevail upon any inconsistencies between the language versions. Law 24 and PR 63 do not provide for any sanction for failure to comply with the above requirements.

Reporting obligations

A company (as defined in the Bank Indonesia foreign exchange activities reporting regulations) intending to obtain offshore loans is required to submit reports to Bank Indonesia in relation to its offshore loan plan by 15 March of the relevant year.

In addition, a company (including state-owned entities) that has offshore loans in place must submit monthly reports to Bank Indonesia and the Ministry of Finance of the Republic of Indonesia on or before the 15th of the

following month. The reports must provide details of the facility agreement and its implementation including the receipt of any disbursements, making interest payments and repaying principal. Subsequent periodic reports must be made in accordance with the prevailing laws and regulations.

Further, any company that has an offshore loan in place must implement prudential principles and submit its implementation reports and financial information to Bank Indonesia.

In addition to the above requirements, certain types of offshore loans must be withdrawn from a bank that is licensed by Bank Indonesia to trade foreign currency ("**Bank Devisa**"). These offshore loans are those arising from one of the following:

- Non-revolving loan agreements.
- Debt securities in the form of bonds, medium-term notes, floating rate notes, promissory notes and commercial paper.
- Any discrepancy between the amount of a new offshore loan being used to refinance an existing offshore loan and the amount of the existing offshore loan that is being refinanced.

The monthly report to Bank Indonesia for this type of loan must be accompanied by a supporting document evidencing that the company has withdrawn the offshore loan from a Bank Devisa.

8. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to the loan documents? If yes, what are the amounts and when are they payable?

Other than the registration fees for the registration of the security as set out in the answer to question 7, no registration tax, documentary tax or other similar taxes are payable under the laws of the Republic of Indonesia in relation to loan and security documents. However, as of 1 January 2021, stamp duty at the rate prescribed under Law of the Republic of Indonesia No. 10 of 2020 on Stamp Duty, i.e., IDR 10,000 is payable on each of the loan and security documents. The stamp duty becomes payable when a document is executed when a document is made, when a document is handed over to the party for whom the document is made, when a document is presented before an Indonesian court, or when a document will be used in Indonesia (if it has been executed outside of the Republic of Indonesia).

In addition to the IDR 10,000 stamp duty, a non-tax state revenue (Penerimaan Negara Bukan Pajak (PNBP)) is payable in relation to certain security documents. The amount of the relevant PNBP is set out in the answer to question 11 of the "If taking security" section.

9. Does the law recognize the subordination of the debt that a debtor owes to one creditor to that which the debtor owes to another creditor? If yes, how is this usually effected?

Indonesian law recognizes the concept of debt subordination. The subordination is effected in a subordination agreement between the debtor, subordinated/junior creditor and the senior creditor. Under the subordination agreement, claims of the subordinated/junior creditor are subordinated to the claims of the senior lender until the debt owed by the debtor to the senior creditor is paid in full.

10. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors (e.g., the claims of employees and tax authorities or the claims of creditors under particular kinds of instrument)? If yes, what classes of creditors are preferred?

Claims are paid in the following descending order of priority:

- Court costs of foreclosure in relation to movable and immovable goods, paid from the proceeds of the foreclosure
- Tax liens
- Secured creditors (e.g., pledgees, hak tanggungan holders and fiducia security grantees)

- Unsecured creditors holding limited privileged claims in relation to specific assets under Article 1139 of the Indonesian Civil Code (ICC)
- Unsecured creditors holding general privileged claims in relation to all assets generally under Article 1149 of the ICC
- All remaining claims, i.e., unsecured or concurrent claims

Limited privileged claims

The limited privileged claims under Article 1139 of the ICC are as follows:

- Court costs and fees (incurred by the court to conduct an auction over the movable or immovable goods of a debtor)
- Claims relating to the leasing of immovable property, including repair costs which are borne by the lessee and all claims relating to any leasing agreement
- Any unpaid purchase price in relation to movable property
- Any costs incurred to preserve goods
- Repairman's costs
- Any unpaid claims of a hotel owner against its guests
- Transportation costs and other additional costs
- Reimbursement of payments made by public officers

General privileged claims

The general privileged claims under Article 1149 of ICC are as follows:

- Court costs (for auction and settlement of inheritance)
- Funeral costs
- Costs for medical treatment
- Laborers' wage claims
- Claims in relation to the supply of food for the preceding six months
- Claims for boarding school fees for the previous year of study
- Claims from underage persons and persons under guardianship in relation to their guardians

11. Are there any consumer protection or similar laws that apply if credit is made available to individuals or other classes of debtor? If yes, what laws are applicable?

There is a consumer protection regulation in relation to the financial services sector administered by the Financial Service Authority (Otoritas Iasa Keuangan (OJK)). The regulation applies to financial services business providers and consumers. The protection provided under the regulation is in relation to the giving of information by the financial services business provider to its consumers. The obligations imposed on the financial services business provider include giving clear and accurate information about products and services and providing the information in either Indonesian language or with a translation of the non-Indonesian language into Indonesian language.

12. Are there any prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of: (a) its own shares or those of any affiliated company; or (b) assets owned by it or any affiliated company?

There is no prohibition under Law no 40 of 2007 on Limited Liability Company (Company Law) in relation to a company giving financial assistance for the purchase of its own shares or those of any affiliated company or assets owned by it or any affiliated company. However, there are some limitations in relation to the purchase by a company of its own shares.

Under the Company Law, the company may repurchase issued shares under the following circumstances:

- The repurchase of those shares does not cause the net assets of the company to become less than the subscribed capital plus the mandatory reserves that have been set aside.
- The total nominal value of the shares repurchased by the company and the pledge of shares or the fiducia security over shares held by the company and/or other companies whose shares are directly or indirectly owned by the company do not exceed 10% of the amount of subscribed capital in the company unless otherwise provided in capital market regulations.

The Company Law further stipulates that the shares repurchased by the company may only be held by the company for a maximum of three years.

The purchase of shares in a company (Company A) by a company (Company B) that is owned directly or indirectly by Company A is prohibited by the Company Law because the purchase will cause a cross-shareholding issue between Company A and Company B.

Furthermore, under the Company Law, there is no prohibition or limitation in relation to a company purchasing assets owned by an affiliated company.

Nevertheless, for transactions involving a listed company or its controlled company (defined in OJK Rule No. 42/POJK.04/2020 on Affiliated Party Transactions and Conflict of Interest Transactions ("**OJK Rule 42**")), capital market regulations in relation to affiliated party transactions and conflict of interest transactions might apply depending on the nature of the transaction, the relationship between the parties, and the value of the transaction. A transaction by a publicly listed company or its controlled company having a certain value that falls under the materiality threshold set out in the prevailing regulation (i.e., OJK Rule No. 17/POJK.04/2020 on Material Transactions and Change of Business Activity) will also be subject to certain procedures.

If taking security

1. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's secured creditors?

There are some claims that rank higher than those of the debtor's secured creditors. Please see the answer to question 10 of the "When Lending to Indonesian Borrowers" section.

2. May security given by a company rank in a specified order so as to secure liabilities owed to different creditors of the company in that order and, if that is not possible, is it viable for parties to enter into a contractual arrangement for the purposes of moderating this order?

Only a hak tanggungan (a security right over a land right) and hypothec over a vessel given by a company may rank in a specified order. If a plot of land is subject to more than one hak tanggungan, they are ranked according to their respective dates of registration. If more than one hak tanggungan is registered on the same date, they are ranked according to the number written on their respective deeds of hak tanggungan. A vessel can be encumbered by more than one hypothec, and they are ranked according to their respective dates and numbers written on their respective deeds of hypothec.

Other than a hak tanggungan and hypothec as described above, it is not possible to enter into a separate security agreement to specify the ranks of the security for other security rights as the law prohibits having double security on certain security rights. In addition, certain security rights such as a hak tanggungan, hypothec and fiducia security will come into existence and they will become perfected when they are registered in accordance with their respective regulations. Without this registration, the security holder will not have a priority right against other security holders. However, it is possible for the creditors to enter into a security sharing agreement where

the parties, among other things, contractually agree to the following: (i) to have different classes of creditors; and (ii) to have a priority mechanism over the proceeds' distribution upon the enforcement of such security.

3. Does this jurisdiction recognise the concept of floating security or similar equivalent (i.e., security over a changing pool of assets that the company giving the security is free to buy, sell and generally deal with)?

Indonesian law does not recognize the concept of floating charge per se. However, under Indonesian law, there is the concept of fiducia security. Fiducia security is the granting of security by which the ownership title of the secured object is transferred by way of fiduciary to the fiducia security holder, but the fiducia security grantor is allowed to use (or continue to use) the secured object. In relation to an item of inventory, the fiducia security grantor is allowed to sell the inventory as long as it is replaced with an object of equal value.

Fiducia security must be registered at a fiducia registration office. Fiducia security can be established in relation to fiducia objects that exist now or that will exist in the future. Therefore, a fiducia security agreement usually includes provisions that oblige the fiducia grantor to provide a periodic update of the fiducia objects and obliges the fiducia security holder to register the fiducia security on receipt of the update. Further details in relation to fiducia security are set out in the answer to question 11 of this section.

4. If so, are there any practical reasons why floating security is difficult to take, maintain or enforce?

Not applicable.

5. May security be granted to a trustee to be held on trust for the lenders from time to time, in such a way that a change of lenders does not require new security to be taken?

Except for the concept of: (i) trustee (wali amanat) as stipulated under Law No. 8 of 1995 on Capital Markets and Law No. 19 of 2008 on Sovereign Sukuk (Surat Berharga Syariah Negara); and (ii) special purpose vehicle (badan pengelola instrumen keuangan) and trust fund manager (pengelola dana perwalian) established to carry out securitization and trust fund activities as stipulated under Law No. 4 of 2023 on Development and Strengthening of the Financial Sector, Indonesian law does not recognize equitable principles in general, including, without limitation, the relationship of a trustee and beneficiary or other fiduciary relationships. Nevertheless, security may be granted to a trustee to be held in trust. However, enforcement of the provisions granting security in favor of third-party beneficiaries and otherwise relating to the nature of the relationship between a trustee (in its capacity as such) and the beneficiaries of a trust in the loan and security documents in the Republic of Indonesia will be subject to an Indonesian court accepting both of the following:

- Foreign law as the governing law of those documents
- Proof of the application of equitable principles under those documents

6. If not, are there any techniques that can be used to achieve substantially the same effect (e.g., parallel debt structures)?

In practice, the parties incorporate the following into the facility agreement:

- A provision stipulating that in relation to a jurisdiction in which the courts would not recognize or give effect to the trust, the relationship of the finance parties to the security trustee will be construed as one of principal and agent.
- A parallel debt provision.

Furthermore, for an onshore security holding in Indonesia under a facility agreement, the parties would typically appoint a security agent rather than a security trustee since the concept of trust is not recognized in Indonesia.

7. If an agent holds security for the lenders rather than a trustee, is it necessary to take new security on a change of lenders? If no, why not? If yes, are there ways to structure the transaction to avoid such a requirement?

Under Indonesian law, a change of lender by way of a transfer certificate or a novation agreement is considered a novation, the effect of which is that the existing security (as an accessory to the facility agreement) would cease to exist. However, Article 1421 of the ICC provides the option for the new lender and any remaining existing lenders to explicitly state that they retain the security created under the security documents to secure the secured liabilities.

Therefore, the parties usually include a provision in the facility agreement that provides that, on the transfer date, each security document and guarantee will be, and the borrower irrevocably confirms that each security document and guarantee continues to be, the legally valid, binding and enforceable obligations of each party to the facility agreement, and the security and guarantee created by each security document and guarantee respectively will continue to be valid and effective.

Please note that there are multiple interpretations of the effect of the application of Article 1421 of the ICC on the security documents. One of the interpretations is that upon the novation, the underlying agreement should be terminated and therefore the security created under the security document should be deemed to be terminated given the accessory nature of the security documents under Indonesian law.

8. Under the laws of this jurisdiction, is there any class of asset over which it is difficult or impossible to grant effective and perfected security, or in relation to which any security granted will be of limited effect?

Generally, there is no class of assets over which it is difficult or impossible to grant effective and perfected security. However, please note the limitations set out below.

Personal rights

It is not possible to grant security over a personal right that cannot be transferred to another person, such as a license.

Pledge

There is still uncertainty in relation to the enforceability of a pledge over a bank account in Indonesia due to the following:

- Fluctuating balance in a bank account.
- The fact that the pledgor still controls the bank account.
- Uncertainty about whether a bank account can be the object of a security right under Indonesian law.

The ICC specifies that a pledgee cannot own the pledged assets. The underlying principle is that a creditor may only obtain the proceeds of the pledged object to repay the debt. To the extent that any of the provisions in a pledge bank account agreement gives a security agent the right to appropriate or own money in the account, the provisions could be construed as inconsistent with the literal meaning of Article 1154 of the ICC. In our view, the underlying presumption of the ICC stipulation is that the pledged object has a market value and that value can only be determined by public auction. In the case of a bank account, the value of the pledged object is the same as the value of the money in the bank account.

There is no concept of second ranking in relation to a pledge. Therefore, it is not possible to create another pledge over an object that has been subject to a pledge.

Fiducia security

Any fiducia security (please see the answer to question 11 for the explanation on fiducia security) over receivables or insurance proceeds will not prevent the obligor(s) or the insurer(s) from the following:

- Discharging their obligations to the fiducia grantor.
- Exercising any set-off rights they may have.

This is until a receipt of acknowledgment is given from the obligor(s) of the granting of the fiducia security by the fiducia grantor to the fiducia grantee or, alternatively, by proper service by a court server of a notice on those obligor(s) in relation to the granting of the fiducia security.

Any fiducia security over receivables or insurance proceeds is enforceable only to the extent that the fiducia security relates to claims arising from an existing contractual relationship between the fiducia grantor and its obligor(s) at the time of execution of the fiducia security. It may not be enforceable to the extent that the fiducia security relates to future claims that do not have their basis in a contractual relationship between the fiducia grantor and its obligor(s) existing at the time of execution of the fiducia security, unless those future claims (which arise from a new contractual relationship) are specifically assigned by the fiducia grantor. The assignment can be effected by notifying the obligors of the receivables of the existence and the granting of the fiducia security over those future claims and the fiducia grantee registering the fiducia security over the future claims in a fiducia registration office.

9. Under the laws of this jurisdiction, are there any restrictions on offshore lenders taking security over any class of asset?

Generally there are no such restrictions.

10. Must a company receive a corporate benefit in return for giving a guarantee or security? In particular, are there restrictions on the grant of upstream and cross-stream guarantees and security? If yes, briefly what is the effect of these laws?

Best interests of the company

There is no restriction on the grant of upstream and cross-stream guarantees and security. However, under the Company Law, the members of the board of directors (BOD) of a company have a duty to manage the company in its best interests. Therefore, there must be a corporate benefit for the company before the BOD can direct the company to grant a guarantee or a security to a third-party borrower.

If there is no corporate benefit to the company in granting a guarantee or security to a third-party borrower and in the future the company suffers a loss due to the granting of the guarantee or security, the directors may be jointly and severally liable for that loss.

Typically, because whether a corporate benefit exists in any particular set of circumstances is an issue of fact, it is prudent for there to be a "whitewash" procedure by which all organs of the guarantor company (i.e., BOD, the Board of Commissioners (BOC) and General Meeting of Shareholders (GMS)) approve the granting of the guarantee.

Another regulatory process may need to be conducted if the guarantor or the borrower is a publicly listed company or a (directly or indirectly) controlled subsidiary of a publicly listed company (referred to below).

Affiliated party transactions

General rule

Under OJK Rule 42, unless exempted, the following are required of a publicly listed company or its (directly or indirectly) controlled subsidiary that carries out an affiliated party transaction (as defined in OJK Rule 42) ("**Affiliated Party Transaction**"):

- Undertake a "procedure" in accordance with the publicly listed company's internal policy to ensure that the Affiliated Party Transaction is implemented according to common business practice (i.e., the transaction must be done at arm's length) ("**Internal Procedure**") and keep the documents that are related to the implementation of the transaction.
- Use an independent appraiser to determine the fair value of the object as well as the fairness of the Affiliated Party Transaction.

- Disclose to the public information regarding the Affiliated Party Transaction in accordance with OJK Rule 42.
- Report the transaction (including submitting the disclosure evidence) to the OJK.
- In addition, unless exempted, certain Affiliated Party Transactions would require approval from the independent shareholders in a GMS in accordance with OJK Rule No. 15/POJK.04/2020 on Planning and Conducting General Meetings of Shareholders of Public Companies ("**OJK Rule 15**") in the following circumstances:
- The value of the Affiliated Party Transaction exceeds the threshold of a material transaction that requires GMS approval as stipulated in OJK Rule No. 17/POJK.04/2020 on Material Transactions and Change of Business Activity.
- The Affiliated Party Transaction may potentially disrupt the continuity of business of the publicly listed company.[1]
- The OJK deems that the Affiliated Party Transaction requires approval from the independent shareholders.
- The disclosure and reporting to the OJK above must be made, at the latest, by one of the following:
- Two business days after the Affiliated Party Transaction has been conducted.
- On the same day as the GMS announcement, if the Affiliated Party Transaction needs to be approved by a GMS.

Exemptions

The following exemptions are available under OJK Rule 42:

- The following Affiliated Party Transactions are some of those that do not need to go through the Internal Procedure, obtain a fairness/valuation from an independent appraiser or be disclosed to the public or reported to the OJK, among other things:
  - A transaction between the following, as long as the transaction has the same terms and conditions as a transaction that has been approved by a GMS:
    - The publicly listed company and its employees, members of the BOD or members of the BOC, or any employees, members of the BOD or members of the BOC of a publicly listed company's controlled company (as defined in OJK Rule 42) ("**Controlled Company**").
    - The Controlled Company and its employees, members of the BOD or members of the BOC, or any employees, members of the BOD or members of the BOC of the publicly listed company.
  - An ongoing transaction commenced after the publicly listed company conducted its public offering or after the registration statement submitted by the publicly listed company has been declared effective, provided the following conditions are met:
    - The transaction has satisfied the requirement under OJK Rule 42.
    - The terms and conditions of the transaction do not change, or if there are changes to the terms and conditions, those changes may not cause losses to the publicly listed company.
- The following Affiliated Party Transactions are some of those that do not need to go through the Internal Procedure, obtain a fairness/valuation from an independent appraiser, or be disclosed to the public, but still need to be reported to the OJK within two business days after the transaction:
  - A transaction whose value does not exceed 0.5% of the paid-up capital of the publicly listed company or does not exceed IDR 5 billion, whichever is lower.
  - A transaction carried out by a publicly listed company as a result of the implementation of applicable regulations or court decisions.

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1 Disruption to the continuity of business" means, for instance, if the proposed transaction, in pro forma, causes the publicly listed company to experience a decrease of 80% or more in its revenue or suffer a net loss (rugi bersih).

- A transaction between a publicly listed company and its Controlled Company whose shares are at least 99% held by the publicly listed company or between Controlled Companies whose shares are at least 99% held by the publicly listed company.

Affiliated Party Transactions that are considered "business activities"[2] of the publicly listed company are exempted from a fairness assessment by an independent appraiser, as well as from a disclosure and reporting obligation, although they still need to do the following: (i) go through the Internal Procedure the first time the transaction is conducted; and (ii) report the transaction in the publicly listed company's annual report or annual financial statements (with a reference in the annual report). If there is a change to the terms and conditions of such an Affiliated Party Transaction that potentially may cause losses to the publicly listed company, the Internal Procedure must be redone.

Conflict of interest transactions

Under OJK Rule 42, in carrying out a conflict of interest transaction (as defined in OJK Rule 42) ("**Conflict of Interest Transaction**"), a publicly listed company must obtain prior approval from the independent shareholders of a company in a GMS in accordance with OJK Rule 15, in addition to securing a fairness opinion from an independent appraiser, disclosing the transaction to the public and reporting the transaction to the OJK. There are certain Conflict of Interest Transactions, however, that are fully exempted from Conflict of Interest Transaction procedures, including the following:

- A transaction between the following, as long as the transaction has the same terms and conditions as a transaction that has been approved by a GMS:
  - The publicly listed company and its employees, members of the BOD or members of the BOC, or any employees, members of the BOD or members of the BOC of a Controlled Company.
  - The Controlled Company and its employees, members of the BOD or members of the BOC, or any employees, members of the BOD or members of the BOC of the publicly listed company.
- An ongoing transaction that commenced after the publicly listed company conducted its public offering or after the registration statement submitted by the publicly listed company has been declared effective, provided that the following conditions are met:
  - The transaction has satisfied the requirements under OJK Rule 42.
  - The terms and conditions of the transaction do not change or, if there are changes to the terms and conditions, those changes do not cause losses to the publicly listed company.

There are also other exemption criteria where the Conflict of Interest Transactions are exempted, but they still must be reported to the OJK, at the latest, two business days after the transaction occurs, including the following:

- A transaction whose value does not exceed 0.5% of the paid-up capital of the publicly listed company or does not exceed IDR 5 billion, whichever is lower.
- A transaction carried out by a publicly listed company as a result of the implementation of applicable regulations or court decisions.
- A transaction between a publicly listed company and its Controlled Company whose shares are at least 99% held by the publicly listed company or between Controlled Companies whose shares are at least 99% held by the publicly listed company.

2 OJK Rule 42 does not provide a definitive definition on what is considered a "business activity," but the transaction should be a business activity that is conducted to generate revenue and should be conducted in a routine, repeated and continuous manner. OJK Rule 17 provides a hint of the definition when it says that "business activities" are business activities that are stated in the public company's articles of association and that have been conducted.

Subsidiary companies

- If the guarantee is provided by a publicly listed company to its subsidiary (whose shares are at least 99% held by that publicly listed company) or provided by that publicly listed company's subsidiary (whose shares are at least 99% held by that publicly listed company) to that publicly listed company, the granting of the guarantee only needs to be reported to the OJK no later than two working days after the Affiliated Party Transactions have been conducted.
- The guarantee is provided by a publicly listed company to its subsidiary (whose shares are less than 99% held by that publicly listed company) or provided by that publicly listed company's subsidiary (whose shares are less than 99% held by that publicly listed company) to that publicly listed company, the Affiliated Party Transaction procedures as elaborated above must be conducted, assuming that there is no other exemption that would be applicable. A further conflict of interest assessment must be done to check whether the Conflict of Interest Transaction procedures must be followed.

11. What type of security interests does your jurisdiction recognise, e.g., pledge, charge, mortgage, hypothecation? In relation to each type of security interest, please state the formalities required to create and perfect that security.

The types of security recognized under Indonesian law are set out below.

Hak tanggungan

A hak tanggungan is a security right over a land right as security for a debt. A land right may include objects that are inseparable from the land (such as buildings and plants). This security right grants a priority right to certain creditors in relation to other creditors.

The creation of a hak tanggungan

The grantor must execute a deed of hak tanggungan (APHT) in Indonesian in favor of the grantee before a PPAT (land deed official). The APHT must clearly mention the identity of the parties, their domiciles in Indonesia, the secured debt, the value of the hak tanggungan, and a description of the land.

A hak tanggungan registration can be made online.

The PPAT is obliged to register the APHT with the Land Office (Kantor Pertanahan) within seven working days from the signing of the APHT. The Land Office must register the hak tanggungan in the hak tanggungan land book on the seventh day after it receives a completed application. On the registration date, the hak tanggungan comes into existence, is perfected, and the grantee becomes a priority creditor.

As evidence of the registration of the hak tanggungan, the Land Office issues to the grantee a certificate of hak tanggungan (which will have executorial power equivalent to a valid and binding court decision). If a plot of land is subject to more than one hak tanggungan, they are ranked according to their respective dates of registration. If more than one hak tanggungan is registered on the same date, they are ranked according to the number written on their respective APHTs.

As of July 2020, lenders and land deed officers may register the hak tanggungan through an online system called the HT-el system.

To be able to become a user of the HT-el system, lenders and PPATs must first register their accounts.

Before a lender submits the application for the registration of the hak tanggungan in the HT-el system, several steps need to be conducted by the PPAT, as follows:

- Land certificate check, which can also be conducted manually if the land data is not yet available in an electronic form and has not yet been provided in the database of the Ministry of Agrarian and Spatial Planning/National Land Agency.

- Reporting of APHT, which includes creating a deed code as an identification of the deed, inputting the data of the deed, uploading the APHT and its supporting data, downloading the deed cover note, and scanning and uploading the signed and stamped cover note.

In general, each of the HT-el services is carried out through the same steps, as follows:

- Submitting a request for the HT-el services by entering certain data according to the service required.
- Uploading the required documents (if any) and confirming the compatibility of the data uploaded by the PPAT and those of the physical document.
- Confirming the request.
- Paying the PNBP based on the transfer order letter.
- Reviewing the draft of the HT-el services output.

There are three types of output produced by the HT-el services, as follows:

- HT-el certificate
- Notes (catatan) of the hak tanggungan on the e-land book
- Notes (catatan) of the hak tanggungan on the land rights certificate

Costs and time frame

The costs for registering a hak tanggungan are as follows:

- The PPATs fee for preparing the APHT would be approximately up to 1% of the transaction value.
- The maximum amount of PNBP to be paid is IDR 50 million (approximately USD 3,300 using the currency rate of USD 15,000/IDR) for a secured value above IDR 1 trillion.

The period from the registration to the issuance of the certificate of hak tanggungan varies between one week and six months, depending on the Land Office and the status of the land.

Hypothec over a vessel

Hypothec over a vessel is a collateral right over a vessel to secure certain loan payments and gives priority rights to certain creditors over other creditors. The definition of "vessel" includes water vehicles of a certain shape or type that move by wind power, mechanical power or other energy, pulled or tugged, including vehicles with dynamic support power, submarine vehicles, and floating tools and fixed floating buildings (such as oil rigs).

The creation of a hypothec over a vessel

Only a vessel that has been registered in the Indonesian Vessel Registry (Daftar Kapal Indonesia) is permitted to be the subject of a hypothec. The main requirements for registration are as follows:

- The vessel has a size of at least seven gross tonnage.
- The vessel is owned by an Indonesian citizen residing in Indonesia or an Indonesian company that is established under Indonesian law.
- If it is owned by a joint venture company, the majority of the shares are owned by an Indonesian citizen.

A hypothec is created by a hypothec deed in Indonesian made before the ship registration and recording official at the place where the vessel is registered and recorded in the Main List of Vessel Registration (Daftar Induk Pendaftaran Kapal). After the registration, the hypothec will constitute a valid priority security interest over the vessel, securing up to the value stated in the hypothec deed.

A grosse deed of hypothec will be issued to the holder of the hypothec, which will have executorial power equivalent to a valid and binding court decision. One or more hypothecs can be created over a vessel. The rank of each hypothec is determined based on the date and number of the hypothec deed.

Costs and time frame

The registration costs for a hypothec include the notary fee, which is calculated from the value of the hypothec stated in the grosse deed of hypothec, and the PNBP, which is calculated from the gross tonnage of the vessel. The process of registration of a hypothec usually takes three to seven days.

Pledge

A pledge is a right of a creditor (pledgee) to movable property that is delivered into the possession of the pledgee by a debtor at the time that the pledge is created, and it gives the pledgee a preferential right to the proceeds from the sale of the pledged property over other creditors. Since the pledged property must be in the possession of the pledgee, the right of the pledgee will terminate if the pledged property is no longer in the possession of the pledgee, except if it is lost or stolen from the pledgee.

The creation of a pledge

The parties enter into a pledge agreement, and the pledgor delivers the pledged goods to the pledgee. There is no public registration. However, for a pledge over intangible property, there is a requirement to notify the party against which the pledge is to be enforced. The perfection of the pledge depends on the type of pledged property, i.e., the perfection of a pledge over intangible goods is done by way of delivery and the perfection of a pledge over intangible goods is done by way of notification.

For a pledge over shares, in addition to the pledge agreement, there is also typically an irrevocable power of attorney, a power of attorney to sell shares, and various notices or forms.

Costs and time frame

The costs for establishing a pledge depend on how the pledge agreement is drawn up and which related steps are taken. The costs increase in the following order, depending on how the pledge agreement is drawn up:

- Drawn up privately
- Drawn up privately and registered with a notary public to evidence that the document already existed at the time of registration
- Drawn up privately and legalized by a notary public to evidence that the signatures are the signatures of the signatories
- Drawn up in notarial deed form as prima facie evidence that the persons executing the agreement are the persons they claim to be and that the content of the agreement is as stated

There is no statutory timetable in relation to the documentation and registration of a pledge.

Fiducia security

Fiducia security is regulated under Law No. 42 of 1999 on Fiducia Security. The fiducia grantor transfers title to its asset in a fiduciary capacity to the fiduciary grantee (secured party). A fiducia security is a security right securing the repayment of a debt over the following:

- Tangible or intangible movable goods.
- Immovable goods that exist now or will exist in the future, can be owned and transferred, registered or unregistered, and cannot be encumbered by a hak tanggungan or hypothec (“Fiducia Property”).

The Fiducia Property, unless otherwise agreed by the parties, also includes the following:

- The products resulting from the Fiducia Property.
- Insurance claims of the Fiducia Property.

Unlike a pledge, Fiducia Property remains in the possession of the fiducia grantor. This security right will grant the fiducia grantee a priority right over other creditors.

The creation of a fiducia security

To establish a fiducia security, the fiducia grantor and fiducia grantee execute the fiducia agreement in Indonesian and in a notarial deed form.

The fiducia grantee (through a notary) registers the fiducia security at the relevant fiducia registration office through an online registration system. The registration office then records the fiducia security in the Registration Book of Fiducia on the same day as the online registration statement is submitted and when the registration fee has been paid. The fiducia security is established on the date it is recorded in the Registration Book of Fiducia.

Costs and time frame

The costs incurred in the registration of fiducia security are as follows:

- The notary's fee for the preparation of the notarial deed, which is calculated as follows:
  - Fiducia security with a value of less than or equal to IDR 100 million and the maximum cost is 2.5% of the fiducia security value.
  - Fiducia security with a value above IDR 100 million and less than or equal to IDR 1 billion and the maximum cost is 1.5% of the fiducia security value.
  - Fiducia security with a value exceeding IDR 1 billion and the maximum cost is 1% of the Fiducia Property.
- The maximum amount of PNBP to be paid, which is IDR 13.3 million (approximately USD 880 using the currency rate of USD 15,000/IDR).

The fiducia security must be registered within 30 days of the date of the deed of the fiducia security agreement. If there is an error on the fiducia security certificate (except in relation to the security value), a request for correction may be submitted no later than 30 days after the fiducia security certificate is issued. For errors or changes to the security value stated on the fiducia certificate, the fiducia certificate will need to be replaced. There is an amendment fee for such request.

Security over warehouse receipts

Security over warehouse receipts is the newest type of security available in Indonesia under Law No. 9 of 2006 on the Warehouse Receipt System as amended by Law No. 9 of 2011 ("**Warehouse Receipt Law**"). It defines a "warehouse receipt" as a document issued by a warehouse manager evidencing the ownership of goods (any movable goods that can be stored for some time and are generally traded) stored in the warehouse. The warehouse receipt is a certificate of title, and it is therefore transferable and can be provided as security. This security grants priority rights to a certain creditor over other creditors. The warehouse receipt can only be encumbered with one security right. The security also includes any insurance claim.

However, due to the lack of implementing regulations, security over warehouse receipts is rarely used in the market.

The creation of a security over warehouse receipts

Under the Warehouse Receipt Law, security over warehouse receipts is created as follows:

- The creditor and the borrower enter into a loan agreement and a deed of security agreement.
- The creditor notifies the Registration Center (currently under PT Kliring Berjangka Indonesia (Persero)) and the warehouse manager that the warehouse receipt has been encumbered with a security to secure the loan.
- After receiving the completed security notification documents, the Registration Center records the security over warehouse receipt in the Registry Book of Security (Buku Daftar Pembebanan Hak Jaminan) and issues a confirmation on the notification of the security encumbrance over the warehouse receipt and a written confirmation to the security grantee, the security grantor and the warehouse manager, the day after the notification at the latest.
- The security grantee holds the warehouse security receipt, and therefore the warehouse receipt cannot be doubly encumbered.

Costs and time frame

The cost for establishing security over warehouse receipts mainly comprises the fees payable to the notary and the Registration Center. This includes the fees for the preparation, execution and notification of the deed of security agreement.

There is no statutory timetable for the notification of security over warehouse receipts.

12. Are there any registration, translation or notarization requirements in relation to security, guarantees, subordination or intercreditor documents?

Please see the answer to question 7 of the "When lending to borrowers" section for registration or notarization requirements in relation to security and guarantee documents. With regard to subordination or intercreditor documents, there is no regulatory requirement for registration or notarization. The answer to question 7 of the "When lending to borrowers" section for translation requirement is also applicable to the security, guarantee and subordination or intercreditor documents.

13. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in respect of security, guarantees, subordination or intercreditor documents? If yes, what are the amounts and when are they payable?

Other than the registration fees set out in the answer to question 8 of the "When lending to borrowers" section, no documentary, registration, notarization or other similar taxes, duties or fees are payable under the laws of the Republic of Indonesia in relation to the loan and security documents, except that stamp duty at the rate of IDR 10,000 is payable on each of the documents.

If things go wrong

1. Please provide a brief description of the insolvency regime. In particular what rights and duties do unsecured and secured lenders have on the insolvency of a debtor? Are there any other matters of concern?

Under the Bankruptcy Law, two types of proceedings may be commenced:

- Bankruptcy proceedings, by which the debtor loses its power to manage and dispose of its assets (i.e., a liquidation type of bankruptcy).
- A legal debt moratorium or suspension of payments proceedings, by which the debtor, on request by a creditor or the debtor itself, is given temporary relief to restructure its debts and continue in business, and ultimately to satisfy its creditors (i.e., a debt reorganization type of bankruptcy).

Bankruptcy proceedings

Application

The Bankruptcy Law requires that the bankruptcy petition be filed by a lawyer admitted to practice before the commercial court having jurisdiction over the debtor's legal domicile. If the debtor is a legal entity, the legal domicile of the debtor is that which is stated in its articles of association. Under the Indonesian insolvency regime, as long as there are two creditors to whom unpaid debts are owed and the debtor has failed to pay in full one of its debts that is already due and payable, a petition can be filed to force the debtor to pay.

Creditors

The creditors affected by the bankruptcy are not all in the same position. Preferred/secured creditors have a priority claim on the proceeds of the sale of any assets that have been granted as security in their favor. Unsecured/concurrent creditors, on the other hand, share in the division of the remaining assets and obtain satisfaction of their debts in a proportionate percentage, i.e., unsecured/concurrent creditors will share in the money proportionately rather than the first creditor that applies being the first to receive payment. From the date of the declaration of bankruptcy, the unsecured/concurrent creditors can obtain satisfaction of their claims only in the bankruptcy procedure and not through individual enforcement proceedings.

The secured creditors' right to enforce their security is stayed for a maximum of 90 days from the date the debtor is declared bankrupt. Following the stay period, the Bankruptcy Law generally refers to a period of two months for the enforcement of security by secured lenders after the debtor enters into an insolvency situation (i.e., if the debtor does not offer any composition plan during the debt registration meeting, the composition plan is rejected or the approval of the composition plan is rejected by a final and binding decision). The stay period does not apply to any secured creditors' claims that are secured by cash and the creditor's right to a set-off.

Only creditors having a claim in relation to the bankrupt debtor at the time of the bankruptcy declaration may claim payment from the proceeds of the bankruptcy estate. Further, all payment obligations of the debtor that occur after the bankruptcy declaration cannot be paid from the proceeds of the bankruptcy estate, unless the fulfillment of the payment obligations brings benefits to the bankruptcy estate.

Claims

The Bankruptcy Law requires that every creditor submit to the curator (similar to a liquidator) its claim in the form of a prescribed written statement that includes whether the creditor concerned has a security right in rem or a statutory priority right. The creditors' claims are then verified at the creditors' meeting.

After all acknowledged creditors have received the full amount of their claims or as soon as the final distribution plan (made by the curator) has become binding, the bankruptcy will end. The curator must announce the completion of the bankruptcy in the same manner as the announcement of the declaration of bankruptcy. The curator will account for its administration and liquidation of the bankruptcy estate to the supervisory judge 30 days after the end of the bankruptcy.

Appeal or review

Any cassation (a type of appeal) or civil review process does not affect any action taken by the curator, who is empowered by law to administer and liquidate the bankruptcy estate. If for any reason the declaration of bankruptcy is reversed in a cassation or civil review, actions that are taken prior to the curator being served notice of that cassation or civil review are legal and binding on the debtor.

Suspension of payments proceedings

Petition

A creditor that foresees that its debtor would not be able to continue to pay its debts when they become due and payable and a debtor that is unable or predicts that it will be unable to pay its debts when they become due and payable may file a petition for the suspension of the payment of debts with the relevant commercial court. The aim of the suspension of payments is to provide the debtor with more time to either meet its obligations or come to an agreement with its creditors to restructure the debts. A suspension of payments can easily be converted into a bankruptcy when it is clear that the suspension will not be successful.

A suspension of payments is initially granted for a maximum of 45 days. This is known as a "temporary" suspension of payments.

Pursuant to the Bankruptcy Law, a debtor may also file a petition for the suspension of payments after a petition for bankruptcy declaration has been filed against it. If petitions for both a suspension of payments and bankruptcy are reviewed by the court at the same time, the petition for the suspension of payments prevails and

it must be decided first. Although it is not a legal remedy as such (i.e., appeal or civil review), a petition for the suspension of payments will effectively postpone the bankruptcy process for a certain period.

Composition plan

The Bankruptcy Law requires the debtor petitioning the suspension of payments ("**Applicant**") to submit its settlement or composition plan with its creditors at the time that or after the debtor files the petition for the suspension of payments. A composition plan with creditors is an agreement made between the Applicant and its creditors for the settlement or arrangement for a discharge of the debts of the Applicant. The composition plan must set out the proposed timetable under which the Applicant will repay its debts and whether the debts will be fully or partially repaid. In order to be valid and effective, a composition plan must be approved at a creditors' meeting by the following:

a. Affirmative votes of more than half of the concurrent creditors that are present at the meeting, provided that concurrent creditors voting in favor hold at least two-thirds of all accepted or provisionally accepted unsecured claims held by the concurrent creditors present at the meeting (Votes are only taken from the concurrent creditors present at the meeting); and

b. Affirmative votes of more than half of the secured lenders that are present at the meeting, provided that secured lenders voting in favor hold at least two-thirds of all accepted or provisionally accepted secured claims held by the secured creditors present at the meeting (Votes are only taken from the secured creditors present at the meeting).

The composition plan, once ratified, binds all of the unsecured creditors and secured creditors (who voted in favor of the plan), including those unsecured creditors that voted against the acceptance of the composition plan and that were not present or represented at the creditors' meeting.

Declaration of bankruptcy if a composition plan is not ratified

If the composition plan is not available at the first hearing, during the temporary suspension of payments or when the creditors have not yet cast votes in relation to the composition plan, the creditors, at the request of the Applicant, may grant an extension so that the suspension of payments situation becomes a "permanent" suspension of payments (i.e., a reference to the period beyond the temporary suspension of payments). However, the total suspension of payments period may not exceed 270 days. During the permanent suspension of payments period, the Applicant and the creditors may continue to negotiate the composition plan. If a permanent suspension of payments is not granted, or if at the expiry of the suspension of payments period there is no decision in relation to the composition plan, the administrator (a person appointed during the suspension of payments proceedings who, together with the debtor, administers the assets of the debtor) must notify the court and the court will immediately declare the Applicant bankrupt.

Effect on the payment of debts and secured creditors

The debtor cannot be forced to pay its debts during the suspension of payments period. However (unlike in a bankruptcy situation), a debtor subject to a suspension of payments may manage or dispose of its assets and obtain loans and secure its unsecured assets, provided that those acts have been authorized by the administrator and/or the supervisory judge.

A secured creditor cannot enforce its rights during a suspension of payments period.

Termination of the suspension of payments

A suspension of payments may be terminated by the commercial court on a request submitted by the administrator, the supervisory judge or any of the creditors, or at the commercial court's initiative in certain circumstances, including if the Applicant transfers rights to any part of its assets without authorization from the administrator or if the Applicant's position is such that a suspension of payments is no longer feasible.

2. Is it possible to obtain a moratorium before insolvency?

Yes. The procedure to obtain a moratorium (known as a suspension of payments in Indonesia) is set out in the answer to question 1 of this section.

3. When a company is the subject of a formal insolvency procedure, can the company's pre-insolvency transactions be set aside?

Yes. Under Indonesian law, there are two different routes by which pre-insolvency transactions can be set aside.

ICC

Under the ICC, any action taken by a debtor may be nullified if:

- That action was not required by law or pursuant to the terms of a bona fide agreement (nonobligatory action).
- The action prejudiced the interests of (other) creditors.
- The debtor and the party that benefited from the action (or counterparty) knew or should have known that the action would prejudice creditors.

Bankruptcy Law

The Bankruptcy Law recognizes the concept of fraudulent conveyance (actio pauliana).

Under the Bankruptcy Law, a transaction or action carried out one year prior to a bankruptcy declaration may be nullified or set aside. There is a legal presumption of deemed knowledge of prejudice of other creditors if the action was performed within the one-year period prior to the bankruptcy declaration and that action:

- Constitutes an agreement under which the obligations of the debtor were more onerous than the obligations of the counterparty.
- Constitutes the payment of or granting of security for debts that were not due and payable.
- Was performed with an affiliated party (which is detailed in the Bankruptcy Law).

In addition, under the Bankruptcy Law, payment of a due and payable debt (or satisfaction of claimable obligations) by the debtor may also be nullified if one of the following can be proved:

- It is evident that the counterparty that received the payment was aware that a petition for a bankruptcy declaration had been filed against the debtor.
- The payment was made pursuant to deliberations (or a collaboration) between the debtor and the counterparty with the intention to pay the counterparty ahead of other creditors.

4. When can a lender enforce its security? Can security be enforced out of court following an event of default (or other contractual trigger event), or is a court order required? Are there any restrictions that apply before a lender may enforce its security?

The lender can enforce the security after the occurrence of an event of default subject to the terms of the relevant security documents. However, a secured lender may need to obtain a court order permitting the enforcement of its security where, for example, the enforcement of security involves a public auction through a court. The qualifications, as well as the enforcement processes in relation to the different types of security, are also set out below.

Qualifications

If the debtor is subject to a declaration of bankruptcy or a suspension of payments, one of the following qualifications will apply in relation to the processes:

- The right of enforcement of the secured creditor (i.e., the lender) after the declaration of bankruptcy is subject to a stay period of up to 90 days (counted from the date of the decision declaring bankruptcy), during which the secured creditor (i.e., the lender) is prevented from enforcing its rights over the security. The stay period will be terminated if, following the declaration of bankruptcy, the debtor enters into an insolvency situation or when the Supreme Court annuls the bankruptcy. This stay period, however, does not apply to creditors that have rights over secured cash deposits or rights to set off debts.
- The right of enforcement of a creditor (i.e., the lender) is deferred during a suspension of payments of the debtor.

As far as we are aware, no restrictions apply before a creditor may enforce its security apart from the stay periods mentioned above.

Specific security interests

Enforcement of a hypothec over a vessel

If there is an event of default, a creditor must serve the borrower with a clear and unequivocal letter of demand to enforce its security rights.

The creditor, without obtaining a court order, may proceed to sell the hypothec object by public action or private sale (if the highest price could be achieved and it would be profitable for all parties concerned) if the following events occur:

- The borrower does not comply with the letter of demand.
- The grosse deed of hypothec contains an agreement or a promise for the holder of the security/creditor (as the hypothec grantee) to sell the object of security on the default of the debtor.

Both the auction and private sale methods must follow the procedure set out in the statutory regulations.

This holder's right of self-enforcement is referred to as simplified enforcement (parate executie) because there is no court involvement in this process.

If the grosse deed of hypothec does not contain an agreement or a promise for the holder of security to sell the object of security on the debtor's default, the holder of hypothec must submit an application of enforcement to the court. After a prescribed process has been completed, the court will issue an auction order for the object of hypothec to be sold by public auction.

If there is resistance from the hypothec grantor at the enforcement stage (even if the deed of hypothec contains an agreement or a promise for the hypothec holder to sell the vessel on the debtor's default), the hypothec grantee may apply to a court for a court order.

Enforcement of a pledge

If the pledgor defaults, the pledgee may serve the borrower with a clear and unequivocal letter of demand, and if it is not complied with, the pledgee can use the letter of demand to establish the borrower's failure to comply.

If the pledgor does not comply with the letter of demand, the pledgee may enforce its right over the pledged property by way of public auction or by private sale if the pledgor and the pledgee agree. It is generally accepted in practice that the pledgee can sell the shares through a private sale, as long as the pledgor has authorized the pledgee to do so.

There are no statutory provisions in relation to the method of enforcement for a pledge over bank deposits. However, in practice, the enforcement can be conducted by means of a set-off of the monies deposited in the account against the outstanding debt. This means that the enforcement of pledge over bank deposits does not follow the general procedures for the enforcement of a pledge.

Enforcement of a fiducia security and a hak tanggungan

A creditor must serve the borrower with a clear and unequivocal letter of demand before enforcing its security rights. There is no strict timeline in relation to when the letter of demand must be served. Unless it is specifically stipulated under the financing documents, the letter of demand can be served on the occurrence of an event of default. If the borrower does not comply with this letter, then the creditor may proceed with the following methods to enforce its security rights:

- Rely on the executory title in the certificate of fiducia security or certificate of hak tanggungan.
- Sell the fiducia object or hak tanggungan object (if the deed of hak tanggungan contains an agreement or a promise for the holder of hak tanggungan to sell the hak tanggungan object on the default of the debtor) by public auction.
- Sell the fiducia object or hak tanggungan object by private sale if the highest price can be achieved and it would be profitable for all the parties concerned.

The private sale must follow the procedure provided for in the statutory regulations (e.g., an announcement regarding the proposed private sale must be published in at least two newspapers circulated in the area where the fiducia object or hak tanggungan object is located).

Enforcement of a security over warehouse receipts

A creditor must serve the borrower with a clear and unequivocal letter of demand before enforcing its security over warehouse receipts. If the borrower does not comply with this letter, then the creditor may proceed with the enforcement of its security rights.

The creditor (the security grantee) can sell the goods without first obtaining a court order. However, it must notify its intention to the owner of the warehouse receipt (the security grantor), the warehouse manager and the Registration Center at least three days before the sale of the goods.

To enforce the security over a warehouse receipt, the creditor can sell the goods as follows:

- By public auction in accordance with the prevailing laws and regulations.
- By private sale if this method will yield the best price that will benefit both parties.

The creditor can apply the sale proceeds to the loan after making deductions for the sale and management costs.

Enforcement of a guarantee

Generally, the procedures of enforcing a guarantee in Indonesia are the same as suing a party that is in default of its contractual obligation. A lender will need to lodge a lawsuit against the guarantor in a court. The guarantor will have a chance to present its pleadings, documentary evidence and witnesses to challenge the enforcement of guarantees.

5. Do any limitation periods apply in relation to bringing an action to enforce security?

The limitation period that applies in respect of bringing an action to enforce security relates to the concept of statutory limitation under the ICC, which generally states that claims in relation to the repayment of a loan are permitted to be filed within 30 years.

If a claim is not brought within 30 years, such claim will be barred. However, Article 1967 of the ICC does not stipulate when the 30-year period commences. Several legal scholars are of the opinion that the 30-year period commences when a right can be exercised (i.e., when the right first arose).

As discussed in the answer to question 1 in this section, after the stay period of up to 90 days following the bankruptcy declaration, the secured creditor only has two months after the debtor enters into an insolvency situation (i.e., if the debtor does not offer any composition plan during the debt registration meeting, the composition plan is rejected or the approval of the composition plan is rejected by a final and binding decision) to enforce its rights over the collateral but subject to the qualifications set out in the answer to question 4 of this section. After the two-month period, the curator has the right to sell all collateral of the debtor to pay off its debts. This includes collateral over which the debtor has granted security. If the curator exercises this right (in practice, after discussions with any secured creditors), the proceeds of the sale in relation to collateral over which the debtor has granted security will be given to the relevant secured creditor.

6. Is there any particular way in which secured assets must be liquidated on enforcement (e.g., by auction or court sale)?

Please see the answer to question 4 of this section in relation to the enforcement of security generally.

7. Are there any particular legal or practical difficulties or delays in enforcing security?

In Indonesia, the process of the enforcement of security is usually subject to challenge by the debtor/obligor (e.g., to seek to invalidate the loan and frustrate the enforcement). In practice, debtors and obligors are often uncooperative during the enforcement process and often take defensive legal action to maintain their assets.

In addition, a provision in a loan or security document that a calculation, determination or certificate will be conclusive and binding will not apply to a calculation, determination or certificate that is given unreasonably, arbitrarily or without good faith, or that is fraudulent or manifestly inaccurate and will not necessarily prevent a judicial enquiry into the merits of any claim.

Further, the enforceability of an obligation in Indonesian-law-governed documents in general may be affected or limited by the following:

- The general defenses available to obligors under Indonesian law in respect of the validity and enforceability of loan and security documents.
- The provisions of any applicable current or future bankruptcy (kepailitan or faillissement), insolvency, fraudulent conveyance (actio pauliana), reorganization, moratorium/suspension of payments (penundaan kewajiban pembayaran hutang or surseance van betaling) and other or similar laws of general application relating to or affecting the enforcement or protection of creditors' rights.

8. In relation to enforcement, are there any specific requirements to be borne in mind if the lender is a foreign entity?

There are no specific requirements for an offshore lender to enforce its security.

9. Is there any reason why you think that arbitration rather than litigation might be advantageous in resolving disputes under the finance documents, and if so, why? Please outline the relative merits of arbitration and litigation, including the ease of enforcement of foreign judgments and foreign awards from different jurisdictions. Is it possible to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit?

It is common for the parties to choose arbitration to resolve their disputes in relation to cross-border transactions, and there are various reasons for doing so. Firstly and most importantly, by virtue of the New York Convention, an arbitration award is enforceable in Indonesia. Secondly, the parties can typically choose arbitrators who have relevant expertise to hear and resolve the dispute. Thirdly, arbitration is a neutral way to resolve the parties' dispute (in contrast to the local courts). Fourthly, the arbitration process is relatively quick in most cases. Although arbitration is generally preferable in a cross-border transaction, the parties should be cautious in choosing the seat of arbitration. The choice of the seat of arbitration will have a significant impact on the arbitration process, as the law governing the arbitration process will be the law of that seat of arbitration.

While there are advantages to choosing arbitration as set out above, there are also some disadvantages. Foreign arbitration awards are not automatically enforceable in Indonesia. Enforcement involves a three-stage process. The award must be registered in Indonesia. On registration, a winning party files an application to obtain leave for enforcement ("**Exequatur**") from the Central Jakarta District Court. Once the Exequatur is granted, a successful party can seek the district court's assistance to enforce the award in Indonesia. There is also a possibility that the opposing party will try to avoid or obstruct the arbitration proceedings by not participating in the constitution process of the arbitral tribunal. Further, if the unsuccessful party does not want to voluntarily honor the award, the court's assistance will be required to enforce the award.

A foreign (non-Indonesian) court judgment is not enforceable in the Republic of Indonesia, although this type of judgment could be admissible as inconclusive evidence in proceedings on the underlying claim in an Indonesian court. Although Indonesian courts are in a position to determine the applicable rules of foreign laws, in practice however they have from time to time applied the laws of the Republic of Indonesia notwithstanding the choice of law provisions in the relevant documents. A non-Indonesian judgment may be given the evidentiary weight an Indonesian court considers appropriate and reexamination of the issues de novo would be required before an Indonesian court to enforce the claim in the Republic of Indonesia. The entire civil proceedings process to obtain a final and binding court judgment in Indonesia up until the Supreme Court level could take more than one year.

With regard to a hybrid provision that allows the parties to opt for either arbitration or litigation, at the outset, the provision is not prohibited under Indonesian law to be included in an agreement based on the freedom of contract principle. However, the Indonesian court may view that there is no "exclusive jurisdiction" for disputes arising from an agreement to be settled through arbitration. Therefore, an Indonesian court may decide that it has jurisdiction over claims submitted by the borrower in relation to the agreement to the Indonesian court.

Further, if the hybrid provision only allows the lenders to opt for arbitration or litigation as they see fit, the Indonesian courts may deem the provision not enforceable on the basis that the arrangement is one-sided (only for the benefit of the lender). Additionally, the court may apply the right to opt for arbitration or litigation to the borrower as well.

10. Are asymmetrical jurisdiction clauses enforceable? (By this we mean clauses that allow the lenders, but not the borrowers, to make certain choices in relation to choice of jurisdiction and how to litigate. These types of clauses allow the lenders, but not the borrowers, to commence proceedings in any court they choose, but restrict the borrowers to commencing proceedings in one jurisdiction only. This may also allow the lenders, but not the borrowers, to choose whether to litigate the finance documents before a court or to submit to arbitration in relation to them, but restrict the borrowers to either litigation or arbitration, as specified in the agreement).

Despite the freedom of contract principle under Indonesian law, there is a risk that Indonesian courts would take the view that asymmetrical jurisdiction clauses are not enforceable because the arrangement is one-sided (only for the benefit of the lender). Further, the risk from an Indonesian court proceedings perspective is that the court may apply the right to choose the jurisdiction and the right to litigate to the borrower as well. This will allow the borrower to bring a claim related to the Finance Documents in a different jurisdiction as it sees fit.

In addition, if the clause allows the lender (only) to choose to litigate through court litigation or arbitration, the Indonesian courts may view that there is no "exclusive jurisdiction" for disputes arising from the Finance Documents to be settled through arbitration. Consequently, an Indonesian court may decide that it has jurisdiction over the dispute submitted by the borrower to the Indonesian court.

Working digitally

1. **Is it possible for documents to be executed electronically (whether by the manual insertion of a digital signature or the use of an e-signing platform) under the laws of this jurisdiction? If so, is this limited to only particular types of finance documents?**

   Indonesian law generally recognizes e-signatures for the following: (i) as a basis to prove an agreement or acceptance; and (ii) for evidentiary purposes. The validity requirement of electronic signatures under Indonesian law indicates that the manual insertion of a scanned signature is not acceptable. Indonesian law only acknowledges electronic signatures generated by e-signature providers and recognizes two types of electronic signatures: certified and uncertified electronic signatures. Certified electronic signatures are signatures generated by locally registered electronic signature providers. Uncertified electronic signatures are signatures generated by unregistered electronic signature providers (e.g., foreign electronic signature providers). Both types of electronic signatures are acknowledged and admissible as evidence in court, but an uncertified electronic signature has less evidentiary value before the courts. Some certified electronic signature providers in Indonesia are PrivyId, Vida, Digisign, Peruri Sign, TekenAja, Tilaka and Xignature.

   However, there are some documents, such as security documents, that must be executed in a notarial deed form and the parties must appear and sign the documents before a notary.

   While there is no specific restriction on the types of documents that can be signed using an electronic signature, in practice, most parties and government agencies in Indonesia still refer to and require manually (wet) signed hard copy documents. Currently, for contracts or documents that may be disputed, the best practice is to obtain a wet signature.

2. **Where the witnessing of a signing is contemplated, is it possible for the witness to verify the signature over a live video call?**

   There is no requirement to have witnesses when signing a document, unless the document is executed in a notarial deed form. The execution of a notarial deed requires at least two witnesses. The witnesses must sign the deed in front of the notary. If the witnesses do not appear before the notary, the document will be deemed to be a privately drawn document and cannot be considered complete evidence (it is considered prima facie evidence to the parties named as signatories thereto only if such parties acknowledge that they signed the document).

3. **Is it possible to register/perfect security electronically without wet ink signatures?**

   Currently, it is not possible to perfect security electronically without wet ink signatures. There are requirements that security documents such as land mortgages, fiducia security and security over warehouse receipts be executed in a notarial deed form. The parties must appear and sign the security document before a notary. Although there is no requirement for a pledge agreement and other Finance Documents to be executed in a notarial deed form, it is common practice to execute them in a notarial deed form. Under Indonesian law, a notarial deed is considered binding and complete evidence (prima facie). It does not need any additional evidence to prove its existence and correctness, unless proven otherwise. If any information contained in a notarial deed is challenged, then the burden to prove the challenge lies solely with the challenger.

   Indonesian law does not require an agreement to be made in notarial deed form. However, for authentication purposes before the court, a notarial deed is considered an authentic deed, as well as binding and complete (prima facie) evidence.

4. **Are there any other legal restrictions that may prevent the parties from executing a finance transaction electronically?**

   No, there are no such restrictions. However, as mentioned above, most parties and government agencies in Indonesia still require manually (wet) signed hard copy documents. For contracts or documents that may be disputed, the best practice is to obtain a wet signature.

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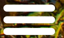
JAPAN



Japan

When considering whether to lend

1. **Is it necessary or advisable for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in this jurisdiction: (a) by reason only of its execution, delivery or performance of the finance documents; or (b) to enable it to enforce its rights under the finance documents?**

In Japan, lending in the ordinary course of business requires a license either under Act No. 59 of 1981, as amended ("**Banking Act**") or under Act No. 32 of 1983, as amended ("**Money Lending Business Act**").

Generally, a foreign bank obtains a banking license as a foreign bank branch (gaikoku ginko shiten) under the Banking Act in order to provide any loan to a borrower in Japan that requires one or more of execution, delivery or performance of the finance documents. If the loan is a one-off, it could be argued that the lender is not acting in the course of its business. However, where a foreign bank that provides loans as part of its business makes the loan, even if the loan is its first in Japan, that argument will be unlikely to succeed.

The arrangement of a syndicated loan by a bank (including a foreign bank) is permitted as part of the bank's "incidental business" (*fuzui gyomu*), as set out in the Banking Act.

Where a nonbank arranges a syndicated loan and acts as an agent or intermediary for the finalizing of the loan agreement on behalf of a bank instead of on behalf of a borrower, it may be required to obtain a bank agent license (*ginko dairigyo*) under the Banking Act.

Similarly, because a facility agent or security agent only undertakes administrative functions, it is not required to obtain a bank agent license. However, if a security agent acts as a security trustee, it must obtain a trust company license, as required by Act No. 154 of 2004, as amended ("**Trust Business Act**").

Apart from the license required for lending in the ordinary course of business referred to above, there is no license or qualification that is required for a lender, arranger, facility agent or security agent to enforce its rights under the finance documents.

2. **Will any lender, arranger, facility agent or security agent be deemed to be resident, domiciled, carrying on business or subject to tax by reason only of the execution, delivery, performance or enforcement of the finance documents?**

No.

3. **Are there any regulatory reporting requirements that lenders must observe in connection with those transactions?**

A bank that has a license under the Banking Act referred to in the answer to question 1 of this section (including a foreign bank that has a license as a foreign bank branch (gaikoku ginko shiten) under the Banking Act) must prepare and lodge a report or file documents in connection with its business or assets when requested to do so by the Financial Services Agency (FSA) as set out under the Banking Act.

A licensed moneylending business operator licensed under the Money Lending Business Act must file a business report every fiscal year as required by that act. Under the Money Lending Business Act, a moneylending business operator may also be required to provide reports if requested by the FSA or the prefectural governor.

In addition, depending on the types and volumes of loans, additional reports may have to be made to the finance minister or the relevant authorities under Act No. 228 of 1949, as amended ("**Foreign Exchange and Foreign Trade Act**").

4. **Is it necessary to establish a place of business in your jurisdiction in order to enforce any provision of the finance documents?**

   No.

5. **Is a foreign bank/financial institution permitted to approach local entities for business?**

   Generally, yes. However, when a foreign bank/financial institution engages in marketing or solicitation in Japan directly or indirectly for its lending or other banking business, it must obtain a license of a Japanese branch of a foreign bank, Japanese banking license or money-lending business license unless it is lawfully conducted through a foreign bank agency licensed as such under the Banking Act.

When lending to borrowers

1. **Are there any restrictions in relation to the type of borrower who may borrow foreign currency or in relation to the term of foreign currency and/or the amount of foreign currency borrowed by local entities?**

   No.

2. **Are there any restrictions on the rate of interest or default interest that may be charged?**

   Act No. 100 of 1954, as amended ("**Interest Rate Restriction Act**") sets the following interest rate ceilings:

   - 20% per annum for loans with a principal amount under JPY 100,000
   - 18% per annum for loans with a principal amount of between JPY 100,000 and JPY 1 million
   - 15% per annum for loans with a principal amount of JPY 1 million or more

   Interest rates that are higher than these rates are void.

   In addition, any loan with an annual interest rate above 20% may trigger criminal sanctions under Act No. 195 of 1954, as amended ("**Act Regulating the Receipt of Contributions, Receipt of Deposits and Interest Rates**").

3. **Are there any restrictions on particular lenders or classes of lender entering into credit transactions with borrowers?**

   No; however, when a credit transaction is considered as a lending in the ordinary course of business, such credit transaction could be subject to the licensing requirements as explained in the answer to question 1 of the "When considering whether to lend" section in relation to the licensing requirements for lenders.

4. **Are there any exchange controls that will apply to payments to be made in foreign currencies or to foreign lenders?**

   In principle, there are no significant restrictions imposed in relation to foreign currency exchange in Japan. However, there is a requirement that an after-the-fact report is filed with the relevant minister. Moreover, if the remittance amount is less than JPY 30 million or its equivalent, this requirement may be set aside.

Generally, a loan (whether in foreign currency or JPY) with a term that exceeds one year made to a company with a principal office in Japan must be reported to the minister of finance. However, there are two exceptions: if the loan is not an inward direct investment (as defined in Article 26 of the Foreign Exchange and Foreign Trade Act) or if it is provided by a financial institution.

Payments or transfers of money (whether in foreign currency or JPY) also generally require an after-the-fact report to be filed with the minister of finance through the Bank of Japan under the Foreign Exchange and Foreign Trade Act.

5. Is there any requirement to deduct or withhold tax from any amounts to be paid or repaid to a lender (whether domestic or foreign)? If so, at what rate must tax be deducted and from what kinds of payment?

Interest paid to a foreign lender providing loans to borrowers in Japan is subject to a withholding tax of 20.42%, which may be reduced or exempted under tax treaties between the relevant lender's country of tax residence and Japan.

6. Are there any "thin capitalization" or other rules that may limit the extent to which interest payments may be deducted for tax purposes?

In addition to the transfer pricing rules, which restrict the tax deductibility of the intercompany interest expenses, if the interest rate is not in accordance with the arm's length principle, there are two rules to limit the interest payment deduction.

One is thin capitalization rules limiting interest payment deductions for companies in Japan that are leveraged in excess of certain thresholds. The rules apply only to foreign-owned Japanese companies that raise funds from foreign controlling shareholders or third parties related to foreign controlling shareholders.

Under the rules, interest payments are excluded from a company's deductible expenses to the extent that those interest payments relate to debt owed to its foreign controlling shareholders and/or third parties related to its foreign controlling shareholders and to the extent that the debt exceeds three times the company's net equity. Therefore, the deduction of interest payments will be denied to the extent those interest payments relate to a taxpayer's debt that exceeds the maximum allowable level.

Another rule is the earning stripping rule that limits the interest payment deductions for companies with higher interest rate costs. Very briefly, if the net interest expense amount paid to foreign corporations and individuals (i.e., the net interest expense paid to not only a foreign shareholder and affiliates that directly or indirectly own 50% or more of the shares of the Japanese corporation but also the foreign third party) exceeds 20% of the adjusted income or equivalent to EBITDA (defined as taxable income, adding back interest expense and depreciation expense but excluding extraordinary income or loss), the net interest paid by the Japanese corporation to them in excess of 20% of the adjusted income is not deductible for Japanese corporate tax purposes. This legislation does not apply if the net interest expense to related parties in the fiscal year is JPY 20 million or less or if the total of the domestic group companies' interest expenses is 20% or less of the total of the domestic group companies' adjusted income.

If both the Japanese earnings stripping rules and thin capitalization rules apply in the same fiscal year, the total disallowed interest for the fiscal year is the larger of the disallowed interest as calculated under each rule.

7. Are there any registration, notarization, translation or reporting requirements in relation to the loan documents?

No.

8. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to the loan documents? If yes, what are the amounts and when are they payable?

The execution of a loan document in Japan triggers Japanese stamp duty. The amount of stamp duty depends on the aggregate principal amount of the loan, as set out in the table below.

Contract amount written in an agreement	Tax amount
Less than JPY 10,000	Nontaxable
Between JPY 10,000 (inclusive) and JPY 100,000 (inclusive)	JPY 200
Between JPY 100,000 and JPY 500,000 (inclusive)	JPY 400
Between JPY 500,000 and JPY 1 million (inclusive)	JPY 1,000
Between JPY 1 million and JPY 5 million (inclusive)	JPY 2,000
Between JPY 5 million and JPY 10 million (inclusive)	JPY 10,000
Between JPY 10 million and JPY 50 million (inclusive)	JPY 20,000
Between JPY 50 million and JPY 100 million (inclusive)	JPY 60,000
Between JPY 100 million and JPY 500 million (inclusive)	JPY 100,000
Between JPY 500 million and JPY 1 billion (inclusive)	JPY 200,000
Between JPY 1 billion and JPY 5 billion (inclusive)	JPY 400,000
Over JPY 5 billion	JPY 600,000
No description of contract amount	JPY 200

The stamps must be affixed to the loan documents and canceled by a signature or seal. Technically, parties to a loan document are jointly liable to pay the stamp duty when the document is executed. In practice, however, the borrower usually bears the stamp duty pursuant to costs and expenses provisions in the loan document.

9. Does the law recognize the subordination of the debt that a debtor owes to one creditor to that which the debtor owes to another creditor? If yes, how is this usually effected?

The nature of the contractual subordination determines whether it will be recognized by a court or insolvency administrator. There are three forms of contractual subordination that may be applicable as explained below.

Contractual subordination under insolvency acts

Act No. 75 of 2004, as amended, Act No. 225 of 1999, as amended, and Act No. 154 of 2002, as amended, ("**Corporate Reorganization Act**") provide for contractual subordination under an agreement between a creditor and a debtor by which the claims of that creditor are subordinated to the claims of the general unsecured creditors of the borrower in the event of insolvency proceedings. This type of contractual subordination will be recognized by a court or insolvency administrator. The effect of this type of contractual subordination is that the priority of the subordinated creditors' claims will fall between the general unsecured creditors' claims and the equity holders' claims.

Contingent claims

Under this type of contractual subordination, the loan agreement stipulates that if a certain trigger event occurs (e.g., an event of default or acceleration), the claims of the mezzanine and/or junior lenders are contingent on the payment in full of the claims of the senior lender. A court or insolvency administrator will, in effect, recognize that under this type of contractual subordination, the claims of the mezzanine and/or junior lender do not exist

(or exist contingently) at the time of the insolvency. This arrangement is sometimes used in Japan for effectively securing the priority of the senior lender, but it is not popular among mezzanine and/or junior lenders as it may yield unacceptable results for them.

Contractual subordination under intercreditor agreements

Where the claims of the mezzanine and/or junior lender remain but are contractually subordinated to the senior lender under an intercreditor agreement, a court or bankruptcy administrator will set aside the contractual subordination and, in the case of secured creditors, distribute the proceeds from the secured assets in accordance with the order of registration or, if registered simultaneously, pro rata among the secured lenders. While a senior lender may rely on the clawback provisions of the intercreditor agreement, where the court or insolvency administrator has made payments to a mezzanine and/or junior lender prior to the satisfaction of the senior claims, the senior lender will then be taking on both the performance risk and credit risk of the mezzanine and/or junior lender.

10. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors (e.g., the claims of employees and tax authorities or the claims of creditors under particular kinds of instrument)? If yes, what classes of creditors are preferred?

Generally speaking, tax claims have first priority among unsecured and unsubordinated claims. Claims arising out of certain matters, such as money to be collected by public entities, social insurance premiums, expenses for the common benefit, salaries, funeral expenses and expenses for the supply of daily necessities, have second priority. These two categories of claims would rank equally with, or above, the claims of the debtor's other unsecured and unsubordinated creditors.

11. Are there any consumer protection or similar laws that apply if credit is made available to individuals or other classes of debtor? If yes, what laws are applicable?

In Japan, there are several laws that provide consumer protection. For example, the Money Lending Business Act, the Interest Rate Restriction Act and the Act Regulating the Receipt of Contributions, Receipt of Deposits and Interest Rates (which protects consumers from excessive interest or excessive use of credit).

These laws are based on the principle of territoriality, and their applicability depends on whether the relevant lending business is conducted in Japan. The governing law of the finance documents is not the decisive factor in determining the applicability of these laws.

12. Are there any prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of: (a) its own shares or those of any affiliated company; or (b) assets owned by it or any affiliated company?

In Japan, there is no concept of "financial assistance" as is typically seen in some Western countries. However, the giving of financial assistance by a company may be considered a violation by the directors of the company of the duty of care or duty of loyalty that those directors owe to the company.

If taking security

1. **Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's secured creditors?**

   Yes, certain classes of claims (referred to in the answer to question 10 of the "When lending to borrowers" section) may rank equally with, or have priority over, the debtor's secured obligations.

2. **May security given by a company rank in a specified order so as to secure liabilities owed to different creditors of the company in that order and, if that is not possible, is it viable for parties to enter into a contractual arrangement for the purposes of moderating this order?**

   Regardless of any agreement between secured creditors to the contrary, the general rule is that the priority of security interests held by different secured creditors over the same asset is determined by the date on which those security interests were perfected. Thus, the parties may arrange a subordination of the security interests by perfecting first (i), the senior lenders' security interests and then (ii) the subordinated lenders' security interests. However, some exceptions exist in relation to certain types of security, such as security assignments and security over dematerialized shares as set out below.

   Security assignments (*joto-tanpo)*

   As a security assignment is established by a transfer of the title to the asset, there is a strong argument that multiple security assignments in relation to that asset are theoretically impossible. Therefore, the question of ranking does not arise.

   Dematerialized shares

   Act No. 75 of 2001, as amended ("**Act Concerning Clearance of Bonds and Stocks, etc.**") provides that a pledge over shares can be created by an agreement between the parties and on the transfer of the shares to a pledge sub-account of the pledgee with a custodian (which can be, for example, a security firm or bank). Although not explicitly provided in the Act Concerning Clearance of Bonds and Stocks, etc., a pledge over book-entry stocks is interpreted as being perfected on registration and entry in the pledge section of the pledgee's sub-account. Under this system, syndicated lenders would be expected to hold a joint account in the name of all of the lenders (including subordinated lenders). Therefore, it is generally considered that ranking cannot be established by the timing of the registration only because a single registration applies to all the lenders. An intercreditor agreement is necessary to determine the ranking of the security interests among the senior/subordinated lenders.

3. **Does this jurisdiction recognise the concept of floating security or similar equivalent (i.e., security over a changing pool of assets that the company giving the security is free to buy, sell and generally deal with)?**

   As the concept of floating security is not recognized in Japan in the same way as it is in the US or the UK, security interests in principle, must be granted on an asset-by-asset basis under Japanese law. However, it is possible to create a single security interest over multiple assets in certain cases as follows:

   - First, by way of a security assignment, by creating a single security interest over the following:
   - A changing pool of movable assets located within a specific physical area (typically, inventory in a warehouse)
   - Multiple present and future receivables
   - Second, in the form of a mortgage under the relevant special law (for example, in the case of a factory or plant, Act No. 54 of 1905 ("**Factory Mortgage Act**"), by creating a single security interest over certain types of groups of facilities such as plants or factories, including land, buildings, machinery, tools and other movable/immovable assets (other than inventory) connected to the facility ("**Foundation Mortgage**").

In addition, under Act No. 52 of 1905, as amended ("**Secured Bond Trust Act**"), all assets of the issuer of a bond may be given as security.

On 20 January 2023, the Ministry of Justice published a draft interim report on the reform of collateral legislation. The draft interim report mentions, among other things, a new type of security interest to be created over the whole business of a company. The government's working group will continue the discussion on the more detailed concept and feasibility under the Japanese legal framework of such a whole-business security interest.

4. If so, are there any practical reasons why floating security is difficult to take, maintain or enforce?

There are some difficulties with creating a Foundation Mortgage (referred to in the answer to question 3 of this section). The setting up of a facility foundation in order to create a Foundation Mortgage tends to take more time than if security interests are created over the constituent assets one by one. This is for several reasons, including the requirement to give public notice of the Foundation Mortgage for one month and up to three months if movable assets are included in the facility foundation. In addition, a particular asset to which a third party has a right and a right over real estate (e.g., an ownership right or a lease right) that is not registered cannot be included in the group of assets that are subject to a Foundation Mortgage.

5. May security be granted to a trustee to be held on trust for the lenders from time to time, in such a way that a change of lenders does not require new security to be taken?

Yes, a security trust can be established where a licensed trustee holds the security interest on trust for the benefit of each lender under Article 3 of Act No. 108 of 2006, as amended ("**Trust Act**"). In that case, each secured party will obtain a trust beneficial interest (TBI) representing its interest in the assets of the security trust. If a lender assigns its loan to a third party, the assignor will also assign its related TBI to the assignee without disturbing the security interest, which remains held by the security trustee.

Nevertheless, due to a lack of judicial precedent involving security trustees and the high costs involved in appointing a licensed trustee, security trust structures are uncommon in the market.

6. If not, are there any techniques that can be used to achieve substantially the same effect (e.g., parallel debt structures)?

Parallel debt would theoretically be possible but such structures have not been widely used in Japan to date. However, due to recent amendments, the amended Civil Code of Japan (Act No. 89 of 1896, as amended ("**Civil Code**") now recognizes, among other things, that joint and several claims may be created by agreement among the parties. This change may promote the use of parallel debt structures in the future.

7. If an agent holds security for the lenders rather than a trustee, is it necessary to take new security on a change of lenders? If no, why not? If yes, are there ways to structure the transaction to avoid such a requirement?

The basic principle under Japanese law is that security must be granted to all lenders directly. Therefore, an agent cannot hold security on behalf or for the benefit of a group of lenders. If a secured lender assigns all or any of its rights under a secured loan to a new lender, the security interest will be automatically or contractually (depending on the nature of the security interest) assigned to the assignee, and therefore the assignment will need to be perfected.

The possible alternatives to the use of a security agent are a security trust structure (see the answer to question 5 of this section) and a parallel debt structure (see the answer to question 6 of this section).

8. Under the laws of this jurisdiction, is there any class of asset over which it is difficult or impossible to grant effective and perfected security, or in relation to which any security granted will be of limited effect?

There are some classes of assets over which it is prohibited, or difficult, to create security as set out below.

Nontransferable assets

There are statutory restrictions on the creation of security over certain assets due to their nature or purpose. For example, the creation of security over rights to receive pensions is prohibited under Act No. 141 of 1959, as amended ("**National Pension Act**") and the creation of security over national health insurance is prohibited under Act No. 192 of 1958, as amended ("**National Health Insurance Act**").

In relation to receivables, the debtor and the payee may agree to prohibit the creation of a pledge over, or a transfer of, the receivables. This is commonly achieved by the use of a non-assignment or non-transfer clause. This type of clause prohibits the granting of security over the receivables (or other benefits under the contract) without the consent of the debtor. Please note that, under the recently amended Civil Code, such prohibition of the assignment of receivables cannot be claimed against the assignee of such receivables unless the assignee has actual knowledge of, or was grossly negligent in not being aware of, such prohibition. However, as the lenders are usually aware of (and are expected to investigate) the existence of such non-assignment or non-transfer clauses in the ordinary course of their due diligence, it is still advisable, even under the amended Civil Code, to obtain consent from the debtor of the relevant receivables as to the creation of security interests.

Security over future claims

It is possible to create a pledge or a security assignment of future claims if any receivables that are subject to the pledge or assignment are appropriately specified. This practice is based on the rulings of the Supreme Court regarding the transfer of future claims (Supreme Court judgment of 29 January 1999), and the recently amended Civil Code expressly stipulates that it is possible to transfer and perfect future claims in the same manner as the current claims. However, please note that the court also implied that it may deny the validity of a security interest over future claims if it is contrary to public policy.

Administrative properties

The creation of security over government administrative properties (whether national or local) is prohibited under Act No. 73 of 1948, as amended, ("**National Property Act**") and Act No. 67 of 1947, as amended ("**Local Autonomy Act**").

9. Under the laws of this jurisdiction, are there any restrictions on offshore lenders taking security over any class of asset?

No.

10. Must a company receive a corporate benefit in return for giving a guarantee or security? In particular, are there restrictions on the grant of upstream and cross-stream guarantees and security? If yes, briefly what is the effect of these laws?

In Japan, there is no concept of "corporate benefit" as typically seen in some Western countries. However, if a company gives a guarantee or security, this may be considered a violation by the directors of the company of the duty of care or duty of loyalty that those directors owe to the company if it is not given for the company's benefit, as required under the Civil Code and Act No. 86 of 2005, as amended ("**Companies Act**").

11. What type of security interests does your jurisdiction recognise, e.g., pledge, charge, mortgage, hypothecation? In relation to each type of security interest, please state the formalities required to create and perfect that security.

Security interests are recognized under statutes or by court precedents.

The statutory security interests include mortgages (*teito-ken*), revolving mortgages (*ne-teito-ken*), pledges (*shichi-ken*) and statutory liens (*sakidori-tokken*) on immovable property.

Security interests recognized by court precedents are security interests by way of assignment (*joto-tanpo*) (security assignments), pre-agreed resale transactions (*sai-baibai-no-yoyaku*) and (although not, strictly speaking, a security interest) retention of title agreements (*shoyuuken-ryuuho*).

The methods for the creation and perfection of security interests vary depending on the type of security interest being granted and the type of asset being provided as security as set out below.

Shares

Under the Companies Act, an unlisted company may, in its articles of incorporation, choose whether or not to issue physical share certificates.

Share certificates issued

Where share certificates are issued, a pledge is established by:

- An agreement between the parties; and
- Delivery of the share certificates to the pledgee

The share pledge is perfected by the pledgee's continuous possession of the share certificates.

Share certificates not issued

Where certificates are not issued, a pledge is established by:

- An agreement between the parties; and
- Registration on the shareholders' register maintained by the issuing company (as perfection)

Lenders generally require the issue of share certificates when establishing a pledge over shares to ensure their control over any subsequent transactions in relation to the shares.

Dematerialized shares of a listed company

When transactions involve dematerialized shares of a listed company, transfers of those shares are conducted through a book-entry system maintained by the Japan Securities Depository Center, Inc. (JASDEC). A pledge over dematerialized shares is created by:

- An agreement between the parties; and
- The record of transfer of the shares to the pledge sub-account of the pledgee at the custodian (i.e., JASDEC system participants)

It is perfected by the electronic recording in the books of accounts.

Receivables

Security over receivables can be established by a pledge or a security assignment. In practice, a pledge is generally used for taking security over receivables (e.g., bank deposits, insurance proceeds and intercompany loans). However, a security assignment is commonly used for taking security over trade receivables.

There are three options for perfecting a pledge or a security assignment over receivables:

- Issuing a date-certified notice to the underlying obligor (generally delivered by certified mail);
- Obtaining the date-certified consent of the underlying obligor (date certification is done by a notary public); or
- Registration of the pledge or assignment at the Legal Affairs Bureau

Movable assets

A security assignment of movable assets is established by an agreement between the parties and perfected either by delivery of the movable assets to the secured party or registration of the security assignment at the Legal Affairs Bureau. Physical delivery of the assets is not required if the parties agree that the security provider has delivered the underlying assets but retains them on behalf of the secured parties.

Real estate

A mortgage over real estate is established by an agreement between the parties and, to be perfected, must be registered at the Legal Affairs Bureau that is local to the relevant property. The application for registration is made by both parties to the mortgage, generally through a qualified judicial scrivener acting on behalf of both parties.

Intellectual property

Registration at the Patents Office is required to establish a pledge over trademarks and patents. A pledge over copyright is established by an agreement between the parties and, to be perfected, must be registered at the Agency for Cultural Affairs or the designated registration organization.

12. Are there any registration, translation or notarization requirements in relation to security, guarantees, subordination or intercreditor documents?

A registration tax is imposed depending on the nature of the secured assets. For example, the registration tax for real estate mortgages is 0.4% of the secured obligations (i.e., the principal amount of the loan). To avoid the registration tax, a mortgage may be registered on a provisional basis until a specified event (such as a default) occurs. The provisional registration must be converted to a full registration prior to any enforcement of the mortgage.

Please also see the answer to question 8 of "When lending to borrowers."

13. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in respect of security, guarantees, subordination or intercreditor documents? If yes, what are the amounts and when are they payable?

Mortgage agreements or pledge agreements are generally not subject to stamp duty. However, a nominal stamp duty is payable when security is created over receivables/real estate by way of a security assignment. Guarantees and intercreditor agreements are subject to stamp duty. The amount of stamp duty payable is usually nominal (e.g., JPY 200), unlike a loan agreement, which is subject to a contract amount (to determine the amount of stamp duty payable in relation to a loan agreement as explained in the answer to question 8 of the "When lending to borrowers" section).

If things go wrong

1. Please provide a brief description of the insolvency regime. In particular what rights and duties do unsecured and secured lenders have on the insolvency of a debtor? Are there any other matters of concern?

There are several types of insolvency proceedings in Japan and they are either of a statutory nature or a voluntary nature.

Statutory proceedings

Statutory proceedings are either:

- Winding-up proceedings:
  - Due to bankruptcy
  - By way of a special liquidation
- Restructuring proceedings by way of:
  - Corporate reorganization
  - Civil rehabilitation

Please note that special liquidation and corporate reorganization are only available to stock companies (*Kabushiki Kaisha*). A stock company is a legal entity incorporated to carry out business and raise funds by issuing shares/stock.

Once statutory insolvency proceedings commence, unsecured creditors are not permitted to enforce against, or take security over, property that belongs to the insolvent debtor. In contrast, secured creditors are permitted to enforce their collateral outside those proceedings, except in the case of a corporate reorganization. In the case of a corporate reorganization, the enforcement of security can be restricted by the court (similar to an "automatic stay" under Chapter 11 of the Federal Bankruptcy Act in the US).

However, note that in relation to bankruptcy, corporate reorganization and civil rehabilitation, the debtor may file a petition with the court to seek permission to extinguish a security interest by allowing the debtor (or a trustee) to pay the amount that is equivalent to the value of the collateral. The court is likely to grant permission in particular circumstances. For example, in a bankruptcy situation, where the court finds that it is in the common interest of creditors or in the case of a corporate reorganization or a civil rehabilitation, where the court finds that the collateral is indispensable for the debtor's business. This may affect the lender's right to enforce the collateral at its discretion.

In addition, creditors (including secured creditors) may be subject to interim injunctions (see the answer to question 2 of this section).

Voluntary proceedings

There are several out-of-court processes. One of the most well-used processes is the "Guidelines for the Out-of-Court Workout," in which the debtor's bank makes a reorganization plan. A corporate debtor can also approach a support organization established by the government and banks such as the Resolution and Collection Corporation.

Voluntary insolvency proceedings are based mainly on agreements between the parties and do not bind creditors in the same way as statutory proceedings.

2. Is it possible to obtain a moratorium before insolvency?

Yes, the courts customarily issue stay orders during the period from the filing of the insolvency petition to the issue of the decree to commence insolvency proceedings. In insolvency proceedings, the courts may issue various orders including interim injunctions to preserve the assets, a cease and desist order to stop any enforcement and a comprehensive prohibition order that prohibits the creditors from pursuing pre-injunction claims.

3. When a company is the subject of a formal insolvency procedure, can the company's pre-insolvency transactions be set aside?

If a transaction is deemed to be a preference transaction (e.g., where one or more creditors received a non-pro rata payment from the borrower when those creditors were aware that the borrower was unable to pay its debts as they fell due), the transaction may be voided (and the amount of the payment may be clawed back).

4. When can a lender enforce its security? Can security be enforced out of court following an event of default (or other contractual trigger event), or is a court order required? Are there any restrictions that apply before a lender may enforce its security?

A lender can enforce its security out of court by completing certain steps if an obligor has not performed its obligations by the due date (either the original due date or an accelerated due date).

A lender can exercise its rights by disposing of the collateral, through a court auction or by voluntary sale, subject to certain restrictions (see the answers to questions 1 and 2 of this section).

Court proceedings are not a popular method for the enforcement of security as they generally take six to 12 months to complete and usually result in large discounts. Importantly, court proceedings are not appropriate where a lender requires some measure of control over who acquires the secured assets. Furthermore, court auction bids must be denominated in Japanese yen. Voluntary sales, on the other hand, may be denominated in currencies other than Japanese yen.

5. Do any limitation periods apply in relation to bringing an action to enforce security?

No.

6. Is there any particular way in which secured assets must be liquidated on enforcement (e.g., by auction or court sale)?

Please see the answer to question 4 of this section.

7. Are there any particular legal or practical difficulties or delays in enforcing security?

Please see the answers to questions 1 and 2 of this section for the restrictions in the case of insolvency proceedings. Please see the answer to question 4 of this section for the downside of court sales.

8. In relation to enforcement, are there any specific requirements to be borne in mind if the lender is a foreign entity?

No. However, where the security is located in Japan, the governing law in relation to a right to the security, including in relation to creation, perfection and execution of the security, is Japanese law, irrespective of its wording, under Act No. 78 of 2006, as amended ("Act on General Rules for Application").

9. Is there any reason why you think that arbitration rather than litigation might be advantageous in resolving disputes under the finance documents, and if so, why? Please outline the relative merits of arbitration and litigation, including the ease of enforcement of foreign judgments and foreign awards from different jurisdictions. Is it possible to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit?

Arbitration has both benefits and drawbacks when compared to litigation.

Japan is a member of the New York Convention and has a sophisticated arbitration law (Act No. 138 of 2003) based on the UNCITRAL Model Act on International Commercial Arbitration. Therefore, it can generally be said that a foreign arbitration award is easier to enforce in Japan than a foreign judgment because the enforcement of a foreign judgment is subject to several conditions including reciprocity, as provided under the Code of Civil Procedure (Act No. 109 of 2006).

There are several other benefits of arbitration including confidentiality and flexibility.

Generally, arbitral proceedings are confidential by default and so they are very suitable for highly sensitive matters. Parties are free to select the arbitrator (for example, an arbitrator with specific skills) and the language of the proceedings, whereas in litigation, cases are randomly assigned to judges within a district (with some exceptions) and all hearings must be in Japanese.

However, there are some drawbacks in relation to arbitration. Arbitration procedures do not permit an appeal to be lodged. Therefore, even if the result of an arbitration or an arbitration award is not satisfactory to a party, it cannot file an appeal against the result or an objection against the arbitration award.

In addition, sometimes arbitration awards may be unreasonably complicated whereas the lenders may expect a simple decision to order the obligor to pay the amount owed.

Although still not very common in the domestic market, a hybrid enforcement provision could be recognized as valid because the principle of party autonomy is generally upheld under Japanese law. However, note that the enforceability of an agreement (including an arbitration clause) is generally subject to the determination of the courts of Japan, which must consider the good order and moral doctrine, the abuse of rights doctrine and Japanese public policy. There is little guidance in Japanese law or reported decisions of the Japanese courts that assists in determining the scope of these concepts, especially in connection with the hybrid enforcement provision.

10. Are asymmetrical jurisdiction clauses enforceable? (By this we mean clauses that allow the lenders, but not the borrowers, to make certain choices in relation to choice of jurisdiction and how to litigate. These types of clauses allow the lenders, but not the borrowers, to commence proceedings in any court they choose, but restrict the borrowers to commencing proceedings in one jurisdiction only. This may also allow the lenders, but not the borrowers, to choose whether to litigate the finance documents before a court or to submit to arbitration in relation to them, but restrict the borrowers to either litigation or arbitration, as specified in the agreement).

There is no judicial view in relation to whether asymmetrical jurisdiction clauses are valid in Japan. Therefore there are risks that an asymmetrical jurisdiction clause may be considered void if it is found contrary to Japanese morality or public policy.

Working digitally

1. **Is it possible for documents to be executed electronically (whether by the manual insertion of a digital signature or the use of an e-signing platform) under the laws of this jurisdiction? If so, is this limited to only particular types of finance documents?**

   Yes, it is generally possible to execute documents electronically because no statutory law or regulation prohibits adopting a digital signature or using an e-signature platform when executing documents in Japan. However, note that the evidential value thereof may still be an issue.

   This has been addressed under the Act on Electronic Signatures and Certification Business (Denshi Shomei oyobi Ninshou Gyoumu ni kansuru Houritsu, Act No. 102 of 2000 ("**E-Signature Act**"). The electronic signature will be recognized under the E-Signature Act as constituting prima facie evidence of the execution of the relevant document when an electronic signature on electronic documents satisfies the following requirements:

   - It is technically designed to indicate that the electronically signed contract has been created by the person who affixed the e-signature.
   - It is technically designed to detect any alteration that is made to the electronically signed contract.
   - It is affixed by a party to the contract by using a unique code and device that is possessed exclusively by that party.

2. **Where the witnessing of a signing is contemplated, is it possible for the witness to verify the signature over a live video call?**

   Under Japanese law, there is no requirement for signatures to be witnessed when executing documents.

3. **Is it possible to register/perfect security electronically without wet ink signatures?**

   In forms of registry at the Legal Affairs Bureau for the purpose of perfection of mortgage or other security over real estate, for example, it is possible to register/perfect security electronically. However, the relevant e-signature must be made with one of the e-signature platforms provided by one of the few service providers listed as permissible by the Ministry of Justice of Japan. Where the relevant parties cannot use the listed e-signature platforms, wet ink signatures will still be required. Furthermore, where an application to register a mortgage is submitted by a judicial scrivener, wet ink signatures will be required for some of the application documents.

4. **Are there any other legal restrictions that may prevent the parties from executing a finance transaction electronically?**

   No.

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MALAYSIA

Malaysia

When considering whether to lend

1. Is it necessary or advisable for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in this jurisdiction: (a) by reason only of its execution, delivery or performance of the finance documents; or (b) to enable it to enforce its rights under the finance documents?

Two parallel banking systems operate in Malaysia: the conventional banking system and the Islamic banking system. The Malaysian Financial Services Act 2013 (FSA) regulates, among other things, the conventional banking industry in Malaysia. Under the FSA, the conduct of a banking business requires a license.

The expression "banking business" is defined as:

a. The business of:

  i. Accepting deposits on a current account, deposit account, savings account or other similar account.

  ii. Paying or collecting checks drawn by or paid in by customers.

  iii. The provision of finance.

b. Such other business as Bank Negara Malaysia (BNM), the central bank of Malaysia, may prescribe.

For an entity to be deemed to be carrying on "banking business," it must be carrying out all three of the activities listed in (a) (i), (ii) and (iii) above.

It is not necessary for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in Malaysia by reason only of its execution, delivery or performance of the finance documents or to enable it to enforce its rights under the finance documents as those acts would only relate to one subparagraph and not all three.

The Malaysian Moneylenders Act 1951 (MLA) regulates the business of moneylending carried on by entities that are not licensed under the FSA. The MLA is relevant to foreign/nonresident unlicensed lenders that undertake the role of a moneylender in Malaysia. Under the MLA, a moneylender is any person who lends a sum of money to a borrower in consideration of a larger sum being repaid to them (i.e., the principal plus interest). Section 5 of the MLA stipulates that no person shall conduct business as a moneylender unless they are licensed under the MLA. Section 15 of the MLA operates to render any contract by an unlicensed moneylender unenforceable.

2. Will any lender, arranger, facility agent or security agent be deemed to be resident, domiciled, carrying on business or subject to tax by reason only of the execution, delivery, performance or enforcement of the finance documents?

No, except that the Malaysian-sourced fees and other income may be subject to withholding tax.

3. Are there any regulatory reporting requirements that lenders must observe in connection with those transactions?

Under the Foreign Exchange Notices issued by BNM ("**FE Notices**"), there are prohibitions on foreign lenders lending to Malaysian residents.

The exchange control regime in Malaysia is governed by the FSA and is supplemented by the FE Notices. Certain foreign loan transactions may fall within the prohibitions set out in the FE Notices and those prohibited transactions cannot be undertaken unless prior written approval from BNM has been obtained. Depending on the nature of the financing transactions (foreign currency borrowings or the provision of a financial guarantee/ security) involving a nonresident, the prior written approval of BNM may be required.

4. Is it necessary to establish a place of business in your jurisdiction in order to enforce any provision of the finance documents?

No.

5. Is a foreign bank/financial institution permitted to approach local entities for business?

Yes, although the prior written approval of BNM is required under the FSA for:

- Acts, among others, of issuing, publishing or disseminating information in any form or advertisements which may lead, directly or indirectly, to the buying, selling, exchanging, borrowing or lending of foreign currency.
- The giving or obtaining of any guarantee, indemnity or undertaking in respect of any debt, obligation or liability.
- Acting on behalf of an unlicensed foreign institution to carry on, among other things, banking business in Malaysia (for the meaning of banking business see the answer to question 1 of this section).

In addition, the FSA prohibits any person from holding themselves out as an authorized person or registered person under the FSA unless authorized or registered under the FSA (as the case may be).

When lending to borrowers

1. Are there any restrictions in relation to the type of borrower who may borrow foreign currency or in relation to the term of foreign currency and/or the amount of foreign currency borrowed by local entities?

Yes. A resident individual, sole proprietor or general partnership is permitted to borrow in foreign currency up to MYR 10 million equivalent in aggregate from a licensed onshore bank or a nonresident, with the sole exception of an immediate family member. The MYR 10 million threshold is computed based on an aggregate of borrowing in foreign currency by the resident individual, sole proprietor or a general partnership owned by the resident individual.

A resident entity is permitted to borrow foreign currency on the following basis:

a. Any amount from a licensed onshore bank.

b. Any amount from resident or nonresident entities within its group of entities.

c. Any amount from its resident or nonresident direct shareholder.

d. Any amount through the issue of foreign currency corporate bond or sukuk to another resident.

e. Up to the MYR 100 million equivalent in aggregate from nonresidents (including a nonresident financial institution and a non-resident special purpose vehicle which is used to obtain borrowing from any person outside the resident entity's group of entities); the MYR 100 million threshold is computed based on an aggregate of borrowing in foreign currency by the resident entity and other resident entity with a parent-subsidiary relationship.

Paragraphs (b) and (c) above do not apply to borrowings in foreign currency by a resident entity from a nonresident financial institution or a nonresident special purpose vehicle that is set up to obtain borrowings from any person who is not part of the resident entity's group of entities.

2. Are there any restrictions on the rate of interest or default interest that may be charged?

No, except as follows:

- Exceptions apply in relation to loans to individuals (see the answer to question 11 of this section).
- BNM has issued guidelines to regulate the charging of default interest. These guidelines are only applicable to financial institutions/entities licensed in Malaysia.

3. Are there any restrictions on particular lenders or classes of lender entering into credit transactions with borrowers?

Yes, a resident borrower may only borrow foreign currency in excess of the relevant threshold applicable to such resident borrower (see the answer to question 1 of this section) if it receives the prior written approval of BNM.

4. Are there any exchange controls that will apply to payments to be made in foreign currencies or to foreign lenders?

Yes, although they do not apply if the payments are related to transactions that are permitted under the FE Notices or related to transactions that have been approved by BNM.

In relation to payments in foreign currency to be made to or by a nonresident foreign lender, a resident is generally allowed to make or receive payments for any purpose, **excluding** payment made for:

- A foreign currency-denominated derivative offered by the resident, unless it is allowed under the FE Notices or it has been approved in writing by BNM.
- Any derivative offered by any nonresident which market price, value, delivery or payment obligation is derived from, referenced to or based on exchange rate, unless it is allowed under the FE Notices or it has been approved in writing by BNM.
- A derivative which is referenced to Malaysian ringgit, unless it is allowed under the FE Notices or it has been approved in writing by BNM.

5. Is there any requirement to deduct or withhold tax from any amounts to be paid or repaid to a lender (whether domestic or foreign)? If so, at what rate must tax be deducted and from what kinds of payment?

Withholding tax is deducted from gross interest income derived from Malaysia and payable to a nonresident lender. The Malaysian domestic withholding tax rate of 15% applies to interest paid to a nonresident, but it may be reduced under double taxation treaties.

6. Are there any "thin capitalization" or other rules that may limit the extent to which interest payments may be deducted for tax purposes?

There are currently no specific thin capitalization rules in Malaysia. However, the Malaysian income tax legislation provides that the Director General of Inland Revenue may disallow an interest deduction if they are of the opinion that the financial assistance granted by a person to an associated person who is a resident is excessive in relation to the fixed capital of that person.

7. Are there any registration, notarization, translation or reporting requirements in relation to the loan documents?

Please see the answers to questions 11, 12 and 13 of the section "If taking security".

8. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to the loan documents? If yes, what are the amounts and when are they payable?

Stamp duty is payable on a loan document within 30 days of the date of its execution (if it is executed within Malaysia) or within 30 days of the loan document being first received in Malaysia (if it is executed outside Malaysia).

With respect to loans denominated in Malaysian ringgit, stamp duty is payable on the principal instrument (typically the facility agreement) at the rate of 0.5% of the loan amount.

With respect to loans denominated in a foreign currency, stamp duty is payable on the principal instrument (typically the facility agreement) at the rate of 0.5% of the loan amount (calculated based on the Ringgit-equivalent amount).*

For stamp duty payable on security documents, please see the answer to question 13 of the section "If taking security."

*Updated after 1 January 2024

9. Does the law recognize the subordination of the debt that a debtor owes to one creditor to that which the debtor owes to another creditor? If yes, how is this usually effected?

Yes, this is legally valid as a matter of Malaysian contract law. In practice, this is most commonly achieved by an intercreditor or subordination agreement between the different classes of creditors and the debtor.

10. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors (e.g., the claims of employees and tax authorities or the claims of creditors under particular kinds of instrument)? If yes, what classes of creditors are preferred?

Yes. The order of payment of those claims is set out in the final two paragraphs of question 1 of the section "If things go wrong".

11. Are there any consumer protection or similar laws that apply if credit is made available to individuals or other classes of debtor? If yes, what laws are applicable?

The Malaysian Consumer Protection Act 1999 (MCPA) does not apply to "professionals who are regulated by any written law." Although "professionals" is not defined in the MCPA, taking the purposive approach would suggest that foreign banks do not fall within the ambit of the MCPA.

Under the Moneylenders Act 1951, interest rates on loans extended to individual borrowers by moneylenders are capped at 12% per annum for secured loans and 18% per annum for unsecured loans. Further, under that Moneylenders Act 1951, the regulator may stipulate further restrictions, as they may think fit, in the license conditions applicable to moneylenders at any time during the duration of the license.

12. Are there any prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of: (a) its own shares or those of any affiliated company; or (b) assets owned by it or any affiliated company?

Yes. Under the Malaysian Companies Act 2016 (MCA), there is a prohibition in relation to a company giving financial assistance for the purchase of its own shares or the shares of its holding company. However, there are four exceptions to this general prohibition:

- Where the loan is given in the ordinary course of a company's business.
- Where the company provides money for the purchase of, or subscription for, fully paid shares in the company or its holding company, by trustees of, or to be held by or for the benefit of, employees of the company or a subsidiary of the company, including any director holding a salaried employment or office in the company or a subsidiary of the company.

- The giving of financial assistance by a company to persons, other than directors, bona fide in the employment of the company or of a subsidiary of the company with a view to enabling those persons to purchase fully paid shares in the company or its holding company to be held by them beneficially.
- The making of a loan or the giving of guarantee or the provision of security in connection with one or more loans made by one or more other persons by a company in the ordinary course of business where the activities of that company are regulated by any written law relating to banking, insurance or takaful or which are subject to the supervision of the Securities Commission and where:
  - The lending of the money or the giving of guarantees or the provision of security in connection with loans made by other persons is done in the course of those activities.
  - The loan that is made by the company or where the guarantee is given or the security is provided in respect of a loan, is made on ordinary commercial terms in relation to the rate of interest or returns, the terms of repayment of principal and the payment of the interest or returns.

Notwithstanding the foregoing, the MCA provides for a financial assistance whitewash procedure. Private and public companies (but not public listed companies) may give financial assistance for the purpose of either:

- Acquisition of their shares or their holding company's shares; or
- Reducing or discharging liability incurred for such an acquisition,

if the following requirements are met:

- A special resolution is passed by shareholders to approve the financial assistance.
- A majority of the directors of the company agree that the company may give the financial assistance, that the giving of the financial assistance is in the best interest of the company, and that the terms and conditions pursuant to the financial assistance are just and reasonable to the company.
- Each director who voted in favor of the financial assistance makes a solvency statement (similar to the statement made for a reduction of capital)
- The aggregate amount of the financial assistance (including financial assistance previously given that has not been repaid) does not exceed 10 percent of the company's current shareholding funds.
- The company received fair value in connection with the giving of the financial assistance.
- The financial assistance is given not more than 12 months after the day the solvency statement was made by the directors.

The solvency statement must be sent to each member of the company within 14 days from the giving of the financial assistance, together with a notice stipulating details of the financial assistance given as set out under the MCA.

The prohibition in relation to a company giving financial assistance does not apply in relation to the purchase of assets owned by it or any affiliated company.

If taking security

1. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's secured creditors?

No.

2. **May security given by a company rank in a specified order so as to secure liabilities owed to different creditors of the company in that order and, if that is not possible, is it viable for parties to enter into a contractual arrangement for the purposes of moderating this order?**

   Yes, this is possible through the execution of an intercreditor agreement specifying the priority and ranking arrangements.

3. **Does this jurisdiction recognise the concept of floating security or similar equivalent (i.e., security over a changing pool of assets that the company giving the security is free to buy, sell and generally deal with)?**

   Yes, a floating charge can be created over any assets of a company. This is usually created over current assets, such as a company's stock-in-trade or book debts. The security is usually conferred under a debenture containing a fixed charge and a floating charge together covering all the available assets of the company.

4. **If so, are there any practical reasons why floating security is difficult to take, maintain or enforce?**

   No.

5. **May security be granted to a trustee to be held on trust for the lenders from time to time, in such a way that a change of lenders does not require new security to be taken?**

   Yes.

6. **If not, are there any techniques that can be used to achieve substantially the same effect (e.g., parallel debt structures)?**

   Not applicable, as a trustee may be appointed.

7. **If an agent holds security for the lenders rather than a trustee, is it necessary to take new security on a change of lenders? If no, why not? If yes, are there ways to structure the transaction to avoid such a requirement?**

   Not applicable, as a trustee may be appointed.

8. **Under the laws of this jurisdiction, is there any class of asset over which it is difficult or impossible to grant effective and perfected security, or in relation to which any security granted will be of limited effect?**

   Although it is possible to take security over intellectual property rights such as trademarks and patents, there is currently no official register in the intellectual property registries that records those security interests. Therefore, there is no system that enables the giving of notice of the security interests to third parties who could be potential buyers of those intellectual property rights.

9. **Under the laws of this jurisdiction, are there any restrictions on offshore lenders taking security over any class of asset?**

   Pursuant to the FE Notices, a resident (which is not a bank) is allowed to give a financial guarantee (in any amount in Malaysian ringgit or in foreign currency) to secure a borrowing obtained by a nonresident except for a financial guarantee given to secure a borrowing:

   a. Obtained by a nonresident borrower that is a special purpose vehicle, or if the underlying borrowing is being utilized by the resident guarantor; or

   b. Where the resident has entered into a formal or informal arrangement to make the repayment of the borrowing in foreign currency other than pursuant to a call-upon of the financial guarantee in the event of default

   The prior written approval of BNM is required for any of the circumstances described in paragraphs (a) or (b) above.

10. Must a company receive a corporate benefit in return for giving a guarantee or security? In particular, are there restrictions on the grant of upstream and cross-stream guarantees and security? If yes, briefly what is the effect of these laws?

Yes, a company must receive a corporate benefit in return for any transaction. It does not need to be a monetary benefit. The test is whether the directors exercise their discretion to enter into a guarantee or security agreement in the best interests of the company.

Ultimately, it is a question of fact in relation to whether a transaction has commercial benefit for a company. Under the MCA, the directors are statutorily required to exercise their discretion and powers in the best interests of the company with reasonable care, skill and diligence. If the transaction is found not to have a commercial benefit for the company, this does not affect the validity of the security but there will be consequences for the directors for acting improperly.

11. What type of security interests does your jurisdiction recognise, e.g., pledge, charge, mortgage, hypothecation? In relation to each type of security interest, please state the formalities required to create and perfect that security.

Mortgage or charge

An individual or company may grant a mortgage or charge over its assets. If a company creates the mortgage or charge, it must be registered within 30 days of the date of its creation.

In addition, depending on the subject matter of the security interest, further registrations must be effected at certain state agencies.

For further details of the registration requirements, see the answer to question 12 of this section.

Assignment

An individual or company may grant an assignment of its rights. Under the Malaysian Civil Law Act 1956, a legal assignment must be an absolute assignment of all rights made in writing and an express written notice of the assignment must be served on the counterparty from whom the assignor would have been entitled to enforce a right or receive or claim a debt. As a matter of practice, there is no need for a separate acknowledgment by the contractual counterparty; however, in Malaysia, it is commonly procured to ensure that the contractual counterparty has full knowledge of the assignment.

12. Are there any registration, translation or notarization requirements in relation to security, guarantees, subordination or intercreditor documents?

Generally, under the FE Notices, the provision of financial guarantee is allowed for types of borrowing which are approved in the FE Notices or otherwise approved in writing by BNM. It is therefore important to consider whether the underlying borrowing is approved in the FE Notices or requires prior written approval of BNM.

In addition, the following registration requirements apply to security interests created under Malaysian law.

Registrable charge

If a company incorporated under the MCA creates a security and if the security is registrable under the MCA, it must be registered with the Companies Commission of Malaysia (CCM) within 30 days of its creation. A prescribed filing fee is payable to the CCM.

A failure to register a registrable charge with the CCM within the prescribed period will result in the charge being void against the liquidator and any other creditors of that company, so that on a liquidation of that company the liquidator can deal with the charged property disregarding any interest that the charge purports to have given to the chargee. Failure to register a registrable charge may also affect the priority of the chargee's claim.

Similar requirements apply to a company incorporated under the Malaysian Labuan Companies Act 1990. Registration with the Labuan Financial Services Authority must occur within 30 days of the creation of the security.

Power of attorney

Where a security document involves the granting of a power of attorney, in order for that security document to be valid, authentication of the power of attorney must follow the prescribed procedure under the Malaysian Power of Attorney Act 1949 and a stamped copy of the power of attorney must be deposited with the High Court of Malaysia for registration purposes.

Legal land charge

Where a legal land charge is created, it must be registered with the relevant land registries. The registration fees payable to the land registries vary from one state to another.

The land charge document must be presented for registration within three months from its date. If it is not presented for registration within the three-month period, a penalty will be imposed. The penalty payable varies from one state to another.

Translation

There is no requirement for the documents to be translated into Malay (the national language).

13. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in respect of security, guarantees, subordination or intercreditor documents? If yes, what are the amounts and when are they payable?

Provided that the full amount of stamp duty due has been paid on the principal instrument (see the answer to question 8 of the section "When lending to borrowers"), a security document, guarantee, subordination agreement and intercreditor agreement would each be deemed to be a subsidiary instrument and would only be subject to a nominal stamp duty of MYR 10.

If things go wrong

1. Please provide a brief description of the insolvency regime. In particular what rights and duties do unsecured and secured lenders have on the insolvency of a debtor? Are there any other matters of concern?

Brief description of the insolvency regime in Malaysia

An insolvent company incorporated under the Malaysian Companies Act 2016 (MCA) may either be wound up by an order of the court or by its members or creditors.

Set out below briefly are the processes for a court winding up, a members' winding up and a creditors' winding up in relation to an insolvent company incorporated under the MCA:

Court winding up	The company itself, a member, liquidator or creditor of the company, or any other interested party can make an application for the compulsory winding up of a company. One of the most common grounds for a compulsory winding up is where the court finds that the company is unable to pay its debts. On hearing the application, if appropriate, the court may grant the winding up order. The appointed liquidator will provide a report on the company's affairs as soon as practicable after the appointment.
Members' voluntary winding up	A members' voluntary winding up takes place where the company is solvent, but the company resolved by special resolution to wind up the company voluntarily and appoint a liquidator during the members' meeting. Before the members' meeting, the directors of the company are required to make a statutory declaration that they have made an inquiry into the affairs of the company and, at the directors' meeting, formed an opinion that the company will be able to pay its debts in full within the period of 12 months after the commencement of the winding up. A declaration of solvency, together with the statement of affairs of the company, is lodged with the CCM.
Creditors' voluntary winding up	A creditors' voluntary winding up takes place where the company is insolvent and the company resolved by special resolution to wind up the company voluntarily and nominate a liquidator during the members' meeting. The liquidator will be appointed at the creditors' meeting. Before the members' and creditors' meetings, the directors of the company are required to make a statutory declaration that the company, by reason of its debts and liabilities, cannot continue its business and to appoint an interim liquidator. Both the members' and creditors' meetings must be summoned within one month of the date of the declaration. The statutory declaration in relation to the inability of the company to continue business is lodged with the CCM.

In the case of a court winding up, an official receiver or interim liquidator (used interchangeably) will be appointed by the court if the petitioners do not wish to appoint a liquidator. Alternatively, the petitioners may engage a private liquidator and, if so, the petitioners are usually obliged to provide a salary or remuneration to the private liquidator before they will agree to act. The private liquidator will usually draw their fees from the assets of the company and, in the absence of any assets, the petitioners will bear those fees. Once the liquidator is engaged or appointed (including an interim liquidator), they will take all the property to which the company is or appears to be entitled into their custody or under their control.

All of the company's property and assets are vested in either the liquidator (for a voluntary winding up) or the Director General of Insolvency of Malaysia under the capacity of an Official Receiver (for a compulsory winding up). They will be distributed in an equitable way among its creditors according to their respective rights. These creditors will be paid in the following order of priority:

- Secured creditors
- Preferential unsecured creditors (as specified in this answer below in relation to unsecured creditors)
- Other unsecured creditors

Nevertheless, unsecured debts in the same class (also see below) shall rank pari passu and shall be paid in full, unless the property of the company is insufficient to meet the debts, in which case the payment shall be reduced and the rate of reduction shall be in equal proportion. Therefore, all creditors are required to prove their debts.

Note that a contributory (which includes past and present members) is not personally liable in relation to payment of the company's debts. However, the liquidator has the power to direct the contributory to pay the amount, if any, unpaid on the issue price of its shares.

Rights of secured creditors on the insolvency of a company

The rights of secured creditors are highly dependent on the terms of the facilities (or other) agreement and the security documents that they have entered into with the company. The secured lenders will take first priority over the secured assets in the insolvency of the company. If there is more than one secured creditor with security over the same asset of the company, the first in time will take precedence (subject to registration where necessary).

If there is a shortfall, the secured creditor should file a proof of debt in relation to the amount owing that has not been repaid from the realization of the secured asset. In those circumstances, the status of the secured creditor will be changed to an unsecured creditor in relation to the amount owing that has not been repaid from the realization of the secured asset (see below). However, on the other hand, if after the realization of the secured asset there is a surplus after the repayment of the amount owing to the secured creditor, the secured creditor must give the remaining proceeds to the liquidator. These remaining proceeds will become part of the company's estate.

Rights of unsecured creditors on the insolvency of a company

Under the MCA, the payment of unsecured debts on the insolvency of a company occurs in the following descending order of priority:

i. The costs and expenses of the winding-up, including the taxed costs payable to a petitioner, the remuneration of the liquidator and the costs of any audit carried out.

ii. All wages and salaries, whether or not earned wholly or in part by way of commission, including any amount payable by way of allowance under any contract of employment or award or agreement regulating conditions of employment of any employee not exceeding MYR 15,000 or such other amount as may be prescribed from time to time whether in relation to time or for piecework in respect of services rendered by them to the company within a period of four months before the commencement of the winding-up.

iii. All amounts due in respect of worker's compensation under any written law relating to worker's compensation accrued before the commencement of the winding-up.

iv. All remuneration payable to any employee in respect of vacation leave, or in the case of their death to any other person in their place, accrued in respect of any period before the commencement of the winding-up.

v. All amounts due in respect of contributions payable during the 12 months immediately before the commencement of the winding-up by the company as the employer of any person under any written law relating to employees' social security contributions and superannuation or provident funds or under any scheme of superannuation or retirement benefit that is an approved scheme under the federal law relating to income tax.

vi. The amount of all federal tax assessed under any written law before the date of the commencement of the winding-up or assessed at any time before the time fixed for the proving of debts has expired.

Other unsecured creditors will be paid only after those listed in paragraphs (i) to (vi) above have been paid.

2. Is it possible to obtain a moratorium before insolvency?

Yes, there is a procedure under the MCA that enables a company to enter into a moratorium by way of an application to the court before insolvency. The court may agree to a moratorium (subject to any alterations or conditions as it thinks just) where a compromise or arrangement is proposed between the company and its creditors that aims to keep the company afloat. The court order will be binding on all creditors.

3. When a company is the subject of a formal insolvency procedure, can the company's pre-insolvency transactions be set aside?

Yes, the following pre-insolvency transactions can be set aside:

- An undue preference, being a transaction between the company and a creditor, or any person on trust for any creditor, where the creditor obtains a preference, priority or advantage over other creditors in the winding-up, unless the transfer or conveyance of the property was made for valuable consideration and without any actual notice of that undue preference.
- Any transfer or assignment by a company of all its property to the trustees for the benefit of all its creditors.
- Any sale at an undervalue or an acquisition at an overvalue of property, business or undertaking for cash consideration where the counterparty is a director or a company with the same director.
- Onerous contracts, such as any estate or interest in land that is burdened with onerous covenants, shares in corporations and unprofitable contracts that may be disclaimed by the liquidator with leave of the court or the committee of inspection.
- A floating charge created within six months of the commencement of the winding-up, which will be invalid unless it is proved that the company was solvent immediately after the creation of the charge, except in relation to the amount of cash paid to the company at the time or following the creation of, and in consideration of, the charge together with 5% interest per annum.

4. When can a lender enforce its security? Can security be enforced out of court following an event of default (or other contractual trigger event), or is a court order required? Are there any restrictions that apply before a lender may enforce its security?

Rights of enforcement of security are contractual in nature and, therefore, depend on the terms of the relevant security documents.

In the case of the enforcement of security over land, an application to the court for an order for sale (which is a lengthy and highly administrative procedure) is required.

Depending on the provisions of the security documents, a lender may also have the right to appoint a receiver and manager to act within the scope of the provisions set out in the security documents (typically a debenture) by carrying on the trade or business arising from the secured assets.

A receiver or receiver and manager shall have the powers and authorities expressly and impliedly conferred by the instrument or by the order of the court, by or under which the appointment was made. A minimum list of powers of a receiver or a receiver and manager is now statutorily codified in the Sixth Schedule of the MCA.

5. Do any limitation periods apply in relation to bringing an action to enforce security?

Yes. The statutory limitation period for a contractual claim is six years from the accrual of the cause of action. In most instances, time starts to run from the date of the infringement of the contract or the default in payment.

Having obtained judgment, a successful claimant has 12 years from the date of the judgment to enforce it, but it should be noted that enforcement proceedings taken after six years from the date of judgment require the leave of the court.

6. Is there any particular way in which secured assets must be liquidated on enforcement (e.g., by auction or court sale)?

No.

7. Are there any particular legal or practical difficulties or delays in enforcing security?

No.

8. In relation to enforcement, are there any specific requirements to be borne in mind if the lender is a foreign entity?

No.

9. Is there any reason why you think that arbitration rather than litigation might be advantageous in resolving disputes under the finance documents, and if so, why? Please outline the relative merits of arbitration and litigation, including the ease of enforcement of foreign judgments and foreign awards from different jurisdictions. Is it possible to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit?

There are, of course, many different arbitration regimes, but generally, in contrast to litigation, arbitration is a quicker process that mostly deals with commercial decisions and technical disputes, e.g., when the quantum of the claim is challenged. Furthermore, by design, the arbitration process is less formal than traditional courtroom litigation (which tends to be more adversarial in nature). If a lender wishes to have a continuing relationship with a borrower, the lender may therefore prefer arbitration. Furthermore, to preserve its goodwill and reputation, in some circumstances, a lender may prefer arbitration, which is held in private rather than in open court.

Under the Malaysian Reciprocal Enforcement of Judgments Act 1958 (REJA), a foreign judgment may be enforceable in Malaysia if it is of a court in a country that is listed in the First Schedule to the REJA and registered under the REJA. A Malaysian court may register a foreign judgment provided that it is satisfied that the Malaysian court rendering the judgment has jurisdiction over the subject matter; that the judgment is not obtained by fraud or contrary to the public policy of Malaysia; and that the defendant was duly served and given the opportunity to defend the action in the foreign courts.

If a foreign judgment is not within the ambit of the REJA, the only method of enforcing it in Malaysia is at common law. The foreign creditor will need to sue on the judgment in the local Malaysian courts as an action in debt.

It is possible to have a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit. However, this may create another dispute as to which is the most suitable dispute resolution avenue.

10. Are asymmetrical jurisdiction clauses enforceable? (By this we mean clauses that allow the lenders, but not the borrowers, to make certain choices in relation to choice of jurisdiction and how to litigate. These types of clauses allow the lenders, but not the borrowers, to commence proceedings in any court they choose, but restrict the borrowers to commencing proceedings in one jurisdiction only. This may also allow the lenders, but not the borrowers, to choose whether to litigate the finance documents before a court or to submit to arbitration in relation to them, but restrict the borrowers to either litigation or arbitration, as specified in the agreement).

This issue has not yet come before the courts.

Working digitally

1. **Is it possible for documents to be executed electronically (whether by the manual insertion of a digital signature or the use of an e-signing platform) under the laws of this jurisdiction? If so, is this limited to only particular types of finance documents?**

   The execution of documents by way of an electronic signature (or e-signature) is recognized under the Electronic Commerce Act 2006 (ECA). An "electronic signature" means any letter, character, number, sound or any other symbol or any combination thereof created in an electronic form adopted by a person as a signature. Subject to the fulfillment of the conditions specified in the ECA, the electronic signature will be legally enforceable.

   However, the ECA does not apply to certain documents, including:

   - Power of attorney (which would be contained in most of the security documents).
   - Documents for creation of trusts.

   While electronically signed documents are legally enforceable under the ECA, other practical issues need to be considered, such as issues in respect of the stamping of such documents (which would affect the admissibility of the documents as evidence in court) and the authenticity of the electronic signature.

2. **Where the witnessing of a signing is contemplated, is it possible for the witness to verify the signature over a live video call?**

   There is no legal provision that expressly recognizes the use of a live video call to witness the execution of documents. In July 2022, the Malaysian Bar Council has approved and adopted a new ruling setting out the conditions for virtual or remote witnessing of execution of a document by solicitors, provided that physical presence is not required or prescribed under any written law.

3. **Is it possible to register/perfect security electronically without wet ink signatures?**

   No. Most of the relevant authorities/state agencies still require wet ink signatures.

4. **Are there any other legal restrictions that may prevent the parties from executing a finance transaction electronically?**

   No. However, parties who would like to execute a finance transaction electronically are encouraged to seek legal advice to ensure that the then requirements are fulfilled.

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PHILIPPINES

Philippines

When considering whether to lend

1. Is it necessary or advisable for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in this jurisdiction: (a) by reason only of its execution, delivery or performance of the finance documents; or (b) to enable it to enforce its rights under the finance documents?

Execution, delivery and performance of the finance documents

Based on Philippine Supreme Court decisions and Securities and Exchange Commission (SEC) opinions, arguably, a foreign lender, arranger, facility agent or security agent is not required to obtain a license from the SEC by reason solely of its execution, delivery or performance of finance documents, provided that the finance documents relate to a single or isolated transaction and there is no purpose or intention to do any other business within the country.

As a rule, a foreign corporation is required to obtain a license from the SEC if the activities that the foreign corporation intends to carry out will constitute the foreign corporation doing business in the Philippines. On the other hand, if the activities that the foreign corporation intends to undertake do not constitute doing business in the Philippines, the foreign corporation is not required to obtain a license from the SEC.

There is no exclusive list of activities that constitute doing business in the Philippines. However, the Foreign Investments Act and its implementing rules provide for a nonexclusive enumeration of specific activities that constitute doing business in the Philippines[1].

The Philippine Supreme Court has ruled that a foreign corporation is not deemed to be doing business if its commercial dealing is limited to a single agreement or is isolated or is an occasional transaction and indicates no element of continuity of conduct in that respect. Further, the SEC has opined that a foreign corporation is not doing business by lending money to a Philippine resident, where the loan is merely incidental to, and not a substantial part of, its corporate business, or where the loan is made offshore. Hence, if the execution, delivery

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1 The implementing rules of the Foreign Investments Act provide that "doing business" will include soliciting orders, service contracts and opening offices, whether liaison offices or branches; appointing representatives or distributors, operating under full control of the foreign corporation, domiciled in the Philippines or that in any calendar year stay in the country for a period totaling 180 days or more; participating in the management, supervision or control of any domestic business, firm, entity or corporation in the Philippines; and any other act or acts that imply a continuity of commercial dealings or arrangements and contemplate to that extent the performance of acts or works, or the exercise of some of the functions normally incident to and in progressive prosecution of commercial gain, or of the purpose and object of the business organization. The following acts will not be deemed "doing business" in the Philippines:

- Mere investment as a shareholder by a foreign entity in domestic corporations duly registered to do business and/or the exercise of rights as such investor
- Having a nominee director or officer to represent its interest in such corporation
- Appointing a representative or distributor domiciled in the Philippines that transacts business in the representative's or distributor's own name and account
- Publishing a general advertisement through any print or broadcast media
- Maintaining a stock of goods in the Philippines solely for the purpose of having the same processed by another entity in the Philippines
- Consignment by a foreign entity of equipment with a local company to be used in the processing of products for export
- Collecting information in the Philippines
- Performing services auxiliary to an existing isolated contract of sale that are not on a continuing basis, such as installing in the Philippines machinery it has manufactured or exported to the Philippines, servicing the same, training domestic workers to operate it and similar incidental services

and performance of the finance documents relate to a single or isolated loan transaction, and there is no purpose or intention to do any other business within the country, it can be argued that the foregoing activities do not constitute doing business in the Philippines and, as such, obtaining a license from the SEC is not required.

The SEC license is also referred to as the primary license of a foreign corporation. In addition to the SEC license, a foreign corporation that will engage in lending activities in the Philippines generally and on a continuing basis is required to obtain a secondary license from other regulatory agencies. Depending on the scope of the lending activities, such a foreign corporation must obtain a secondary license to operate either as a bank, a financing company or a lending company.

Enforcement of the finance documents

Whether a license is required to enable a foreign corporation to enforce its rights under the finance documents depends on whether the foreign corporation is doing business in the Philippines.

It is not necessary for a lender, arranger, facility agent or security agent that is not "doing business in the Philippines" to be licensed for it to enforce its rights under the finance documents. Conversely, a lender, arranger, facility agent or security agent that is doing business in the Philippines without a license is barred from filing or intervening in any action, suit or proceeding in any court or administrative agency of the Philippines, unless it obtains the required license to transact business in the Philippines. However, it may be sued in relation to any valid cause of action recognized under Philippine law.

2. Will any lender, arranger, facility agent or security agent be deemed to be resident, domiciled, carrying on business or subject to tax by reason only of the execution, delivery, performance or enforcement of the finance documents?

No. However, the income of any lender, arranger, facility agent or security agent is subject to tax if the income originated from sources within the Philippines. Interest income is deemed to originate from sources within the Philippines if the debtor is a resident of the Philippines or the loan is used in the Philippines.

3. Are there any regulatory reporting requirements that lenders must observe in connection with those transactions?

Generally, reporting requirements are imposed by the Bangko Sentral ng Pilipinas (BSP), the Philippine central bank, on BSP-supervised institutions (such as banks that are operating in the Philippines). Further, for foreign loans of residents, the reporting requirements under Philippine foreign exchange regulations are imposed on the resident borrower.

4. Is it necessary to establish a place of business in your jurisdiction in order to enforce any provision of the finance documents?

If a foreign corporation is deemed to be "doing business" in the Philippines, it is required to obtain a license from the SEC. To obtain the license, the SEC requires the foreign corporation to establish a principal place of business in the Philippines.

On the other hand, if a foreign corporation is not considered to be doing business, it is not necessary to obtain a license from the SEC and, for that purpose, establish a principal place of business.

5. Is a foreign bank/financial institution permitted to approach local entities for business?

If a foreign bank/financial institution that is not licensed in the Philippines goes to the Philippines and approaches or solicits local entities for business, such institution may be deemed to be doing business without the required licenses from the SEC and the BSP.

The possible consequences of a foreign bank being deemed to be "doing business" in the Philippines without authorization include the foreign bank being barred from maintaining or intervening in any legal or administrative action or proceedings and the imposition of a fine, imprisonment of the responsible directors and officers, or both, at the court's discretion.

When lending to borrowers

1. Are there any restrictions in relation to the type of borrower who may borrow foreign currency or in relation to the term of foreign currency and/or the amount of foreign currency borrowed by local entities?

We are not aware of any specific restrictions in relation to the type of borrower that may borrow foreign currency. However, in general, if the lender or guarantor is a bank operating in the Philippines, the total amount of loans, credit accommodation and guarantees extended by it to any borrower must not exceed 25% of the net worth of that bank. Loans secured by acceptable (low-risk) security are considered non-risk loans and are generally excluded from this limit.

Further, except with the prior approval of the BSP, the combined outstanding loans and guarantees extended by a bank to a single director, officer or stockholder of such bank and its related interest should not exceed 15% of the bank's total loan portfolio or 100% of the bank's net worth, whichever is lower. Dealings of a bank with any of its directors, officers or stockholders and their related interest will be upon terms as favorable to the bank as the terms offered to others.

2. Are there any restrictions on the rate of interest or default interest that may be charged?

With the removal of interest ceilings on loans or forbearance of money, goods or credits by the BSP, contracting parties are generally free to stipulate the interest rates to be imposed in relation to monetary obligations. However, courts may invalidate interest rates if found to be excessive or unconscionable.

Where interest is agreed to be paid but the interest rate is not stated in the relevant agreement, the default rate of interest prescribed under BSP regulations is 6% per annum.

3. Are there any restrictions on particular lenders or classes of lender entering into credit transactions with borrowers?

There are generally no restrictions on particular lenders or classes of lender entering into credit transactions with borrowers in the Philippines.

However, where a foreign lender or lenders intend to engage in the lending business in the Philippines, it is necessary to obtain, in addition to a license from the SEC, a secondary license as either a bank, a financing company or a lending company. The type of secondary license will depend on the scope of lending activities that the foreign lenders will engage in, and the granting of such license is subject to meeting the requirements under the relevant laws and regulations.

4. Are there any exchange controls that will apply to payments to be made in foreign currencies or to foreign lenders?

Yes. Unless specifically exempt under the relevant BSP regulations, prior BSP approval must be obtained for foreign loans (i.e., loans from foreign lenders regardless of denomination) or foreign currency-denominated loans of (a) public sector entities or (b) private sector entities if guaranteed by government corporations and/or government financial institutions.

Further, other foreign currency-denominated loans extended by foreign lenders to private sector borrowers are generally required to be registered with the BSP to enable the borrower to purchase foreign exchange from the Philippine domestic banking system to service payment of the loan obligations.

5. Is there any requirement to deduct or withhold tax from any amounts to be paid or repaid to a lender (whether domestic or foreign)? If so, at what rate must tax be deducted and from what kinds of payment?

Interest payments to foreign entities are subject to withholding tax. Under Philippine tax law, a nonresident foreign corporation not engaged in trade or business in the Philippines is generally subject to a 20% final withholding tax on gross interest received in relation to loans granted to Philippine residents. The 20% final withholding tax on gross interest may be reduced under the provisions of Philippine tax treaties with the country where the nonresident foreign corporation is domiciled.

6. Are there any "thin capitalization" or other rules that may limit the extent to which interest payments may be deducted for tax purposes?

Under Philippine law, the amount of interest paid or incurred within a taxable year will be allowed as a deduction but should be first reduced by 20% of the interest income of the taxpayer subjected to final tax, if any.

7. Are there any registration, notarization, translation or reporting requirements in relation to the loan documents?

Yes. Registration with the BSP of a foreign currency loan extended by a foreign lender to a private sector entity is required if foreign exchange will be purchased from the local banking system to service payments on the loan (principal and interest).

Notarization

Notarization is not required for the validity or enforceability of a loan document.

Further, under BSP regulations, no public and/or publicly guaranteed foreign loan that is submitted to the BSP for approval and/or registration will be approved and/or registered if the loan documents are notarized.

However, notarization is useful. Under evidence rules, a notarized document is presumed to be signed by the person whose name appears on the document and the document can be presented in court without further proof of its due execution and authenticity.

Credits without special privilege that appear in a public (i.e., notarized) instrument are granted preference as provided in Article 2244 of the Civil Code of the Philippines ("**Civil Code**"). However, under BSP regulations, no public and/or publicly guaranteed foreign loan that is submitted to the BSP for approval and/or registration will be approved and/or registered if the loan documents are notarized.

Translation

Translation of loan documents into the local language is not required under Philippine law.

Reporting

See the response under question 3 in the section "When considering whether to lend" for the reporting requirements of the BSP.

For income tax purposes, the withholding agent (i.e., the borrower) must report the loan transactions to the Bureau of Internal Revenue on remittance of the withholding tax.

8. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to the loan documents? If yes, what are the amounts and when are they payable?

For loan agreements, Philippine law generally requires the payment of a document stamp tax (DST) at a rate of PHP 1.50 (USD 0.03) for every PHP 200 (USD 4) of the amount of the loan. At the time of publication, the notarization of each document costs from PHP 200 to PHP 400 (USD 4 to USD 8).[2]

9. Does the law recognize the subordination of the debt that a debtor owes to one creditor to that which the debtor owes to another creditor? If yes, how is this usually effected?

Yes. Philippine law recognizes subordination agreements, subject to the concurrence and preference of certain credits prescribed under Philippine law. These are discussed in the answer to question 10 of this section and in question 1 of the section "If taking security."

10. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors (e.g., the claims of employees and tax authorities or the claims of creditors under particular kinds of instrument)? If yes, what classes of creditors are preferred?

See the response to question 1 of the section "If taking security."

Further, the Foreign Rehabilitation and Insolvency Act (FRIA) prescribes the order of priority in which the obligations of a debtor must be paid in an insolvency situation (after the debtor's assets are liquidated), as follows:

a. Special preferred debts under the Civil Code in relation to specific personal or movable property of the debtor and in relation to specific real or immovable property and real rights of the debtor.

b. Ordinary preferred debts under the Civil Code, provided that, for the purposes of implementing the liquidation plan under the FRIA, debts for services rendered to the debtor by employees or laborers have first preference.

c. Ordinary claims, which are claims approved and allowed in the liquidation proceedings and not falling into (a) or (b) above.

Within each of the above three categories (i.e., special preferred debts, ordinary preferred debts and ordinary claims), the Civil Code lists the specific classes of debts that are preferred as discussed in the response to question 1 of the section "If taking security." The debts due to the creditors are satisfied in accordance with the list based on a descending order of priority. For example, under the first category of special preferred debts in relation to the debtor's specific movable property, the first item in the list, which is duties, taxes and fees due to the government, enjoys preference over all other claims listed within that category.

11. Are there any consumer protection or similar laws that apply if credit is made available to individuals or other classes of debtor? If yes, what laws are applicable?

Yes. The Truth in Lending Act and the BSP Manual of Regulations for Banks and Manual of Regulations for Non-Bank Financial Institutions apply. BSP Regulations on Financial Consumer Protection also detail how creditors must deal with customers in relation to disclosure and transparency, protection of client information, fair treatment, effective recourse and financial education.

12. Are there any prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of: (a) its own shares or those of any affiliated company; or (b) assets owned by it or any affiliated company?

There are no specific prohibitions or limitations under Philippine law.

2 Conversion of PHP to USD is at an assumed exchange rate of USD 1 = PHP 50

However, a Philippine corporation may provide financial assistance in connection with the acquisition of shares in itself or its parent corporation if the following events occur:

- Its articles of incorporation do not contain an express restriction prohibiting the financial assistance.
- The extension of the financial assistance is authorized in the purpose clause of the articles of incorporation, and it can reasonably be shown to be for the benefit of and in furtherance of the corporation's primary purposes.
- The applicable corporate approvals are obtained.

If taking security

1. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's secured creditors?

The Civil Code provides for the preference of credits classified into the following categories:

- Special preferred credits listed under Articles 2241[3] and 2242[4]
- Ordinary preferred credits listed under Article 2244[5]

Credits not included in Articles 2241, 2242 and 2244 enjoy no preference

Under each of Articles 2241 and 2242, duties, taxes and fees due to the government enjoy first-tier preference. All other special preferred nontax credits stand on the second-tier preference to be satisfied equally and pro rata out of any residual value (after payment of the taxes) of the specific property to which the credits relate.

In satisfying several preferred credits that are registered with the Register of Deeds, the rule is the priority of credits in the order of the time of registration.

With reference to other property of the debtor to which no specific liens attach under Articles 2241 and 2242, Article 2244 enumerates claims and credits that enjoy preference in the order stated. However, the Philippine Supreme Court has ruled that credits of laborers (i.e., employment claims) under Article 2244 will enjoy first-tier preference. On the other hand, the last preferred credits in Article 2244(14) enjoy preference among themselves in the order of priority of the dates of the instrument and the judgments.

2. May security given by a company rank in a specified order so as to secure liabilities owed to different creditors of the company in that order and, if that is not possible, is it viable for parties to enter into a contractual arrangement for the purposes of moderating this order?

Yes. Philippine law does not prohibit the ranking of security to secure liabilities owed to different creditors by contractual stipulation, subject to the statutory preference of credits discussed in question 1 of this section.

3. Does this jurisdiction recognise the concept of floating security or similar equivalent (i.e., security over a changing pool of assets that the company giving the security is free to buy, sell and generally deal with)?

No. Philippine law generally does not recognize the concept of floating security.

The Civil Code recognizes specific types of security — guarantee/surety, real estate mortgage, antichresis — and the creation of security interests over personal property under the Personal Property and Security Act.

A security agreement may provide for the creation of security interest in future property, but the security interest in that property is created only when the grantor acquires rights in it or the power to encumber it.

3 Article 2241 of the Civil Code provides the following.

With reference to specific movable property of the debtor, the following claims or liens will be preferred:

- duties, taxes and fees due thereon to the state or any subdivision thereof
- claims arising from misappropriation, breach of trust or malfeasance by public officials committed in the performance of their duties, on the movables, money or securities obtained by them
- claims for the unpaid price of movables sold, on the movables, so long as they are in the possession of the debtor, up to the value of the same; and if the movable has been resold by the debtor and the price is still unpaid, the lien may be enforced on the price; this right is not lost by the immobilization of the thing by destination, provided that it has not lost its form, substance and identity; neither is the right lost by the sale of the thing together with other property for a lump sum when the price thereof can be determined proportionally
- credits guaranteed with a pledge, so long as the things pledged are in the hands of the creditor or those guaranteed by a chattel mortgage, upon the things pledged or mortgaged, up to the value thereof
- credits for the making, repair, safekeeping or preservation of personal property, on the movable thus made, repaired, kept or possessed
- claims for laborers' wages, on the goods manufactured or the work done
- for expenses of salvage, upon the goods salvaged
- credits between the landlord and the tenant, arising from the contract of tenancy on shares, on the share of each in the fruits or harvest
- credits for transportation, upon the goods carried, for the price of the contract and incidental expenses, until their delivery and for 30 days thereafter
- credits for lodging and supplies usually furnished to travelers by hotel keepers, on the movables belonging to the guest as long as such movables are in the hotel, but not for money loaned to the guests
- credits for seeds and expenses for cultivation and harvest advanced to the debtor, upon the fruits harvested
- credits for rent for one year, upon the personal property of the lessee existing on the immovable leased and on the fruits of the same, but not on money or instruments of credit
- claims in favor of the depositor if the depositary has wrongfully sold the thing deposited, upon the price of the sale

In the foregoing cases, if the movables to which the lien or preference attaches have been wrongfully taken, the creditor may demand them from any possessor within 30 days from the unlawful seizure.

4 Article 2242 of the Civil Code provides the following.

With reference to specific immovable property and real rights of the debtor, the following claims, mortgages and liens will be preferred and will constitute an encumbrance on the immovable or real right:

- taxes due upon the land or building
- for the unpaid price of real property sold, upon the immovable sold
- claims of laborers, masons, mechanics and other workpeople, as well as of architects, engineers and contractors, engaged in the construction, reconstruction or repair of buildings, canals or other works, upon said buildings, canals or other works
- claims of furnishers of materials used in the construction, reconstruction or repair of buildings, canals or other works, upon said buildings, canals or other works
- mortgage credits recorded in the Registry of Property, upon the real estate mortgaged
- expenses for the preservation or improvements of real property when the law authorizes reimbursement, upon the immovable preserved or improved
- credits annotated in the Registry of Property, in virtue of a judicial order, by attachments or executions, upon the property affected and only as to later credits
- claims of co-heirs for warranty in the partition of an immovable among them, upon the real property thus divided
- claims of donors of real property for pecuniary charges or other conditions imposed upon the donee, upon the immovable donated
- credits of insurers, upon the property insured, for the insurance premium for two years

5 Article 2244 of the Civil Code provides the following.

With reference to other property of the debtor, to which no specific liens attach, the Civil Code states that the following claims or credits will be preferred in the order named:

- proper funeral expenses for the debtor or children under their parental authority who have no property of their own, when approved by the court
- credits for services rendered to the insolvent by employees, laborers or household helpers for one year preceding the commencement of the proceedings in insolvency
- expenses during the last illness of the debtor or of their spouse and children under their parental authority, if they have no property of their own
- compensation due the laborers or their dependents under the laws providing for indemnity for damages in case of a labor accident or illness resulting from the nature of the employment
- credits and advancements made to debtors to themselves and their families, during the last year preceding the insolvency
- support during the insolvency proceedings and for three months thereafter
- fines and civil indemnification arising from a criminal offense
- legal expenses and expenses incurred in the administration of the insolvent's estate for the common interest of the creditors, when properly authorized and approved by the court
- taxes and assessments due the national government other than those taxes and assessments on specific property of the debtor form a lien on such property
- taxes and assessments due any province other than those taxes and assessments on specific property of the debtor that form a lien on such property
- taxes and assessments due any city or municipality other than those taxes and assessments on specific property of the debtor that form a lien on such property
- damages for death or personal injuries caused by a quasi-delict
- gifts due to public and private institutions of charity or beneficence
- credits which, without special privilege, appear in (a) a public instrument or (b) in a final judgment, if they have been the subject of litigation; these credits will have preference among themselves in the order of priority of the dates of the instrument and of the judgments, respectively

4. If so, are there any practical reasons why floating security is difficult to take, maintain or enforce?

See the answer to question 3 of this section.

5. May security be granted to a trustee to be held on trust for the lenders from time to time, in such a way that a change of lenders does not require new security to be taken?

Under Philippine law, the assignment of a credit includes all the accessory rights, such as a guarantee, mortgage, pledge or preference. Further, legal and contractual subrogation (i.e., change in lenders) transfers to the persons subrogated (i.e., the new lenders) the credit with all the rights thereto, either against the debtor or against third persons, be they guarantors or mortgagors. Hence, it is not necessary to create or take a new security in the event of a change of lenders. However, in a contractual subrogation, the original lender, debtor, security provider and new lender must consent to the subrogation. The consent of the debtor and security provider may be given in advance in the relevant documentation.

6. If not, are there any techniques that can be used to achieve substantially the same effect (e.g., parallel debt structures)?

Not applicable.

7. If an agent holds security for the lenders rather than a trustee, is it necessary to take new security on a change of lenders? If no, why not? If yes, are there ways to structure the transaction to avoid such a requirement?

No. See answer to question 6 of this section.

8. Under the laws of this jurisdiction, is there any class of asset over which it is difficult or impossible to grant effective and perfected security, or in relation to which any security granted will be of limited effect?

Certain activities or areas of investment are subject to foreign equity restrictions pursuant to the Philippine Constitution and statutes. These activities or areas of investment are listed in the Foreign Investment Negative List.

Among the activities that are subject to foreign equity restrictions is the ownership of land in the Philippines. Only Philippine citizens and corporations or associations, at least 60% of whose capital is owned by Philippine citizens, may own land in the Philippines.

Real property, including land, may be mortgaged to secure the performance of obligations. However, if the mortgagee is disqualified to own land in the Philippines, the mortgagee is not permitted to bid or take part in any foreclosure sale of the mortgaged property, but may take possession after default for the purpose of foreclosure for a period not exceeding five years from actual possession. On the other hand, foreign banks that are authorized to do banking business in the Philippines are allowed to bid and take part in foreclosure sales of real property mortgaged to them, as well as to avail of enforcement and other proceedings and, accordingly, take possession of the mortgaged property for a period not exceeding five years from the actual possession. However, title to the property will not be transferred to the foreign bank. If the foreign bank is the winning bidder, during the five-year period, it will transfer its rights to a person or entity that is qualified to own land in the Philippines.

In relation to shares of stock, a stockholder may pledge or constitute a chattel mortgage over its shares of stock in a Philippine corporation in favor of a foreign lender. However, if the Philippine corporation is subject to a foreign equity limitation, the foreign lender can acquire and take title to the pledged or mortgaged shares only to the extent of the applicable foreign equity limitation.

9. Under the laws of this jurisdiction, are there any restrictions on offshore lenders taking security over any class of asset?

There are generally no restrictions to offshore lenders taking security over assets in the country. However, their resulting interest in the security may be limited by foreign ownership restrictions in place over a certain class of assets. For instance, in foreclosure of land used as collateral for the loan, the foreign lender may not participate in the public auction or in any other manner obtain ownership over the land. On the other hand, foreign banks that are authorized to do banking business in the Philippines are allowed to bid and take part in foreclosure sales of real property mortgaged to them, as well as to avail of enforcement and other proceedings and, accordingly, take possession of the mortgaged property for a period not exceeding five years from the actual possession. However, title to the property will not be transferred to the foreign bank.

10. Must a company receive a corporate benefit in return for giving a guarantee or security? In particular, are there restrictions on the grant of upstream and cross-stream guarantees and security? If yes, briefly what is the effect of these laws?

Yes. Philippine law requires a corporate benefit to be received before a Philippine corporation can provide a guarantee or pledge or mortgage of its assets as security for the performance of the loan obligations of another person or corporation.

The Philippine Supreme Court has held that the primary obligation of the directors of a corporation is "to seek the maximum amount of profits for the corporation" and it characterized a director's position as a "position of trust." In line with the directors' fiduciary duty, directors who willfully and knowingly vote for or assent to patently unlawful acts of the corporation or who are guilty of gross negligence or bad faith in directing the affairs of the corporation are liable jointly and severally for all damage suffered by the corporation, its stockholders and other persons as a result of those acts by those directors.

11. What type of security interests does your jurisdiction recognise, e.g., pledge, charge, mortgage, hypothecation? In relation to each type of security interest, please state the formalities required to create and perfect that security.

The Civil Code recognizes four types of security arrangements — guarantee/surety, real estate mortgage, antichresis — and the creation of security interests over personal property through security agreements. A description of the common types of security and their formalities are set out below.

Guarantee/surety

In a contract of guarantee, a person, known as a guarantor, is bound to the creditor to fulfill the obligation of the principal debtor if the principal debtor fails to do so. If the guarantor is bound with solidary (i.e., jointly and severally) with the principal debtor, the guarantee contract is called a suretyship and the guarantor a surety.

A guarantee must be in writing. A guarantee is not presumed; it must be express and it cannot extend to more than what is stipulated therein.

Subject to certain exceptions, a guarantor cannot be compelled to pay the creditor, unless the latter has exhausted all the property of the debtor and resorted to all legal remedies against the debtor (known as exhaustion). On the other hand, a surety is not entitled to the benefit of exhaustion.

Real estate mortgage

A mortgage is a contract whereby the debtor guarantees to a creditor the fulfillment of an obligation by subjecting specific real properties as security in the event of the nonfulfillment of the secured obligation. The essential requisites are as follows:

- The real estate mortgage must be constituted to secure the fulfillment of a principal obligation.
- The mortgagor must be the absolute owner of the property.
- The mortgagor must have free disposal of its property. In the absence thereof, the mortgagor must be legally authorized for the purpose.

To be binding against third persons, a real estate mortgage must be in writing and recorded in the Registry of Deeds.

Security agreement over personal property

Philippine law permits parties to freely enter into any form of security arrangement over movable property, if the arrangement is consistent with the rules in the Personal Property Security Act.

To be valid, a security agreement must be contained in a written contract signed by the parties. The following perfect security interests: (a) registration of a notice with the registry; (b) possession of the collateral by the secured creditor; and (c) control of the investment property and deposit account.

12. Are there any registration, translation or notarization requirements in relation to security, guarantees, subordination or intercreditor documents?

See the answer to question 11 of this section.

Translation of security, guarantee, subordination or intercreditor documents into the local language is not required under Philippine law. However, under the Personal Property Security Act, the security agreement for the creation of security over personal assets must provide for the language to be used in agreements and notices. The grantor must be given the option to have the agreement and notices in Filipino.

13. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in respect of security, guarantees, subordination or intercreditor documents? If yes, what are the amounts and when are they payable?

A DST must be paid to the Bureau of Internal Revenue. The DST is imposed on pledges or mortgages based on the secured amount at the following rates:

- DST of PHP 40 (USD 0.8), when the amount secured does not exceed PHP 5,000 (USD 100)
- Additional tax of PHP 20 (USD 0.4) on each PHP 5,000 or a fractional part of it in excess of PHP 5,000 (USD 100)

The Registry of Deeds requires the payment of a registration fee based on the value of the consideration of the security transaction.

At the time of publication, the notarization of each document costs from PHP 200 to PHP 400 (USD 4 to USD 8).

If things go wrong

1. **Please provide a brief description of the insolvency regime. In particular what rights and duties do unsecured and secured lenders have on the insolvency of a debtor? Are there any other matters of concern?**

Several remedies are available to financially distressed individuals or corporations. Individuals may apply for the suspension of payments or liquidation, while corporations may seek: (a) corporate rehabilitation (or restructuring), which may be either (i) court-supervised rehabilitation, (ii) pre-negotiated rehabilitation or (iii) an out-of-court restructuring agreement; or (b) liquidation.

Corporate rehabilitation is available to debtors that may be restored to a condition of successful operation and solvency. A court-supervised rehabilitation occurs when a rehabilitation court is appointed to resolve the matter of rehabilitation. In a pre-negotiated rehabilitation, the insolvent debtor, by itself or jointly with any of its creditors, petitions the court for the approval of a pre-negotiated rehabilitation plan that has been endorsed or approved by a certain number of creditors as required under the law.[6] In an out-of-court restructuring agreement, there is a rehabilitation plan, but it does not need court approval to be effective.

Lenders should file their claims with the rehabilitation court at least five days before the initial hearing date. During the pendency of rehabilitation proceedings, secured lenders retain their rights to the security but actions in connection with their claims, including the enforcement against the security, are stayed until the court orders otherwise or until the rehabilitation proceedings are terminated. The rehabilitation receiver will call a meeting with the debtor and all classes of creditors to discuss the rehabilitation plan. All classes of lenders and creditors can vote on the approval of the rehabilitation plan to be proposed by the rehabilitation receiver.

Liquidation proceedings are based on the fact that the debtor does not have enough assets/property to cover its obligations. Liquidations may be voluntary (i.e., applied for by the debtor itself) or involuntary (i.e., applied for by three or more creditors that satisfy the relevant requirements).

If the court finds the petition or motion for liquidation sufficient in form and substance, it issues a liquidation order. A liquidation order is an order issued by the court that declares that the debtor is insolvent and orders the liquidation or dissolution of the debtor. On the issuance of the liquidation order, the debtor is dissolved, and legal title and control of its assets are vested in the liquidator. The effects of the liquidation order are different for secured and unsecured creditors.

An unsecured creditor is not permitted to bring a separate action against the debtor for the collection of debts owing to the unsecured creditor. Any action already pending will be transferred to the liquidator to accept or settle or to contest. The court will hear and resolve the matter, and any final and executory judgment against the debtor will be filed and allowed in court.

A liquidation order will not affect the right of a secured creditor to enforce its security. Therefore, a secured creditor may do either of the following:

- Waive its right under its security, prove its claim in the liquidation proceedings and share in the distribution of assets of the debtor
- Maintain its rights under the security or lien

6 Under the Republic Act No. 10142, the pre-negotiated rehabilitation plan must be endorsed or approved by creditors holding at least two-thirds of the total liabilities of the debtor, including secured creditors holding more than 50% of the total secured claims of the debtor and unsecured creditors holding more than 50% of the total unsecured claims of the debtor.

2. **Is it possible to obtain a moratorium before insolvency?**

Yes, but only for financially distressed individuals who may apply for a suspension of payments.

For financially distressed entities, the moratorium, pursuant to a stay or liquidation order, is only issued upon an application for insolvency (i.e., either corporate rehabilitation or liquidation).

3. **When a company is the subject of a formal insolvency procedure, can the company's pre-insolvency transactions be set aside?**

Yes. Any transaction by the debtor or involving its assets entered into prior to the issuance of the stay order or liquidation order may be rescinded or declared null and void on the grounds that it was executed with the intent to defraud the creditor or creditors or that it constitutes an unfair preference.

4. **When can a lender enforce its security? Can security be enforced out of court following an event of default (or other contractual trigger event), or is a court order required? Are there any restrictions that apply before a lender may enforce its security?**

The requirements for a lender to be able to enforce its security depend on the type of security that will be enforced. The types of security and their requirements for enforcement are discussed below.

Guarantee

Generally, a guarantor (but not a surety) cannot be compelled to pay the creditor unless the following events occur:

- All of the property of the principal debtor has been exhausted.
- The creditor has exhausted all of its legal remedies in relation to the principal debtor.

Therefore, the creditor must perform the following:

- The creditor must first file a case against the principal debtor alone.
- In that case, the creditor must ask the court to notify the guarantor.

The creditor may hold the guarantor liable only after judgment has been obtained against the principal debtor and the principal debtor is unable to pay.

On the other hand, the benefit of exhaustion does not apply to a surety. Hence, the creditor may sue, separately or together, the principal and the surety.

Real estate mortgage

A real estate mortgage may be enforced extrajudicially if the mortgage instrument expressly allows extrajudicial foreclosure. On the other hand, if there is no stipulation allowing extrajudicial foreclosure, the mortgage must be enforced judicially.

In an extrajudicial foreclosure, the foreclosure sale at public auction can proceed after the filing of an application for extrajudicial foreclosure with the executive judge that has jurisdiction over the area where the relevant real property is located and upon compliance by the applicant with all of the requirements. The sheriff will conduct the foreclosure sale.

For judicial foreclosure, a petition for foreclosure must be filed in the proper court that has jurisdiction over the area where the relevant real property (or a portion of the real property) is situated.

Security arrangement over personal property

A secured creditor may take possession of the collateral without a judicial process if the security agreement so stipulates. However, this is assuming possession may be taken without breach of the peace. If possession cannot be taken without breach of the peace, the secured creditor is entitled to an expedited hearing for a court order granting possession of the property.

After default, a secured creditor may sell or otherwise dispose of the collateral, publicly or privately. It may also propose to the debtor and grantor to take all or part of the collateral in total or partial satisfaction of the secured obligation.

5. Do any limitation periods apply in relation to bringing an action to enforce security?

Yes. Under the Civil Code, an action to enforce a right arising from written contracts must be enforced within 10 years from the time the cause of action accrues (i.e., upon failure by the debtor to perform the secured obligation when due).

6. Is there any particular way in which secured assets must be liquidated on enforcement (e.g., by auction or court sale)?

Upon the default of the secured obligation, the creditor is not entitled to automatically appropriate the pledged or mortgaged property. The creditor is permitted to recover its credit from the proceeds of the foreclosure sale of the property at public auction through a public officer in the manner provided by law.

The proceeds of the foreclosure sale of a pledged or mortgaged property will be applied in the following order:

- The costs of the sale
- The amount of the principal obligation and interest
- The junior encumbrances

In a pledge, the sale of the pledged property extinguishes the principal obligation, whether or not the proceeds of the foreclosure sale are equal to the amount of the principal obligation, interest and expenses in a proper case. If the proceeds are more than the principal obligation, the debtor is not entitled to the excess unless there is a contrary stipulation in the pledge agreement. If the proceeds are less, the creditor is not entitled to recover the deficiency and a contrary stipulation is void.

In a mortgage, if the proceeds from the foreclosure sale are not sufficient to satisfy the mortgage debt, the creditor is entitled to obtain a deficiency judgment. The deficiency judgment may be satisfied from other properties of the debtor.

7. Are there any particular legal or practical difficulties or delays in enforcing security?

Generally, as set out in the answer to question 4 of this section in relation to the enforcement of a guarantee, the guarantor (but not a surety) cannot be compelled to pay the creditor unless all of the property of the principal debtor has been exhausted. The creditor may hold the guarantor (but not a surety) liable only after judgment has been obtained against the principal debtor and the principal debtor is unable to pay. This benefit of exhaustion is subject to exceptions, such as insolvency or an express waiver by the guarantor.

The creditor cannot automatically appropriate the security or dispose of it in the event of default. Any stipulation to the contrary is void. A foreclosure sale conducted in accordance with the prescribed requirements and procedure is necessary to enforce a mortgage. Further, in the case of insolvency, as discussed in the answer to question 1 of this section, the right of a creditor to enforce a security may be suspended by the court on the commencement of the rehabilitation proceedings of the insolvent debtor until the proceedings are terminated either due to the failure of the rehabilitation or the successful implementation of the rehabilitation plan.

Another practical consideration is that cases in the Philippines generally take considerable time to be decided. Securities that are sought to be enforced through court proceedings for foreclosure are often not immediately enforced. Therefore, creditors typically prefer extrajudicial proceedings.

8. In relation to enforcement, are there any specific requirements to be borne in mind if the lender is a foreign entity?

See the answer to question 8 of the section "If taking security."

In addition, security agents and trustees are typically Philippine residents.

9. Is there any reason why you think that arbitration rather than litigation might be advantageous in resolving disputes under the finance documents, and if so, why? Please outline the relative merits of arbitration and litigation, including the ease of enforcement of foreign judgments and foreign awards from different jurisdictions. Is it possible to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit?

Arbitration is generally more advantageous to foreign lenders than litigation. Disputes submitted to arbitration are more speedily resolved. Furthermore, the rules on arbitration are more favorable to foreign investors as the parties mutually agree on these rules. A valid arbitration clause in a loan contract allows a foreign awardee to enforce an award in the Philippines. The disadvantage of arbitration is that it is a more costly process in the Philippines than litigation proceedings.

10. Are asymmetrical jurisdiction clauses enforceable? (By this we mean clauses that allow the lenders, but not the borrowers, to make certain choices in relation to choice of jurisdiction and how to litigate. These types of clauses allow the lenders, but not the borrowers, to commence proceedings in any court they choose, but restrict the borrowers to commencing proceedings in one jurisdiction only. This may also allow the lenders, but not the borrowers, to choose whether to litigate the finance documents before a court or to submit to arbitration in relation to them, but restrict the borrowers to either litigation or arbitration, as specified in the agreement).

The validity of asymmetrical jurisdiction clauses has not yet been decided in the Philippines. It may be argued that these clauses are valid under the "freedom to contract" clause provided in the Civil Code, i.e., that "contracting parties may establish such stipulations, clauses, terms and conditions as they may deem convenient, provided they are not contrary to law, morals, good customs, public order or public policy."

However, the Philippine Supreme Court has invalidated clauses granting exclusive jurisdiction to non-Philippine courts. The court's reasoning was that a Philippine court's jurisdiction, being determined by law, cannot be limited by mere stipulation.

Moreover, asymmetrical dispute resolution clauses providing for litigation and arbitration, with options given to the lender but not the borrower, might be viewed as being contrary to public policy.

Working digitally

1. **Is it possible for documents to be executed electronically (whether by the manual insertion of a digital signature or the use of an e-signing platform) under the laws of this jurisdiction? If so, is this limited to only particular types of finance documents?**

   Yes, Philippine law permits the use of e-signatures on electronic documents without any limitation as to the type of finance document involved. An electronic signature on the electronic document will be equivalent to the signature of a person on a written document, if that signature is proved by showing that a prescribed procedure, not alterable by the parties interested in the electronic document, existed when the following occurs:

   - A method is used to identify the party sought to be bound and to indicate that party's access to the electronic document necessary for its consent or approval through the electronic signature.
   - The method is reliable and appropriate for the purpose for which the electronic document was generated or communicated, considering all circumstances, including any relevant agreement.
   - It is necessary for the party sought to be bound, in order to proceed further with the transaction, to have executed or provided the electronic signature.
   - The other party that is authorized and enabled to verify the electronic signature and to make the decision to proceed with the transaction is authenticated by the same.

2. **Where the witnessing of a signing is contemplated, is it possible for the witness to verify the signature over a live video call?**

   It is possible for the witness to verify the signing over a live video call. However, if the document is to be notarized, witnessing over video call is not permitted. Under the 2020 Interim Rules on Remote Notarization of Paper Documents, when there is a witness to the instrument, the principal should provide the notary public with a video showing proof that the witness actually saw the principal sign and each witness should declare that they personally witnessed the signing of the instrument or document.

3. **Is it possible to register/perfect security electronically without wet ink signatures?**

   Yes, under the Electronic Commerce Act, all offices and agencies of the government that accept the filing of documents and/or issue permits, licenses or certificates of registration will accept the creation, filing or retention of documents in the form of electronic data messages or electronic documents. Thus, government agencies are bound to accept electronic documents with electronic signatures.

   However, where notarized documents are required, then the wet ink signature of the notary is required. The Rules on Remote Notarization do not permit Philippine notaries public to notarize a document using their e-signature. Instead, the document is to be couriered to them for them to sign the document.

4. **Are there any other legal restrictions that may prevent the parties from executing a finance transaction electronically?**

   Yes. As stated in the answer to question 3 of this section, in the case of documents required to be notarized, the notarization may not be done electronically.

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SINGAPORE

Singapore

When considering whether to lend

1. Is it necessary or advisable for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in this jurisdiction: (a) by reason only of its execution, delivery or performance of the finance documents; or (b) to enable it to enforce its rights under the finance documents?

Whether a lender, arranger, facility agent or security agent must be licensed, qualified or otherwise entitled to carry on business in Singapore depends on the type of business in which it is involved. Certain business activities are regulated by statute, so an entity must first be licensed under the relevant statute before it may engage in that business activity. Two examples are banking business, for which a license under the Banking Act 1970 ("**Banking Act**") or the Monetary Authority of Singapore Act 1970 is needed, and moneylending, for which a license under the Moneylenders Act 2008 ("**Moneylenders Act**") is needed. These are briefly discussed below.

Generally, where a lender, arranger, facility agent or security agent is not carrying on business or performing any regulated activity in Singapore (or if carried on wholly outside Singapore, and in a manner so as to not bring the activity within the regulatory ambit of the relevant Singapore legislation[1]), the mere execution, delivery or performance of, or the enforcement of rights under, the finance documents does not require that entity to be licensed to carry on business in Singapore from a regulatory perspective. If, however, the lender, arranger, facility agent or security agent is carrying out a regulated activity under the finance documents, it may be required to obtain the necessary license or approval from the regulator under one of the statutes referred to in the paragraph above, the failure to do so may result in penalties, and the finance documents may become unenforceable because of illegality.

Bank license

A person who wishes to carry on banking business in Singapore is required to possess a valid license granted under the Banking Act. "Banking business" is defined to include the business of receiving money on current or deposit account, paying and collecting checks drawn by or paid in by customers, the making of advances to customers. and includes any other business that the central bank of Singapore, the Monetary Authority of Singapore (MAS), may prescribe.

The advantage of a banking license is that a licensed bank falls within the category of "excluded moneylenders" under the Moneylenders Act and is not required to hold a separate license under the Moneylenders Act in respect of its lending activity. A lender that is not licensed as a bank is required to hold a moneylender's license, unless it falls under a different category of "excluded moneylenders" (discussed below).

For completeness, similar licensing requirements apply to deposit-taking businesses, and there is an express prohibition from soliciting deposits from Singapore persons unless the entity (whether in or outside Singapore) has a valid license in Singapore.

1 Note that any solicitation from or offer to Singapore persons will more likely than not result in an offshore entity falling within the regulatory ambit of the relevant Singapore legislation, even if the offshore entity conducts its activities wholly outside Singapore.

Moneylender's license

A person who lends a sum of money in consideration of a larger sum being repaid is, until the contrary is proved, presumed to be a moneylender under the Moneylenders Act. Under the Moneylenders Act, no person is permitted to carry on the business of moneylending in Singapore without a moneylender's license unless that person is an "excluded moneylender" or "exempt moneylender."

An "excluded moneylender" includes a lender that lends money solely to corporations, limited liability partnerships, trustees or trustee-managers of business trusts, trustees of real estate investment trusts and/or accredited investors[2].

Other licenses

Please note that there are other activities, such as product financing[3] and providing custodial services for specified products[4], that are separately regulated in Singapore under the Securities and Futures Act 2001 (SFA). These are not considered in further detail here but if a lender, arranger, facility agent or security agent carries on business that constitutes those regulated activities, a capital markets services license may be required. Similarly, if a lender, arranger, facility agent or security agent acts as a payments intermediary or otherwise arranges for the transfer of monies from one party to another, a license under the Payment Services Act 2019 (PSA) may be required.

Note that there are extraterritorial provisions in the SFA where a foreign entity may be caught by the licensing regime if it conducts regulated activities partly in Singapore or wholly outside Singapore but where the acts have substantial and reasonably foreseeable effect in Singapore.

The PSA, similar to the Banking Act, has express provisions prohibiting any person (in or outside Singapore) from soliciting persons in Singapore to engage in payment services unless the person has the appropriate license under the PSA.

2. Will any lender, arranger, facility agent or security agent be deemed to be resident, domiciled, carrying on business or subject to tax by reason only of the execution, delivery, performance or enforcement of the finance documents?

Residence

Under Singapore law, whether a company is resident in Singapore is relevant for tax purposes. The test for tax residency for a company set out in the Income Tax Act 1947 ("Income Tax Act") is whether the "control and management" of its business is exercised in Singapore. Where "control and management" is exercised is a question of fact but is usually exercised through the meetings of the company's board of directors. Being a resident for the purposes of "service of process" is determined by certain rules relating to whether a company is carrying out business (discussed below) and whether it is registered.

Therefore, execution, delivery, performance or enforcement of the company's own finance documents does not result in that company being "resident" in Singapore.

In relation to the service of process on a company, a company's residency status is not strictly relevant. As long as a company is incorporated in Singapore with a registered address with the Accounting and Corporate Regulatory Authority (ACRA), court papers may be served on the company by leaving the papers at, or sending them by post to, the company's registered office.

2 "Excluded moneylender" is defined in section 2 of the Moneylenders Act. "Accredited investors" is defined in Section 4A of the Securities and Futures Act.

3 Credit facility, advance or loan to facilitate subscription, purchase or continued holding of securities, securities- based derivatives (other than futures contracts) and units in collective investment scheme that are listed or to be listed.

4 Defined as securities, securities- based derivatives (other than futures contracts) and units in collective investment schemes

Similarly, for foreign companies that are incorporated overseas, service of process in Singapore can be effected by: (i) leaving the papers at, or sending them by post to, the company's registered office in Singapore; (ii) addressing the papers to an authorized representative of the company and leaving them at, or sending them by post to, their registered address; or (iii) if the foreign company has ceased to maintain a place of business in Singapore, leaving the papers at, or sending them by post to, its registered office in its place of incorporation.

Subject to Singapore tax

Singapore has a territorial system of taxation. Under Singapore domestic laws, income tax is payable on income that is sourced in or derived from Singapore and foreign-sourced income brought into or received in Singapore or deemed received in Singapore (unless an exemption applies).

The question of where the income is sourced depends on the nature of the income and the case's facts and circumstances. Generally, the income is regarded as sourced at the place where the income-producing activities take place. For example, this may be where the operations are conducted or where the contracts are concluded in the case of trade or business income. As such, in general, if the lender, arranger, facility agent or security agent executes, delivers, performs or enforces finance documents in Singapore, this may potentially give rise to a Singapore income tax risk for the lender, although the level of risk (if any) would depend on the facts and circumstances of the particular case.

There are also rules that provide for certain payments to be deemed sourced in Singapore. For example, the Income Tax Act provides for interest to be deemed sourced in Singapore if it is borne by a person resident in Singapore. As explained in the answer to question 5 of the "When lending to borrowers" section, these payments would trigger withholding tax obligations if they are made to another person not known to be resident in Singapore. The application of these deemed-sourced rules generally does not depend on whether the finance documents are executed, delivered, performed or enforced in Singapore.

3. Are there any regulatory reporting requirements that lenders must observe in connection with those transactions?

Reporting requirements may vary depending on whether a particular statute regulates the lender, arranger, security agent or facility agent in relation to its business activities in Singapore. For example, in relation to licensed banks in Singapore, while there is no general requirement for banks to report specific loan and credit transactions to the MAS, there may be certain circumstances under which reporting obligations exist. In particular, under the Banking Act, the MAS may issue notices giving directions or imposing requirements on or relating to the operations or activities of banks regulated under the Banking Act. These directions or requirements may include reporting obligations. An example is MAS Notice 757, which requires banks licensed under the Banking Act to provide monthly reports to the MAS in respect of their aggregate outstanding loans of Singapore dollars to nonresident financial institutions.

4. Is it necessary to establish a place of business in your jurisdiction in order to enforce any provision of the finance documents?

It is not a legal or statutory requirement for a plaintiff or claimant to have established a place of business in Singapore to be able to enforce provisions of a finance document by the commencement of legal proceedings in Singapore. However, before commencing an action, a potential plaintiff or claimant should consider if Singapore is the appropriate forum to commence proceedings or risk having the action stayed, i.e., stopped, on the basis that there is clearly a more appropriate forum elsewhere. A potential plaintiff or claimant with few links to Singapore may also be required by the Singapore courts to provide security for the defendant's costs.

5. Is a foreign bank/financial institution permitted to approach local entities for business?

Generally, approaching local entities to provide banking services, such as offering loans or carrying out any other regulated activities in Singapore, may trigger licensing issues in Singapore for the foreign bank or financial

institution. Please see our answer to question 1 above, including in particular the description of "banking business" activities that would require a valid license granted under the Banking Act and other activities that require a license under the SFA.

If the foreign bank/financial institution has obtained the relevant license/approval in Singapore (e.g., numerous foreign banks have registered branches in Singapore and obtained the relevant licenses and approvals from the MAS in respect of their Singapore branch), they may carry out such activities through the Singapore branch, subject to such conditions and restrictions as may be imposed by the MAS.

However, this does not mean that the head office and/or representatives of the head office of the foreign bank may approach local entities to offer regulated activities or carry out licensable activities. For example, if a foreign bank carries out activities through its head office or representatives of its head office, e.g., offers loans to Singapore persons that would be booked at the head office rather than the Singapore branch, regulatory issues may still arise for the foreign bank, notwithstanding that it has a registered branch in Singapore. Therefore, such foreign banks should ensure that they consult internal guidelines on cross-border dos and don'ts or a legal counsel on whether there are licensing issues and/or any applicable exemptions.

When lending to borrowers

1. Are there any restrictions in relation to the type of borrower who may borrow foreign currency or in relation to the term of foreign currency and/or the amount of foreign currency borrowed by local entities?

Currently, there are no foreign exchange controls restricting the amount of currency that may be imported or exported in relation to the rights and obligations of parties under a loan agreement.

Further, no limitations nor consent requirements exist for a foreign company or bank to provide loans to Singapore persons. However, the making of loans may constitute the carrying on of banking business (as discussed in the answer to question 2 in the "When considering whether to lend" section) and if so, a banking license must be obtained.

2. Are there any restrictions on the rate of interest or default interest that may be charged?

There is no cap on interest rates that may be charged by banks. However, default interest may be unenforceable if a Singapore court decides that it constitutes a penalty. Further, a term that accelerates interest due under a loan upon an event of default may also constitute an unenforceable penalty: see Ethoz Capital Ltd v. Im8ex Pte Ltd [2023] SGCA 3.

3. Are there any restrictions on particular lenders or classes of lender entering into credit transactions with borrowers?

If a lender is a foreign lender and not regulated (and not required to be regulated) by a regulatory authority in Singapore in relation to its lending activity, there are generally no restrictions under Singapore law on the foreign lender entering into a credit transaction with a borrower in Singapore.

If, however, the lender is based in Singapore or caught by the licensing purviews in Singapore and regulated in Singapore in relation to its lending activity, the restrictions that may be imposed on that lender entering into credit transactions depend on the lender's licensing status and the terms of the applicable license terms. For example, a licensed bank in Singapore is generally not restricted from entering into credit and financing transactions with any borrower in Singapore. However, the MAS may impose restrictions in certain circumstances or in relation to categories of credit transactions, such as the following:

- Unsecured credit facilities: There are restrictions in relation to the grant of unsecured non-card credit facilities (except for certain excepted loans made for certain specified purposes) to an individual who is a citizen of Singapore or a permanent resident unless they have an annual income of at least SGD 20,000 at the time of the application for the unsecured credit facility.
- Counterparty limits: There are set limits in relation to a bank's permissible exposure to a single counterparty group.
- Residential property: There are restrictions on banks intending to grant credit facilities for the purchase of residential property or that are secured by residential property. These restrictions include a limit on the total credit facilities and the tenure of credit facilities that may be granted, prohibitions on interest-only loans and loans involving, or giving effect to, interest absorption schemes, requirements in relation to checks to be conducted with credit bureaus (and the Housing Development Board, if relevant) and a requirement that the borrower also serves as a mortgagor in relation to the residential property used to secure the relevant credit facility.
- Debt Service Ratio: There are restrictions in relation to the implementation of the Total Debt Servicing Ratio (TDSR) framework, which requires financial institutions to consider any other outstanding debt obligations when granting property loans to a borrower. Under the TDSR framework, credit facilities that may be granted by financial institutions to individuals (including sole proprietorships and vehicles set up by an individual solely to purchase the property) must not exceed a TDSR threshold of 55%.

Ultimately, the restrictions, if any, that may apply to a particular lender or group of lenders entering into credit transactions depend on the particular circumstances of that transaction. As stated above, the lender's licensing status, the type of transaction being entered into and the type of borrower involved are some of the considerations that may be relevant in determining the restrictions that may apply, but they do not represent an exhaustive list of factors.

4. Are there any exchange controls that will apply to payments to be made in foreign currencies or to foreign lenders?

No, there are currently no exchange controls effective in Singapore. The operation of the Exchange Control Act 1953 has been suspended since June 1978.

5. Is there any requirement to deduct or withhold tax from any amounts to be paid or repaid to a lender (whether domestic or foreign)? If so, at what rate must tax be deducted and from what kinds of payment?

Under Section 12(6) read with Sections 45/45A of the Income Tax Act, the following payments are subject to Singapore withholding tax if they are made to a non-Singapore resident unless any specific exemptions apply:

- Interest, commission, fees or any other payment in connection with any loan or indebtedness or with any arrangement, management, guarantee, or service relating to any loan or indebtedness that is:
- Borne, directly or indirectly, by a person resident in Singapore or a permanent establishment in Singapore except in respect of any business carried on outside Singapore through a permanent establishment outside Singapore or any immovable property situated outside Singapore; or
- Deductible against any income accruing in or derived from Singapore; or
- Any income derived from loans if the funds provided by those loans are brought into, or used, in Singapore.

Notwithstanding the above, as an administrative concession, payments liable to be made to a branch in Singapore of a nonresident company are exempt from withholding tax.

Under the Income Tax Act, a "resident of Singapore," in relation to a company or body of persons, is defined as a company or body of persons the control and management of whose business is exercised in Singapore.

The domestic withholding tax rate for interest payments that are neither derived from any trade or business carried on in Singapore nor effectively connected with any permanent establishment in Singapore is 15%. This may be reduced under the applicable tax treaties, subject to the requisite conditions for treaty benefits being met.

6. Are there any "thin capitalization" or other rules that may limit the extent to which interest payments may be deducted for tax purposes?

There are no thin capitalization rules for Singapore tax purposes. The Income Tax Act provides for a tax deduction for interest expenses incurred in relation to any money borrowed by such taxpayer where the Comptroller of Income Tax is satisfied that such interest is payable on capital employed in acquiring income. Further, transactions between related parties should be on an arm's length basis and will generally need to be supported by contemporaneous transfer pricing documentation unless specific exemptions apply.

7. Are there any registration, notarization, translation or reporting requirements in relation to the loan documents?

There are no registration, notarization or reporting requirements in relation to loan agreements.

8. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to the loan documents? If yes, what are the amounts and when are they payable?

The following documents (among others) are chargeable with stamp duty under the Stamp Duties Act 1929:

- Loan agreements that contain security trust provisions in respect of trust property that includes immovable property situated in Singapore and/or shares.
- Security documents that create security over immovable property situated in Singapore and/or shares and are not signed under hand only.

This is subject to the general rule that instruments relating exclusively to things to be done outside Singapore are exempt from stamp duty.

A nominal stamp duty of SGD 10 would apply to a loan agreement containing a security trust provision that is chargeable with stamp duty.

Ad valorem duty subject to a maximum of SGD 500 would apply to a security document chargeable with stamp duty, at the following rates:

- For a security (other than an equitable mortgage) for the payment or repayment of money, 0.4% of the amount of said money.
- For an equitable mortgage for the payment or repayment of money, 0.2% of the amount of said money.

Stamp duty has to be paid within 14 days of execution if it is executed in Singapore or within 30 days after it is received in Singapore if it is executed only outside Singapore. Please note that specific rules as to when an instrument is executed or received may apply if the instrument is an electronic instrument for stamp duty purposes, and this will depend on the relevant facts and circumstances.

9. Does the law recognize the subordination of the debt that a debtor owes to one creditor to that which the debtor owes to another creditor? If yes, how is this usually effected?

Yes, Singapore law recognizes the subordination of debts.

Generally, subordination of debts is effected by way of contract.

There is no legislation in Singapore in relation to the validity of contractual subordination in the event of the insolvency of the debtor company. Therefore, case law will determine the position in Singapore in relation to this question.

In the 2006 English case of Re SSSL Realisations (2002) Ltd (in liquidation) and another company [2006] EWCA Civ 7, the English Court of Appeal gave weight to the commercial expectation of the parties and held that if group companies enter into subordination agreements of this nature with their creditors while solvent, they and their creditors should be held to the bargain when the event for which the agreement was intended to provide (insolvency) occurs.

The court held that a subordination agreement is valid and binding. It is likely that the Singapore courts would adopt the same position.

10. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors (e.g., the claims of employees and tax authorities or the claims of creditors under particular kinds of instrument)? If yes, what classes of creditors are preferred?

Yes. The order of payment of those claims is set out in the answer to question 1 of the "If things go wrong" section.

11. Are there any consumer protection or similar laws that apply if credit is made available to individuals or other classes of debtor? If yes, what laws are applicable?

Singapore's consumer protection regime is made up of generic consumer laws supplemented by industry-specific requirements. The relevant governing legislation for consumer protection is set out in the Sale of Goods Act 1979, the Unfair Contract Terms Act 1977 and the Consumer Protection (Fair Trading) Act 2003.

The Consumer Protection (Fair Trading) Act was amended in 2009 to govern unfair practices in relation to all financial products and financial services regulated by the MAS and also all commodity trading under the Commodity Trading Act 1992. The ambit of the Consumer Protection (Fair Trading) Act covers the following:

- All banking activities under the Banking Act.
- Financial products provided by a financial adviser under the Financial Advisers Act.
- Activities relating to dealing in securities, fund management, marketing collective investment schemes and trading in futures and leveraged foreign exchange under the SFA.

The MAS, as the central bank, also maintains tight supervision on consumer products offered in the financial market. Certain more complex products such as structured deposits, structured notes and unit trusts are categorized as Specified Investment Products (SIPs). Customers will have to pass certain knowledge assessments before they are allowed to trade in SIPs.

Consumers who have disputes with financial institutions may also approach the Financial Industry Disputes Resolution Centre Ltd (FIDReC), which facilitates the mediation and adjudication of consumer disputes.

Finally, in practice, regulated banks also adhere to industry codes established by the Association of Banks in Singapore, such as the Code of Consumer Banking Practice.

12. Are there any prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of: (a) its own shares or those of any affiliated company; or (b) assets owned by it or any affiliated company?

Private companies

As of 1 July 2015, there is no prohibition in relation to financial assistance being given by private companies (other than private companies that are subsidiaries of public companies).

Public companies

The Companies Act 1967 ("**Companies Act**") prohibits a public company (or its subsidiary) from providing financial assistance for the acquisition of its own shares and the shares of its holding company.

There is, however, an exception in the Companies Act and the giving of financial assistance is not prohibited if:

- Giving the financial assistance does not materially prejudice the following:
- The interests of the company or its shareholders
- The company's ability to pay its creditors
- The company's board of directors passes a resolution ordering the following:
- That the company should give the financial assistance
- That the terms and conditions under which the financial assistance is proposed to be given are fair and reasonable to the company
- The directors' resolution sets out, in full, the grounds for the directors' conclusions and resolutions are lodged by the company with the Accounting and Corporate Regulatory Authority known as ACRA.

The Companies Act also contains a further list of transactions that are expressly carved out from the financial assistance prohibition.

If the above exception and carve-outs do not apply, prohibited financial assistance may still be allowed if it is "whitewashed" under the prescribed "whitewash" procedures. There are generally three "whitewash" methods, which are as follows:

- Director-approved financial assistance
- Shareholder-approved financial assistance
- A court-sanctioned whitewash procedure

If there is a breach of the prohibition in relation to financial assistance in the Companies Act, each officer of the company in default is guilty of an offense and liable on conviction to a fine not exceeding SGD 20,000 and/or to imprisonment for a term not exceeding three years.

If taking security

1. **Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's secured creditors?**

   Yes. The order of payment of those claims is set out in the answer to question 1 of the "If things go wrong" section.

2. **May security given by a company rank in a specified order so as to secure liabilities owed to different creditors of the company in that order and, if that is not possible, is it viable for parties to enter into a contractual arrangement for the purposes of moderating this order?**

   Yes. Creditors may enter into contractual arrangements (usually an intercreditor agreement or deed of priority) to regulate the order of priority of their security interests and the respective rights that they will have in relation to their respective debts.

3. Does this jurisdiction recognise the concept of floating security or similar equivalent (i.e., security over a changing pool of assets that the company giving the security is free to buy, sell and generally deal with)?

Yes. Security may be granted by way of a floating charge, typically by way of a debenture (i.e., a security document that is usually entered into when creating a fixed and floating charge), and is generally created over a class of assets, present and future, belonging to a chargor.

4. If so, are there any practical reasons why floating security is difficult to take, maintain or enforce?

Creation

While an individual, a company or another type of entity is permitted to create a fixed charge, an individual is not permitted to create a floating charge.

Maintaining assets

The class of assets subject to a floating charge changes or fluctuates from time to time in the ordinary course of the chargor's business. Therefore, when a floating charge is taken, the arrangement is that, until some future step is taken by, or on behalf of, the chargee (for example, crystallizing the floating charge into a fixed charge), the chargor will carry on its business in the ordinary way in relation to that class of assets (including disposing of those assets) without the chargee's prior consent.

The chargor's freedom to deal with its assets before a floating charge is crystallized into a fixed charge is highly advantageous to a chargor as it gives the chargor flexibility in relation to how it chooses to deal with its assets. At the same time, however, this presents the lender/chargee with the problem of how to prevent the chargor from disposing of all the assets secured by the floating charge. Therefore, a lender usually prefers to take a fixed charge over specific assets of significant credit value and a floating charge over the chargor's other assets.

Priority and enforcement

The holder of a floating charge has several disadvantages compared to a fixed-charge holder, particularly on insolvency, such as the following:

- A floating charge is more susceptible to being avoided on insolvency.
- A floating-charge holder is only paid out of asset realizations after fixed-charge holders, expenses of the insolvent estate and any preferential creditors have been paid in full.

5. May security be granted to a trustee to be held on trust for the lenders from time to time, in such a way that a change of lenders does not require new security to be taken?

Yes, trustee structures are recognized in Singapore, and a security trustee may hold security on trust for the benefit of a class of potentially fluctuating lenders. There is no need to execute new security documents each time the composition of the group of lenders changes.

6. If not, are there any techniques that can be used to achieve substantially the same effect (e.g., parallel debt structures)?

Not applicable.

7. If an agent holds security for the lenders rather than a trustee, is it necessary to take new security on a change of lenders? If no, why not? If yes, are there ways to structure the transaction to avoid such a requirement?

Yes, if an agent holds security for the lenders, it will be necessary to enter into new security documents. Under an agency structure, the original lender transfers its security interests to the new lender by way of novation. The existing agreement between the original lender and the borrower is dissolved and replaced by a new agreement each time a novation takes place. Therefore, the security is discharged each time a novation is executed, and parties need to enter into fresh security documents.

A trust structure is usually adopted to avoid this requirement.

8. Under the laws of this jurisdiction, is there any class of asset over which it is difficult or impossible to grant effective and perfected security, or in relation to which any security granted will be of limited effect?

In general, there are no restrictions on most types of assets that may be provided as security. The type of security interests, and the relevant formalities required to create and perfect the security, vary depending on the type of asset being provided. Please note, however, the following restrictions when creating security:

- An individual will generally not be able to create a floating charge over their property.
- Security over contractual rights can only be created when there is no contractual prohibition or limitation against assignment or when such prohibition or limitation has been waived by the counterparty. In addition, rights under a contract that are "personal" to the contractual parties are not assignable. Examples of such contracts include employment contracts and motor insurance policies.
- Security created over a bare right to litigate, such as a right of action in tort or in restitution, is generally void since such a right is not assignable as a matter of public policy.

9. Under the laws of this jurisdiction, are there any restrictions on offshore lenders taking security over any class of asset?

No, but see the responses to question 8 of this section (which would apply equally to an offshore lender wishing to take security).

10. Must a company receive a corporate benefit in return for giving a guarantee or security? In particular, are there restrictions on the grant of upstream and cross-stream guarantees and security? If yes, briefly what is the effect of these laws?

In Singapore, directors of a company must act in the interests of the company. The Companies Act provides that a director must at all times act honestly and use reasonable diligence in the discharge of the duties of his/her office. The phrase "act honestly" has been interpreted to mean "acting bona fide in the interests of the company in the performance of the functions attaching to the office of director." Directors in Singapore also owe fiduciary duties to act in the interests of the company at common law.

When considering the grant of an upstream or cross-stream guarantee or security, directors must continue to act in the best interests of the company. If a guarantee is given by a subsidiary to secure obligations of its holding company or another subsidiary of the same holding company, directors must be able to show that valid consideration was provided, generally by way of a corporate benefit. A director may take into account factors such as corporate benefit in the form of intercompany loans or by way of other indirect benefits that may flow to the guarantor. These may include a reduced cost of funding or stronger or maintained financial capabilities of the parent or other subsidiary.

Further, a corporate benefit must accrue to the company and not just to another company in the group. What is considered a "corporate benefit" depends on the facts of each case. If the matter is brought to court, this is ultimately a question for the court.

If, at the time of entering into a guarantee, there is any uncertainty in relation to whether there is a corporate benefit, it would be prudent for the directors' resolution to set out the corporate benefit which would accrue to the guarantor and a unanimous shareholders' resolution ought to be obtained. However, even if a shareholders' resolution is obtained, a liquidator may still challenge this because, when the company is insolvent, directors owe their duties to creditors as well as to shareholders.

11. What type of security interests does your jurisdiction recognise, e.g., pledge, charge, mortgage, hypothecation? In relation to each type of security interest, please state the formalities required to create and perfect that security.

Creation

The main forms of security interest that can be created under Singapore law are a mortgage, a charge, a pledge and a lien.

Mortgage

A mortgage involves the transfer of title to an asset by way of security for particular obligations, on the express or implied condition that it will be retransferred when the secured obligations are discharged. A mortgage can generally be applied to tangible and intangible assets. A mortgage over land is created by deed. If the subject matter of the mortgage is not land, a mortgage does not need to be executed by deed.

Charge

A charge is essentially a security interest evidenced by way of an agreement between a creditor and a debtor by which a particular asset is appropriated by the chargor to the satisfaction of a debt owed to the creditor. The chargor does not transfer the legal or beneficial interest in the asset to the chargee but gives the chargee the right to have recourse to the charged asset to realize it towards payment of the debt. In addition, unlike possessory securities such as a pledge and lien, the effectiveness of a charge is not dependent on the chargee obtaining and retaining possession of the charged property. A charge can be either fixed or floating.

Pledge

A pledge is created with the actual or constructive delivery of an asset by the pledgor to the pledgee by way of security, but with ownership of the asset remaining with the pledgor. The pledgee retains possession of the pledged asset until the secured debt is satisfied. If the pledgor does not repay the debt, the pledgee is entitled to sell the pledged asset and use the proceeds to satisfy the debt.

Lien

A lien is a creditor's right to retain possession of a debtor's property until the debt has been repaid, while a contractual lien normally extends by way of contract between the parties. A lien may be created by common law, by contract or by statute.

Perfection

Perfection refers to the requirement to give public notice of a security interest to enable the creditor to enforce its security right against third parties. The main methods by which a security interest can be perfected include registration of the security interest in a public register, taking possession of the asset subject to security or giving actual notice to relevant parties. The perfection requirements in relation to a mortgage, charge, pledge and lien are set out below.

Mortgage

A mortgage over assets created by a Singapore company must be lodged with ACRA (please refer to the answer to question 12 of this section for more information). Additional documents must be lodged in relation to particular classes of assets. For example, in relation to land, a caveat, a mortgage and a memorandum of mortgage must be lodged with the Singapore Land Authority.

Charge

A charge that is created by a company incorporated in Singapore (or the branch of a foreign corporation registered in Singapore) and to which Section 131 of the Companies Act applies must be registered with ACRA (please refer to the answer to question 12 of this section for more information). Non-registration results in the security interest intended to be created by the charge being invalid and unenforceable against the liquidator and other creditors of the company in the event of the company's insolvency or liquidation.

Pledge and lien

Some security interests, such as pledges and liens, are not registrable. In these cases, the usual practice is to give notice to, and obtain acknowledgment from, the applicable third party. A lender also often requires the security provider to represent and warrant that there is no existing security interest over the asset. The possession by the security interest holder of the assets subject to the security interest can also constitute perfection.

12. Are there any registration, translation or notarization requirements in relation to security, guarantees, subordination or intercreditor documents?

Under Singapore law, there are registration requirements in relation to certain security documents (as listed below). However, notarization is not required for security documents that are executed in Singapore.

Registration requirements

If a charge to which Section 131 of the Companies Act applies (listed below) is created by a Singapore-incorporated company, the charge must be registered with ACRA.

Under Section 131 of the Companies Act, the following charges must be registered:

- A charge to secure any issue of debentures.
- A charge on uncalled share capital of a company.
- A charge on shares of a subsidiary of a company which are owned by the company.
- A charge created or evidenced by an instrument which, if executed by an individual, would require registration as a bill of sale.
- A charge on land wherever situated or any interest in the land but not including any charge for any rent or other periodical sum issuing out of land.
- A charge on book debts of the company.
- A floating charge on the undertaking or property of a company.
- A charge on calls made but not paid.
- A charge on a ship or aircraft or any share in a ship or aircraft.
- A charge on goodwill, on a patent or license under a patent, on a trademark, or on a copyright or a license under a copyright, or on a registered design or a license to use a registered design.

In addition, certain assets (particularly assets such as land, ships, aircraft and scripless shares where title to that asset is entered into a register) have specific registration requirements depending on the form of security being created.

Timeline

The company must lodge a statement of particulars of charge with ACRA within (a) 30 calendar days (if executed in Singapore); or (b) 37 calendar days (if executed outside Singapore), of the creation of the charge.

If the charge is not registered, the charge will be void against the liquidator and any creditor of the company in the event of the company's insolvency or liquidation.

13. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in respect of security, guarantees, subordination or intercreditor documents? If yes, what are the amounts and when are they payable?

Stamp duty

Please see the answer to question 8 of the "When lending to borrowers" section.

Registration

ACRA fees for registration of a charge are currently SGD 60. Registration fees vary across other registers (such as those registers relating to land, ships, aircraft and scripless shares) depending on the registration.

If things go wrong

1. Please provide a brief description of the insolvency regime. In particular what rights and duties do unsecured and secured lenders have on the insolvency of a debtor? Are there any other matters of concern?

In Singapore, the usual process by which a company is dissolved is known as a winding-up. Other insolvency-related processes in Singapore include judicial management, a scheme of arrangement and receivership. The Insolvency, Restructuring and Dissolution Act 2018 (No. 40 of 2018) (IRDA) is the main piece of insolvency legislation in Singapore.

Winding-up

When a company is wound up, its assets or the proceeds of its assets are used to pay off creditors, after which the balance, if any, is distributed pro rata among shareholders. Companies may be wound up voluntarily or compulsorily. A company may initiate a members' or creditors' voluntary winding-up (the former only when the company is insolvent at the time of the winding-up). A compulsory winding-up may take place by order of the court. The IRDA specifies certain persons and classes of stakeholders who may apply to the court to wind up the company. The court may order the winding-up of the company in certain circumstances. The usual ground is when the company is unable to pay its debts. The most common method of establishing the company's inability to pay its debts is to serve on the company a statutory demand for an undisputed debt exceeding SGD 15,000. A company is deemed unable to pay its debts if, among others, it fails to pay or secure or compound the amount within three weeks after the demand is served. In both types of winding-up, a liquidator will be appointed to realize and distribute the company's assets in accordance with the IRDA.

Ranking of debts

Subject to the bankruptcy/insolvency laws discussed below, generally speaking, to the extent that the loan is unsecured, a lender's claim against the borrower would rank pari passu with other unsecured claims. If the loan is secured by security over an asset of any security provider, then to the extent of the value of the asset subject to the security that may be realized through the enforcement of that security, the lender's claims against the security provider will generally have priority over the claims of other creditors of that security provider.

The IRDA sets out certain exceptions to the general pari passu principle and provides for preferential debts to be paid in priority to all other unsecured debts. These are (in the following order and priority):

- Costs and expenses of the winding-up, including the following:
- Those incurred by the official receiver as the liquidator of the company, including the costs, expenses and remuneration of a licensed. insolvency practitioner to act as liquidator in the place of the official receiver.

- The liquidator's remuneration and the costs of any audit carried out under the IRDA.
- The applicant's costs for the winding-up order payable under the IRDA.
- All wages or salary (whether earned wholly or in part by way of commission), including any amount payable by way of allowance or reimbursement under any contract of employment, award or agreement regulating conditions of employment of any employee up to a limit as prescribed by the minister by order published in the Singapore Gazette (presently prescribed as SGD 13,000 as at the date of this publication).
- The amount due to an employee as a retrenchment benefit or ex gratia payment under any contract of employment, award or agreement that regulates conditions of employment, whether that amount becomes payable before, on or after the commencement of the winding-up to a limit as prescribed by the minister by order published in the Singapore Gazette (presently prescribed as SGD 13,000 as at the date of this publication).
- All amounts due in relation to work injury compensation under the Work Injury Compensation Act 2019 accrued before, on or after the commencement of the winding-up.
- All amounts due in relation to contributions payable during the 12 consecutive months before, on or after the commencement of the winding-up by the company as the employer of any person under any written law relating to employees' superannuation or provident funds or under any scheme of superannuation that is an approved scheme under the law relating to income tax.
- All remuneration payable to any employee in respect of vacation leave or, in the case of their death, to any other person in their right, accrued in respect of any period before, on or after the commencement of the winding-up to a limit as prescribed by the minister by order published in the Singapore Gazette (presently prescribed as SGD 13,000 as at the date of this publication).
- The amount of all tax assessed and all goods and services tax due under any written law before the commencement of the winding-up or assessed at any time before the time fixed for the proving of debts has expired.

The above preferential debts (except the amounts due in relation to workers' injury compensation under the Work Injury Compensation Act 2019 and taxes) must be paid out of the proceeds of any property subject to any floating charge created on the company's property, in priority to the claims of the holder of the floating charge, if the company's assets available for payment of general creditors are insufficient to meet any of these preferential debts.

The IRDA also provides that where any winding-up assets have been recovered under an indemnity for costs of litigation given by certain creditors, protected or preserved by the payment of moneys or the giving of an indemnity by creditors, or where expenses in relation to which a creditor has indemnified a liquidator have been recovered, a Singapore court may make any order that it thinks just in relation to the distribution of those assets and the amount of the expenses recovered with a view to giving those creditors an advantage over others in consideration of the risks run by them in taking that action.

Further, rescue financing may be extended to the debtor company during a scheme of arrangement or judicial management. If such arrangements preceded winding-up, it would rank as the costs and expenses of the winding-up above all preferential debts. Such rescue financing may also be secured by the debtor company's assets. In such cases, it may rank below, equally or even above existing security interests, depending on whether the financing could have been obtained without such security and on whether there is adequate protection for existing security holders.

2. Is it possible to obtain a moratorium before insolvency?

There are two corporate rescue mechanisms in Singapore that allow for a moratorium to be obtained before the commencement of any winding-up proceedings namely judicial management and schemes of arrangement.

Under the judicial management regime, an interim moratorium will be effective from the date an application is made for a judicial management order. However, an application for judicial management ought only to be made if, among other things, the applicant considers that the company is or is likely to be unable to pay its debts. This, therefore, means that a company may make an application to the court for itself to be placed under the judicial management of a judicial manager even if it is not technically insolvent, as long as it is facing impending insolvency.

Conversely, the scheme of arrangement regime does not require there to be insolvency or impending insolvency. There are two routes by which a company may apply for a moratorium in support of a scheme or proposed scheme.

The first is under Section 64 of the IRDA ("**Section 64 Stay**"), where the company may apply for a moratorium when it proposes or intends to propose a scheme, as long as it, among others, undertakes to make a scheme application as soon as practicable. A Section 64 Stay may (subject to the court's order) apply to acts outside of Singapore. An automatic 30-day moratorium arises once an application for a Section 64 Stay is made. Related companies, i.e., subsidiaries, holding and ultimate holding companies, of the scheme company may also apply for a moratorium if, among other requirements, they play a necessary and integral role in the scheme and the scheme will be frustrated if such a moratorium is not granted.

The second is under Section 210(10) of the Companies Act. This is a more limited form of moratorium that does not come with the automatic stay (but a company can apply for one), the worldwide effect or the possibility of related companies moratoriums available under the Section 64 Stay. However, unlike the Section 64 Stay, the application under Section 210(1) of the Companies Act may be made in a summary way by any member, creditor or holder of units of shares of the company, and is not expressly subject to the same extensive disclosure requirements (both on application and post-application) or the carve-outs for netting and other arrangements. However, an application under Section 210(10) of the Companies Act may only be made after a scheme is proposed, with the scheme being of sufficient particularity for the court to make a broad assessment that there is a reasonable prospect of the scheme working and being acceptable to the general run of creditors. However, this scheme need not be of the same degree of particularity or of the same terms as the plan that is to be presented to the creditors for voting.

3. When a company is the subject of a formal insolvency procedure, can the company's pre-insolvency transactions be set aside?

Briefly, under Singapore insolvency laws, if a Singapore company enters into a winding-up, certain transactions (including the granting of security or guarantees) may be set aside by order of court on application of the liquidator or judicial manager. There are several grounds for setting aside transactions and they are discussed below.

Transactions at an undervalue

A transaction entered into by the company at any time within three years prior to the commencement of its winding-up or judicial management may be set aside if it was at an undervalue and if, at the time the transaction was entered into, the company was insolvent or became insolvent as a consequence of the transaction. A transaction is deemed to be entered into at an undervalue if it was entered into with a person on terms that meant that the company receives either no consideration or a consideration worth significantly less than the value of the consideration provided by the company to the person. The company's insolvency at the time of the transaction is presumed unless proven otherwise if the person who entered into the transaction is connected (otherwise than by reason only of being the company's employee) to the insolvent company. However, a transaction at an undervalue will not be set aside if the court is satisfied that the company entered into the transaction in good faith and for the purpose of carrying on its business and that at the time the company did so, there were reasonable grounds for believing that the transaction would benefit the company.

Unfair preferences

Any act of the company carried out within one year prior to the commencement of the winding-up or judicial management of the company (or within two years prior to the commencement of the winding-up or judicial management of the company for transactions involving associates of the company) may be set aside if classified as an unfair preference. The requirement is satisfied if, at the time the act was done, the company was insolvent or became insolvent as a consequence of the act, and that act has the effect of putting the person preferred in a better position than that person would have been in if the act had not been carried out. However, a Singapore court would not make an order setting aside the act as an unfair preference if it was satisfied that the company, when giving the preference, was not influenced by a desire to put that person in a better position.

Extortionate credit transactions

Where a company is in judicial management or is being wound up, any transaction involving the provision of credit to the company within three years prior to the commencement of the winding-up or judicial management of the company that is extortionate may be set aside by order of court on application by the liquidator or judicial manager. Unless proved to the contrary, a transaction is presumed to be extortionate if, with regard to the risk accepted by the person providing the credit, the terms require grossly exorbitant payments to be made (whether unconditionally or in certain contingencies) in relation to the provision of the credit or if the terms are harsh and unconscionable or substantially unfair.

Registrable but unregistered charges

Any security created by a registrable but unregistered charge is void against the liquidator of the company or any creditor of the company. This applies to a company incorporated in Singapore and the branch of a foreign company registered in Singapore.

Floating charges for past value

A floating charge in relation to the undertaking or property of the company created within one year of the commencement of the winding-up or judicial management (or within two years for transactions involving person connected with the company) or on or after the commencement of judicial management of the company up to the date the company enters into judicial management is invalid except in relation to the amount of any money received or reduction in its debts, or a reduction of an interest owing to the chargee at the time of, or after, the creation of, and in consideration for, the charge. Where the chargee is not connected with the company, the floating charge will not be invalidated unless the company is insolvent at the time the charge is created or becomes insolvent in consequence of the transaction under which the charge is created.

The IRDA now expressly empowers liquidators and judicial managers to assign proceeds of actions relating to, among others, transactions at an undervalue, unfair preferences and extortionate credit transactions. This provides the option for liquidators to obtain third-party funding to pursue claims related to the categories above, which would otherwise not have been pursued.

4. When can a lender enforce its security? Can security be enforced out of court following an event of default (or other contractual trigger event), or is a court order required? Are there any restrictions that apply before a lender may enforce its security?

Generally, when and how a lender can enforce its security depends on the contractual agreement between the lender and the borrower. A lender can generally enforce its security without court involvement. The security document will typically provide when the security is enforceable. For instance, on the occurrence of an event of default such as failure to pay, breach of certain obligations and insolvency and/or if the lender has accelerated the loans. The type of security interest that the lender holds also affects how the security can be enforced. A well-drafted security document would usually expressly provide for the right to possession, a power of sale or the option to appoint a receiver, which the lender can enforce out of court based on the terms of the agreement, usually on default (or a continuing default) by the borrower. These remedies can be cumulative and not mutually exclusive. Enforcement powers may also be implied by statute and common law if not expressly provided.

There may be overriding restrictions or limitations on the lender's enforcement power. If there is a Section 64 Stay, a moratorium pursuant to Section 210 (10) of the Companies Act, or a moratorium following a judicial management application, then enforcement of any security over the debtor company may not be possible except with leave of court. Further, Section 440 of the IRDA also renders void any contractual provisions that purport to:

a. terminate or amend, or claim an accelerated payment or forfeiture of the term under any agreement with the company; or

b. terminate or modify any right or obligation under any agreement with the company

at any time after the commencement of judicial management or scheme of arrangement proceedings by reasons only that the proceeds are commenced or that the company is insolvent.

Enforcement powers might also be contractually limited, such as when there are intercreditor arrangements governing enforcement and standstill agreements that restrict enforcement over specified periods of time. Additionally, foreclosure as a remedy can only be effected by an order of the court.

5. Do any limitation periods apply in relation to bringing an action to enforce security?

No action is permitted to be brought to enforce a mortgage or charge after the expiration of 12 years from the date when the right to receive the money secured by the mortgage or charge has accrued. Additionally, no foreclosure action in relation to mortgaged personal property is permitted to be brought after the expiration of 12 years from the date on which the right to foreclose accrued. However, the right to foreclose on the property subject to the mortgage or charge is not deemed to accrue as long as that property comprises any future interests or any life insurance policy that has not matured or been determined.

Further, no action to recover arrears of interest payable in relation to any sum of money secured by a mortgage or other charge or payable in respect of the proceeds of the sale of land (or to recover damages in respect of those arrears) is permitted to be brought after the expiration of six years from the date on which the interest became due.

6. Is there any particular way in which secured assets must be liquidated on enforcement (e.g., by auction or court sale)?

A lender is under a duty to act in good faith and to take reasonable steps to obtain a fair price when exercising a power of sale. The lender would be entitled to choose when to sell the secured property and need not wait until the potential sale price improves before selling it. However, the lender has a duty to obtain the best price that can be reasonably obtained at the time of sale. In addition, the lender would have to act with reasonable care and skill and to act fairly in exercising its power of sale.

Most sales by secured parties are carried out without the need to obtain a court order to effect the sale. A court is unlikely to interfere in the sale as long as the lender complies with its duties as mentioned above. However, these duties mean that the lender would not be permitted to sell the assets to itself, unless it does so through a court sale. A common and reasonable way of ensuring that a lender properly discharges its duties is by having the secured assets sold through a public auction.

7. Are there any particular legal or practical difficulties or delays in enforcing security?

Enforcement of security is usually the last resort for a lender because enforcement can have very serious and far-reaching consequences for the borrower. These include cross-default by the borrower under any other security agreements that it has entered into and the eventual winding-up of the borrower. Therefore, in practice, a lender would usually explore and exhaust other options in relation to a borrower's default before exercising its right of enforcement.

If the lender decides to enforce its security, the borrower or third-party creditors may also challenge the validity of that security. This may cause delays in the enforcement process. It is therefore common for a lender to seek a security review by its lawyers, which would examine the effectiveness and enforceability of its security, before proceeding with enforcement.

As mentioned in the answer to question 4 of this section, if there are intercreditor arrangements, standstill agreements and statutory restrictions, these may cause difficulties in relation to the enforcement of security. In addition, if winding-up proceedings have already commenced or if the borrower is under judicial management, or steps are taken to enter into a scheme of arrangement, the company may be protected by a moratorium which prohibits enforcement against the secured assets by lenders except with permission from the court.

Another difficulty that arises in relation to the enforcement of security is if the debtor's assets either cannot be located or have been removed from Singapore. With respect to locating the debtor's assets, if the lender has obtained a judgment or an order for payment against the debtor, it may apply to the court for an order that the debtor or the debtor's officers attend before a registrar of the court and be orally examined in relation to where the property is situated. In relation to the risk of the debtor removing assets out of Singapore, the lender may seek a Mareva injunction to restrain the debtor from doing so, pending the outcome of any legal action commenced against the debtor.

Note that the remedy of possession is rarely used in commercial transactions. One reason for this is the possibility of the lender being exposed to liabilities while in possession of the asset, e.g., the possibility of becoming liable for environmental damage if the asset in possession is land. Another reason is the additional burden placed on the lender in possession to account to the borrower for any income and profit received. Further, if the lender takes possession of a profit-yielding asset, it is under a duty to ensure that reasonable profits are continually collected in relation to that asset. If profits (in excess of the sum due to the lender) that would have been received were not received due to the willful neglect of the lender (e.g., if the lender did not lease out the property when it could have done so), it could be liable to the borrower for the loss of those profits that are in excess of the sum owing to the lender. Because of these concerns, a receiver's appointment is generally preferred over a lender taking possession of the secured assets by itself.

For personal and corporate guarantees, the enforcement is typically through the commencement of legal proceedings. Usually, a claim under a guarantee should be fairly straightforward and therefore capable of being summarily disposed of without the need for discovery or trial. However, in practice, these summary disposals of enforcement actions are sometimes not possible if the guarantor or primary debtor raises issues such as duress, undue influence or misrepresentation in relation to the execution of the guarantee. In these situations, the lender may find that it has to incur the substantial time and expense to enforce the guarantee.

Finally, in most security documents involving international parties, it is fairly common for parties to provide for arbitration (or other alternative dispute resolution mechanisms, e.g., mediation or expert determination) as the mode of dispute resolution as opposed to having recourse to national courts. In such cases, there may be a risk that enforcement may be met by arguments by the debtor alleging that its liability is disputed and ought to be determined by way of arbitration before enforcement can be resorted to. This presents a risk of delay in enforcing the security — particularly if recourse to national courts is required as part of the enforcement process (e.g., court-ordered receivers, foreclosure, etc.).

8. In relation to enforcement, are there any specific requirements to be borne in mind if the lender is a foreign entity?

There are generally no specific requirements in relation to enforcement actions by a foreign entity. However, if a foreign lender commences court proceedings in Singapore against a defaulting borrower, the foreign lender may, on the application of the defendant borrower, be ordered to pay security for the defendant's costs in the proceedings if it appears that the foreign lender will be unable to pay the defendant's costs if the defendant is successful. In such cases, the legal proceedings may be stayed until that security is provided.

A foreign entity could be classified as a moneylender under the Moneylenders Act. If so, a loan granted by an unlicensed moneylender, together with the security given under that loan, will be unenforceable. Therefore, it is advisable to check if the lender falls into the classification of a moneylender under the Moneylenders Act (as discussed in the answer to question 1 of the "When considering whether to lend" section) and for the lender to be licensed if it does not qualify for an exemption or fall under a category of excluded moneylender.

9. Is there any reason why you think that arbitration rather than litigation might be advantageous in resolving disputes under the finance documents, and if so, why? Please outline the relative merits of arbitration and litigation, including the ease of enforcement of foreign judgments and foreign awards from different jurisdictions. Is it possible to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit?

Enforcement

The main advantage of arbitration is the general ease of enforcement of an arbitral award in more than 150 countries under the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958, to which Singapore is a signatory. The convention lays down a system for the mutual recognition and enforcement of arbitral awards among countries that are parties to the convention without reviewing the merits of the arbitral award. The result is that arbitral awards receive greater recognition internationally than most national court judgments.

Flexibility

Flexibility is another key advantage of arbitration because an arbitral tribunal must conduct the arbitration according to the parties' agreement and their reasonable requirements. The parties are free to choose their arbitration rules or select their own procedures in their arbitration agreements. Parties can select a neutral forum. They can also decide on the arbitrators with subject matters expertise in the areas of dispute. Conversely, in litigation, rules of court dictate the procedures and these are often more rigid than arbitration rules.

Confidentiality

Confidentiality is another compelling advantage of arbitration if the parties want to avoid publicity or if the dispute involves commercially sensitive matters. Furthermore, the private and less formal settings in arbitration tend to be more collegial than traditional courtroom litigation, therefore better for preserving business relationships between the parties.

Time

Time could also be a reason for preferring arbitration to litigation. On the one hand, arbitration is generally regarded as the more efficient dispute resolution mechanism when compared to litigation. However, with the greater flexibility in arbitration rules, the length of arbitrations could also greatly depend on the parties' conduct. For example, the parties may attempt to delay arbitration for tactical reasons by repeatedly seeking for extensions of arbitration timelines. On the other hand, Singapore's courts are widely perceived to be efficient and reliable. Therefore, it is arguable that there is no clear advantage in efficiency when preferring arbitration to litigation in Singapore.

Costs

Costs are traditionally considered to be lower for arbitration than for litigation. However, this may not necessarily be the case; instead, increasingly, the opposite might be true. The cost of commencing arbitration is generally more expensive than filing a claim in court. The fees of a three-arbitrator tribunal are also likely to be high, depending on the choice of arbitrators. Comparatively, the cost of litigation is relatively standard but can also be high if, for example, the process involves extensive discovery and protracted interlocutory applications.

Right of appeal

A disadvantage of arbitration is the possibility of inconsistent outcomes as compared to litigation in common law jurisdictions, including Singapore, which follow the principle of stare decisis, i.e., where precedents from higher courts are binding on the lower courts. Arbitral awards are also usually final with limited scope for appeal on the merits. Conversely, litigants generally have a right to appeal on the merits against a court judgment. However, the finality of arbitral awards could be an advantage for parties seeking to move on quickly from the dispute rather than having disputes drag on for years due to the possibility of an appeal.

Election of the dispute resolution mechanism

Asymmetric arbitration clauses (i.e., allowing only one party to elect between arbitration and litigation) are generally enforceable in Singapore.

10. Are asymmetrical jurisdiction clauses enforceable? (By this we mean clauses that allow the lenders, but not the borrowers, to make certain choices in relation to choice of jurisdiction and how to litigate. These types of clauses allow the lenders, but not the borrowers, to commence proceedings in any court they choose, but restrict the borrowers to commencing proceedings in one jurisdiction only. This may also allow the lenders, but not the borrowers, to choose whether to litigate the finance documents before a court or to submit to arbitration in relation to them, but restrict the borrowers to either litigation or arbitration, as specified in the agreement).

An asymmetric jurisdiction clause freely entered into between the parties will generally be enforced by the Singapore courts. Similarly, asymmetric arbitration clauses are also enforceable in Singapore.

Working digitally

1. Is it possible for documents to be executed electronically (whether by the manual insertion of a digital signature or the use of an e-signing platform) under the laws of this jurisdiction? If so, is this limited to only particular types of finance documents?

Yes, the electronic execution of a document (including the insertion of a digital signature and digital signing using e-signing platforms) is valid under Singapore law for most contractual documents, as recognized by the Electronic Transactions Act 2010 (ETA).

However, there are various documents and transactions, which are set out in the First Schedule to the ETA, that are excluded from the scope of operation of the provisions in the ETA that enable electronic signatures to satisfy legal requirements for wet ink signature. The excluded documents include (1) documents for the creation, performance or enforcement of an indenture (i.e. a legal document that sets out rights and obligations of lenders and borrowers, or mortgagees and mortgagors); (2) documents that create a declaration of trust or power of attorney; and (3) the transfer of any interest in immovable property.

Declarations of trusts or powers of attorney are typically not executed as standalone documents in a financing transaction, but are embedded as provisions in financing documents such as security documents, which should be executed as deeds.

Under common law, the requirements for the formation of a deed are that the deed must be: (i) in writing; (ii) signed; (iii) sealed; (iv) attested; and (v) delivered. For borrowers who are Singapore companies, deeds may be executed by: (a) affixation of the company's common seal of the company in accordance with the terms of its constitution;[5] or (b) without its common seal by signature of prescribed officials of the company.[6] Attestation requires physical attestation, and witnessing over virtual means is not advisable. Given the requirement of physical attestation for execution of deeds by borrowers who are individuals and execution of deeds by borrowers who are Singapore companies (executing the deed by way of section 41B(1)(c) of the Companies Act or by way of affixing

5 The constitution of most Singapore companies would provide that every instrument to which the common seal is affixed shall be signed autographically by a director and the secretary or a second director or some other person appointed by the directors.

6 Under section 41B of the Companies Act, a Singapore-incorporated company may execute a document described or expressed as a deed without affixing a common seal onto the document by signature:

- on behalf of the company by a director of the company and a secretary of the company;
- on behalf of the company by at least two directors of the company; or
- on behalf of the company by a director of the company in the presence of a witness who attests the signature.

the common seal)[7] and the inability to rely on the ETA for such deeds, "wet ink" signatures are thus required for such financing documents that are executed as a deed.

Mortgage over land

As a mortgage over land is a security document that involves the transfer of interest over immovable property, it is thus excluded from the scope of the ETA. Therefore, electronic signatures cannot be used as an alternative to wet ink execution of a mortgage over land. Further, mortgages over land require registration in Singapore, and the Land Titles Registry requires an original hardcopy of the mortgage instrument and original title deeds (if applicable) to be submitted for registration. Due to this requirement, the mortgage cannot be signed electronically.

2. Where the witnessing of a signing is contemplated, is it possible for the witness to verify the signature over a live video call?

It is not clear if virtual witnessing (i.e., witnessing a signing over a live video call) is valid under Singapore law. The present view is that witnessing requires physical presence in order to satisfy legal execution formalities. Witnessing over virtual means is not advisable.

3. Is it possible to register/perfect security electronically without wet ink signatures?

As mentioned in our answer to question 11 of the "If taking security" section, perfection refers to the requirement to give public notice of a security interest to enable the creditor to enforce its security right against third parties. The validity of perfection of security electronically in relation to a mortgage, charge, pledge and lien is set out below:

Mortgage

In general, a mortgage over assets created by a Singapore company must be lodged with ACRA and this can be done electronically without wet ink signatures. However, additional documents may need to be lodged in relation to particular classes of assets that cannot be signed electronically. For example, in relation to land, the Land Titles Registry requires an original hard copy of the mortgage instrument and original title deeds (if applicable) to be submitted for registration. Due to this requirement, the mortgage cannot be signed electronically.

Charge

A charge that is created by a Singapore company incorporated in Singapore (or the branch of a foreign corporation registered in Singapore) and to which Section 131 of the Companies Act applies must be registered with ACRA. This can be done electronically without wet ink signatures.

Pledge and lien

With regard to the perfection of certain pledges and liens, giving notice to and obtaining acknowledgement forms from the applicable third party can be done electronically without wet ink signatures.

4. Are there any other legal restrictions that may prevent the parties from executing a finance transaction electronically?

Please refer to our answers to questions 1 to 3 of this section above.

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7 If the Borrower executes the deed by way of section 41B(1)(c) of the Companies Act with one director signing in the presence of an attesting witness, physical attestation would be required. In addition, if the Borrower executes the deed by way of affixation of the common seal, a physical copy of the document would be required to affix the common seal thereon.

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TAIWAN

Taiwan

When considering whether to lend

1. **Is it necessary or advisable for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in this jurisdiction: (a) by reason only of its execution, delivery or performance of the finance documents; or (b) to enable it to enforce its rights under the finance documents?**

   Yes. Only a licensed bank, insurance company or other entity with permission from the Financial Supervisory Commission (FSC) is allowed to conduct the business of lending money.

   However, if the finance documents are executed and delivered outside Taiwan, a lender, arranger, facility agent or security agent may enforce them in Taiwan without being licensed, qualified or otherwise entitled to carry on business in Taiwan.

2. **Will any lender, arranger, facility agent or security agent be deemed to be resident, domiciled, carrying on business or subject to tax by reason only of the execution, delivery, performance or enforcement of the finance documents?**

   If a lender, arranger, facility agent or security agent (being a licensed bank, insurance company or other entity with permission from the FSC, as mentioned in our answer to question 1 of this section) executes, delivers and performs the finance documents in Taiwan, it may be held to be conducting the business of lending money, and be subject to tax, in Taiwan.

   In the case of a foreign lender, arranger, facility agent and security agent, if the finance documents are signed offshore and the loan(s) are disbursed to bank account(s) outside Taiwan, and no business activity is conducted in Taiwan, they will not be deemed to be resident, domiciled or carrying on business in Taiwan by reason only of the execution, delivery, performance or enforcement of the finance documents.

3. **Are there any regulatory reporting requirements that lenders must observe in connection with those transactions?**

   Yes. If a lender is a public company, it must disclose its lending amount in its financial report in accordance with the relevant guidelines for the preparation of financial reports. If a lender is a financial institution, it must keep all documentation in connection with the transactions, which are subject to the FSCs periodic inspection.

4. **Is it necessary to establish a place of business in your jurisdiction in order to enforce any provision of the finance documents?**

   No. According to Supreme Court decisions and the Civil Procedure Act of Taiwan, an unrecognized foreign entity (i.e., a foreign entity that has not obtained registration or other legal recognition in Taiwan or does not have a representative office or branch in Taiwan) is allowed to initiate legal proceedings in Taiwan through its representative (being an individual) in Taiwan.

   In relation to the possible difficulties that could be encountered by foreign entities when taking and enforcing security interests over assets in Taiwan, see the answer to question 9 of the "If taking security" section.

5. **Is a foreign bank/financial institution permitted to approach local entities for business?**

   No. In Taiwan, business and related activities conducted by financial institutions are highly regulated. A foreign bank/financial institution is not permitted to conduct any business or related activity in Taiwan, such as approaching local entities for business unless it obtains the approval of/permission from the FSC to establish a branch in Taiwan.

When lending to borrowers

1. **Are there any restrictions in relation to the type of borrower who may borrow foreign currency or in relation to the term of foreign currency and/or the amount of foreign currency borrowed by local entities?**

   No.

2. **Are there any restrictions on the rate of interest or default interest that may be charged?**

   Yes. The Legislative Yuan of Taiwan passed an amendment to the Civil Code that specifies that if the rate of interest (ROI) exceeds 16% per annum, the portion of interest exceeding 16% is invalid. This latest amendment took effect in July 2021.

3. **Are there any restrictions on particular lenders or classes of lender entering into credit transactions with borrowers?**

   Yes. As mentioned in the answer to question 1 of the "When considering whether to lend" section, only limited types of licensed financial institutions with permission from the FSC are allowed to act as a lender (or arranger, facility agent or security agent) in connection with an onshore loan facility.

4. **Are there any exchange controls that will apply to payments to be made in foreign currencies or to foreign lenders?**

   Taiwan nationals may convert an aggregate amount of New Taiwan dollars equivalent to no more than USD 50 million (in the case of a legal entity) or USD 5 million (in the case of a natural person) into foreign currencies each year without approval from the Central Bank of the Republic of China (Taiwan) (CBC) (although all remittances (including inbound and outbound) and foreign exchange transactions exceeding the equivalent of TWD 500,000 must be reported to the CBC). If the total conversion amounts in a year exceed USD 50 million (in the case of a legal entity) or USD 5 million (in the case of a natural person), CBC approval is required.

5. **Is there any requirement to deduct or withhold tax from any amounts to be paid or repaid to a lender (whether domestic or foreign)? If so, at what rate must tax be deducted and from what kinds of payment?**

   A 5% gross business receipts tax applies to interest and fees paid to a Taiwanese financial institution. In practice, borrowers generally agree to pay the gross business receipts tax.

   Interest and fees paid to a foreign bank or lender (regardless of whether it is a bank or not) and an arranger, facility agent and security agent without a branch office in Taiwan are subject to a 20% withholding tax. However, as of 30 June 2023, Taiwan has double taxation agreements with 34 countries, most of which offer a preferential withholding rate of 10% that applies to interest. The following countries have entered into double taxation agreements with Taiwan: Australia, Belgium, Denmark, France, Germany, Malaysia, New Zealand, the Netherlands, Sweden, Switzerland, the UK, Singapore, Indonesia, South Africa, Vietnam, Gambia, Eswatini, North Macedonia, Senegal, Israel, Paraguay, Hungry, India, Slovakia, Thailand, Kiribati, Luxembourg, Austria, Japan, Italy, Canada, Poland, the Czech Republic and Saudi Arabia.

6. Are there any "thin capitalization" or other rules that may limit the extent to which interest payments may be deducted for tax purposes?

The "thin capitalization rule" under the Taiwan Income Tax Act only applies to loans and interest payments between related parties. Excess interest payments are not considered an expense or loss if the proportion of related party debt to equity of a profit-seeking enterprise exceeds a specified ratio (currently, the ratio is 300%).

However, this "thin capitalization rule" does not apply to interest payments to banks, credit cooperatives, financial holding companies, bills finance companies, insurance companies and securities firms.

7. Are there any registration, notarization, translation or reporting requirements in relation to the loan documents?

No. In relation to the registration of mortgages over real property and chattels, see the answer to question 11 of the "If taking security" section. Furthermore, if a foreign institution is going to lend to a Taiwanese borrower, the Taiwanese borrower may opt to report that "foreign debt" to the CBC for its records, which will facilitate the outward payment and repayment of the loan (see the answer to question 4 of this section in relation to foreign exchange control mechanisms).

8. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to the loan documents? If yes, what are the amounts and when are they payable?

No. In relation to duties and fees chargeable in respect of security, guarantees, subordination or intercreditor documents, see the answer to question 12 of the "If taking security" section.

9. Does the law recognize the subordination of the debt that a debtor owes to one creditor to that which the debtor owes to another creditor? If yes, how is this usually effected?

Yes. A debtor may agree with a creditor ("**first creditor**") that it will not pay down the debt owed to another creditor ("**second creditor**") before the full repayment of the debt owed to the first creditor. The debtor, the first creditor and the second creditor may enter into a subordination agreement to record their agreement or the second creditor may enter into a subordination undertaking in favor of the first creditor.

10. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors (e.g., the claims of employees and tax authorities or the claims of creditors under particular kinds of instrument)? If yes, what classes of creditors are preferred?

Yes. The claims of all unsecured and unsubordinated creditors rank equally, except for the following, which — together with the claims referred to in paragraph 1 of the "If taking security" section — rank above the claims of the other unsecured creditors and in the following order:

- The fees and expenses of the enforcement proceedings.
- Land value increment tax, land value tax, house tax and/or business tax levied on the property/goods auctioned by a court or an administrative enforcement agency.
- Unpaid wages owed to the employees (up to six months' wages) of the debtor under their labor contracts, retirement pensions that the debtor has failed to disburse and severance payments.
- Other unpaid taxes.

11. Are there any consumer protection or similar laws that apply if credit is made available to individuals or other classes of debtor? If yes, what laws are applicable?

Yes. There are protection mechanisms in the Financial Consumer Protection Act that apply to agreements between a financial institution and a "financial consumer," such as requirements imposed on a financial institution to conduct a mandatory risk tolerance assessment in relation to each financial consumer and to give reasonable disclosure of the standard bank forms adopted by a financial institution when that financial institution provides any product or service to a financial consumer. A financial institution that fails to comply with these requirements and causes harm to a financial consumer is liable for damages to the financial consumer.

The term "financial consumer" means a person that receives financial products or services provided by a financial institution, but it does not include the following:

- A qualified institutional investor
- An individual or legal entity with a prescribed level of financial capacity or professional expertise

12. Are there any prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of: (a) its own shares or those of any affiliated company; or (b) assets owned by it or any affiliated company?

Under the Taiwan Company Act and the Regulations Governing Lending of Funds and Making of Endorsements or Guarantees by Public Companies ("**Lending or Guarantees Regulations**"), a Taiwanese company is prohibited from lending to any of its shareholders or any other person except in the following circumstances:

a. Where an intercompany or interfirm business transaction calls for the lending arrangement.

b. Where an intercompany or interfirm short-term financing facility (not more than one year) is necessary.

If the lending entity is a public company and the ground for the lending is item (a) above, the amount of the loans under exception (a) must be equivalent to the value of the intercompany transaction (such as the supply, sale or distribution transaction) between the lending company and the borrower. The amount of the short-term financing facility under exception (b) must not exceed 40% of the net worth of the lending company. Any responsible persons of a lending company (such as the directors, supervisors and managers) who violate these regulatory restrictions will be liable, jointly and severally, with the borrower for the repayment of the loan and any damage suffered by the lending company because of any violations.

In relation to financial assistance in the form of providing guarantees, see the answer to question 9 of the "If taking security" section.

If taking security

1. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's secured creditors?

The enforcement fees incurred and paid to the court in accordance with the applicable laws and the following preferential rights to payment provided by law have priority over secured claims as described below:

- Land value increment tax, land value tax, house tax and business tax levied on property/goods auctioned by a court or administrative enforcement agency have priority over all other claims and mortgages.
- Fines, costs and payments for pollution remediation under the Soil and Groundwater Pollution Remediation Act take priority over all creditor and mortgagee rights.

The following preferential secured claims rank ahead of other secured claims:

- When a contract is for work on the construction of a building or other works on land or for vital repairs in relation to that building or those works, an unsecured contractor may demand that the proprietor register a mortgage in favor of the contractor over the building or the land, or the building to be constructed, to secure the remuneration and payments to be made to the contractor. The mortgage would rank above any mortgage registered earlier to the extent of the value of the work.
- If an act of a mortgagor is likely to cause a reduction in the value of the mortgaged property, the mortgagee may demand the cessation of the act and take any necessary action to safeguard the mortgaged property. The mortgagor bears the costs incurred for a demand or specified disposition and the claims for those costs have priority over claims secured by any mortgage on the property.
- When a lien holder takes possession of or retrieves the relevant property of a chattel secured transaction (such as a chattel mortgage) in accordance with the Chattel Secured Transaction Act, a bona fide lien holder's expenditure for the repair or addition of work to the relevant property of the chattel secured transaction, which increases the value of the chattel, is given priority of satisfaction, to the extent of the increase in value, over any chattel secured rights that were previously established in accordance with the Chattel Secured Transaction Act.

Further, when an employer has suspended or liquidated its business or has been declared bankrupt, the following rights of the employees rank equally and pro rata with those of the holders of any first priority security interests:

- Unpaid wages for less than six months.
- Pensions that the employer has failed to disburse in accordance with the Labor Standards Act.
- Severance pay that the employer has failed to disburse in accordance with the Labor Standards Act or the Labor Pension Act.

2. May security given by a company rank in a specified order so as to secure liabilities owed to different creditors of the company in that order and, if that is not possible, is it viable for parties to enter into a contractual arrangement for the purposes of moderating this order?

Yes, but this is only applicable to a mortgage of real property and chattels (such as machinery, equipment, tools, raw materials, semi-finished products, finished products, vehicles, forestry, fishery, agricultural and livestock products, livestock and vessels), in respect of which registration with the relevant authority or authorities would cause it to:

- Become effective in the case of a mortgage of real property.
- Be effective against a bona fide third party in the case of a mortgage of chattels.

In these cases, the mortgagor and the mortgagee may determine and designate the priority of multiple mortgages in relation to the same property.

3. Does this jurisdiction recognise the concept of floating security or similar equivalent (i.e., security over a changing pool of assets that the company giving the security is free to buy, sell and generally deal with)?

No. Under the laws of Taiwan, there is no floating charge concept, and a charge over a changing pool of assets is not possible. Each time there is a change of assets in the pool, the changed pool of assets must be repledged or remortgaged and (if required) reregistered.

4. If so, are there any practical reasons why floating security is difficult to take, maintain or enforce?

Not applicable.

5. May security be granted to a trustee to be held on trust for the lenders from time to time, in such a way that a change of lenders does not require new security to be taken?

No, this type of trust regime is not recognized. However, a trust in relation to a mortgage or pledge is permissible for securitization purposes only, in which case the security interest concerned may be held by a trustee, as provided under the Financial Asset Securitization Act.

6. If not, are there any techniques that can be used to achieve substantially the same effect (e.g., parallel debt structures)?

The lenders may appoint an agent that is also a lender and that has joint and several rights with the lenders to act for and on behalf of the lenders to hold the security interest and may be registered as the mortgagee or possess the pledged property and any documents evidencing it.

7. If an agent holds security for the lenders rather than a trustee, is it necessary to take new security on a change of lenders? If no, why not? If yes, are there ways to structure the transaction to avoid such a requirement?

No. When an agent is appointed by the lenders to hold the security on behalf of the lenders, the security agreement (e.g., a mortgage agreement or pledge agreement) is signed by the security provider and by the agent (being the mortgagee or pledgee) only. In the case of a mortgage that must be registered, only the agent is registered as the mortgagee. Therefore, a change to a lender (or lenders) that is not the agent does not require the creation of new security.

The legal relationship between the lender or lenders (that is/are not the agent) and the security provider is via the agent. If any lender (that is not the agent) changes by way of assignment and transfer, the new lender will assume the rights and benefits of the original lender. Therefore, the rights against the obligors remain unchanged and the security documents will not need to be amended.

If, however, there is a change to a lender that is also the agent, the amendment of the security documents or new security will be required.

8. Under the laws of this jurisdiction, is there any class of asset over which it is difficult or impossible to grant effective and perfected security, or in relation to which any security granted will be of limited effect?

It is difficult to grant an effective and perfected security interest over a changing pool of assets, such as inventories to be sold and deposits in a bank account. See the answer to question 3 of this section.

9. Under the laws of this jurisdiction, are there any restrictions on offshore lenders taking security over any class of asset?

Previously, foreign companies had to obtain recognition pursuant to the Company Act of Taiwan to become eligible to take a security interest over assets located in Taiwan. After the abolishment of the concept of recognition of foreign companies under the Company Act, a foreign company without a local presence is still unable to be registered as a secured party for chattel mortgages. For chattel mortgages, registration is not required for a chattel mortgage to be valid but it is necessary for the chattel mortgage to be enforceable against a bona fide third party. Furthermore, foreign entities may only acquire rights over land in Taiwan if their countries of incorporation, pursuant to treaties or their domestic laws, allow Taiwanese nationals and entities to the same rights. Under Taiwanese law, a real estate mortgagee agreement has to be registered to be valid. Hence, to allow a foreign company to take security interest over real estate located in Taiwan, the country of incorporation of such entity must allow Taiwanese entities to enjoy the same right. Furthermore, a foreign company without a local presence is still unable to be registered as a secured party for real mortgages. In addition, if a foreign lender would like to take security over scripless shares, they may encounter difficulties as the scripless shares would have to be deposited into a securities account opened by the foreign lender with a securities firm and some Taiwanese securities firms would refuse to allow foreign lenders to use their securities accounts for such purpose.

10. Must a company receive a corporate benefit in return for giving a guarantee or security? In particular, are there restrictions on the grant of upstream and cross-stream guarantees and security? If yes, briefly what is the effect of these laws?

Neither the Regulations Governing Lending of Funds and Making of Endorsements or Guarantees by Public Companies ("**Lending or Guarantees Regulations**") nor any other legislation requires a company to receive a corporate benefit in return for giving a guarantee or security. However, directors and managers of a Taiwanese company have a duty to act in good faith for the benefit of the company when considering giving a guarantee or security.

Under the Taiwan Company Act, a Taiwanese company must not act as a guarantor of any type (including giving security to secure a third party's indebtedness) unless otherwise permitted by other laws or by the Articles of Incorporation (AOI) of the company. A responsible person who violates this restriction is personally liable under the guarantee or security and for any damage to the company that results from it.

A Taiwanese public company that is permitted to give guarantees or security to secure a third party's indebtedness under its AOI must also comply with the Lending or Guarantees Regulations and establish internal rules accordingly. The Lending or Guarantees Regulations provide that a Taiwanese public company may provide a guarantee, an endorsement of a payment instrument or security for a third party's indebtedness for the following companies:

- A company with which it does business.
- A company in which it directly or indirectly holds more than 50% of the voting shares.
- A company that directly or indirectly holds more than 50% of the voting shares in the Taiwanese public company.

A Taiwanese public company, and any company in which it holds, directly or indirectly, 90% or more of the voting shares, may provide an endorsement/a guarantee/security for a third party's indebtedness to each other, but the amount of the endorsement/guarantee must not exceed 10% of the net worth of the Taiwanese public company. However, this restriction does not apply to an endorsement/guarantee/security for a third party's indebtedness made between companies in which the public company holds, directly or indirectly, 100% of the voting shares.

11. What type of security interests does your jurisdiction recognise, e.g., pledge, charge, mortgage, hypothecation? In relation to each type of security interest, please state the formalities required to create and perfect that security.

There are four major types of security interest:

- A mortgage over real property
- A mortgage over chattels
- A pledge over personal property
- A pledge over rights

The formalities for each type of security interest are set out below.

Mortgage over real property

The mortgagor and the mortgagee enter into a mortgage agreement and file for registration of the mortgage with the land office where the mortgaged real property is located.

Mortgage over chattels

The mortgagor and the mortgagee enter into a mortgage agreement and file it with the competent authority to ensure it will be effective against a third party.

Pledge over personal property

The creation of a pledge becomes effective by the transfer of possession of the pledged personal property from the pledgor to the pledgee. In practice, it is advisable for the pledgor and pledgee to enter into a pledge agreement to record their respective rights and obligations.

Pledge over rights

The pledge is created in writing. If there is any document evidencing the pledged rights, the pledgor must deliver it to the pledgee.

The pledgor and the pledgee must notify the debtor of the pledge.

12. Are there any registration, translation or notarization requirements in relation to security, guarantees, subordination or intercreditor documents?

Yes, registration is necessary for mortgages over real property and chattels. A real estate mortgage agreement has to be registered to be valid. A chattel mortgage agreement has to registered to be enforceable against a bona fide third party. Real estate mortgage agreements and chattel mortgage agreements need to be made in a bilingual version or accompanied by a Chinese translation for registration purposes.

13. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in respect of security, guarantees, subordination or intercreditor documents? If yes, what are the amounts and when are they payable?

A registration fee must be paid when applying for a mortgage registration, as set out below.

Registration of a mortgage over real property

A fee equal to one-tenth of 1% (0.1%) of the amount of the secured indebtedness is payable.

Registration for a mortgage over chattels

The fees are as follows:

- Registration fee (including certificate fee): TWD 900
- Amendment registration fee (including certificate fee): TWD 450
- Registration cancellation fee: free of charge

If the amount of the secured claim in relation to a mortgage over chattels is TWD 90,000 or less, the administrative fees set out above are reduced by 50%.

No other fees are payable.

If things go wrong

1. Please provide a brief description of the insolvency regime. In particular what rights and duties do unsecured and secured lenders have on the insolvency of a debtor? Are there any other matters of concern?

There are three distinct statutory corporate insolvency regimes:

- Liquidation/winding up
- Bankruptcy
- In the case of a public company, reorganization

Secured lenders rank above unsecured lenders

If an event of default occurs, a lender usually first applies to the court with jurisdiction for a provisional seizure order in respect of the debtor's assets and then initiates enforcement proceedings.

Liquidation/Winding Up

A creditor may not institute liquidation proceedings against an insolvent Taiwanese company. Those proceedings may only be instituted by the company itself through a shareholder's resolution or by a Taiwan governmental agency. On the appointment of liquidator(s) to the company, the liquidator(s) issue public notices requesting the creditors to declare their claims unless a creditor is known to the liquidator. The liquidator must notify individually creditors that are known to the liquidator. The liquidator will then repay all creditors on behalf of the company after liquidating the assets of the company.

Bankruptcy

Where the value of the assets of a company is less than the value of its debts, then (unless reorganization proceedings are in progress) the board of directors of the company must file for bankruptcy, or the creditors of the company may petition for a declaration of bankruptcy against the company. Each secured creditor that had a security interest over the company's assets prior to the declaration of bankruptcy is entitled to a right of exclusion. In that case, it is not required to participate in the bankruptcy proceedings and may enforce its claims outside those proceedings. The secured creditor may file a claim in accordance with the bankruptcy proceeding for any portion of the debts due to it that remain unsettled after the exercise of the right of exclusion. A moratorium on the enforcement of the claims of all unsecured creditors comes into effect during bankruptcy, and unsecured creditors may only seek satisfaction of their claims, on a pro-rata basis, by participating in the bankruptcy proceedings.

Reorganization

When a company that publicly issues shares or corporate bonds suspends its business due to financial difficulties or when there is a concern that it may do so but there remains a possibility of the company being rehabilitated or restructured, the company or its interested parties (which/who are shareholders who have continuously held shares representing 10% or more of the total number of issued shares for a period of six months or longer or creditors of the company who have claims equivalent to 10% or more of the capital from the total number of issued shares) may apply to the court for reorganization. In these circumstances, the enforcement of security and the realization of collateral are suspended after the grant of a reorganization order by the court and during a period of emergency stay, and are subject to a reorganization plan approved by the creditors and the court. Subject to the preferential claims set out in the answer to question 1 of the "If taking security" section, secured creditors enjoy priority in the order of repayment. However, the claims of all creditors must be exercised in accordance with the reorganization plan and the reorganization procedures.

2. Is it possible to obtain a moratorium before insolvency?

It is only possible to obtain a moratorium before insolvency in the case of reorganization proceedings of a public company. In that case, and as mentioned above, the enforcement of security and the realization of collateral are suspended after the grant of a reorganization order by the court and during a period of emergency stay and are subject to a reorganization plan approved by the creditors and the court. However, the debtor, the creditor and/or any interested third party may seek modification of the plan.

If a petition for a bankruptcy order is filed with the court against a debtor, the court may, at the request of a creditor or ex officio, issue a preservation order to restrict the right of creditors to take enforcement action against the debtor.

3. When a company is the subject of a formal insolvency procedure, can the company's pre-insolvency transactions be set aside?

Certain pre-insolvency transactions can be set aside in relation to a bankruptcy procedure. In a bankruptcy procedure, the bankruptcy administrator may revoke the following pre-insolvency transactions if made by a

bankrupt person or entity within six months before the declaration of bankruptcy:

- The creation of a security interest to secure any existing indebtedness
- The prepayment of any indebtedness that has not yet matured

The setting aside of pre-insolvency transactions does not apply to a liquidation/winding-up.

4. When can a lender enforce its security? Can security be enforced out of court following an event of default (or other contractual trigger event), or is a court order required? Are there any restrictions that apply before a lender may enforce its security?

A lender may enforce its security when there is an event of default by the borrower or the security provider, as the case may be. An enforcement clause may be included in the finance documents (i.e., a clause about the consequences of an event of default), giving the lender the right to enforce its rights against the borrower or the mortgaged/pledged assets once an event of default occurs. At the time a security interest is created, the parties may agree to enforce the security interest out of court and choose an agreed method of enforcement. However, in the case of reorganization proceedings (see the answer to question 1 of this section), the enforcement of collateral is suspended during an emergency stay and after the grant of the reorganization order as the collateral is subject to the reorganization plan. If there are liquidation/winding-up or bankruptcy proceedings, the enforcement of security may be excluded from them and the lender may continue with enforcement.

5. Do any limitation periods apply in relation to bringing an action to enforce security?

Yes. The limitation period (also known as the prescription period) for the claim of a loan repayment is 15 years. For a claim secured by a mortgage, however, if the claim for the repayment of a loan is extinguished due to the lapse of the prescription period, the mortgagee has an additional five-year period, which commences on the last date of the prescription period, during which the mortgage must be claimed and enforced.

6. Is there any particular way in which secured assets must be liquidated on enforcement (e.g., by auction or court sale)?

A sale of a secured asset can occur through a public or private auction, and the manner of that auction may be agreed upon in the mortgage or pledge agreement. A mortgagee or pledgee that has not received payment by the maturity of a claim may enter into a contract to acquire the ownership of the mortgaged/pledged property or dispose of it by any means other than an auction unless doing so would be prejudicial to the interests of the other mortgagees/pledgees.

7. Are there any particular legal or practical difficulties or delays in enforcing security?

The enforcement of security may be delayed when a debtor, or any third party or interested party, files for bankruptcy or reorganization against the debtor.

8. In relation to enforcement, are there any specific requirements to be borne in mind if the lender is a foreign entity?

A foreign entity that does not have a local presence but that has a representative in Taiwan may file a petition with a court in Taiwan or initiate legal proceedings in Taiwan. A foreign company without a local presence cannot be registered as a secured party for chattel mortgages and real estate mortgages. Under Taiwanese law, a real estate mortgagee agreement has to be registered to be valid. For chattel mortgages, registration is not required for a chattel mortgage to be valid, but it is necessary for the chattel mortgage to be enforceable against a bona fide third party.

Given the above, specific legal advice should be taken regarding the enforceability of security interests in Taiwan in favor of a foreign lender or security agent.

9. Is there any reason why you think that arbitration rather than litigation might be advantageous in resolving disputes under the finance documents, and if so, why? Please outline the relative merits of arbitration and litigation, including the ease of enforcement of foreign judgments and foreign awards from different jurisdictions. Is it possible to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit?

Cause of action and costs

Litigation may be more advantageous when the cause of action is clear and the documentary evidence is sufficient. In some cases, arbitration may be more time-consuming than litigation and the cost may be higher.

Application for recognition

After the court has granted an application for recognition, foreign court judgments and foreign arbitral awards are binding on the parties and have the same force as a final judgment of a Taiwanese court. The criteria for a court to review an application for recognition are set out below.

Foreign court judgments

In the case of an application to a Taiwanese court for recognition and enforcement of a foreign judgment, the judgment will be enforced by the Taiwanese court if:

- In the case of a default judgment, the relevant process was served on the defendant in the foreign court's jurisdiction or on the defendant with Taiwanese judicial assistance.
- The judgment is not contrary to the public order or good morals of Taiwan.
- According to Taiwanese laws, the foreign court had jurisdiction over the case.
- Judgments of Taiwanese courts are reciprocally recognized by the foreign courts.

Foreign arbitral awards

The court will dismiss an application for recognition of a foreign arbitral award in one or both of the following cases:

- Where the recognition or enforcement of the arbitral award is contrary to the public order or good morals of Taiwan
- Where the dispute cannot be resolved by arbitration under the laws of Taiwan

The court may (but is not bound to) also dismiss an application for recognition of a foreign arbitral award if the country where the arbitral award is made or whose laws govern arbitral awards does not recognize the arbitral awards of Taiwan.

"Reciprocal recognition" principle

In light of the criteria in the Civil Procedural Laws and the Arbitration Law respectively, the main difference between the requirements for recognition of foreign judgments and foreign arbitral awards is the "reciprocal recognition" principle. The "reciprocal recognition" principle is a "must" for the recognition of foreign court judgments but a "may" for the recognition of foreign arbitral awards. Therefore, it is relatively easier to obtain a court order that recognizes a foreign arbitral award than a foreign judgment.

Hybrid enforcement provision

There are court precedents where the Supreme Court held that a provision in the contract giving the parties the right to opt for either arbitration or litigation as they see fit is valid. Therefore, it is possible to rely on a hybrid enforcement provision that allows lenders to opt for either arbitration or litigation as they see fit.

10. **Are asymmetrical jurisdiction clauses enforceable? (By this we mean clauses that allow the lenders, but not the borrowers, to make certain choices in relation to choice of jurisdiction and how to litigate. These types of clauses allow the lenders, but not the borrowers, to commence proceedings in any court they choose, but restrict the borrowers to commencing proceedings in one jurisdiction only. This may also allow the lenders, but not the borrowers, to choose whether to litigate the finance documents before a court or to submit to arbitration in relation to them, but restrict the borrowers to either litigation or arbitration, as specified in the agreement).**

    No. The choice of court or arbitration forum must be fair to both parties. The court that has jurisdiction must be specified or ascertainable by reference to information available to the parties (e.g., the jurisdiction would be the court where the lender's registered office is located).

Working digitally

1. **Is it possible for documents to be executed electronically (whether by the manual insertion of a digital signature or the use of an e-signing platform) under the laws of this jurisdiction? If so, is this limited to only particular types of finance documents?**

    Pursuant to the Electronic Signatures Act of Taiwan (ESA), it is permissible to sign documents using electronic signatures with the counterparty's consent. In addition, where a digital signature meets the requirements listed in the ESA (e.g., being supported by a certificate issued by an approved certification service provider and being valid and within the purposes of use), it can be employed in an electronic document. Although the ESA provides no statutory limitation on the types of documents that can be executed by electronic signatures, it provides flexibility for the government authorities to make exceptions regarding the use of electronic signatures by stipulating laws or regulations. For example, the FSC, the competent authority for the financial services industry in Taiwan, imposes a restriction on the application of electronic signatures to a negative pledge undertaking as mentioned in Article 30 of the Banking Act, being a written document where a borrower, mandator or the party on behalf of which the guarantee is issued makes an undertaking not to provide its assets as collateral for obligations owed to a third party.

2. **Where the witnessing of a signing is contemplated, is it possible for the witness to verify the signature over a live video call?**

    Under Taiwanese law, there is no witness requirement when signing a finance document. Therefore, whether a document is required to be signed under witness is subject to the agreement of the parties. It is therefore possible for the witness to verify the signature over a live video call if the financial institution that is a party to a financing transaction is willing to accept such an approach.

3. **Is it possible to register/perfect security electronically without wet ink signatures?**

    No. The relevant authorities/state agencies still require wet ink signatures.

4. **Are there any other legal restrictions that may prevent the parties from executing a finance transaction electronically?**

    No.

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THAILAND

Thailand

When considering whether to lend

1. Is it necessary or advisable for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in this jurisdiction: (a) by reason only of its execution, delivery or performance of the finance documents; or (b) to enable it to enforce its rights under the finance documents?

It is not necessary for any person or entity that acts as a lender to be licensed or qualified to carry on lending activities in Thailand because of the execution, delivery or performance of any finance documents to which it is a party or to enforce its rights under those finance documents.

However, if that lender also carries out activities in Thailand that fall within the scope of commercial banking business activities under the Financial Institution Business Act B.E. 2551 (2008) (FIBA), as amended from time to time, then a commercial banking license will be required prior to the commencement of that activity in Thailand and for that lender to enforce its rights under the finance documents that fall within the scope of commercial banking business.

Under the FIBA, "commercial banking business" is defined as the business of the following:

- Accepting deposits of money from the public that are subject to withdrawal on demand or at certain periods
- Buying and selling negotiable instruments
- Buying and selling foreign currency

Please note that the following licenses are also required if any lender, arranger, facility agent or security agent is involved in the following activities in Thailand.

Consumer finance business license

If the lender intends to grant loans to individuals in the ordinary course of business without providing other banking services (i.e., non-bank), licenses relating to a consumer finance business may be required.

Certain types of consumer finance businesses in Thailand are regulated and require the operator to obtain the relevant license from the Ministry of Finance (MOF), through either the Bank of Thailand (BOT) or the Fiscal Policy Office (FPO), depending on the type of financing offered. However, not all consumer finance businesses are currently regulated under specific laws (e.g., the hire-purchase and leasing of vehicles and machinery are excluded).

The Declaration of the Revolutionary Council Decree No. 58 determines which consumer finance businesses are regulated and requires the business operator to obtain a license from the MOF for pico-finance[1], nano-finance[2], or

1 "Pico-finance under supervision" means lending, purchasing, discounting, or rediscounting bills or any negotiable instruments to an individual with or without assets or property as collateral, in the province where the head office of the business operator is located, whereby the interest, fines, service fees and other fees exceed the permissible rate under the Civil and Commercial Code of Thailand. The following are not regarded as pico-finance under supervision: (i) travel loans for overseas employment; (ii) loans for staff welfare where the employer has signed a contract with the business operator; or (iii) any other loans as may be prescribed by the FPO in the future

2 "Nano-finance" means lending, purchasing, discounting, or rediscounting bills or any negotiable instruments, or hire-purchase transactions or leasing to an individual, without assets or property as collateral, with the borrower intending to use the money to carry on a business or for their occupation. The following are not regarded as nano-finance under supervision: (i) hire purchase; lease and sale and lease back of goods that are normally sold by the operators, cars and motorcycles and any other goods as may be prescribed by the BOT in the future; (ii) loans with vehicle registration certificate as collateral; (iii) travel loans for overseas employment; and (iv) other loans as may be prescribed by the BOT in the future

personal loans[3]. These licenses allow the lender to operate and collect interest from borrowers that are individuals that is higher than the interest rate permitted by the general laws (i.e., 15% per annum under the Civil and Commercial Code of Thailand). These financing activities offered to individuals differ in their purposes, permissible interest rates and fees, qualifications of the borrowers, credit assessment criteria, and the maximum credit amount, etc.

The different licensing schemes can be briefly summarized as follows:

- A pico-finance license is required for a business to make secured or unsecured loans to individuals within a designated jurisdiction (i.e., provincial level).
- A nano-finance license is required for a business to make unsecured loans to individuals for occupational purposes.
- A personal loan license is required for a business to make unsecured loans to individuals for the purpose of personal consumption or for non-specific purposes and also covers loans for occupational purposes. Under the personal loan licensing scheme, there are also other sub-categories that the lender is able to operate, which includes the vehicle registration loan[4] and the digital personal loan[5].

Foreign business license

If a foreign person or entity acts as an arranger, facility agent or security agent in Thailand, depending on the nature of that particular activity, it may be considered to be carrying on the business of providing services under the Foreign Business Act B.E. 2542 (1999) as amended (FBA). Under the FBA, foreign nationals are restricted from operating those businesses that are only permitted to be carried on by Thai nationals (and these businesses include service businesses) without a license. Generally, an activity that involves the performance of any valuable action, deed or effort to satisfy a requirement or fulfill a demand or the sale of intangible products (e.g., time, energy and expertise) for the benefit of customers in exchange for a valuable consideration is considered a service business.

Effective from 9 June 2017, the Ministry of Commerce issued a ministerial regulation removing certain businesses from the category of restricted business activities, which included businesses governed by the laws on financial institutions, including those operating a commercial banking business, acting as a banking agent and acting as an agent in receiving payments (collecting agent) or accepting applications.

The operation of a service business in Thailand is a restricted activity under the FBA. A foreigner is not permitted to operate a service business without a license. Any foreign arranger, facility agent or security agent carrying on a service business (other than those that have been removed from the category of business activities) would be required to obtain a "foreign business license" prior to providing the relevant arranging and/or agency services in Thailand.

3 "Personal loan under supervision" means lending, purchasing, discounting, or rediscounting bills or any negotiable instruments to an individual, with or without the borrower aiming to receive goods or services, including lending with the objective of using the money to carry on a business or as a part of the borrower's occupation, without assets or property as collateral. Personal loans under supervision also include: (i) lending originating from the hire-purchase and lease of goods that are not normally sold by the business operator (except for vehicles and machinery); and (ii) vehicle registration loans. The following are specifically excluded from the definition: (i) loans for education; (ii) travel loans for overseas employment; (iii) loans for medical treatment; (iv) loans for staff welfare if the employer has signed a contract with the business operator; and (v) any other loans as may be prescribed by the BOT in the future

4 "Vehicle registration loan" is defined as lending money to a person who holds ownership of the vehicle, and: (i) the business operator accepts the vehicle registration or arranges for an agreement, document, or any other evidence that: (a) results in the vehicle registration being transferred in advance as collateral; or (b) allows the business operator to sell the vehicle or take any other action with the vehicle to repay the loan; and (ii) the debtor can still possess and use the vehicle as usual

5 In September 2020, the BOT introduced a sub-category type of personal loan business — the digital personal loan business. The intention was to promote financial inclusion and utilization of technologies and alternative data. Digital personal loan business operators are able to offer loans of up to THB 20,000 per customer with a tenure of no more than six months for each loan agreement via digital channels and methods. Under this scheme, there is more flexibility for the business operators in assessing the credit of the borrowers using new technologies (e.g., the ability or willingness to pay) without having to rely on the information provided by the credit bureau

2. Will any lender, arranger, facility agent or security agent be deemed to be resident, domiciled, carrying on business or subject to tax by reason only of the execution, delivery, performance or enforcement of the finance documents?

An offshore entity is subject to tax if, by its execution, delivery, performance or enforcement of the finance documents, that offshore entity is considered to be conducting business in Thailand. The act of "conducting business in Thailand" is broadly defined under the Revenue Code as follows:

A juristic company or partnership incorporated under a foreign law that has an employee, a representative, or a broker in Thailand for carrying on its business and thereby derives income or gains in Thailand, such juristic company or partnership shall be deemed to be carrying on business in Thailand.

According to the interpretation of this definition by the Revenue Department, an employee, a representative or a broker does not need to be stationed permanently in Thailand to fall within the scope of this definition.

In principle, any activity undertaken by an offshore entity that involves its employee, representative or broker carrying out the execution, delivery, performance or enforcement of any agreement that generates income for the offshore entity will likely be subject to tax. However, it will depend on the facts of each case.

An offshore entity receiving certain types of income from Thailand must pay income tax at a fixed percentage of the gross income. The party in Thailand that pays the income is generally required to withhold the tax at the payment source.

3. Are there any regulatory reporting requirements that lenders must observe in connection with those transactions?

There are some regulatory reporting requirements for lenders that are engaged in a "commercial banking business," regulated personal loan business or regulated retail loan business in Thailand (see the answer to question 1 of this section). There are no other regulatory reporting requirements that a lender must observe in relation to those transactions.

4. Is it necessary to establish a place of business in your jurisdiction in order to enforce any provision of the finance documents?

No.

5. Is a foreign bank/financial institution permitted to approach local entities for business?

Yes. The foreign bank/financial institution must obtain a license if the transactions intended to be executed between the foreign bank/financial institution and its local customer fall within the scope of the following prior to carrying on those regulated activities in Thailand:

- A "commercial banking business license," under the FIBA, is required for banking business.
- "consumer finance business licenses" (i.e., pico-finance, nano-finance or personal loan) are required for the lending activities granted to individuals. If the lender already holds the licenses to operate as a financial institution under the FIBA (e.g., a licensed commercial bank), such lender would be exempted from obtaining the consumer finance business licenses.

When lending to borrowers

1. **Are there any restrictions in relation to the type of borrower who may borrow foreign currency or in relation to the term of foreign currency and/or the amount of foreign currency borrowed by local entities?**

   No.

2. **Are there any restrictions on the rate of interest or default interest that may be charged?**

   The charging of interest (that is not default interest) on a loan by a foreign financial institution is limited to a maximum interest rate of 20% per annum.

   Moreover, although the compounded reference rate is a method used to calculate interest rate (and not a concept of compounded interest as prohibited by law), due to the lack of a Supreme Court decision on this matter, the enforceability of any provision in the facility agreements with reference to the compounded reference rate as part of the applicable interest rate and the payment of interest on the compounded rate loan is uncertain.

   There is no restriction regarding the rate of default interest under Thai law. However, Thai courts have the discretion to review and subsequently reduce any default interest rate agreed between parties if the courts determine that the rate is disproportionately high. The default interest rates that have been successfully challenged in the past are those where the claiming party would earn significantly more from the default interest rate than from the contract if it had not been breached.

   By virtue of the latest amendment to the Civil and Commercial Code of Thailand, default interest for any loan with amortizing repayments that becomes overdue from 11 April 2021 can only accrue on the principal amount of the relevant repayment installment that is overdue. Due to the lack of a Supreme Court decision on this matter, the enforceability of any provision in the facility agreement that entitles the lender to charge default interest on all outstanding loans in the event of interest payment default or non-payment default is uncertain.

3. **Are there any restrictions on particular lenders or classes of lender entering into credit transactions with borrowers?**

   No.

4. **Are there any exchange controls that will apply to payments to be made in foreign currencies or to foreign lenders?**

   Under the Notice of the Competent Officer on Rules and Practices Regarding Currency Exchange ("**Notice**"), Thai residents can generally make payments in foreign currencies or to foreign lenders provided that:

   a. The payment is not made for the purposes set out in the negative list under the Notice

   b. The payment does not exceed the applicable limit set out under the Notice

   c. The relevant supporting documents evidencing the purpose of the payment can be submitted to the satisfaction of a commercial bank acting as a remittance bank in Thailand

   If the conditions above are not satisfied, the Thai residents are required to obtain prior approval from the BOT to make such payment.

   Fund remittance for the purposes of a loan repayment, interest payment and enforcement of guarantee or security interest under a security agreement are generally permitted up to the amount set out in the supporting documents in (c) above.

5. **Is there any requirement to deduct or withhold tax from any amounts to be paid or repaid to a lender (whether domestic or foreign)? If so, at what rate must tax be deducted and from what kinds of payment?**

No deduction or withholding tax is applicable to the repayment of any loan principal amounts.

There are taxes applicable to the payment of interest. A lender has an obligation to pay withholding tax on interest and default interest.

However, in relation to interest paid to a lender that is a commercial bank established under the commercial banking law of Thailand, the following points apply:

- No withholding tax is imposed on interest or default interest
- The payments of interest, default interest, front-end fees, commitment fees and other fees and expenses to a lender that is a commercial bank established under Thai commercial banking law are treated as gains from a lending transaction, and are therefore subject to a specific business tax at the rate of 3% on the amount paid.

If the lender is not a commercial bank established under the commercial banking law of Thailand, withholding tax at the rate of 15% is levied on interest and default interest. The withholding tax rate would generally be reduced if that lender were a financial institution that has tax residency in a country or jurisdiction that is party to a treaty for the avoidance of double taxation with Thailand. The amount of the rate reduction would depend on the terms of the treaty.

In relation to interest paid to a lender providing loans from outside Thailand, the following points apply:

- Withholding tax at the rate of 15% is levied on interest and default interest. The withholding tax is generally reduced to 10% if that lender is a financial institution that has tax residency in a country or jurisdiction that is party to a treaty for the avoidance of double taxation with Thailand.
- No specific business tax is imposed on interest or default interest.
- Default interest for late payment, front-end fees, commitment fees or other fees and expenses paid for the account of a lender providing loans from outside Thailand may be treated as income in a similar way to interest on loans or gains from a lending transaction and therefore may be subject to withholding tax as described in the first bullet point above.

6. **Are there any "thin capitalization" or other rules that may limit the extent to which interest payments may be deducted for tax purposes?**

There are no thin capitalization or similar rules that would limit the extent to which interest payments may be deducted for tax purposes. However, interest payments that are deductible as expenses for tax purposes are the only payments in relation to a business that are subject to tax in Thailand.

7. **Are there any registration, notarization, translation or reporting requirements in relation to the loan documents?**

No registration, notarization or translation is required for a loan agreement or a facility agreement for the purpose of their validity. However, registration with the relevant governmental agencies is currently required to create and perfect a mortgage or business security related to the loan or finance documents.

To be admissible as evidence in the courts of Thailand, documents in foreign languages are required to be translated into the Thai language. However, if the case is brought to the Central Bankruptcy Court or the Central Intellectual Property and International Trade, a document in English may be admitted by the court if the parties agree not to translate it and the court is of the opinion that the document is not evidence in a major issue of the case.

The borrower does not have any reporting requirements in relation to the loan documents.

8. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to the loan documents? If yes, what are the amounts and when are they payable?

The original of any loan or facility agreement is subject to stamp duty at the rate of 0.05% of the amount of the total commitment under the agreement, but the amount payable is capped at THB 10,000 (approximately USD 300). Each duplicate copy of or counterpart to the original loan or facility agreement is subject to a nominal stamp duty of THB 5 per document.

This stamp duty is generally due and payable within 15 days after the date of execution of the relevant loan or facility agreement and a stamp is affixed to the relevant document to evidence the payment. However, according to the Notification of the Director-General of the Revenue Department on Stamp Duty (No. 37) dated 2 December 1995, a lender that is a commercial bank in Thailand or a branch of a foreign bank in Thailand is required to pay stamp duty at the local revenue office in place of affixing a stamp duty, as follows:

- If the loan or facility agreement is executed between the first and the 15th day of the month, stamp duty must be paid by the 22nd day of the same month.
- If the loan or facility agreement is executed between the 16th and last days of the month, stamp duty must be paid by the seventh day of the following month.

If the loan or facility agreement is executed outside Thailand, stamp duty is payable within 30 days from the date when the duly executed original of the relevant agreement is brought into Thailand. This requirement is normally applicable to a lender providing a loan to an entity not incorporated in Thailand.

Additionally, each appointment of an agent (i.e., facility agent or security agent) under a loan or facility agreement is subject to a maximum stamp duty of THB 30 for each appointment of an agent in relation to each principal.

9. Does the law recognize the subordination of the debt that a debtor owes to one creditor to that which the debtor owes to another creditor? If yes, how is this usually effected?

Thai law recognizes the concept of subordination of debt. Debt subordination is usually effected by a contractual agreement between a senior lender and a subordinated lender.

10. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors (e.g., the claims of employees and tax authorities or the claims of creditors under particular kinds of instrument)? If yes, what classes of creditors are preferred?

Among unsecured creditors, the Bankruptcy Act B.E. 2483 (1940) (as amended) prescribes that the debtor's assets must be used to pay its debts in the following order of priority:

- Expenses for the administration of a deceased debtor's estate.
- Expenses of the receiver in managing the debtor's assets.
- Funeral expenses of a deceased debtor appropriate to their status.
- Fees for the collection of assets in relation to any appeal regarding a claim for the payment of a debt.
- Fees of the petitioning creditor and counsel's fee, as the court or the receiver may prescribe.
- Taxes that have become due for payment within six months prior to the insolvency and wages.
- Other debts.

If the amount realized from the debtor's assets is insufficient to fully discharge the sum in any of the debt categories specified above, the creditors in each debt category must be paid equally.

11. Are there any consumer protection or similar laws that apply if credit is made available to individuals or other classes of debtor? If yes, what laws are applicable?

There are two subordinate pieces of legislation issued under the Consumer Protection Act B.E. 2522 (1979) that regulate the format (including the scope of terms and conditions) of loan agreements and credit card contracts to be entered into between individuals and a corporate lender or credit provider that provides loans or credit in its ordinary course of business. They are as follows:

- Notification of the Committee on Contracts re: Declaring Consumer Loan Business of Financial Institutions to be A Controlled Business
- Notification of the Committee on Contracts re: Declaring Credit Card Business to be A Controlled Business

These Notifications provide, among other things, that the following is applicable to the relevant contract:

- Must be available in Thai
- Does not contain any terms which create an unreasonable advantage for the credit provider over individual consumers, or which are unfair to individual consumers.

12. Are there any prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of: (a) its own shares or those of any affiliated company; or (b) assets owned by it or any affiliated company?

There is no specific law governing the offer or receipt of financial assistance.

However, if the provision of financial assistance is a transaction between a listed company or its subsidiary and any connected person (e.g., management, a major shareholder, a controlling person or persons to be nominated as management or a controlling person of the listed company or its subsidiary) of the listed company, or a transaction between a subsidiary company and any of its connected persons, that financial assistance is deemed to be a "connected transaction" within the meaning of the Notification of the Board of Governors of the Stock Exchange of Thailand (SET) Re: Disclosure of Information and Other Acts of Listed Companies Concerning Connected Transactions 2003 (as amended) ("**Connected Transaction Rules**"). In accordance with the Connected Transaction Rules, a listed company is subject to certain disclosure and corporate approval requirements depending on the value of the transaction, as set out below.

Disclosure of information

A listed company is required to disclose its connected transactions in its annual report and make different levels of disclosure to the SET, depending on the type and value of the transaction to be undertaken.

Corporate approval

In the case of a transaction by which a listed company or its subsidiary offers financial assistance to a connected person who is a natural person or a juristic entity in which the listed company or subsidiary holds shares at a lower ratio than the ratio of shares held by any other connected persons, the following points apply:

- If the transaction value is less than THB 100 million or 3% of the net tangible asset value (whichever is lower), approval of the listed company's board of directors must be obtained.
- If the transaction value is greater than or equal to THB 100 million or 3% of the net tangible asset value (whichever is lower), approval of the listed company's shareholders by a majority, formed from at least 75% of all total eligible votes in the shareholders' meeting, must be obtained.

In all other cases involving the grant or receipt of financial assistance other than as described above, the following points apply:

- If the transaction value is greater than THB 1 million or 0.03% of the net tangible asset value, but less than THB 20 million or 3% of the net tangible asset value (whichever is higher), approval of the listed company's board of directors must be obtained.
- If the transaction value is equal to or greater than THB 20 million or 3% of the net tangible asset value (whichever is higher), approvals of both the board of directors and the shareholders of the listed company must be obtained (in the latter case, by a majority of at least 75% of all total eligible votes in the shareholders' meeting).

The Connected Transaction Rules set out the bases for calculating the value of transactions by which:

- a listed company or a subsidiary of a listed company offers financial assistance to a connected person.
- a listed company or a subsidiary of a listed company receives financial assistance from a connected person.

If taking security

1. **Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's secured creditors?**

   No.

2. **May security given by a company rank in a specified order so as to secure liabilities owed to different creditors of the company in that order and, if that is not possible, is it viable for parties to enter into a contractual arrangement for the purposes of moderating this order?**

   Security given by way of a mortgage or a business security under the Business Security Act B.E. 2558 (2015), which came into force in early July 2016 ("**Business Security Act**") may be ranked in a specified order on a "first in time" basis. In other words, where multiple security interests are registered over the same property as security for different underlying debts, the claim of a secured party (or a group of secured parties) that registers its security over that property will be, based on prior registration, senior to or will have priority over the claims of subsequent secured parties.

   A mortgage can be created over land, buildings, machinery, ships or vessels weighing not less than five tons, floating houses or rafts, and certain animals that can be used as vehicles (such as buffaloes and oxen).

   A business security under the Business Security Act can be created over specific assets or an entire business enterprise (which is likely to include contractual rights and movable property used in the business of the security provider such as machinery, inventory, raw materials and intellectual property).

   A simple contractual arrangement cannot be used to vary such order, but it may be moderated and varied by managing the deregistration and reregistration of the mortgage or the business security.

3. **Does this jurisdiction recognise the concept of floating security or similar equivalent (i.e., security over a changing pool of assets that the company giving the security is free to buy, sell and generally deal with)?**

   Thai law has recently recognized the concept of floating security following the introduction of the Business Security Act. It is now possible to create security over a "business" or "enterprise" as a going concern, which is broadly defined as all assets (including inventory and related rights) used in the operation of the security provider's business on a non-possessory basis. This most recently available security interest under the Business Security Act has attributes similar to those of a "floating charge."

4. If so, are there any practical reasons why floating security is difficult to take, maintain or enforce?

The creation of security over a changing pool of assets does not align with the fundamental concept in civil law systems that security must only be taken over an identifiable asset and that the asset must be specifically identified when taken as security. Many issues under the Business Security Act remain debatable, and further guidance and regulations from the authorities will be necessary for its successful implementation as intended. As it will take some time for the act to function smoothly, a considerable transition period is expected. As the act is implemented and tested over time, any difficulties in relation to the taking, maintenance and enforcement of floating security should become clearer.

Additionally, under the Business Security Act, individuals and juristic persons can become security providers under the act, but only "financial institutions" and those specifically designated under a ministerial regulation can accept business security as secured creditors. In this context, "financial institutions" refers to insurance companies under Thai insurance laws and financial institutions under the FIBA only. Note that foreign banks without a branch in Thailand participating in loan syndication with Thai financial institutions are also entitled to accept business security as secured creditors.

Therefore, foreign banks without a license to carry on commercial banking activities in Thailand that are not a party to a syndicate with Thai financial institutions are effectively excluded from taking business security as secured creditors under the current Business Security Act.

5. May security be granted to a trustee to be held on trust for the lenders from time to time, in such a way that a change of lenders does not require new security to be taken?

The Civil and Commercial Code of Thailand prohibits the establishment of a trust by any will or by any juristic act, unless the trust is established in accordance with a specific law for the establishment of a trust, i.e., under the Trust for Capital Market Transactions Act B.E. 2550 (2007), which specifically empowers parties in capital market transactions to establish a trust for specific purposes. There are currently no laws in Thailand that provide for the establishment of a trust in relation to non-capital market transactions. As the borrowing and lending of monies by financial institutions are not regarded as capital market transactions, the obligation of any designated agent to hold any property or rights "in trust" for the secured parties may not be recognized or enforceable as a trust under Thai law.

Therefore, the use of a security trustee is not common in relation to loans that are governed by Thai law. In a transaction where there is more than one lender and a security agent is appointed, the security agent itself usually executes security documents in two capacities, namely as follows:

- For and on behalf of the lenders and other secured parties (if any)
- For and on its own account as the security agent

In this way, a principal and agent relationship is created between the lenders and the security agent. The security agent is duly singly empowered to act for and on behalf of the lenders in relation to a number of aspects of a transaction, such as the execution of security agreements and the holding of certain secured assets, such as pledged share certificates, for the benefit of the secured parties.

Notwithstanding this, a security agent may not be registered as the sole mortgagee on behalf of all secured parties in relation to a mortgage or as the sole secured party on behalf of all parties in relation to a business security. Instead, Thai mortgage law and the Business Security Act require every lender and secured party taking security over mortgageable property or assets of the business (as the case may be) in relation to the same underlying debt to be individually registered as a mortgagee or security holder.

6. If not, are there any techniques that can be used to achieve substantially the same effect (e.g., parallel debt structures)?

No. Please note that parallel debt structures are not recognized by Thai courts.

7. If an agent holds security for the lenders rather than a trustee, is it necessary to take new security on a change of lenders? If no, why not? If yes, are there ways to structure the transaction to avoid such a requirement?

As mentioned in the answer to question 5 of this section, the security agent itself usually executes security documents in two capacities, namely:

- For and on behalf of the lenders (under the doctrine of agency rather than as a trustee)
- For and on its own account as the security agent

Therefore, on a change of lenders, there is no need to re-execute the security documents because the security agent can act on behalf of the new lender, provided that the new lender duly and legally accedes to the finance documents (in which the provisions authorizing and appointing the security agent to act for and on behalf of the secured parties are also set out).

However, specific legal requirements governing the formalities for perfecting certain security interests (such as share pledges and mortgages) may require certain amendments to be made to existing security documents or additional actions to be taken to ensure that the new lender is granted effective and enforceable security. For example, notwithstanding the fact that share certificates are only required to be physically pledged with the security agent, the name and address of each individual lender taking security over the pledged shares as pledgee must be duly recorded in the share register book of the company that issued the pledged shares. In these circumstances, the new lender must also be recorded as a pledgee in that company's share register book.

Additionally, as stated in the answer to question 5 of this section, in relation to a mortgage and a business security created under the Business Security Act, each individual lender and secured party must be registered as a secured party. Therefore, an additional filing must also be made to register a new lender as a secured party.

8. Under the laws of this jurisdiction, is there any class of asset over which it is difficult or impossible to grant effective and perfected security, or in relation to which any security granted will be of limited effect?

Although a pledge over bank accounts is typically required as part of the security package in lending transactions as a matter of market practice in Thailand, a pledge over bank accounts (or more accurately, the pledge of the rights to the cash deposits in those bank accounts) is not clearly recognized as a valid security interest under Thai law. In fact, a number of Supreme Court judgments consistently follow the interpretation that a pledge cannot be created over a changing pool of cash deposited in a bank account.

Further, as mentioned in the answer to question 4 of this section, eligible persons that can become security holders under the Business Security Act are insurance companies under Thai insurance laws, financial institutions under the FIBA, and those specifically designated under a ministerial regulation to accept business security as secured creditors, which includes foreign banks that participate in a loan syndication with Thai financial institutions. Foreign banks without a license to carry on commercial banking activities in Thailand that are not party to a syndicate with Thai financial institutions are excluded from taking business security as secured creditors under the current Business Security Act.

9. Under the laws of this jurisdiction, are there any restrictions on offshore lenders taking security over any class of asset?

No.

10. Must a company receive a corporate benefit in return for giving a guarantee or security? In particular, are there restrictions on the grant of upstream and cross-stream guarantees and security? If yes, briefly what is the effect of these laws?

No statutory requirement stipulates that a guarantee or security must be given in return for a corporate benefit. If the act of giving a guarantee or any other form of collateral to secure the debts of a third party is within the scope of the company's objectives, as registered with the Ministry of Commerce, a company may give a guarantee or security for no consideration.

11. What type of security interests does your jurisdiction recognise, e.g., pledge, charge, mortgage, hypothecation? In relation to each type of security interest, please state the formalities required to create and perfect that security.

Valid security interests under Thai law

At present, a pledge, a mortgage and business security under the Business Security Act are the only forms of valid security interests that can be created over assets recognized by Thai law.

Pledge

A pledge can be created over movable property through the physical delivery of the pledged property to the pledgee's custody. Negotiable instruments such as bills of exchange, promissory notes, checks and negotiable certificates of deposit can also be pledged by endorsement and delivery of the instrument to the custody of the pledgee.

For a pledge of shares, the pledgor is required to physically deliver the share certificates representing the pledged shares to the pledgee and record that pledge in the share register book of the company that issued the pledged shares.

A pledge becomes automatically discharged if and once the pledged property has returned to the physical possession of the pledgor.

Mortgage

A mortgage can be created over land, buildings, machinery, ships or vessels weighing not less than five tons, floating houses or rafts, and certain animals that can be used as vehicles (such as buffaloes and oxen).

A mortgage will be created on the execution of a mortgage agreement made in the relevant official form by the mortgagor and the mortgagee and its registration with the relevant authority. A mortgage agreement must be only made in Thai language, but the parties can attach a supplement to the official mortgage agreement that contains additional specific terms agreed between the mortgagor and mortgagee. The mortgage agreement and its supplemental agreement must be executed in the presence of a competent officer at the time of filing an application for registration with the relevant authority. The secured amount of the mortgage must be stated in Thai baht in the mortgage agreement. Each individual lender must also be named as a mortgagee in the mortgage agreement and be registered as a mortgagee to be recognized as a secured creditor under Thai bankruptcy law.

Business security

Business security under the Business Security Act is created when the parties enter into a business security agreement (which must contain prescribed contents) in writing, and it is registered with the Ministry of Commerce via an electronic registration system. The business security agreements may be made in Thai or English, but the registration particulars required for registration must be in Thai.

Other rights

In practice, the parties may enter into any other form of contract (e.g., a guarantee, conditional assignment, subordination or option agreement) as part of the security package. However, these agreements will be enforceable between the parties but will not be recognized as having priority over other creditors under Thai law (in particular, under Thai bankruptcy law). In other words, they will be treated as unsecured debts, and a beneficiary under a guarantee and an assignee will be paid as unsecured creditors.

These arrangements can be effected as set out below.

Guarantee

A guarantee (suretyship) is a contractual right given by a third party to secure the performance of an obligation by a debtor. If the debtor defaults in the performance of its obligations under a separate underlying agreement, the guarantor must assume the payment obligations of the debtor. In order to be enforceable in court between the parties, the guarantee agreement must be made in writing and must be signed by the guarantor. It is not necessary for the creditor to sign a guarantee agreement.

A guarantor has rights of subrogation. After a guarantor has made a payment under the guarantee, the guarantor will have rights of recourse against the debtor for the amount paid.

Assignment

In project financing transactions, it is common for a debtor to be required to assign its rights (and/or obligations) under the major project agreements to secure the performance of its obligations under the financing agreements and/or to facilitate the enforcement of secured assets in relation to the project. However, it should be noted that there is uncertainty in relation to the legal operation of an assignment as a form of security in practice, due to the lack of legislation governing the matter.

Assignments of property lease rights and accounts receivable are the most common in business transactions.

The creation of an assignment of rights and/or obligations under a contract is made by way of a written agreement between the assignor and the assignee with notification to and/or consent from the counterparty of the contract under which the assignor's rights and/or obligations have been assigned. It is important to note that in the case of an assignment or transfer of an obligation by way of "novation," the written consent of the assignor's counterparty must also be obtained.

12. Are there any registration, translation or notarization requirements in relation to security, guarantees, subordination or intercreditor documents?

There is a registration and translation requirement for mortgages and business security as previously explained in the answer to question 11 of this section.

There is no notarization requirement for other security interests or other contractual security arrangements. However, in effecting the registration of mortgages, the competent officer may request that the supporting documents executed or sent from outside Thailand be notarized (and, if applicable, legalized) prior to its submission to the officer.

To be admissible as evidence in the courts of Thailand, documents in foreign languages are required to be translated into the Thai language. However, if the case is brought to the Central Bankruptcy Court or the Central Intellectual Property and International Trade, a document in English may be admitted by such court, should the parties agree not to translate it and if the court is of the opinion that the document is not evidence in a major issue of the case.

13. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in respect of security, guarantees, subordination or intercreditor documents? If yes, what are the amounts and when are they payable?

Stamp duty

The original of any guarantee is subject to stamp duty of THB 10 and each duplicate copy of the guarantee is subject to nominal stamp duty of THB 5.

A pledge agreement is subject to stamp duty of THB 1 for every THB 2,000 of underlying obligations that that pledge secures (or only THB 1 for underlying obligations that the pledge secures that does not have a specified monetary value or pledge amount) and each duplicate copy of the pledge agreement is subject to nominal stamp duty of THB 5. A pledge is exempted from stamp duty when the pledge secures obligations under a loan agreement in respect of which the applicable stamp duty has already been paid.

The stamp duty for guarantees and pledge agreements is due and payable within 15 days after the date of execution of the relevant agreement. If the agreement is executed abroad, the stamp duty is payable within 30 days of the original being physically brought into Thailand.

Each appointment of an agent (i.e., facility agent or security agent) under an intercreditor agreement is subject to a maximum stamp duty of THB 30 per appointment of an agent per each principal.

Registration

The registration of a mortgage is subject to registration fees, payable to the relevant authority at the time of registration. The fees below relate to assets that are usually the subject of a mortgage:

- For a mortgage of land and buildings, 1% of the mortgage value, but not exceeding THB 200,000 for each mortgage
- For a mortgage of machinery, 0.1% of the mortgage value, but not exceeding THB 120,000 for each mortgage
- For a mortgage of a condominium, 1% of the mortgage value for each mortgage

The registration of business security is subject to the following registration fees, payable to the relevant authority at the time of registration:

- For business security over land, 1% of the maximum secured value, but not exceeding THB 200,000 for each business security
- For business security over assets other than land, 0.1% of the maximum secured value, but not exceeding THB 1,000 for each business security

If things go wrong

1. Please provide a brief description of the insolvency regime. In particular what rights and duties do unsecured and secured lenders have on the insolvency of a debtor? Are there any other matters of concern?

Personal bankruptcy

Personal bankruptcy in the Thai system commences exclusively by a creditors' petition being filed with the Bankruptcy Court. Thai law does not provide for the institution of voluntary bankruptcy proceedings. After receiving a bankruptcy petition, the court will set a first hearing date at which objections to the bankruptcy petition will be considered. At the hearing, the court will examine the bankruptcy petition. If the petitioning creditor can verify the debtor's state of insolvency and there are no reasons why the debtor should not be adjudged bankrupt, the court will accept the bankruptcy petition and issue an absolute receivership order. This order triggers the official receiver to locate and collect the debtor's assets and remove the debtor from having control over its assets.

One special feature of Thai law is the ability of a creditor to seek a temporary receivership order, through an ex parte injunction, to freeze the debtor's assets or require the debtor to provide security. This special pre-bankruptcy action is designed to prevent a debtor from liquidating its assets to the detriment of its creditors.

Prior to the first meeting of creditors, the debtor may propose to the official receiver a compromise of debts (i.e., an arrangement that specifies the amount that creditors will receive (which would be a lesser amount than they are owed)) or the method of management of the business and assets, and provide details of any security. Creditors may agree to accept a compromise of debts by a special resolution of a meeting of creditors, requiring the approval of creditors representing 75% of the debt by a majority of the creditors in attendance at the meeting. If the approval of a compromise of debts fails, the debtor will be declared bankrupt, and the seizure and liquidation of the debtor's assets will be carried out by the official receiver and distributed according to the creditors' preferential ranking.

The debtor can be released from bankruptcy by a post-bankruptcy compromise of debts and discharged from bankruptcy under the Bankruptcy Act B.E. 2483 (1940) (as amended) on any of the following four grounds:

- That no creditor assists the official receiver in the collection of assets
- That the debtor should not be adjudged bankrupt
- That the debts of the bankrupt have been paid in full
- That during the 10-year period after the closure of the bankruptcy action, the official receiver has been unable to collect any further assets of the bankrupt entity

Corporate bankruptcy

There are three types of procedures available for corporate debtors as set out below. The features of the three types of procedures are also discussed below.

Creditor-initiated bankruptcy

Under a creditor-initiated bankruptcy, the successful verification by the creditor of the debtor's insolvency leads to a court order of absolute receivership and the process falls under judicial supervision.

Debtor-initiated bankruptcy

A debtor-initiated bankruptcy occurs through voluntary liquidation. The shareholders may by a special resolution, if its contributions or shares are fully paid up and if its assets are insufficient to meet its liabilities, apply to the court through a liquidator to have the entity declared bankrupt.

Business reorganization procedure

A business reorganization procedure, either creditor-initiated or debtor-initiated, is available with the objective of rehabilitating the business. A reorganization planner ("**Planner**") or plan administrator ("**Administrator**") operates this procedure with judicial oversight.

Features of a debtor-initiated bankruptcy and a creditor-initiated bankruptcy

Thai courts tend to rely heavily on the balance sheets of the company. Therefore, in cases where a debtor attempts to inflate its assets to create a positive balance sheet in relation to a debtor-initiated bankruptcy, creditors will require strong proof to convince the court that the debtor is insolvent.

The ability to seek a temporary receivership order, the ability of the corporate debtor to propose a compromise of debts, and the methods of release from bankruptcy are also applicable to corporate bankruptcy.

The process for corporate bankruptcy is the same as it is for a personal bankruptcy. After receiving the bankruptcy petition, the court will set a first hearing date, at which objections to the bankruptcy petition will be considered. If the bankruptcy is accepted by the court, an absolute receivership order will be issued, and the official receiver will seize and assume control over all of the debtor's assets.

Features of a business reorganization procedure

The debtor, its creditor or relevant government authorities may submit a petition for a business reorganization. On the submission of the petition and the court's acceptance of the petition, an automatic stay will come into effect and parties will be prohibited from taking certain actions regarding the debtor. These actions include the following:

- Commencing litigation proceedings or requesting the court to wind up the debtor
- Taking a bankruptcy action against the debtor
- Enforcing a judgment against the debtor's assets for debts incurred prior to the date that the court issues an order to approve the reorganization or rehabilitation plan
- Transferring, disposing of, leasing out, incurring debts or undertaking any action that creates a burden over the debtor's property, except as is necessary for normal trade activities

Similar to typical bankruptcy proceedings, the court will set an enquiry hearing date at which objections to the petition will be considered. Following the court's order to reorganize the debtor's business, all powers to manage the debtor company will pass to the Planner and then to the Administrator after the court approves the reorganization or rehabilitation plan (except where the debtor acts as its own Planner or Administrator). After the Planner's details are published in the Government Gazette, creditors have one month to lodge their creditor claims with the official receiver, failing which, their creditor claims will be barred.

The reorganization or rehabilitation plan must be approved by the affirmative votes of the following:

- A simple majority of creditors (i.e., 50% of creditors where each creditor has one vote) in each group of creditors, provided that the creditors voting in favor of the plan in each group hold debts representing at least two-thirds of the debts owed to that group
- A simple majority of the creditors in at least one group of creditors provided that: (i) the creditors in that group hold debt representing at least two-thirds of the debt owed to that group; and (ii) the total debt owed to creditors in all groups who voted in favor of the plan represents at least 50% of the total debt owed to all creditors in all groups

In this regard, the majority creditors can impose a plan on minority creditors, including a plan relating to any difference between the amount of a particular debt and the security relating to that debt. Under Thai law, any debt that is forgiven under a reorganization or rehabilitation plan is exempt from taxation.

Subsequently, the court must approve or reject the reorganization or rehabilitation plan. In this regard, the court is required to examine any objections to the plan. If the plan is rejected, the court may simply revoke the order granting permission to reorganize the debtor's business and return the debtor to a state of normal business operations, or if there is a pending bankruptcy lawsuit against the debtor, order those pending bankruptcy proceedings to continue.

Clawback

An important feature of both the Thai bankruptcy and reorganization laws is the ability to have fraudulent acts, acts of undue preference and executory contracts invalidated during the bankruptcy or reorganization process.

The Planner, Administrator or official receiver may ask the court to cancel a fraudulent act by filing a motion with the court. A "fraudulent act" is defined as an act conducted by the debtor with the knowledge that the relevant act would prejudice its creditors. However, this nullification does not apply if the third party that received the benefit in relation to that act gave fair value for the act and did not know, at the time of the act, that the act would prejudice the debtor's creditors. The prescription period to request nullification of a fraudulent act is within one year from the time the creditor knew of the cause for nullification of the act or within ten years from the occurrence or commission of the act. If the alleged fraudulent act was conducted within one year of the filing of the application for bankruptcy or reorganization, it is presumed that the debtor and the third party had knowledge that it would prejudice the debtor's creditors.

When there appears to have been a transfer of assets or any other act that the debtor has committed or allowed to be committed within the three-month period prior to or after the filing of the bankruptcy or reorganization petition, with the intent to place any creditor in an advantageous position over other creditors, the Planner, Administrator or official receiver may file an application with the court requesting the nullification of that transfer or act.

In addition, within two months from the date that the Administrator is informed of the court's approval of the reorganization or rehabilitation plan, the Administrator has the right to refuse to accept rights under a contract where the obligations exceed the benefits to be received, provided that those rights were included as part of the reorganization or rehabilitation plan approved by the creditors' meeting and the court.

2. Is it possible to obtain a moratorium before insolvency?

Yes, a creditor may seek a temporary receivership order, through an ex parte injunction, to freeze the debtor's assets or set up a bankruptcy action against the debtor. If the court finds the debtor to be insolvent, it makes an order that places the debtor in absolute receivership, by which the debtor is suspended from any action related to its assets and any legal challenge in relation to the debtor's assets is put on hold.

3. When a company is the subject of a formal insolvency procedure, can the company's pre-insolvency transactions be set aside?

Transactions in which a creditor allows a debtor to create additional debts even though the creditor knew at the time (e.g., because the debtor had not been servicing the relevant debt for several years) that the debtor was insolvent (i.e., assets are less than debts) can be set aside. A creditor that allows the additional debts to be created will be barred from filing a claim to recover the amount of those additional debts.

The additional debt does not include debts permitted to be created so that the debtor can continue its ordinary business operations.

4. When can a lender enforce its security? Can security be enforced out of court following an event of default (or other contractual trigger event), or is a court order required? Are there any restrictions that apply before a lender may enforce its security?

Security can be enforced upon the breach of the underlying obligations that the security secures, subject to contractual terms and conditions. The enforcement requirements differ depending on the type of security and they are set out below.

Valid security interests under Thai law

Pledge

A pledge can be enforced out of court. To enforce a pledge, a written demand notice must be given to the debtor requiring it to perform the obligations and all accessory acts within a reasonable time (as stated in the notice). If the debtor fails to comply with the notice within the prescribed period, the pledgee is entitled to sell the pledged property but it must be sold by public auction.

Mortgage

A mortgage can be enforced by a court order to either foreclose or sell the mortgaged property by public auction.

To enforce a mortgage, a written demand notice must be given to the debtor by the creditor requiring the debtor to perform the obligations and pay for all related charges within a reasonable time (as stated in the demand notice, which in any case must not be less than 60 days from the receipt of the creditor's written demand notice). In the case of a third-party mortgagor, the creditor is also required to serve a demand written notice on that third-party mortgagor within 15 days after the date of its demand notice to the debtor. If the creditor fails to serve the required written demand notice within the 15-day period, the third-party mortgagor is relieved from any liability for all interest, compensation and accessorial charges arising after that prescribed period.

Business security

A business security created under the Business Security Act can be enforced once an enforcement event (as specified in the business security agreement and the registration record) occurs. The enforcement in relation to specific assets and entire businesses are subject to different procedures.

In relation to specific assets, the creditor can choose one of the following:

- Foreclosure
- Sale of the secured assets by public auction by serving an enforcement notice on the security provider

Once the notice is served, the security provider is prohibited from disposing of the secured assets or causing the value of the secured assets to decrease and it is required to surrender them to the secured creditor that will then be entitled to take possession of the secured assets. No court proceedings are required except where the security provider refuses to surrender the secured assets to the secured creditor.

In relation to an entire business, enforcement must proceed through a duly licensed security receiver authorized to enforce the security. The parties appoint the security receiver by serving an enforcement notice on the security receiver. The security receiver will be responsible for the investigation in relation to whether an enforcement event has occurred. Once the security receiver determines that an enforcement event has occurred, the managerial power and shareholders' rights over the business (except rights to dividends) will be transferred to the security receiver. The security provider is required to deliver the entire business, related documents and related rights and liabilities to the security receiver within seven days after the receipt of the enforcement order from the security receiver. The security receiver is in charge of managing the business until it is sold, selling the business and allocating the sale proceeds.

Other security interests

Guarantee

To enforce a guarantee, upon a default by the debtor, the creditor must serve a written demand notice on the guarantor within 60 days of the default. The creditor may not demand that the guarantor perform its obligation before the written demand notice reaches the guarantor. If the creditor fails to serve a written demand notice within the 60-day period, the guarantor is relieved from any liability in relation to all interest, compensation and related charges arising after the prescribed period.

If the creditor is entitled to demand that the guarantor perform the obligations of the debtor after the default by the debtor, the guarantor can choose to do one of the following:

- Perform that obligation in its entirety
- Exercise its right to perform only the specific portion of the debtor's obligations for which the guarantor is liable under the terms and conditions of the obligations agreed between the debtor and the creditor prior to the default

In these circumstances, the guarantor will be exempted from paying interest at the default interest rate. If no payment is made within the period specified in the demand notice, the creditor may file a lawsuit in court.

Assignment

To enforce an assignment of rights, the relevant parties may give a demand notice to the counterparty stating their intention to enforce their rights under the assigned agreement. If there is no payment within the specified period under the demand notice, the creditor may file a lawsuit in court.

5. Do any limitation periods apply in relation to bringing an action to enforce security?

The limitation period for bringing an action under a loan is ten years from the date when the relevant claims can be enforced. The barring of claims because of an elapsed limitation period or time prescription does not prevent a mortgagee or a pledgee from being entitled to enforce its security in relation to the secured assets. However, enforcement in relation to the outstanding interest is only permitted for the amount outstanding in the five years preceding the enforcement proceedings.

6. Is there any particular way in which secured assets must be liquidated on enforcement (e.g., by auction or court sale)?

Secured assets must only be liquidated on enforcement by public auction.

7. Are there any particular legal or practical difficulties or delays in enforcing security?

A mortgage can only be enforced by a court order and the secured assets must be sold by public auction. The judicial process can take a considerable amount of time before a final judgment is obtained. Sometimes, no bidders may participate in the auction and this may further prolong the enforcement process.

In our experience, the enforcement of business security under the Business Security Act is still unprecedented.

8. In relation to enforcement, are there any specific requirements to be borne in mind if the lender is a foreign entity?

There are no specific requirements that apply to foreign entities in relation to the enforcement of security in Thailand. However, foreign entities should be aware that there are issues in relation to the recognition and enforcement of foreign court judgments. Thai law does not specifically provide for the direct enforcement or recognition of foreign court judgments in Thailand. Moreover, Thailand is not a party to any treaty or agreement by which the judgment of a foreign court is entitled to be recognized and enforced in Thailand. Therefore, new judicial proceedings based on the merits of the case must be initiated in Thailand. However, foreign court judgments and documentary evidence generated during any foreign litigation process, including settlement negotiations, may be admissible as evidence in new court proceedings initiated in Thailand.

9. Is there any reason why you think that arbitration rather than litigation might be advantageous in resolving disputes under the finance documents, and if so, why? Please outline the relative merits of arbitration and litigation, including the ease of enforcement of foreign judgments and foreign awards from different jurisdictions. Is it possible to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit?

The advantages of arbitration over litigation are as follows:

- An arbitral award is likely to be obtained in a shorter time than court judgments because a court judgment is likely to be subject to subsequent appeal proceedings before two superior courts before it becomes final.
- An arbitral award is final and binding on the parties in the arbitration proceedings. Under the Arbitration Act B.E. 2545 (2002) ("**Arbitration Act**"), neither party can appeal against the merits of the arbitral award, whether to the arbitral tribunal or the courts in an action for the enforcement of the arbitral award.
- Thai courts generally recognize and enforce arbitration awards whether they are made in Thailand or elsewhere. However, the courts are more likely to enforce foreign arbitration awards if the parties involved are entitled to rely on the terms of relevant international conventions to which Thailand is a party. At present, Thailand is a member state of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (also known as the New York Convention 1958), and the Convention on the Execution of Foreign Arbitral Awards 1927 (also known as the Geneva Convention 1927). Therefore, an arbitral award made in a member state under either of these conventions will be recognized and enforced by Thai courts. Nevertheless, as discussed in the answer to question 8 of this section, Thai law does not specifically provide for the direct enforcement or recognition of foreign court judgments in Thailand.
- In litigation proceedings before the courts of Thailand, the trial and all documentary submissions and pleadings must be conducted in Thai. However, in arbitration proceedings, although the seat of arbitration may be in Thailand, parties can agree to have the arbitration conducted in another acceptable language.

It is also possible under Thai law to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit.

10. Are asymmetrical jurisdiction clauses enforceable? (By this we mean clauses that allow the lenders, but not the borrowers, to make certain choices in relation to choice of jurisdiction and how to litigate. These types of clauses allow the lenders, but not the borrowers, to commence proceedings in any court they choose, but restrict the borrowers to commencing proceedings in one jurisdiction only. This may also allow the lenders, but not the borrowers, to choose whether to litigate the finance documents before a court or to submit to arbitration in relation to them, but restrict the borrowers to either litigation or arbitration, as specified in the agreement).

We are not aware of any precedent judgment or decision in relation to this type of asymmetrical jurisdiction clause. In principle, Thai law does not prohibit the agreement for the submission by any person to the jurisdiction of a foreign court, but an agreement of this type does not prevent Thai courts from having jurisdiction over the case if, by virtue of the Civil Procedure Code of Thailand, it has jurisdiction over the case. It is likely that Thai courts would exercise their jurisdiction over any case within their power regardless of any contractual restriction.

In relation to the choice between litigation and arbitration, under the Arbitration Act, when the agreement to arbitrate exists and it is valid, the parties are prohibited from filing a lawsuit before any court and they are bound to refer the dispute to arbitration. If any party files a lawsuit before any court in breach of the arbitration agreement, the other party may ask the court to stay the litigation proceedings so that the case can be referred to arbitration. Unless this arbitration agreement is void or unenforceable, Thai courts will usually give effect to it and will stay the litigation proceedings.

Working digitally

1. **Is it possible for documents to be executed electronically (whether by the manual insertion of a digital signature or the use of an e-signing platform) under the laws of this jurisdiction? If so, is this limited to only particular types of finance documents?**

   The Electronic Transaction Act B.E. 2544 (2001) (ETA) supports the legal effect of the e-signature much like the traditional signature on paper, provided that the criteria of being an e-signature under the ETA is met. The Electronic Transaction Development Agency recently published a recommendation on the ICT standard for electronic transactions in June 2023. This is also subject to further general legal formalities for each type of finance document (such as security documents) to ensure the validity of such document.

2. **Where the witnessing of a signing is contemplated, is it possible for the witness to verify the signature over a live video call?**

   In a case where the law requires the signature of a witness, it is arguable whether the witness has to be "present physically" at the same place as the parties that are signing the agreement, or whether electronically witnessing from a distance via a live video call would suffice. Both e-transaction-related laws must be met and general legal formalities for each document/transaction must be followed to ensure the legal validity of such document/transaction.

3. **Is it possible to register/perfect security electronically without wet ink signatures?**

   The registration system of mortgages in Thailand currently requires documents to be executed in the presence of the officer in wet ink.

   Other forms of security may be executed with an e-signature, but the legal requirements in relation to the perfection requirements, as mentioned in question 11 of the section "If taking security" will still apply.

4. **Are there any other legal restrictions that may prevent the parties from executing a finance transaction electronically?**

   No.

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VIETNAM

Vietnam

When considering whether to lend

1. **Is it necessary or advisable for any lender, arranger, facility agent or security agent to be licensed, qualified or otherwise entitled to carry on business in this jurisdiction: (a) by reason only of its execution, delivery or performance of the finance documents; or (b) to enable it to enforce its rights under the finance documents?**

   No. However, we note that there are only regulations of the State Bank of Vietnam (SBV) on syndicated loans of credit institutions that allow the appointment of a foreign lender among the syndicated lenders to handle the roles of lender, arranger and security agent. It is unclear if a foreign lender can play these agency roles if it is not a lender in the lending transaction.

   From a practical perspective, in relation to medium - and long - term offshore loans, since the identity of the facility agent and the security agent is described in the application for registration of the foreign loan with the SBV, it is arguable that if the foreign loan documentation has been examined and the foreign loan registration certificate recording the identity of the facility agent and the security agent has been issued by the SBV, the SBV is deemed to consent to the proposed foreign agency arrangement.

2. **Will any lender, arranger, facility agent or security agent be deemed to be resident, domiciled, carrying on business or subject to tax by reason only of the execution, delivery, performance or enforcement of the finance documents?**

   No; however, there is a requirement for the borrower to deduct withholding tax (currently set at 5%) from the amount of interest and fees payable to the lender under the finance documents (see the answer to question 5 of the "When lending to borrowers" section).

3. **Are there any regulatory reporting requirements that lenders must observe in connection with those transactions?**

   Foreign lenders are not required to report their transactions in Vietnam. However, credit institutions that provide account services for payments in relation to offshore loans are subject to a specific statistical reporting regime under the regulations of the SBV.

4. **Is it necessary to establish a place of business in your jurisdiction in order to enforce any provision of the finance documents?**

   No.

5. **Is a foreign bank/financial institution permitted to approach local entities for business?**

   Yes, if the approach is on a limited basis, i.e., made one-to-one and not to the public. This is because a general approach to potential customers in Vietnam for offering loans could be regarded as "advertising," which may only be provided by licensed advertising agencies in Vietnam.

When lending to borrowers

1. **Are there any restrictions in relation to the type of borrower who may borrow foreign currency or in relation to the term of foreign currency and/or the amount of foreign currency borrowed by local entities?**

   There are no restrictions on the type of borrower that may borrow foreign currency or on the terms of those loans, or generally on the amount of foreign currency loans. However, certain borrowers must satisfy certain conditions for borrowing offshore loans, including limitations on the amount of offshore loans that an enterprise may borrow. The form of the enterprise of the borrower and its investment/enterprise registration certificate determines whether those limitations apply to a particular borrower.

   Under the foreign exchange regulations, in principle, individuals may obtain offshore loans in accordance with the government's regulations. However, the government has not yet issued any regulations in relation to the borrowing of offshore loans by individuals, and therefore, the SBV is likely to take the view that, because there is no explicit permission, it is not permitted. Given the foregoing, in practice, offshore loans may not be granted to individuals.

2. **Are there any restrictions on the rate of interest or default interest that may be charged?**

   Vietnamese laws do not restrict the rate of interest or default interest in relation to offshore loans. However, as a matter of practice, if the rate of interest is too high compared to the market standard, the SBV may challenge the registration of the loan (referred to in the answer to question 7 of this section) and the parties will need to explain the reason for the high rate of interest. The SBV may refuse to register a loan if it considers the interest rate to be too high. There is also a criminal penalty for usury in Vietnam but, in practice, it is unlikely that an offshore lender would be subject to a usury penalty.

   The remittance bank in Vietnam may also challenge the payment of interest that is too high (at the bank's discretion) if there is concern in relation to a potential breach of Vietnam's anti-money laundering regulations.

   Under applicable exchange control regulations, the governor of the SBV may determine the ceiling on borrowing costs for each interest period. However, we are not aware of the governor ever having imposed a ceiling on the borrowing costs for offshore loans.

3. **Are there any restrictions on particular lenders or classes of lender entering into credit transactions with borrowers?**

   No. However, please note that there may be restrictions on the role that an offshore lender may take in relation to cross-border syndicated loans. Under Vietnamese laws, an offshore lender is not permitted to act as the paying agent in relation to a syndicated transaction.

4. **Are there any exchange controls that will apply to payments to be made in foreign currencies or to foreign lenders?**

   No. However, for:

   - Medium- or long-term offshore loans with a term of more than one year;
   - Short-term loans whose principal payment period is extended so that the total term is over one year; and
   - Short-term loans without any renewal agreement whose term is over one year from the first utilization date unless the borrower fully completes its debt repayment obligation within 30 working days from the first anniversary of the first utilization date,

   that, in each case, are not guaranteed by the government, drawdown of the loans and payment of debts (including the principal and interest) contemplated under the facility agreement can only be made after the registration of the loans with the SBV (except in the case of the drawdown and partial repayment in the first year of a short-term loan which is being extended to a medium- or long-term loan).

5. Is there any requirement to deduct or withhold tax from any amounts to be paid or repaid to a lender (whether domestic or foreign)? If so, at what rate must tax be deducted and from what kinds of payment?

If the lender is an offshore entity, the borrower is required to deduct withholding tax (currently set at 5%) from the amount of interest and fees payable to the lender under the finance documents. The borrower must file and pay the tax it has withheld within 10 days after each payment of interest or fee.

The foregoing requirement does not apply to Vietnamese lenders.

6. Are there any "thin capitalization" or other rules that may limit the extent to which interest payments may be deducted for tax purposes?

There are no "thin capitalization" rules under the current regulations.

An interest payment may not be deductible if, among others:

- It does not meet all of the following requirements:
- The actual interest payment incurred is related to the enterprise's business operations.
- There are sufficient and valid invoices in relation to the interest payments and proof of those interest payments can be shown as required by the tax regulations.
- For each invoice for an interest payment of VND 20 million or above, there is proof of the corresponding non-cash payment.
- The payment of interest or the related loan payment relates to the enterprise's late equity contribution.

7. Are there any registration, notarization, translation or reporting requirements in relation to the loan documents?

Yes. Under Vietnamese foreign exchange regulations, medium- or long-term offshore loans (i.e., offshore loans with a term of above one year, including short-term loans being extended to medium- or long-term loans) that are not guaranteed by the government are required to be registered with the SBV. The information to be provided on registration must include information about the offshore lender.

Loan documents can be made in any foreign language, with Vietnamese translations required for SBV registration purposes, with the accuracy to be certified by the borrower.

Vietnamese borrowers must also submit a written report on the status of the implementation of the offshore loan on a monthly basis or, in the case of unexpected or urgent events, on an extraordinary basis upon the request of the SBV.

8. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to the loan documents? If yes, what are the amounts and when are they payable?

No, SBV registration for foreign loans is free of charge.

For stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in relation to security documents, see the answer to question 13 of the "If taking security" section below.

9. Does the law recognize the subordination of the debt that a debtor owes to one creditor to that which the debtor owes to another creditor? If yes, how is this usually effected?

Except for the case where credit institutions and foreign bank branches in Vietnam are permitted to issue subordinated debts pursuant to the regulations on prudential ratios and limits for operations of credit institutions and foreign bank branches of the SBV, Vietnamese law is silent on the subordination debt of enterprises. Vietnamese laws only provide that the order of priority for payment between the jointly secured parties may be changed if the jointly secured parties reach an agreement on changing the order of priority for payment between themselves. As a matter of practice, a creditor is entitled to contractually agree that its rights are subordinated

to the rights of another creditor, subject to the fact that the rights of the parties may be limited by bankruptcy, insolvency, liquidation, reorganization and other laws of general application relating to or affecting the rights of creditors. The manner in which a subordination agreement is treated may be affected by how the Vietnamese courts exercise their inherent discretion.

If a bankruptcy process has been initiated in respect of the borrower, its indebtedness is paid in accordance with the hierarchy set out in the bankruptcy regulations (and therefore not necessarily as agreed between the lenders and borrowers). For the hierarchy of payments in relation to bankruptcy, see the answer to question 10 of this section.

10. Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's other unsecured and unsubordinated creditors (e.g., the claims of employees and tax authorities or the claims of creditors under particular kinds of instrument)? If yes, what classes of creditors are preferred?

If a bankruptcy process has been initiated in respect of the borrower, the order of the distribution of its assets is prescribed by the bankruptcy regulations and claims are paid in the following descending order of priority:

- Bankruptcy costs.
- Employees' unpaid wages, severance allowances, social insurance and health insurance, and other benefits under labor contracts and collective labor agreements.
- Debts arising after the commencement of bankruptcy proceedings that serve the purpose of business recovery of the enterprise or cooperative in accordance with the bankruptcy regulations.
- Financial obligations to the state, unsecured debts payable to the creditors named in the list of creditors and secured debts not yet paid as the value of their secured assets is insufficient for the debt payment.
- The members or shareholders of the enterprise (as the case may be).

If the value of the available assets is insufficient to pay all the creditors in any of the above categories, the debt due to each creditor in that category will be reduced on a pro rata basis.

11. Are there any consumer protection or similar laws that apply if credit is made available to individuals or other classes of debtor? If yes, what laws are applicable?

For onshore loans, the rights and obligations of creditors and debtors are subject to the SBV's regulations in relation to borrowing.

For offshore loans, creditors and debtors are free to agree upon their specific rights and obligations in the relevant offshore loan agreement.

However, although it is untested in practice, regulations in relation to consumer protection likely apply to parties to an offshore loan. Therefore, legal counsel should carefully review the loan agreement to ensure its provisions are enforceable.

12. Are there any prohibitions or limitations on the extent to which a company can give financial assistance for the purchase of: (a) its own shares or those of any affiliated company; or (b) assets owned by it or any affiliated company?

Technically, providing financial assistance may be deemed to constitute "lending," which requires a license from the SBV. Therefore, non-credit institutions in Vietnam may not provide loans to a third party for the purpose of purchasing shares or other assets.

Vietnamese foreign exchange regulations require borrowers to borrow offshore loans for a limited number of purposes, as follows:

If the borrower is a credit institution or foreign bank branch:

- To supplement capital for credit extension activities according to the borrower's credit growth
- To refinance the borrower's offshore loans

It would appear that if the borrower is a credit institution or foreign bank branch it is not allowed to use offshore loans for purchasing shares or other assets.

If the borrower is not a credit institution or foreign bank branch:

- For mid- or long-term loans to:
- Implement the borrower's investment project
- Implement the production and business plan, or other projects of the borrower
- Refinance the borrower's offshore loans
- For short-term loans:
- To refinance offshore loans
- To repay short-term loans (in accordance with accounting law) payable in cash (excluding principals of onshore loans) of the borrower, which are incurred during the implementation of investment projects, production and business plans and other projects of the borrower
- in cases where the borrower is subject to prudential ratios according to specialized laws, for the borrower's professional business activities, provided the loan term is no more than 12 months after the utilization date

Therefore, if offshore loans are used for purchasing shares or other assets, the specific utilization should be categorized within the scope of:

- For mid- or long-term loan: the approved investment project/production and business plan/other projects of the borrower, which should be certified by the SBV. It is unlikely that the SBV will certify the offshore loans for the purposes of purchasing shares unless the borrower already has existing investment in the target company such that the purchase of shares would arguably be considered further investment by it in the target company.
- For short-term loan: the borrower's professional business activities, e.g., securities investment activities conducted by professional securities investors.

If taking security

1. **Are there any classes of unsecured and unsubordinated creditor whose claims against a debtor would rank equally with or above those of the debtor's secured creditors?**

   No. The claims of secured creditors have priority over the claims of unsecured creditors.

2. **May security given by a company rank in a specified order so as to secure liabilities owed to different creditors of the company in that order and, if that is not possible, is it viable for parties to enter into a contractual arrangement for the purposes of moderating this order?**

   By law, the order of priority of the payment of secured transactions is determined by the order of the times when the secured transactions become enforceable against third person(s) (or, if none are enforceable against a third person, the order of their creation) and payments in relation to transactions that are enforceable against third persons will be made before payments in relation to transactions that are not enforceable against third persons.

Security will be enforceable against a third person from when the security is registered or when the secured party keeps or holds the secured assets. However, that order may be changed by agreement between the creditors in the circumstances set out in the following paragraph.

If one asset is used to secure debts due to more than one creditor, those creditors may agree on a specified order of payment that differs from the order provided by law. The party granted priority under an agreement of this type only has a right to a priority payment up to the scope (value) of the security to which the party granting the priority under that agreement is entitled.

3. Does this jurisdiction recognise the concept of floating security or similar equivalent (i.e., security over a changing pool of assets that the company giving the security is free to buy, sell and generally deal with)?

No. Floating security is not recognized under Vietnamese law. However, there are special regimes for the following:

- A mortgage of circulating goods used in the manufacturing and trading process.
- A mortgage of goods in storage.

Both of these regimes have features similar to the usual principles that apply to floating security. Notable features of these regimes are as follows:

- For a mortgage of circulating goods used in the manufacturing and trading process, the mortgagor may sell or replace the mortgaged asset without the consent of the mortgagee. If there is a sale of goods, in substitution for the sold mortgaged assets, the mortgage will attach to the sale receivables, sale proceeds or to the assets purchased with the sale proceeds. If there is a replacement of goods, the replacement goods will become the mortgaged assets in substitution of the replaced goods.
- For a mortgage of goods in storage, the mortgagor may replace the goods placed in storage without the consent of the mortgagee. However, the mortgagor must ensure that the value of the goods after the replacement is the same as before the replacement.

4. If so, are there any practical reasons why floating security is difficult to take, maintain or enforce?

This is not applicable, as floating security is not recognized under Vietnamese law. Nevertheless, there are practical issues in relation to taking and maintaining a mortgage of circulating goods used in the manufacturing and trading process and a mortgage of goods in storage, as described in the answer to question 3 of this section.

The mortgagee is typically concerned about how to ensure that the mortgagor honors its undertaking and that the value of the mortgaged assets does not fall below the initially agreed value when the mortgagor has the right to dispose of the mortgaged assets without the mortgagee's consent. The mortgagee will typically request the mortgagor to agree to the appointment of a supervisor by the mortgagee who will supervise the mortgaged assets frequently to ensure that any disposal of the mortgaged assets complies with the mortgage terms.

5. May security be granted to a trustee to be held on trust for the lenders from time to time, in such a way that a change of lenders does not require new security to be taken?

No. Trusts are not recognized under Vietnamese law.

6. If not, are there any techniques that can be used to achieve substantially the same effect (e.g., parallel debt structures)?

In a syndicated loan transaction, one lender may act as the security agent for all of the lenders. The security agent may take security on behalf, and secure the debts, of all the lenders and may sign the security documents on behalf of all of them. The security agent can be an onshore or an offshore lender. However, offshore lenders are prohibited from taking security over land use rights and assets attached to land in Vietnam regardless of whether an onshore security agent is appointed to take the security over such land use rights and assets attached to land in Vietnam for and on behalf of offshore lenders. In this scenario, if the syndication only consists of offshore

lenders, the lenders may engage a Vietnamese finance party providing a nominal facility amount or issuing a nominal standby letter of credit in favor of the foreign lenders to secure the obligations of the borrower to the foreign lenders to take security over land use rights and assets attached to land in Vietnam and the foreign lenders may take security over the surplus from the proceeds of an enforcement of the security over land use rights and assets attached to land in Vietnam (after deducting the amount payable to the Vietnamese finance party). The finance parties and the borrower will then agree on sharing all proceeds from the enforcement of the security over land use rights and assets attached to land in Vietnam. However, such mechanisms have not been tested before Vietnamese courts.

7. If an agent holds security for the lenders rather than a trustee, is it necessary to take new security on a change of lenders? If no, why not? If yes, are there ways to structure the transaction to avoid such a requirement?

No. A change of lenders does not require a change to the security documents and it does not require new security to be taken.

8. Under the laws of this jurisdiction, is there any class of asset over which it is difficult or impossible to grant effective and perfected security, or in relation to which any security granted will be of limited effect?

Land use rights and assets attached to land in Vietnam may only be mortgaged to, except for certain irrelevant cases, onshore credit institutions that are licensed to operate in Vietnam. Further, if an enterprise wishes to mortgage its land use rights, it must pay the land use right fees or rent in full and in a lump-sum payment for the entire lease term to the state authority. If an enterprise wishes to mortgage its land use rights and the relevant lands are located in the industrial zone, it is further required that the industrial zone developer must pay the fees or rent in full and in a lump-sum payment for the entire lease term to the state authority.

Specifically, if the industrial zone developer has leased a land use right in the industrial zone from the state and it has fully paid the rent in a lump-sum payment for the entire lease term, it can sublease that land use right to the sublessee with the rent to be paid as a lump-sum payment for the entire sublease term or with the rent to be paid annually. A land use right in an industrial zone subleased from the industrial zone developer can be mortgaged by the sublessee only if the sublessee has paid the rent to the developer in a lump-sum payment for the entire sublease term and the industrial zone developer has also paid the rent for that land use directly to the state in a lump-sum payment for the entire lease term.

In practice, if offshore lenders are involved, the structure described in the answer to question 6 of this section is advisable.

9. Under the laws of this jurisdiction, are there any restrictions on offshore lenders taking security over any class of asset?

The current laws bar offshore lenders from taking security interests over land use rights and assets attached to the land in Vietnam, as discussed in the answer to question 8 of this section.

10. Must a company receive a corporate benefit in return for giving a guarantee or security? In particular, are there restrictions on the grant of upstream and cross-stream guarantees and security? If yes, briefly what is the effect of these laws?

No. However, regarding upstream and cross-stream security, since the beginning of 2012, we have been aware of four precedents whereby four Vietnamese courts did not recognize a mortgage created over a third party's land use rights and immovable assets. We do not believe that it is a correct interpretation of applicable legal documents. The Ministry of Justice (MOJ), the SBV and the Vietnam Banks Association have sent official letters to the Supreme People's Court of Vietnam requesting that the Supreme People's Court of Vietnam give an interpretation of relevant legal documents with a view to recognizing the mortgage of land use rights created by

a third party that is not concurrently an obligor. We are not aware of any precedents where Vietnamese courts did not recognize a mortgage created over a third party's movable assets. This issue has recently been resolved under the new government's decree on security arrangements.

11. What type of security interests does your jurisdiction recognise, e.g., pledge, charge, mortgage, hypothecation? In relation to each type of security interest, please state the formalities required to create and perfect that security.

Vietnam law provides the following types of security for performing civil obligations.

Pledge of assets

A pledge of assets is created by a pledgor delivering its own assets to a pledgee as security for the performance of an obligation.

Mortgage of assets

Mortgage is the most common form of security interest granted over assets in Vietnam. By definition, a "mortgage" is a transaction in which the mortgagor uses its own assets to secure the performance of an obligation to the mortgagee without giving possession of such assets to the mortgagee. The core feature of a mortgage is that the mortgagor retains the use and possession of the mortgaged assets. This feature distinguishes a mortgage from a pledge in which the pledgee takes possession of the assets.

Performance bond

One party delivers a sum of money, precious metals, gemstones or other valuable objects to another party for a period of time as security for entering into or the performance of a contract.

Security deposit

The lessee of a movable asset delivers a sum of money, precious metals, gemstones or other valuable objects to the lessor for a period of time as security for the return of the leased asset.

Escrow deposit

An obligor deposits a sum of money, precious metals, gemstones or other valuable papers into an escrow account at a credit institution as security for the performance of an obligation.

Reserve of ownership (retention of title)

Pursuant to a purchase and sale contract, the ownership right to assets may be reserved by the seller until the time when the obligation to make a payment has been fully discharged. The reserve of ownership right must be made in writing in a separate document or it must be stated in the purchase and sale contract.

Guarantee

A third person undertakes to perform an obligation on behalf of an obligor if the obligation falls due and the principal fails to perform or incorrectly performs the obligation.

Fidelity guarantee

A sociopolitical organization at the grassroots level may provide a fidelity guarantee in order that poor individuals and households are able to borrow sums from credit institutions for the purposes of production, business or consumption in accordance with the law. The loan guaranteed by a fidelity guarantee must be made in writing and it must be certified by the sociopolitical organization providing the fidelity guarantee in terms of the conditions and situation of the borrower. The agreement providing a fidelity guarantee must specify the loan amount, the purpose of the loan, the term of the loan, the interest rate, and the rights, obligations and responsibilities of the borrower, the lending credit institution and the sociopolitical organization that provides the fidelity guarantee.

Retaining assets (lien)

A retaining assets arrangement (or lien) means that the obligee (known as the retaining party) that lawfully holds the assets that are the subject matter of a bilateral contract is permitted to continue to retain the assets when the obligor fails to perform the obligation or incorrectly performs the obligation.

Please refer to the answer to question 12 of this section for formalities required to perfect the security.

12. Are there any registration, translation or notarization requirements in relation to security, guarantees, subordination or intercreditor documents?

Registration

Mandatory registration

To be valid and enforceable, registration of the following security arrangements is mandatory:

- Registration with the district or provincial land use right registration office under the provincial Department of Natural Resources and Environment (DONRE) of the district, province or city where the asset is located:
  - Mortgage over land use rights
  - Mortgage over houses, assets attached to the land with ownership certificate
  - Mortgage over investment projects using land for which the mortgagor pays the fees or rents in full and in a lump-sum payment for the entire lease term to the state authority
- Registration with the municipal division of the Vietnam Maritime Administration of the province or city where the vessel is registered: mortgage or retention of title over vessel

Voluntary registration

Registration of the following security arrangements is recommended to secure the priority of payment, even though registration is not required for the secured transaction to be valid:

- Registration with DONRE:
  - Mortgage over houses, assets attached to and to be formed in the future
  - Mortgage over established assets attached to the land other than houses, which are not required by law to be registered, and the ownership rights of which have not been registered upon request
  - Transition of registration of mortgage over property rights arising from a sale and purchase of houses or other assets attached to the land to registration of mortgage over such houses or other assets attached to land
- Registration with the Vietnam Securities Depository and Clearing Corporation (VSDCC): security over securities centrally registered at VSDCC
- Registration with the National Registration Agency for Security Transactions (NRAST) under the MOJ:
  - Mortgage, retention of title, pledge, deposit, security collateral or escrow over movable assets (other than aircraft and vessel)
  - Security over securities, dividends, and property rights arising from securities that have not been centrally registered at VSDCC
  - Security over assets attached to land being annual plants, temporary works
- Registration with the Civil Aviation Authority of Vietnam (CAAV): mortgage, pledge or retention of title over aircraft. We note that registration of security over aircraft was explicitly stipulated as a mandatory registration. However, the language indicating that such registration is mandatory was removed as of 15 January 2023 in light of the enactment of the new legal document. The said security arrangements may also be registered with the International Registrar under the Convention on International Interests in Mobile Equipment (also known as the Cape Town Convention) to which Vietnam is a contracting state.

Notarization

A mortgage of land use rights and assets attached to land must be notarized by the public notary in the province or city where the asset is located before registration is permitted.

Translation

For registration purposes, foreign language documents must be:

- Translated into Vietnamese; and
- Notarized or certified the translator's signature

13. Are there any stamp, documentary, registration, notarization or other taxes, duties or fees chargeable in respect of security, guarantees, subordination or intercreditor documents? If yes, what are the amounts and when are they payable?

There is a fee for notarization. The amount of the notarization fee depends on the value of the secured transaction. The fee will not exceed VND 70 million. Notarization fees are due at the time of notarizing the relevant document.

Registration fees are as follows:

- For each registration with NRAST and the municipal division of the Vietnam Maritime Administration: VND 64,000
- For each registration with the district or provincial land use right registration office under the provincial DONRE: subject to the decision of the competent provincial People's Council, depending on the application dossier for registration, the number of land use rights certificates, the number of land parcels and assets attached to land that are recorded on a certificate in the application dossier for registration or other registration cases
- For each registration with the Civil Aviation Authority of Vietnam: from VND 1.4 million to VND 14.4 million, depending on the value of the secured transaction
- For each registration with the VSDCC: VND 80,000

Registration fees are due at the time of registration.

Other than these registration and notarization fees, there are no stamp, documentary, registration or other taxes, duties or fees chargeable in respect of security documents under Vietnam law.

If things go wrong

1. Please provide a brief description of the insolvency regime. In particular what rights and duties do unsecured and secured lenders have on the insolvency of a debtor? Are there any other matters of concern?

In Vietnam, an enterprise is considered insolvent when it fails to perform its obligation to repay a debt within three months from the maturity date and an insolvent enterprise is bankrupt when it is so declared by the court.

A lender's main rights on the insolvency of an enterprise are as follows:

- File a petition for the commencement of bankruptcy proceedings on the expiration of the period of three months from the maturity date of a debt in respect of which the debtor fails to perform its obligation to repay (except that a fully secured creditor does not have this right).

- As the petitioner for the bankruptcy procedure, nominate the asset management officer (an individual responsible for managing and liquidating assets during a bankruptcy procedure) or the asset management and liquidation enterprise (an enterprise established by one or more asset management officers with the same function as an asset management officer) to the court before the commencement of bankruptcy proceedings.
- Request individuals, bodies or organizations keeping and managing the documents and/or evidence relating to the lenders' legitimate rights and interests to provide those documents and/or evidence for submission to the court.
- Request the judge, asset management officer or asset management and liquidation enterprise to verify and/or collect documents and/or evidence that the lender is unable to do or seek an examination, valuation and/or appraisal of the value of the assets.
- Request that the judge audit the insolvent enterprise and summon witnesses.
- Access, take notes and/or make copies of the documents and/or evidence presented by other participants in the bankruptcy proceedings or collected by the judge.
- Request the application, change or cancellation of interim injunctive relief.
- Receive valid notices for the lender to exercise their rights and obligations.
- Protect or ask another person to protect their legitimate rights and interests.
- Attend the creditors' meetings.
- Request a replacement of the asset management officer or asset management and liquidation enterprise in accordance with the law.
- Request the asset management officer or asset management and liquidation enterprise to add creditors to the list of creditors and/or debtors to the list of debtors.
- Make a recommendation to the asset management officer or asset management and liquidation enterprise on the recovery of the debtors' money and assets.
- Participate in the asset management and liquidation as requested by the judge, the civil judicial enforcement office and/or the asset management officer or asset management and liquidation enterprise.
- Request a review of the court's decisions in accordance with the law.
- A lender's main duties on the insolvency of an enterprise are as follows:
- As the petitioner for the bankruptcy procedure, pay the bankruptcy fee and make an advance payment of bankruptcy costs.
- Satisfy requests from the judge, the asset management officer or asset management and liquidation enterprise, and/or the civil judicial enforcement office in accordance with the law.
- Provide documents and/or evidence relating to the bankruptcy resolution.
- Present itself as requested by the asset management officer or asset management and liquidation enterprise, or as summoned in writing by the court, and compliantly implement the court's decisions in relation to a bankruptcy resolution.

2. Is it possible to obtain a moratorium before insolvency?

Moratorium

There is a process in Vietnam known as the "recovery of business operations." It is a process by which an insolvent enterprise is intended to be returned to a state of solvency. A moratorium (together with other measures for the recovery of business operations (if any) and the conditions, time limit and plan for the payment of debts) must be included in the plan for the recovery of business operations of the insolvent enterprise. This is prepared by the insolvent enterprise (if the meeting of creditors passes a resolution for the application of the procedures for the

recovery of business operations), reviewed by the creditors, the asset management officer or asset management and liquidation enterprise, and the judge and it is submitted to the meeting of creditors for consideration and approval. The judge will issue a decision to acknowledge the approval of the plan for recovery of the insolvent enterprise's business operations by meeting creditors.

Time Limit

The time limit for the implementation of the plan for the recovery of the insolvent enterprise's business operations is subject to the creditors' approval in a meeting of creditors. If the meeting of creditors fails to specify the time limit, the applicable time limit is three years or less from the date the plan is approved.

Conditions

The conditions for the validity of a meeting of creditors approving the plan for the recovery of the insolvent enterprise's business operations are as follows:

- The number of creditors attending the meeting must represent at least 51% (in value) of the total unsecured debts. Any creditor that did not attend the meeting of creditors but sent its written approval or disapproval of the plan to the judge before the date of the meeting is deemed to have attended the meeting.
- The asset management officer or asset management and liquidation enterprise assigned to resolve the petition for the commencement of bankruptcy proceedings must attend the meeting of creditors.

Approval of the plan at the creditors' meeting

A resolution of the meeting of creditors is passed when the plan is approved by at least 51% of the total number of unsecured creditors attending the meeting and representing at least 65% (in value) of the total unsecured debts. If a plan for recovery of the insolvent enterprise's business operations involves the use of assets that are subject to a security granted by the enterprise in favor of secured creditors, the resolution must be approved by the creditors whose obligations are secured by the collateral, specify the period that those assets are permitted to be used and include a plan for the enforcement of the security.

Recognition of decision

The judge recognizes a resolution approving the plan for the recovery of the insolvent enterprise's business operations passed at the meeting and it is binding on all participants in the bankruptcy proceedings. As from the effective date of the resolution approving the plan for the recovery of the insolvent enterprise's business operations, the insolvent enterprise is no longer subject to prohibitions on and the supervision of its business operations.

The court will send the judge's decision recognizing the resolution of the meeting to the insolvent enterprise, all creditors and the Supreme People's Procuracy of Vietnam that corresponds with the relevant court within seven working days from the date of issue of the decision.

No meeting or no resolution

If no meeting of creditors is held or if the meeting is held but it fails to pass a resolution as set out above, the court will declare the insolvent enterprise bankrupt.

3. When a company is the subject of a formal insolvency procedure, can the company's pre-insolvency transactions be set aside?

Transactions that are deemed invalid

A transaction carried out by the insolvent enterprise within six months (or within 18 months if the transaction is conducted with a related person) before the date on which the court issues a decision to commence bankruptcy proceedings is deemed invalid if it falls into one of the following categories:

- A transaction related to a transfer of assets that is not at market value.
- The conversion of an unsecured debt into a debt that is fully or partially secured by the insolvent enterprise's assets.
- A payment or set-off that benefits a creditor in respect of a debt that has not yet become due or with a sum that is bigger than a debt that has become due.
- A donation of assets.
- A transaction outside the purpose of the business operations of the insolvent enterprise.
- A transaction for the purpose of disposing of the insolvent enterprise's assets.

In addition, the following transactions of an insolvent enterprise that are carried out after a decision to commence bankruptcy proceedings are prohibited and deemed invalid:

- A concealment, disposal or donation of any assets of the insolvent enterprise.
- A payment of any unsecured debts (except for unsecured debts arising after the commencement of bankruptcy proceedings and the payment of wages to employees as stipulated by law).
- The abandonment of any right to claim a debt.
- The conversion of unsecured debts into debts secured wholly or partly by the insolvent enterprise's assets.

Termination or temporary suspension of the performance of effective contracts

The insolvent enterprise or a creditor may request the court to issue a decision to temporarily suspend the performance of a contract (except for the settlement of secured debts in accordance with the law) if it finds that the performance of the contract (which has come into effect and is either being performed or has not yet been performed) may result in a disadvantage to the insolvent enterprise. This type of request must be made within five working days from the date on which the court accepts jurisdiction over a petition for the commencement of bankruptcy proceedings.

Within five working days from the date on which the court issues a decision to commence bankruptcy proceedings, it must review any temporarily suspended contract to decide on one of the following options:

- Continuing the performance of the contract if it is currently effective and being performed or if the performance will cause no disadvantage to the insolvent enterprise.
- Terminating the performance of the contract.

If the court decides not to commence bankruptcy proceedings, it must annul any decision for temporary suspension.

4. **When can a lender enforce its security? Can security be enforced out of court following an event of default (or other contractual trigger event), or is a court order required? Are there any restrictions that apply before a lender may enforce its security?**

Enforcement timeline

Upon the occurrence of an enforcement event, the lender or its security agent shall deliver an enforcement notice to the securing party and other registered secured parties, if any.

A lender can only enforce its security after the expiry of the waiting period as from the date of the enforcement notice. The waiting period can be either:

- The period as agreed between the parties; or
- A reasonable period as decided by the lender in the absence of a mutually agreed period, but no less than 10 days for moveable assets or 15 days for immovable assets

However, if the secured asset is in danger of damage resulting in it diminishing in value or the loss of its entire value, the lender can enforce immediately and concurrently deliver the enforcement notice.

Enforceability

Security can be enforced out of court following an event of default or another contractual trigger event. However, the lender may need to rely on the cooperation of the securing party to a certain extent for an efficient enforcement process. If the securing party is not cooperative and repossession of the collateral is necessary for enforcement purposes, the secured party will, in most cases, have to resort to the agreed dispute resolution forum, which could cost significant time and expense.

Restriction on enforceability

Within five working days from the date the court accepts jurisdiction of a bankruptcy matter, the enforcement of security given by the insolvent enterprise to secured creditors will be temporarily suspended by the competent authorities.

After the commencement of bankruptcy proceedings, the asset management officer or asset management and liquidation enterprise must make a recommendation to the judge on the settlement of secured debts where the payment has been temporarily suspended.

If secured assets that are subject to a security granted by the enterprise in favor of secured creditors are used for the recovery of the insolvent enterprise's business, the enforcement of the secured assets will be decided in the resolution of the creditors' meeting referred to in the answer to question 2 of this section.

If the recovery of the insolvent enterprise's business is not approved or the secured asset is not required for carrying out the recovery of the insolvent enterprise's business, the settlement of secured debts that have become due is permitted to be satisfied in accordance with the timing specified in the relevant agreement. In the case of secured debts that have not become due, before declaring the insolvent enterprise bankrupt, the court must terminate the contract and settle the secured debts. Secured debts established before the court's acceptance of the jurisdiction of the petition for the commencement of bankruptcy proceedings are repaid out of the secured asset. If the value of the secured asset is not enough to repay the debt, the unpaid part of the debt is repaid in the course of the liquidation of the assets of the bankrupt enterprise. If the value of the secured asset exceeds the amount of the debt, the difference is included in the value of the assets of the insolvent enterprise.

After the court accepts the jurisdiction of a bankruptcy matter or the commencement of bankruptcy proceedings, if the secured asset is at risk of destruction or a considerable decrease in value, the asset management officer or asset management and liquidation enterprise must recommend that the judge permit the immediate realization of the secured asset. The enforcement of the secured asset must be in accordance with the above principles. However, the issue of whether a secured loan with first ranking security interests over a secured asset will have the priority of repayment by such secured asset over other loans with lower ranking security interests in the bankruptcy procedures has not been tested before Vietnamese courts.

5. Do any limitation periods apply in relation to bringing an action to enforce security?

By law, the limitation period for initiating civil lawsuits is three years, starting from the date the claimants knew or should have known that their lawful rights and interests had been infringed. Commercial disputes are subject to a two-year limitation period from the date when the lawful rights and interests of the claimant(s) are breached. Although it is not entirely clear, such limitation periods may be applicable in relation to bringing an action before the dispute resolution authorities to enforce security. Under the regulations on the settlement of secured debts (as discussed in the answer to question 4 of this section), the settlement of debts in bankruptcy proceedings may be effected only after the commencement of bankruptcy proceedings or when the secured asset is at risk of destruction or a considerable decrease in value.

6. Is there any particular way in which secured assets must be liquidated on enforcement (e.g., by auction or court sale)?

No.

7. Are there any particular legal or practical difficulties or delays in enforcing security?

In practice, the enforcement of security requires the cooperation of the securing party, especially in respect of the repossession of secured assets by the secured party. If the securing party is not cooperative and the repossession of the secured assets is necessary for the purpose of enforcement, in most cases, the secured party will have to bring the dispute to the agreed dispute resolution forum to enforce it, which could cost significant time and expense.

8. In relation to enforcement, are there any specific requirements to be borne in mind if the lender is a foreign entity?

In the case of equity enforcement, a foreign lender may be subject to certain foreign ownership limitations and regulatory approvals imposed by Vietnamese law if the foreign lender takes an assignment of the secured assets in satisfaction of the prompt and complete payment and performance in full of the secured obligations. However, the foreign lender can also sell or assign the secured assets by way of a public sale, private sale or otherwise to avoid such circumstance.

Further, security enforcement proceeds arising from Vietnam must be carried out through a bank or branch of a foreign bank incorporated and operating in Vietnam ("**Security Supporting Bank**") before remitting to the foreign lender/security agent. Details of the Security Supporting Bank must be registered with the SBV in the application for foreign loan registration. For foreign loans that are already registered with the SBV before 15 November 2022, although Vietnamese law does not require the registration to be updated with the details of the Security Supporting Bank, considering that the enforcement proceeds must be carried out through a Security Supporting Bank, lenders should consider registering the Security Supporting Bank with the SBV for those registered loans.

9. Is there any reason why you think that arbitration rather than litigation might be advantageous in resolving disputes under the finance documents, and if so, why? Please outline the relative merits of arbitration and litigation, including the ease of enforcement of foreign judgments and foreign awards from different jurisdictions. Is it possible to rely on a hybrid enforcement provision that allows the lenders to opt for either arbitration or litigation as they see fit?

A decision or judgment by any court other than a Vietnamese court is unlikely to be recognized and enforced in Vietnam, as Vietnam is not a member of the Convention of 1 February 1971 on the Recognition and Enforcement of Foreign Judgments in Civil and Commercial Matters. However, a Vietnamese court may consider recognizing and enforcing a civil judgment or decision made by a foreign court where the foreign country is a party to a judicial assistance agreement with Vietnam or it is a participant or signatory to a relevant international treaty to which Vietnam is also a participant or signatory, or such judgment is permitted to be recognized and enforced under Vietnamese law or on a reciprocal basis.

Vietnam is a signatory to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards; therefore, an arbitral award given by an arbitration center of another New York Convention member country will be recognized and enforced in Vietnam by a competent court of Vietnam, unless the court deems that the said award is contrary to "fundamental principles of Vietnamese laws." However, as the "fundamental principles of Vietnamese laws" have not been explicitly and completely provided in any legal documents, except for the fundamental principles of civil law and commercial law, the recognition and enforcement of a foreign arbitral award will be subject to the court's discretionary interpretation of the "fundamental principles of Vietnamese laws".

Vietnamese law also anticipates parties constructing a hybrid arbitration-litigation clause in a contract, as further discussed in the answer to question 10 of this section.

10. Are asymmetrical jurisdiction clauses enforceable? (By this we mean clauses that allow the lenders, but not the borrowers, to make certain choices in relation to choice of jurisdiction and how to litigate. These types of clauses allow the lenders, but not the borrowers, to commence proceedings in any court they choose, but restrict the borrowers to commencing proceedings in one jurisdiction only. This may also allow the lenders, but not the borrowers, to choose whether to litigate the finance documents before a court or to submit to arbitration in relation to them, but restrict the borrowers to either litigation or arbitration, as specified in the agreement).

To our knowledge, this question has not been tested in Vietnam. However, Vietnamese law recognizes agreements whereby the parties agree to use either arbitration or the court to resolve the dispute (except for certain cases where the dispute will fall under the jurisdiction of the court regardless of the agreement of the parties) in accordance with the following:

- Where the claimant submits the dispute to arbitration before requesting the court to resolve the dispute or submits the dispute to arbitration when the court has not yet accepted jurisdiction over the dispute, the court will reject jurisdiction to resolve the dispute. If the court has already accepted jurisdiction over the dispute, the court will suspend the resolution of the dispute as not being subject to the court's jurisdiction and it will return the statement of claim and accompanying documents.
- Where the claimant requests that the court resolve a dispute, after receiving the statement of claim, the court must immediately determine whether one of the parties has submitted the dispute to arbitration. If the respondent or the claimant has not submitted the dispute to arbitration, the court will consider accepting jurisdiction over the dispute for resolution. Where the court discovers that the dispute was submitted to arbitration before it accepted jurisdiction over the dispute, the court will issue a decision suspending the resolution of the dispute as not being subject to the court's jurisdiction and it will return the statement of claim and accompanying documents.

Working digitally

1. Is it possible for documents to be executed electronically (whether by the manual insertion of a digital signature or the use of an e-signing platform) under the laws of this jurisdiction? If so, is this limited to only particular types of finance documents?

Loan agreements can be made in the form of electronic data messages (i.e., in the form of electronic data exchange, electronic documents, electronic mail, telegram, telegraph, fax or other similar forms). Vietnamese law also provides certain legal frameworks for the parties to execute transactions electronically, for example, via the internet and, signing documents with electronic signatures (e-signatures) in lieu of prevalent wet-ink signatures.

An e-signature is: (a) created in the form of words, letters, numbers, symbols, sounds or other forms by electronic means; (b) logically associated or incorporated with electronic contracts (e.g., in the form of common PDF or Word files); and (c) capable of certifying the signatory and their approval of the content of the signed electronic contract. There are three common forms of e-signature:

- Scanned signature: a signatory of each party signs a hard copy of a document in wet ink; then, the document with the signatures is converted into electronic form by scanning and is sent to the counterparty by email.
- Image signature: a signatory inserts an image of their signature into the signature box of an electronic file of a document; then, the file including the image signature is sent to the counterparty by email.
- Digital signature: parties use a specialized platform and device provided by a digital signature authentication service provider to create digital signatures; then, such digital signature is attached to an electronic file of a document to be signed.

Not all e-signatures have equal legal validity to pen-and-paper signatures. Equal validity for an e-signature is only legally recognized if the e-signature in question satisfies the following requirements:

- The method of creating the e-signature allows for the identification of the signatory and indicates their consent to the contents of the contract/agreement.
- Such method is sufficiently reliable and appropriate for the purpose for which the contract/agreement was originated and sent.

However, there has been no further official implementation guidance or clarifications of these requirements. A digital signature is officially recognized as a type of e-signature. Documents signed by digital signature do not require stamps and do not give rise to the validity issue. In practice, due to the higher level of security it offers in comparison to other forms of e-signatures, a digital signature that has been certified by a licensed certificate authority in Vietnam is legally considered a secured e-signature and it is more likely to be recognized by Vietnamese competent authorities and courts. However, although there have been a tremendous number of documents signed with signatures created through foreign digital signature services such as DocuSign or Adobe Sign, it is not certain whether such documents and signatures will be recognized as legally valid by the courts in the event of disputes.

In practice, for finance documents pertinent to loan or security interests that need to be registered with the competent authorities (e.g., long-term offshore facility/loan agreements), the authorities usually require such finance documents to be signed with wet-ink signatures and delivered in hard copies.

2. Where the witnessing of a signing is contemplated, is it possible for the witness to verify the signature over a live video call?

Depending on the types of documents, the physical presence of the signatory that executed the document will be required (e.g., real estate-related agreements such as mortgage agreements over assets attached to land). Except for limited cases where the entity is able to register its specimen signature at the notarial practice organization, the contract can be signed beforehand. However, a notary will compare the signature in the contract with the specimen signature before notarization.

According to the law, notarization requesters, witnesses and interpreters must sign the contracts in the presence of the notary. The law does not specifically say whether such presence can be virtual. Thus, it would likely be permissible for the notary to witness the execution by videoconference. However, parties should understand that the burden of proof falls on them when the execution is witnessed virtually.

3. Is it possible to register/perfect security electronically without wet ink signatures?

The competent authorities often require the applicant for security registration/enforcement to submit and present documents stamped and signed with wet-ink signatures.

4. Are there any other legal restrictions that may prevent the parties from executing a finance transaction electronically?

No.

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