NEWSLETTER

ASIA

FEBRUARY 2015

I. China : Shanghai Free Trade Zone (FTZ) and its expansion

On December 28th, 2014, the NPC Stand Committee issued a decision[1] regarding the creation of three new FTZs and the expansion of the Shanghai FTZ, which will soon take effect on March 1st, 2015.

Three new FTZs are to be inaugurated, located respectively in Guangdong Province, Fujian Province and Tianjin Municipality. Meanwhile, the Shanghai FTZ is to expand to include Lujiazui Financial Zone, Zhangjiang Hi-tech Park and Jinqiao Development

[1] *Decision of the NPC Standing Committee on Authorizing the State Council to Temporally Adjust the Administrative Approvals Provided by the Laws in the China (Guangdong) Free Trade Pilot Zone, the China (Tianjin) Free Trade Pilot Zone, the China (Fujian) Free Trade Pilot Zone and the Expansion Area of the China (Shanghai) Free Trade Pilot Zone*

Zone all located in Pudong New District, the area of which has thus been increased by four times, i.e. 120.7 sq. km, compared to the original 28.78 sq. km, having a size similar to those of the three new FTZs.

Launched in September 2013, the Shanghai FTZ has initiated a wide variety of innovative policies with the aim to act as the testing ground for China's economic reforms and to spread afterwards the successful policies across the country. The tasks of the Shanghai FTZ are mainly: facilitating free trade, liberalization of foreign investment regulation, and financial reform. Although the more than one-year operation has fallen short of investors' expectations and even achieved nothing substantial in terms of financial reform, we have seen improvements in the liberalization of foreign investment and expect it to expand to the Expansion Area very soon.

Among others, a "Negative List" approach has been adopted to regulate foreign investment. As promised by the government to be shortened from time to time, the list sets out the restricted and prohibited industry sectors for foreign investment, whereas outside the negative list foreign investors will be regulated as domestic investors.

For example, in order to set up a foreign-invested advertising company, the foreign investor is no longer required to have certain years' experience in advertising, which is still required outside the zone; foreign-invested medical institutions can be set up in the form of wholly foreign owned enterprises and are no longer subject to the investment amount threshold of RMB 20 million and a short duration of 20 years.

Along with the Negative List is the simplified and accelerated administrative procedure. In order to set up a company in the FTZ, foreign investors no longer need to wait long time for the administrative approval and go through heavy formalities with different government authorities, instead we only need to file a one-stop application with all the government authorities. The process lasting for three to six months outside the FTZ can be completed within one month in the FTZ if the business scope does not involve any business contained in the negative list.

Now the Shanghai FTZ has expanded to cover Lujiazui, the city commercial and financial center headquartered many MNCs and major banks, as well as the nearby Jinqiao Development Zone and Zhangjiang Hi-tech Park ("**Expansion Area**"). Different from the previous zones, the Expansion Area are not bonded zones that are far away from the city center and they assume different economic functions, that is, Lujiazui focuses on financial innovation and high-end service sectors, Zhangjiang Hi-tech Park focuses on technology and innovation, and Jinqiao development zone on manufacturing services and high-end manufacture supply chain. The Expansion Area, according to the FTZ officials, has diversified the original FTZ in terms of functions which was mainly based on trading and is to test policy innovations in a wider scale.

Although policies in the Expansion Area are yet to be released and whether all regulations in the FTZ including the Negative List will be applicable in the Expansion Area is still uncertain, it is certain that foreign investment in the Expansion Area will be subject to a record-filing instead of an administrative approval pursuant to the decision on December 28, just like the process in the Shanghai FTZ. Although reform in the Shanghai FTZ has been prudent, with the recent expansion to the city center and the arising competition from the new FTZs, we expect reforms in the Shanghai FTZ to be significant and favorable in foreign investment.

II. Japan : Dealing with Parallel Imports (Part 1)

Landry Guesdon, Avocat - Attorney at law (GJB), Iwata Godo Law Office
lguesdon@iwatagodo.com

The main channel for importing high quality goods in Japan is through retailers and other official intermediaries: products are imported by Japanese wholesalers, distributors or agents (who are often structured as a local subsidiary of the intellectual property rights (IP) owner). An alternative route is that of parallel imports, which involves the import and resale of non-counterfeit goods without the IP owner's consent. These goods are commonly exchanged in the “grey market” which thrives on price differentiation between countries.

In the 1960s, parallel imports of genuine goods were considered a violation of the local brand distributor's IP rights and were condemned by case law (*Parker pens, Nestlé coffee, Bayer aspirin, etc.)*. However, in another Parker case, the Osaka District Court ruled in 1970 that, under certain circumstances, parallel imports of genuine products did not amount to a specific violation of the rights of Parker's official distributors. In 1972, the Ministry of Finance issued a directive stating that parallel imports of genuine goods did not, in principle, amount to a trademark infringement. The key legislation under Japanese competition law is the 1947 Antimonopoly Act (the Act).

The Japan Fair Trade Commission (JFTC) now considers parallel imports to be beneficial to consumers. This view is clearly stated in its "*Guidelines concerning distribution systems and business practices under the Antimonopoly Act*" dated 11 July 1991. The obstruction of parallel imports, if it is conducted to achieve price maintenance of the products covered by an exclusive distribution contract (and not, say, to prevent consumer misunderstanding due to differing product specifications or a false indication of origin or to protect consumer health or safety caused by the deterioration of quality) is a problem under Article 19 of the Act.

The implementation of measures seeking to restrict parallel imports solely to maintain the price of a product marketed under an exclusive distribution contract is in breach of Article 19 of the Act. Unfair trade practices are detailed in Article 2 of the Act and in a list published by the JFTC. The list includes interference with a competitor's transactions and obstruction of parallel imports as an instance of unfair trade practice.

Whilst a number of legal rulings have been made in this area, particularly in the late 1990s, they have become less common in recent years. The cases involved very diverse sectors and products, for instance, Parker pens, Steinways pianos, Seagull water purification devices, Herend china, Nike footwear, Häagen Dazs ice cream and Dunlop tyres.

The decisions typically involved a foreign IP owner that manufactured goods for sale by a Japanese distributor and a parallel importer acting independently. The parallel importer purchased goods from foreign wholesalers or other official distributors, who then became subjected to commercial pressure, duress or retaliation from the IP owner. In some instances, the IP owner withheld supply to those distributors selling to parallel importers in an attempt to end the parallel chain of supply.

In the majority of cases, the JFTC would start investigating and if the practice does not stop, it will issue a cease and desist order to the IP owner demanding that the IP owner cease its wrongful behaviour (in breach of Article 19). As a result, impeding parallel imports is generally a prohibited practice in Japan. Any attempt to hinder a parallel importer's advertising or promotional activities would be considered illegal (importers are able to use the brand and its logo on their shop windows and websites, provided this does not harm the brand in Japan or amount to an unfair trade practice).

Any attempt to obstruct the purchase of goods in foreign markets destined to be sold as parallel imports in Japan is prohibited on a similar basis. If a parallel importer considers that the aim of an IP owner's actions is to impede its imports, it can file a report to the JFTC who may initiate an enquiry. Consequently, taking measures against parallel importers remains a sensitive matter.

There are a few secondary measures which could help restrict parallel imports including the commencement of legal proceedings on the grounds of a copyright infringement. However, such legal proceedings often lead to pyrrhic victories as the parallel importer is not seriously affected. For example, the unauthorised use of visuals on a parallel importer's website (assuming the copyrights are owned by the manufacturer and not an advertising company) or of a manufacturer's text would be unlawful if prior consent was not granted by the IP owner, and in either case the IP owner could demand their withdrawal. Proceedings can also be commenced on the grounds of trademark infringement if a visual is combined with the logo and the brand by a creative parallel importer.

Unfair competition, even that which results in increased competition, is another angle of attack. The burden of proof lies on the plaintiff who must prove that the parallel importer's activities create confusion in the mind of the public. An example would be a parallel importer suggesting or implying that it and the official importer belong to the same group or are operating under a close business relationship. In general, a market study would need to be conducted in order to prove unfair competition

(to be continued in our next newsletter)

III. India : GST : India's biggest tax reform

Seen as the biggest tax reform since 1947, the most-awaited GST will be discussed in the upcoming session of Parliament.

On December 19th, 2014, the Finance Minister, Arun Jaitley, tabled the most-awaited Constitution (122 Amendment) Bill, 2014 (**GST Bill**) introducing the Goods and Services Tax (**GST**) in the lower house of the Parliament.

The Finance Minister has described the GST Bill as the single most important tax reform after 1947. The reform proposes to replace the current multi-tiered Indian tax regime seen as one of the most complex tax regimes in Asia-Pacific[2] by a unified (but still dual) GST to be levied concurrently by the Centre and the States. The proposed tax system will subsume a variety of central and state levies, thereby simplifying the complicated tax structure, reducing compliance costs and removing trade barriers on the form of cascading effects of taxation.

Currently, the Centre imposes excise duty on manufacture of goods, and service tax on provision of services (other than customs duty on imports). The States separately impose Value Added Tax (VAT) on the supply of goods and a portfolio of specific taxes such as entertainment tax, excise duties on alcohol for human consumption and medicinal and toilet preparations (MTP), entry tax and octroi. For mixed supply of services and goods (e.g. restaurants), both service tax and VAT apply on the respective components. This results in a multiplicity of taxes with limited cross credits and differential tax regimes between States.

GST, which would apply on the supply of any goods or services[3] or both, would replace these multiple taxes: CENVAT, service tax, central excise duty, octroi and entry tax, additional excise duties, excise duties levied under the MTP (Excise Duties)

[2] 2014 Asia Pacific Tax Complexity Survey, Deloitte

[3] However some goods have been excluded from the purview of the GST such as petrol and alcohol for human consumption

Act, 1955, service tax, additional customs duty (countervailing duty or CVD), special additional duty of customs (SAD), central surcharges and cesses, State VAT, State sales tax, entertainment tax not levied by local bodies, luxury tax, taxes on lottery, betting, and gambling, tax on advertisements, State cesses and surcharges related to supply of goods and services. However, some levies such as stamp duty has been excluded from the proposed GST model, not fully eliminating the cascading impact of taxes for businesses.

As per the GST Bill, the Centre and the States would be conferred concurrent taxing powers to introduce the GST in the country and a GST Council[4], which would become the apex indirect tax policy making body of the country, would be set up to administer the GST. The GST Council would, among others, determine the rate and exemptions of tax, threshold limits, frame model laws, etc.

Determining the rate of GST is one of the many contentious issues. Initially structured as a three-tiered rate (12% on essential goods, 16% on services and 20% on goods), the last single proposed rate reached 26.68% (whereas the GST average rate in Asia Pacific is 12.5%[5]). Such a high rate would not only impact cost of services such as telecom service, which is seen as an essential tool of growth[6] but would also mean that the reform might fail at boosting overall growth as India won't gain any competitive advantage over most of its leading trading partners.

The GST Bill also seeks to resolve the contentious issue of CST compensation to States by seeking to 'Constitutionally Guarantee' compensation.

In spite of the efforts of the government to gain consensus between the States by diluting their initial apprehensions, there are still certain roadblocks which need to be cleared for expeditious implementation of GST and consensus is still to be gained on key aspects such as rates, delimitation of taxing powers, issue of revenue loss, exemptions to achieve a smooth transition to GST.

If passed by the Parliament, GST is expected to come into force in April 2016.

[4] With representatives from both the Centre and the States

[5] 2013 Asia Pacific Indirect Tax Country Guide, KPMG

[6] '*The telecom services have been recognized the world-over as an important tool for socio-economic development for a nation. It is one of the prime support services needed for rapid growth and modernization of various sectors of the economy*' http://www.dot.gov.in/about-us/telecom-glance

IV. Singapour : Changes to the directors' indemnity provision in the Companies Act and the implications for companies in Singapore

Bill Jamieson from CNP Law
Contributed by : Alfred Pang

Introduction

One amendment to the Companies Act (Cap. 50) (the "**Act**") due to come into force in the second quarter of this year that has not received much attention is the clarification to the indemnity provision for directors (i.e. Section 172 of the Act).

This particular change in the legislation was made in response to the increased recognition of directors' exposure to personal claims from third parties. To quote from the report of the Steering Committee for review of the Companies Act, "[a]s Singapore companies become more globalised, the risk of them (directors) being exposed to liabilities to third parties, for example, arising from the frequent class actions by groups of shareholders in the US, is real and should be addressed. The Steering Committee is of the view that the Companies Act should be amended to expressly allow a company to provide indemnity to its directors for claims brought by third parties."

It is advisable that companies review their articles of association to check they reflect these particular amendments. In addition, company directors should check if the indemnity in their service agreement needs updating to safeguard their interests to the extent permitted under the revised statutory provisions.

Directors' indemnity under the revised Act

The revised Act has been amended to clarify that a company is allowed to indemnify its directors against liability incurred by the directors to third parties, subject to certain qualifications. The indemnity shall not apply where it is against (a) any liability of the officer to pay a fine in criminal proceedings or a penalty to a regulatory authority for non-compliance with any regulatory requirement; or (b) any liability incurred by the officer in defending criminal proceedings where he is convicted or in defending civil proceedings brought by the company or a related company where judgment is given against him or where an application for relief is rejected by the court.

Suggested approach

The approach which we propose is to set out in the articles and service agreements that the company shall indemnify the directors to the maximum extent permitted by law subject to any exclusion as may be determined by the directors from time to time. It bears mentioning that the exclusions/qualifications in the directors' indemnity provision under the Act sets out the minimum standard and the company has the discretion to add further exclusions/limitations to that. Adopting this approach will provide the directors with a certain level of assurance that they are protected to the extent permitted under the law and at the same time provide the company with the flexibility to protect its interests by scaling back the indemnity provided to the directors as appropriate (discussed below).

As a matter of practice, we would recommend that the indemnity provision be included in both the articles of association of the company as well as a director's service agreement. The articles should contain the more general exclusions stipulated in the Act while the service agreement could incorporate more specific qualifications as these could be subject to negotiation between the company and an individual director.

We would also recommend that the articles provide that the company may purchase and maintain D&O insurance which would provide coverage for the directors' liability in connection with any negligence, default, breach of duty or breach of trust in relation to the company.

Types of exclusions/limits which the board might consider including in an indemnity

- Cap on liability, i.e. the company will only indemnify the directors up to a certain amount.
- Reclaim incentive components of remuneration from executive directors and key management personnel in exceptional circumstances of misstatement of financial results, or of misconduct resulting in financial loss to the company.
- Exclusion for fraud or dishonesty.
- Exclusion in the event of a director being a "bad leaver", i.e. when the director departs the company in circumstances justifying summary dismissal of the director.
- Exclusion for any directors who have left the board prior to the implementation date.
- Agreement by the indemnified director to observe a prescribed course of conduct regarding any negotiations, arbitration or proceedings in connection with any matter to which the indemnity relates, including giving the company on request sole conduct of any such proceedings.

The above are suggestions of ways in which the board may seek to limit the coverage of the indemnity provided to directors and our proposed language to be included in the articles and service agreements will give the company the discretion to review the exclusions/ limits periodically.

V. Vietnam : New guidance decree on the Labor Code

Decree 05/2015/ND-CP (Decree 05) dated January 12th, 2015 has been issued by the Government of Vietnam and provides guidance on a number of articles of the Labor Code. Indeed, it namely sets out the contents required in a labor contract, requirements for amending these and regulations for terminating a contract. Some key points are listed below:

- Decree 05 gives the circumstances in which a labor contract can be terminated unilaterally by an employer "*due to economic reasons*". Economic reasons would include "*economic crisis or recession*" and "*implementation of the State's policies when restructuring the economy or implementation of commitments to international treaties";*

- Decrees 05 gives confirmation that employers must only pay retrenchment allowance (and not severance allowance) if a labor contract is terminated due to restructuring, technological change or economic reasons;

- Decree 05 also sets out the required contents of internal labor rules, their registration and procedures for handling labor issues. For instance, disciplinary hearings can only be organized when all the required participants are present.

Decree 05 is applicable from March 1st, 2015.