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New York International Chapter News

A publication of the International Law and Practice Section
of the New York State Bar Association

A Word from Our Chair

The International Law and Practice Section has experienced a remarkable burst of activity over the past several months, I am pleased to report. Starting with the very successful Fall Meeting in Amsterdam through the substantive legal program presented at the Barreau de Quebec in Quebec City and the Executive Committee's Retreat in Montreal, both held in early June, through the planning for the upcoming Seasonal Meeting in Santiago de Chile to be held in November, the Section has been and continues to be involved in a wide range of activities. I would like to both thank the members of the Section responsible and to give some indication of the breadth of our recent activities.

Thanks to Marco Blanco, the Section's current Secretary, and Steve Schuit in Amsterdam, as well as my predecessor as Section Chair, Jim Duffy, the Fall Meeting was a great success. The substantive legal programs were, I believe, probably the best ever and our visit to the International Court of Justice at The Hague and our meeting with Judge Thomas Buergenthal was a high point. Organized by Jim Duffy, the first meeting of the Chapter Chairs of the Section held in Amsterdam was very productive for both the Chapter Chairs in attendance, mainly from Europe, and the officers of the Section. A Chapter Chairs Meeting also will be held in Santiago and it is hoped that all of the Chapter Chairs in Latin America, and at least a few from Europe and Asia, will be in attendance.

The Annual Meeting similarly was a great success. Organized by the Section's current Chair-Elect, Bob Leo, the morning program was comprised of three panels, including one on "The Impact of 9/11/01 on Latin America," chaired by Oliver Armas (Chair of the Meeting in Santiago in November), and including Francis Lackington (Chapter Chair in Santiago), Renata Neeser and Guillermo Malm Green (from Buenos Aires); a second chaired by Don Prutzman (Co-Chair of the Intellectual Property Committee) featuring Federal Trade Commissioner Mozelle W. Thompson and Nuala O'Connor Kelly, Director of Privacy for the Department of Home-

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land Security, which was outstanding; and a third very practical panel on "The Duty of New York Lawyers to Check Conflicts of Interest in Cross-Border Cases," chaired by current Executive Vice Chair Jack Zulack, that included Janis M. Meyer, Helena Sprenger and Meryl P. Sherwood speaking on the conflicts procedures in three different size law firms.

The luncheon was the highlight of the day, and possibly of the entire NYSBA Annual Meeting at the New York Marriott Marquis, in that it featured Jim Duffy, the outgoing Section Chair, presenting the Albert S. Pergam International Law Writing Competition Award to Babback Sabahi, a Boston University LLM student, whose winning paper on the "ICJ's Authority to Invalidate the Security Council's Decisions under Chapter 7: Legal Romanticism or the Rule of Law" was a wonderful, if coincidental, segue into Jim Duffy's presenting the Section's Annual Award for Distinction in International Law and Affairs to Judge Thomas Buergenthal of the International Court of Justice in The Hague. The Judge was prevented from traveling to New York to accept the award in person as had been anticipated, due to his hearing the argument that day on the Mexico/United States case relating to the rights of Mexican defendants to consular consultation in the United States. The Section rose to the occasion by utilizing video conferencing for Jim and NYSBA President Tom Levin, who also was present at the Section luncheon, to present the award to Judge Buergenthal in his home. The Judge rewarded those present in New York with a lengthy period of remarks and answers to numerous questions from the audience. He declined, however, to comment on the thesis of Babback Sabahi's paper that the International Court of Justice had the authority to overrule a decision of the Security Council of the United Nations.

The Executive Committee also has been busy, holding meetings on January 27th at the Penn Club, on March 30th at Alston & Bird and June 4th and 5th in Montreal (described on p. 40 in this issue). In addition to creating several new chapters in Panama, Pakistan, Moscow and Shanghai (bringing the total to 36) and creating a new Committee on South Asian Law (Babar Sattar, Chair), the Executive Committee also named a number of new Chapter Chairs (Mahnaz Malik in Pakistan, Juan Francisco Pardini in Panama, Mads S. Loewe and William R. Spiegelberger in Moscow and Jens Eggenberger in Berlin), as well as several new Committee Co-Chairs, Stefano Crosio for the Western European (EU) Law Committee, Junji Masuda for the Asian Pacific Law Committee, Pablo Bentes and Renata Neeser for the Inter-America Law/Free Trade in the Americas Committee and John Hanna and Andrew Otis for the International Environmental Law Committee. In addition, the following were named to the Executive Committee: Len Quigley as Vice-Chair for Canadian Affairs, Lorraine Power Tharp as Diversity Coordinator and Steve Krane as Liaison with International Bar Associations. The Executive Committee also addressed a number of issues of concern to the members of the Section. Among them have been the decision of the International Court of Justice on the U.S.-Mexico case, the Immigration and Nationality Committee's opposition to pending legislation regarding immigration consultants and the repeal of the Extra Territorial Income Tax.

Another significant issue still under active consideration is the negotiation with the CCBE (Council of European Bar Associations) regarding the requirements for admission to practice law and cross-border legal practice generally in New York State and in Europe, as well as discussions with the Law Society of Upper Canada on similar subjects held in the spring by Jim Duffy, Len Quigley and Founding Chair Lauren Rachlin. A meeting with the Executive Director of the CCBE (Jonathan Goldsmith) and with the Presidents and International Section Chairs of 12 other state bar associations was held Friday, August 6th, in Atlanta, in conjunction with the Annual Meeting of the American Bar Association. Past NYSBA President and the current Liaison with the Executive Committee of the NYSBA, Tom Levin, as well as past Section Chairs Mike Maney and Ken Schultz, and Terry Cone (the leading authority on multijurisdictional practice issues) joined me in Atlanta for the Meeting with the CCBE, although two other members of the delegation, Jim Duffy and Steve Krane (another NYSBA Past President), are unable to participate due to professional or personal scheduling conflicts.

As Chair, I also have named Peter Woodin, Chair of the International Dispute Resolution Committee, and Thomas Pieper, Chair of the Section's International Litigation Committee, to a task force of the NYSBA Committee on Arbitration to determine whether there is need and support for an Arbitration Section of the NYSBA. A meeting of the task force was held on March 25th and another meeting is scheduled for the late summer. Similarly, John Blyth and Birgit Kurtz have been named as observers from the Section to the New York Commission on Uniform State Laws Committee on the Uniform Recognition of Foreign Judgments Act.

There also has been much activity on the part of many of the committees of the Section. The Tax Aspects of International Trade & Investment Committee (of which Marco Blanco and Javier Asenio are Co-Chairs) has been conducting a series of midday programs (at Curtis, Mallet & Prevost, Colt & Mosle, with lunch provided by Cuatrecasas) of interest to international tax lawyers; three have been held thus far and two more are scheduled for the fall. The Committees on International Human Rights and on the United Nations & Other International Organizations jointly presented a

program on June 30th at the United Nations with NYU Professor Howard S. Schiffman speaking on "The Vienna Convention on Consular Relations and Foreign Nationals on Death Row." The Immigration and Nationality Committee has presented a series of public service programs on immigration law and procedures at the Ukrainian Consulate (with the cooperation of the Committee on Central & Eastern European and Central Asian Law), the Brazilian Consulate and several other consulates. The Women's Interest Networking Group joined with the Womens Interest Group of the ABA in organizing a program for women lawyers as part of the ABA Section of International Law and Practice Meeting held at the Plaza in April. Several Members of the Section were active on the Steering Committee of that meeting, including Javier Villasante—now in Madrid—and Hernan Slemenson as Co-Chairs, and I served on the Steering Committee as well, representing the NYSBA IL&PS. Lastly, under the dynamic new leadership of Katie Friedman, the Western New York Chapter has held two very successful luncheon programs at the Erie County Bar Association in Buffalo, the first in February, and the second more recently in July featuring Second Circuit Court of Appeals Judge Richard Wesley and the U.S. Attorney for the Western District of New York speaking on the topic of the USA Patriot Act.

Moreover, the Section has been working with the International Law Association (American Branch) in the organization of International Law Weekend in October to increase the number of panels on private international law topics at that conference, as well as with The European Union Studies Center of the Graduate Center, CUNY, where Eberhard Rohm spoke on June 22nd, along with several European ambassadors on the "European Union—2500—Opportunities and Pitfalls."

In addition, I wish to express my personal thanks to the Editors of the Section's publications, David Detjen and Tom Backen of the *International Law Practicum* and Rick Scott and Oliver Armas—with the great assistance of Soraya Bosi—of the *New York International Chapter News*, each of which now has been published twice since the first of this year. Based upon the number of communications I receive as Chair which mention an article or news item read in either the *Practicum* or the *Chapter News*, I have a greater appreciation than ever of the importance of the Section's publications in providing information to the IL&PS Membership around the world. The Section remains grateful to Lester Nelson, as Editor-in-Chief; Professor Charles Biblowit, as Faculty Advisor; and the students of St. John's University School of Law for the Section's other bi-annual publication, the *New York International Law Review*.

Looking ahead, the Executive Committee will meet again on September 13th at Executive Vice Chair Jack Zulack's firm's offices, and Ollie Armas, with the assistance of the Santiago Chapter Chair, Francis Lackington, and a Local Organizing Committee led by Michael Grasty, are planning an extraordinary combination of substantive legal programs and social events that will justify its name, The Latin American Summit, at the Santiago Meeting in November.

Paul M. Frank, Chair
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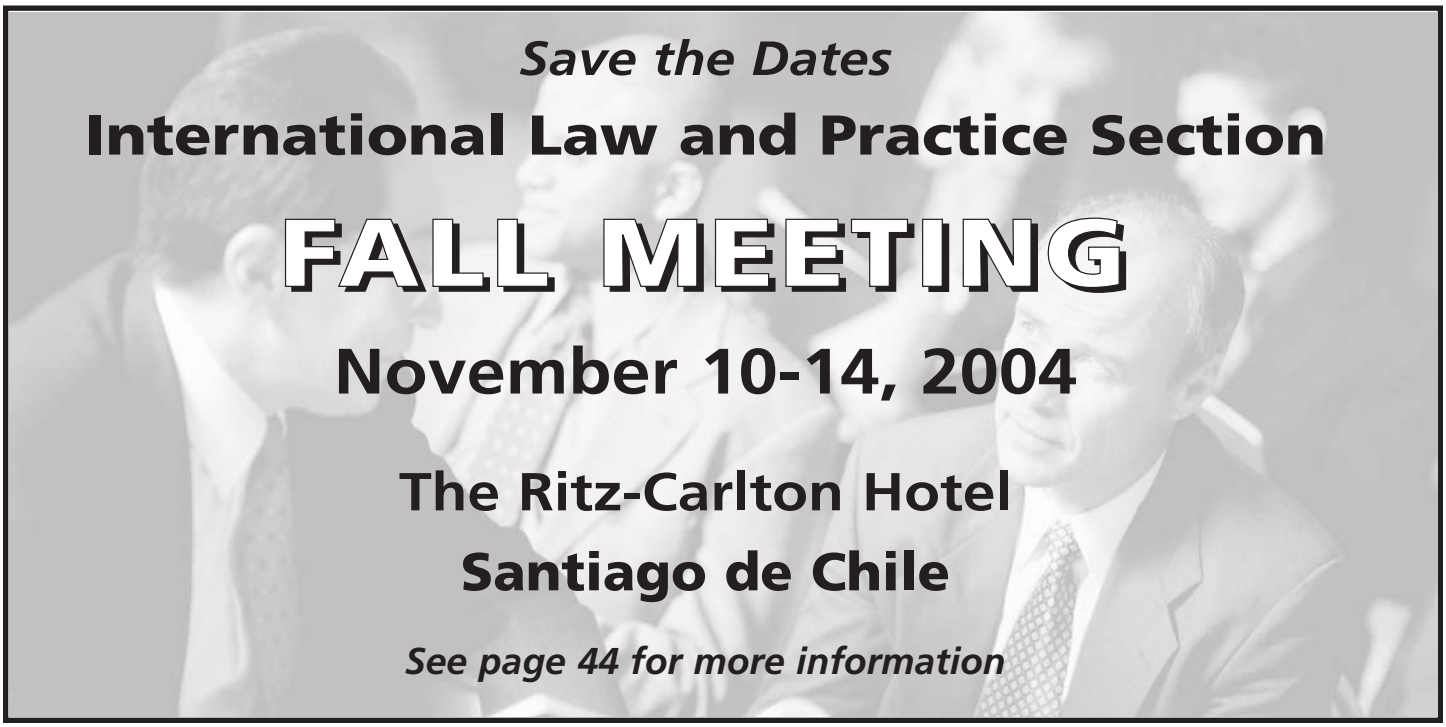

Our Co-Editor

One year has passed since my appointment as the Co-Editor for the NYSBA *New York International Chapter News*; and I am grateful for the support of all our readers and contributors. Without you and your contributions, our Section's newsletter would not be possible.

My firm, Fraser Milner Casgrain LLP (FMC), strongly advocates and encourages professional and practical growth within our organizational structure, so my partners and I value the opportunities to be actively involved with the New York State Bar Association International Law and Practice Section. In fact, I am pleased to report that our New York office is engaged in assisting with the organization and development of various aspects of the Section's 2004 Fall Meeting in Santiago, Chile.

The meeting this year is designed to go beyond national boundaries and aims at being a true "Latin American Summit." The guest and panel speakers will be legal and business leaders who focus on an international scope, including the U.S., Europe and of course, Latin America. In order to maintain a sense of balance, there will be a plethora of social events taking place. Your involvement and support of this meeting and its events is welcome and encouraged. Sponsorship is an excellent way to raise the visibility of your firm and increase your exposure among top international law firms and in-house counsel from global Fortune 500 companies. White & Case LLP has already committed to be the Exclusive Premiere law firm sponsoring this meeting, and all sponsorship opportunities are on a first-come, first-serve basis, so if you are interested in expanding your involvements with the 2004 Fall Meeting in Santiago, Chile, please contact Soraya E. Bosi, at (212) 218-2995 or via e-mail at Soraya.bosi@fmc-law.com.

Additionally, keeping in line with the firm's commitments to support the expansion of worldwide professional and practical growth in the legal industry, it pleases me to inform you that Gordon Esau, of Fraser Milner Casgrain LLP, has been appointed to Chair the New York State Bar Association International Law and Practice Section's Committee on International Entertainment. Gordon is a corporate partner in the Vancouver office and is recognized throughout the world as one of the leading lawyers in Canada in the Entertainment Industry. If you are interested in becoming involved with this committee or simply finding out more information on its upcoming plans, please contact Soraya E. Bosi for further information at soraya.bosi@fmc-law.com. Your involvement is always welcomed.

Also, during the course of the Section's Executive Retreat this June, FMC arranged a television interview for our Section's Chair and Partner of Alston & Bird, Paul M. Frank, to appear on *SqueezePlay*, ROBTV's (Report on Business Television) prime-time business affairs program. Among other things, Paul addressed issues of the NYSBA-ILPS and its role with foreign attorneys practicing in the U.S. and trends in the globalization of New York law firms. If you would like to view that interview, please contact Melissa Howard, at melissa.howard@fmc-law.com.

Finally, a thank-you goes out to Paul M. Frank and the Executive Committee for reinstating the Section's internship program that was supervised by Soraya E. Bosi, from the New York office of FMC. The program provided the ILPS with a blend of U.S. and Latin American assistance, which was most helpful in the preliminary organization of the upcoming meeting in Santiago. Beyond assisting the Committee Chairs, the interns were also involved in writing memos, research projects and formulating responses to issues that affect the global community. The program also afforded the interns a great amount of practical experience, rotating between law firms and having the opportunity to work alongside some of the most prominent attorneys from prestigious international law firms throughout the United States. This is a valuable program and both the Section and law students benefit greatly from sharing this experience.

Overall, this newsletter continues to expand and make clear to its readership the value of providing New York and the international legal community with a vehicle that addresses a multi-jurisdictional response to the ever-changing global business and the international legal environments. Through this publication, we are able to respond by informing, being informed and interchanging ideas on the constant amendments and modifications that continually transpire within the international marketplace.

We hope that you will be able to join us in Santiago and look forward to receiving your next valuable contribution for the upcoming issue of the newsletter.

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IL & P Country News

Argentina

New Legislation Related to Isolated Acts of Foreign Companies in Argentina

As part of the new regulations enacted to enhance the control over the activities of the foreign companies developed within the territory of Argentina, the Public Registry of Commerce of the city of Buenos Aires has rendered a new Resolution No. 8/2003 dated October 21 creating, within the jurisdiction of the city of Buenos Aires, a registry for isolated acts conducted by foreign corporations (hereinafter, the "Registry").

Said Registry will incorporate the registrations of those acts involving real estate property located in the jurisdiction of the city of Buenos Aires, in relation to the constitution, acquisition, transfer or cancellation of *in rem* rights over said real estate property, with the participation of companies incorporated abroad, that the Real Estate Registry of the city of Buenos Aires reports to the Public Registry of Commerce as performed under the qualification of isolated or non-regular acts.

The report to be provided to the Registry shall contain information related to the instrument filed before the Real Estate Registry and the data of the notary public participating in the act, the data of the parties (in the case of the foreign company, it shall contain the reference to the original domicile, the representative involved in the act, his personal domicile and the one declared for purposes of the act), the nature of the act, the accurate identification of the asset or right subject to the act, the economic amount involved in the transaction, and the information related to any other prior act that could be also considered as isolated.

The Public Registry of Commerce will elaborate, together with the Real Estate Registry, the conditions for the provision of the information to be incorporated in the Registry created by means of the new Resolution.

It is important to mention that the Public Registry of Commerce will evaluate the information obtained from the Real Estate Registry in order to determine if the activity performed by the foreign company becomes, due to its reiteration, the economic meaning, the destiny of the assets or other circumstances related to the celebration of the act, its habitual or even its main activity.

In order to conduct such analysis, the Public Registry of Commerce may request further information related to the performance of those acts to: (i) those representing the company incorporated abroad in the act considered as isolated; (ii) the notary public participating in the act; (iii) those considered as sellers of the assets, or debtors by means of a mortgage guaranty; (iv) the assignors of mortgage rights; (v) the Argentine IRS (*"AFIP"*) limited to the information already provided to such agency by the foreign company; and (vi) the management of the building where the real estate property is located. The Public Registry of Commerce may also conduct, solely or together with other governmental institutions, inspections at the real estate property, with the purpose of verifying the destiny and economic conditions of the premises, as well as the actual location of the company management.

With respect to the representatives of the foreign company, the Resolution establishes that in case the (i) domicile of the foreign company is located in a country with limited or even no tax obligations, (ii) value or destiny of the assets involved in the act, or (iii) reiteration of those acts, it may result presumably in the existence of the circumstances provided in Sections 118 or 124 of the Corporate Law (formalities to be complied with by those foreign companies with regular activities within Argentina), then such representatives might be obliged to provide the Registry with the information established by Resolution 7/2003 of the Public Registry of Commerce. Said information refers to the existence of prohibitions or legal restrictions to conduct the main activity of the company at their own countries, and the legal authorizations granted by their local authorities in this sense; the existence of branches or other permanent representations abroad; the participation in other companies registered in the foreign company balance sheet as fixed assets, and the ownership of fixed assets abroad.

It is also important to bear in mind which are the consequences of the results of the aforementioned analysis: in case the Public Registry of Commerce concludes that the activity of the foreign company is subject to the provisions of the Corporate Law for regular activities developed within the territory of Argentina (section 118), it will be compelled to comply with all the registrations established by said Law, including all the necessary amendments to its corporate by-laws. Otherwise, the Public Registry of Commerce might request the judicial liquidation of the assets and operations of the foreign company, and its subsequent dissolution and liquidation.

In addition, the Public Registry of Commerce may extend the regime provided by the new Resolution to acts filed before other registries (i.e., related to machinery, aircrafts, etc.), both national or provincial, in order

to obtain information also from said registries regarding isolated acts performed by foreign companies in Argentina.

Finally, the new Registry will be in force after a 180-day term counted from the date of validity of the Resolution, which will be in force after a 30-day term counted from its publication in the *Official Gazette*.

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Canada

Biotechnology and Canada—The Reasons to Invest

Biotechnology is one of the world's fastest-growing technologies and Canada continues to hold its position as one of the top countries in this vital new field. The reasons for Canada's high international standing in biotechnology is a reflection of leading-edge research, a proven entrepreneurial approach that emphasizes clusters and partnerships as well as a strong commitment by the federal government in the industry.

I. Leading-Edge Technology

Canada has a strong base of scientific expertise and continuously invests in research and development, both factors which affect its steady growth in the biotech industry. According to the Government of Canada, sixteen Canadian universities are affiliated with a network of more than 100 teaching hospitals and research institutes. This Canadian research base has won an international reputation in fields such as genomics, proteomics, bio-informatics, immunotherapies, protein engineering and new drug delivery systems. Taken together, the research in Canada's universities, government laboratories, and other research organizations has made Canada a world leader in developing and commercializing products associated with key areas of "hot technologies" in the fields listed above.

II. Canada's Clusters of Biotechnology Excellence

The following are examples of Canadian biotechnology clusters:

a) Toronto, Ontario, the base of approximately 40% of Canada biotech industry, has developed strengths in all of the biotechnology fields.

b) Nearly every global pharmaceutical company has a presence in Montreal, Quebec. Although these companies play an important research and development role, many impressive innovations are coming from smaller biopharmaceutical companies.

c) One of the world's leading centers for agriculture biotechnology is Saskatoon, Saskatchewan. In fact, Innovation Place, situated in Saskatoon, is the home to more than 100 companies and organizations, making it one of the most successful university-related research parks.

d) According to the Government of Canada, British Columbia is now recognized as the 16th largest biotechnology community in North America. Health and genomics are the biotechnology areas of strength of British Columbia.

III. Canadian Government's Commitment to Biotechnology

The federal government's strong commitment to the biotech industry has contributed to Canada's success in the field. The federal government has stimulated the development of a critical mass of research infrastructure, large pools of post-graduate and post-doctoral researchers, world-class academics and, public- and private-sector research investigators, entrepreneurs and a renewed vision for the sector through the Canadian Biotechnology Strategy (CBS). For example, the Government of Canada has given Genome Canada, a not-for-profit corporation dedicated to enabling Canada to become a world leader in genomics and proteomics research, grants of $375 million. This funding is levering similar investment from other levels of government, private-sector institutions and international sources. Similarly, the federal government increased the level of funding to the Canadian Foundation for Innovation (CFI) by $500 million, increasing its support to $3.65 billion. Established by the Government of Canada in 1997, CFI is an independent corporation with the goal of strengthening the capability of Canadian universities, colleges, research hospitals and not-for-profit institutions to carry out world-class research and technology development.

According to the Government of Canada, Canada's attractiveness in the biotechnology industry is related to the following factors: Canada's research and development environment ranks first in terms of cost-competitiveness for biomedical research and development compared with other industrial nations, including the U.S., Europe and Japan; as a location for manufacturing, Canada has the lowest costs to establish and operate a manufacturing facility when compared to all other G-7 countries; and the overall skill level of Canada's workforce ranks first among competing countries. All of the foregoing is in addition to the following tax incentives provided by both the federal and provincial governments.

IV. Liability for Canadian and Quebec Income Tax

In general terms, the income taxes payable in Canada by a corporate investor will depend upon its residence and the source and type of income. In this regard, all corporations incorporated in Canada[1] after April 26, 1965, are deemed to be resident in Canada. In other instances, the residence of a corporation is where its central management and control abides. The Canadian-resident corporate investor will generally be liable to tax on his worldwide income under both federal and provincial tax legislation, and will, in most instances, be granted a credit against tax payable in foreign jurisdictions on income earned in those jurisdictions. Subject to applicable tax conventions, non-residents are taxed only on certain types of passive income, capital gains realized on the disposition of taxable Canadian property[2] and income from carrying on a business in Canada.

The Government of Canada levies and collects an income tax on resident corporations at a rate calculated as a percentage of taxable income. The current corporate rate on active business income is 22.12 percent, and 35.79 percent on passive income. A Canadian-controlled private corporation (a "CCPC") may be entitled to a rate reduction on a portion of its active business income.[3] Finally, large corporations that carry on business in Canada will also generally be required to pay a tax at a rate of 0.225 percent on their taxable capital in excess of $10 million.[4]

Quebec provincial corporate tax rates are in most cases the lowest in Canada for corporations controlled by non-residents. The current rate on active business income for such corporations is 8.9 percent, and 16.25 percent on passive income. Elsewhere in Canada, the current rate on active business income for such corporations may vary between 12 percent and 17 percent. Corporations that carry on business in Quebec will also generally have to pay a tax at a rate of 0.6 percent on their paid-up capital.

Canadian Federal Incentives

V. Research and Development ("R&D")

The Government of Canada provides valuable tax incentives to corporations that conduct R&D in Canada. Generally, eligible R&D consists of work, the purpose of which is to achieve a technological advance, through a process of systematic investigation aimed at overcoming a technological uncertainty. Commercial work is excluded from the definition of R&D, although it is common for experimental development projects with a commercial focus to include both eligible and ineligible work. If a business is a Canadian-controlled private corporation with less than $250,000 of taxable income in the preceding year, it may receive a refundable tax credit of 35 percent of its R&D expenditures (expenditure limit of $2 million). The credit is 100 percent and 40 percent refundable on current and capital expenditures, respectively. In excess of the expenditure limit, the tax credit is reduced to 20 percent, of which 40 percent is refundable on both current and capital expenditures. The tax credit is earned on current and capital R&D expenditures carried out in Canada, including: wages, materials, etc. R&D expenditures can be forwarded indefinitely: if they are not deducted in the year in which they were incurred, they can be deducted in any later year. Generally, capital expenditures can also be fully deducted in the year they were incurred. Corporations other than CCPCs are also entitled to a non-refundable 20 percent tax credit on current and capital expenditures.

VI. Multinational Clinical Trials

Multinational clinical trials, i.e., collaborative research where the work is distributed among various countries, may also, in part, be eligible for federal R&D tax credits. To be eligible, the work carried on in Canada with respect to multinational clinical trials, by the claimant and/or on behalf of the claimant, must meet the definition of R&D.

The work carried on in Canada by qualified researchers[5] as part of a multinational clinical trial involving the accrual of study subjects in Canada would generally be considered to be eligible R&D when: (i) the multinational clinical trial attempts to advance scientific knowledge; (ii) Canadian researchers provide input such as developing an evaluation of the scientific content of the proposed research and evaluating the balance of foreseeable harm in comparison with anticipated benefits of the experimental treatment; and (iii) the clinical trial the Canadian researchers conduct in Canada is based on a protocol that includes a hypothesis, scientific rationale and systematic method of biomedical experimentation.

Quebec Provincial Incentives

VII. R&D

In addition to the federal R&D incentives, the province of Quebec offers additional tax incentives. The Quebec program provides for the full deductibility of eligible current and capital expenditures on R&D activities. And, unlike the other provinces of Canada, in Quebec, eligible expenditures will not be reduced by amounts received pursuant to the federal R&D program. In addition, a taxpayer incurring R&D expenditures is entitled to a 17.5 percent refundable tax credit on salaries paid in Quebec. The 17.5 percent rate may be increased to 35 percent on the first $2,000,000 in expenditures incurred for the payment of salaries in Quebec for any private or publicly held Canadian-controlled corporation.[6] Where R&D activities are per-

formed on behalf of a resident or non-resident corporation that carries on business in Canada by a university or public research center, the rate of refundable tax credit related to the R&D expenditures will be 35 percent without any expenditure limit.[7]

As demonstrated by the federal and Quebec R&D programs, Canada is a strategic place to carry out R&D projects. For instance, the combined application of the federal and Quebec R&D programs would allow the expenditure of approximately $1,800 in R&D activities for every $1,000 of investment (divided equally in salaries and current expenditures).[8]

VIII. Quebec Tax Reduction for Foreign Researchers

The Quebec R&D program also offers a five-year provincial income tax reduction for foreign researchers coming to Quebec in order to get involved in R&D projects. Under this program, a foreign researcher may deduct, in the computation of his taxable income, for Quebec provincial income tax purposes, an amount equal to 75 percent of his salary from such an activity.[9]

IX. Biotechnology Financing

The Government of Quebec has implemented a program called "Bio-Levier." This program is open to growing biotechnology corporations, i.e., those that are beyond the start-up phase of development. The amount of the loan potentially available under this program can match the contribution made by outside investors. For example, for a given investment in the form of equity capital, with a minimum of 20 percent coming from outside Quebec, the Government of Quebec may grant equivalent financing in the form of a loan.

To be eligible to this program, a minimum investment of $7 million in equity capital is generally required. The maximum loan to be granted to any one corporation is $20 million. One additional advantage is that corporations receiving loans under this program will have a grace period of three years on principal payments and ten years to repay the loan. However, the government will charge the corporation interest and will generally require participation therein.

Conclusion

Canada offers a unique business and legal environment to foreign investors who can benefit from a flexible legal system where almost any legal vehicle may be used to carry on business. Through generous tax incentives, the federal and provincial governments of Canada show great respect for entrepreneurship. Fraser Milner Casgrain LLP, comprising over 500 lawyers in six cities across Canada and one office in New York, N.Y., has had extensive experience representing and advising foreign investors in many areas such as corporate and commercial law, taxation, international trade, litigation, labour law, intellectual property, entertainment, environmental and resource law and public policy.

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This text is of general nature only and is not intended to be legal or tax advice to any particular person. Consequently, one should consult his or her own legal or tax advisor with respect to his or her particular circumstances before taking any action. Moreover, this summary might not present or contain the current rules as they are or have been adopted by the competent authorities, from time to time.

Endnotes

1. Under federal or provincial legislation.
2. Only 50 percent of which is taxable.
3. Reducing the tax rate on such portion to 13.12 percent on the first $250,000 of taxable income for 2004.
4. Large corporations tax may be reduced if the corporation is liable to income tax in the year.
5. Clinical investigators and corporate scientists.
6. Other than a "Large Corporation."
7. Other special credits may also apply such as: pre-competitive research, catalyst projects, environmental innovation technology projects consortium, etc.
8. This implies that the tax refunds are invested in R&D activities by a CCPC that is not eligible to any special program, with assets worth less than $25 million, expenses less than $2 million and income from the preceding year less than $225,000.
9. The Quebec provincial income tax rates for an individual are as follows: up to $27,095: 16 percent; $27,096–$54,195: 20 percent; and over $54,195: 24 percent.

Chile

Chile Tax, Financial and Political Conflict Underlying the Royalty to Foreign Mining Companies

Chile seems to have an enormous tax conflict. Indeed, exacerbated spirits reigned in the speeches of EXPOMIN 2004, one of the largest exhibitions of the mining industry in the world, carried out in Santiago, Chile, between the 20th and the 24th of April, 2004.

On one hand, the representatives of the large mining companies addressed a very hard speech against President Lagos' administration, because of the latter's infringement of the legal and regulatory framework currently in force in Chile. This was caused by the bill to establish a "Royalty" for the mining industry. In turn, President Lagos replied in equivalent hard terms,

about the convenience for the country of establishing this Royalty, as a backup and palliative measure for the exploitation of non-renewable resources.

This rough encounter of President Lagos and the mining companies reflects only a part of the whole problem: the existence of a severe tax, financial and political conflict, in which the government is not willing to take charge, nor are said companies.

The Chilean Government's Actions

It is quite clear that the Chilean tax system has impressed First World countries due to the very low tax evasion rate and the towering level of tax compliance. The Chilean government and the Chilean internal revenue service ("SII") boast about it worldwide, but things are not as good as they seem. In fact, SII has been for several years transferring the costs of the tax administration to the taxpayers, when forcing them to prepare and pay tax declarations through the Internet and to render by such means certain accounting data on the most diverse matters, in order to be able to cross the information at minimum costs for the SII. For instance, Chilean companies complain for the sustained growth of their accounting and finance departments and/or their tax advisers increasing their costs.

These technological tools have allowed, by means of simply crossing the information, the thorough investigation of local and foreign companies' tax compliance level covering all aspects. In fact, SII's National Director has set as a main target of investigation for this year the compliance of income tax applicable to non-residents. Additionally the SII has become terribly severe regarding the collection of fines for tax infringement. Finally, since the SII is also a Tax Court of Justice (in the first courts level), tax justice in Chile is rather utopian.

We all agree that thorough investigations must be carried out, but also tax compliance needs to be facilitated, especially regarding those foreign companies whose transactions are difficult to investigate by the SII due to their high costs. We can say that we do not know of any company in Chile that does not have, in one way or another, tax compliance problems.

The government's permanent need for more money has caused an increasing pressure against the large companies to pay more taxes, and has ended up promoting improper and discriminatory actions against large foreign mining companies instead of applying the current Law.

Large Mining Companies' Actions

Should the Chilean Income Tax Law be really fair, it is quite possible that taxpayers would not be so willing to "compensate" for the lack of real tax justice, therein planning their tax exposure. It is a fact that income tax in Chile actually affects net profits rather than gross income, especially at the level of the company's final owners. For instance, there are a number of cases in which, pursuant to the aforementioned law, expenses rightfully incurred by a company must be treated as profit withdrawals of the foreign partners, subject to 35% withholding tax, such as automobile expenses, representation expenses (applicable only to the public sector), among many other unfair situations.

Given the investment amounts required by the large mining companies, international tax structures have been created to make tax and financial benefits applicable, beyond what seems reasonable.

Any Base for a Royalty to the Mining Industry in Chile?

In our opinion, a Royalty for the large mining industry in Chile, be this 3% (or 10%) on the gross sales of mineral depending on the operating income of each company, is an unconstitutional, illegal, and certainly inconvenient measure for Chile.

a) Unconstitutional: The mining concession system designed in the Constitutional Mining Statute contains all the legal attributes required to safeguard both the national and the private investor's interests. Accordingly, a registered owner (concessionaire paying a *patente minera*, or mining license) may freely exploit, enjoy, and dispose of its concession and the concession may not be taken away from its concessionaire except by means of an expropriation.

In our view, the Royalty is an act of expropriation applied on intangible or tangible assets (operational income), and therefore it must be fairly indemnified.

Additionally, the Royalty as proposed contains all the elements to be considered a tax increase. On this regard, the Chilean Constitution demands fair tax rates and their equitable application, as well as respect for the Constitutional spirit. The Constitution also forbids a particular destination (like a technology development fund) for taxes levied.

Finally, from our view, there is a breach of the Constitution where the Royalty, as proposed by the Chilean government, might be arbitrarily discriminating Codelco-Chile, the state-owned mining company, that might not be affected by the Royalty.

b) Illegal: The Royalty, in our opinion, also infringes on the Chilean Foreign Investment Statute, commonly referred to as "DL 600," created by the State of Chile as a stability guarantee

for foreign investors, the text of which was last amended in the Congress back in 1993, by a widely consented decision.

Pursuant to DL 600, a foreign investor (industrial and extractive investments of US $50 million or more) may agree to submit to a 42% income tax rate for up to twenty years in order to get the benefit of an invariable income tax regime. The foreign investor then gets exempted from any tax increases in the regular tax regime that may occur during that period. Likewise, DL 600 entitles the foreign investor to include in its foreign investment contract a clause to freeze the Value Added Tax regime (currently at 19%) and import tariffs regime on capital goods for the project, at the rate effective on the date of the investment. Finally, a special regime for large projects was introduced in 1985 to reduce tax uncertainty and facilitate the development of foreign investments requiring high levels of external credits and financing. Available for a period of up to 20 years, this regime allows an investor or recipient company to use accounting in foreign currency and to lock into existing practices on matters such as asset depreciation, carry-over of losses and the tax treatment of start-up expenses.

All such rights to foreign investors were granted in accordance with the common Constitutional Mining Statute, and the international treaties for the protection of foreign investment currently in full force and effect in Chile.

The Royalty is a new burden that certainly affects the invariability set forth in DL 600 as explained in the foregoing paragraph.

c) Groundless: The Royalty may not be conceived as fair consideration for the use of non-renewable natural resources. The mining concession is subject to the payment of a mining license (*Patente Minera*). The amount of this mining license is determined by the total land under the mining concession and the type of mineral underneath.

Therefore, and technically speaking, the "use of non-renewable resources" cannot be the justification of the Royalty, where it is already of the mining licenses. Otherwise there would be a *non bis in idem* breach.

Thus we do not anticipate any legal disadvantages in raising the mining licenses to reasonable levels.

d) Inconvenient: The mining industry is a particularly random business and requires huge investments in infrastructure, with long-term payoff and profitability, made in difficult-to- access locations. This is why a stable legal general statute is a key issue in the business. It is obvious that the Royalty would break the stability required and therefore adversely affect foreign investment in Chile.

It is important to have in mind that around the mining sector there is an enormous industry of suppliers of all kinds of goods and services that will also suffer the consequences of the Royalty.

Abuse of Right in Chile

Clearly we are in the presence of what legal doctrine calls "Abuse of Right": the Chilean government is trying to impose the Royalty against foreign mining companies, infringing the good faith and the "spirit" of both the DL 600 and mining license regulations in Chile. DL 600 does not contain a "Hardship Clause," allowing any of the parties to a Foreign Investment Contract-Law (State of Chile and the Investor) to request an amendment to the contract in order to adapt it to the circumstances changes; then the government is not entitled to request from the companies the renouncement to the tax invariability set forth in the DL 600, under the threat of a royalty.

The application of a Royalty to the mining industry as a fair consideration for the exploitation of non-renewable resources would be a gross legal and tax error on the part of the Chilean government, and susceptible in our opinion of being challenged before international organizations. Notwithstanding, it is necessary to take a look at how foreign mining companies have been acting in Chile to see they have been abusing of their rights as well, when infringing the spirit of the Chilean tax regulations.

Indeed, large mining companies, permanently advised by the big auditing firms and tax advisors as referred by government authorities, have used certain strategies in order to have tax losses and yet financial profits. Among others, these legal strategies include transfer pricing, assets depreciations, off-shore branches or agencies located in tax shelters, foreign loans by related entities in order to disguise taxable profits (affected by 35% tax rate) as interest payment (affected by 4% tax rate), and losses duplication by means of mergers and acquisitions. Such strategies have nearly prevented foreign mining companies from paying income taxes in Chile, which naturally differs from the law's intention. It is not strange then that the same auditing firm does the auditing of the financial state-

ments of the mining companies, breaching the necessary independence necessary in such activity.

In view of the above it is quite clear that the large mining companies have gone too far trying to minimize income tax in Chile. However, this should not be a surprise for the government because the Codelco-Chile's Board takes tax advisory from the same counsels in order to pay lower taxes to the Treasury.

Business Ethics

Business ethics is certainly not present in the business when maximizing resources, but it is more serious in the public sector. In our opinion, the control of business ethics cannot be left only to corporate governance self-imposed regulations, as it is the case in Chile. It is necessary to have efficient and transparent audit mechanisms, and a true independence between legal advisors and auditing firms.

Therefore, in our opinion, the government is mistaken when trying to impose the Royalty in order to recover part of the taxes that these companies did not pay based upon the aforementioned tax advice. In fact, the Chilean government is in possession now, and has been for years, of the necessary means to make the outgoing flows pay taxes properly in Chile, without the Royalty, such as transfer pricing regulations, fully and long effective. Then it is not a valid argument saying that foreign companies evade taxes by means of transfer pricing strategies, because that would be admitting the ineptitude of the Chilean government in finding illegal mechanisms, or even worse, the corruption of the public bureaucracy, both under the political responsibility of the government.

Indeed, the SII, by means of a simple inspection and seizure of files and computers, would be able to determine whether the large mining companies have been acting according to Chilean law or otherwise, and to apply legal penalties in the event of tax evasion. This procedure is rather ordinary in the USA and could hardly be taken as an arbitrary measure.

It is quite amazing that in Chile a regulation similar to the Sarbanes-Oxley Act, safeguarding the due independence of auditing firms and legal advisors, has not been put in force yet.

Future of Chile

In our opinion the Chilean government is willing to avoid opening a "Pandora's box" that could not only put an end to the government's intention to make large mining companies pay due taxes, but also affect other companies that have been using the same strategies to reduce tax impact. An inspection in such terms could result in a real financial and tax scandal, with consequences in Chile similar to those of the so-called Enron case.

Nevertheless, a thorough investigation of the reasons behind the tax consulting might be the best choice for the government, because it would not imply a change of the rules for foreign investors, but perhaps the revelation of a large-magnitude scandal concerning all the large foreign mining companies. If this were the case, said companies would probably accept any kind of measure taken by the government in this regard, including the change of their corporate structures into stock corporations subject to the surveillance and control by the Chilean SEC (*Superintendencia de Valores y Seguros*).

Thus, the real conflict and the choices in the hand of the Chilean government are as follows: (i) to perform a real fiscal auditing on each one of the large mining companies based on law currently in effect, without any new regulations; or, (ii) to negotiate privately and calmly with the large mining companies, in order to avoid losing international competitiveness, trying to reach an agreement on a new tax regime to be applicable in the future.

In our opinion the USA opened the way when leaning for the first transparency alternative; we hope Chile solves this situation in the same form.

Large mining companies would then have the following choices: (i) should the Royalty be finally applied, to request before international organizations the application of sanctions against the State of Chile, and in turn, to negotiate the acceptance of a larger credit against taxes applicable abroad; (ii) to proactively propose to the government the performance of investigation and auditing legal procedures to prove that they have not incurred tax evasion; and, (iii) to accept the Royalty proposed by the government as the best choice, in order to prevent a harmful financial and tax scandal. Certainly, the first two choices seem the most reasonable ones.

It is quite clear for us that the creation of new taxes on the mining industry is not legitimate, where the SII, the Customs Agency and the Central Bank already count with means of investigation. If it is true that the large mining companies took loans at higher rates than the market rate, and carried out operations at prices different to those prevailing in the market for such operation, then both the SII and the Central Bank should act accordingly and the government should accept its responsibility in this regard. In the near future, we hope that the incompatibility that should exist between "independent" advisors and "independent" auditors be established, just as the U.S. already did.

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Chile—Platform Investment Law and Permanent Regulations

Antecedents

It took no more than four months last year for the Chilean Congress to expeditiously discuss a bill aiming at the establishing of the legal framework for the existence of special investment companies set up in Chile for purposes of investing whether in Chile or abroad pursuant to certain terms and conditions, amongst which are those dealing with income tax exemptions for companies funded with foreign capital that carry out investments outside Chile. In fact, the bill was enacted as Law 19,840 and published in the *Official Gazette* of 23 November 2002 (the "Law").

By contrast it took the Chilean Inland Revenue Service much more time to publish its Permanent Regulations as issued by means of Circular No. 43 of 22 August 2003, published in the Official Gazette of 26 August 2003 (the "Regulations").

The bill was supported by the notion that Chile could present distinct comparative advantages to foreign business concerns by establishing in the country a business/investment platform from which to deal with more tax effectively at a regional level in a mid- to long-term range. The experiences of Singapore, the Netherlands and Ireland were cited.

Under pre-Law 19,840 days, if a corporate foreign investor from, say, Germany would have attempted to manage and control its investments in other countries within South America (Ecuador, for example) through Chile, then any income deriving from the investment would be subject to triple taxation: that of Germany, Chile and Ecuador in our example. Admittedly, some tax relief could be obtained if treaties to avoid double taxation were in place; however, the Law comes as a remedy to the lack of such treaties.

The key contents of the Law consist then of amendments to Chilean Decree Law No. 824 on Income Tax Law, of 1974, as amended, ("DL 824") by establishing a special tax regime in favour of foreign companies setting up Chilean subsidiaries funded with capital contributed from outside Chile for the main but not exclusive purpose of investing outside Chile.

Law 19,840

The main features of the Law are embodied in new Section 41 D, Paragraph 6, of DL 824 dealing with "Norms Relative to International Double Taxation," according to which:

1. The income tax benefits/exemptions are available to joint stock companies set up in Chile as a private company or a listed corporation (the "Investment Platform Company" or "IPC").
2. The IPC's exclusive object is to carry out investments in Chile or abroad. As to the former, the IPC may only invest in joint stock companies of any type established in Chile.
3. Notwithstanding the exclusive object, the IPC may render remunerated services in Chile or abroad to companies and enterprises set up abroad and formally established outside Chile.

4 The equity participation in/capital contribution to an IPC has to be taken/supplied in the aggregate amount of at least 25% of the total capital by investors domiciled or residing abroad.

5. The capital of an IPC could be contributed in foreign currency or in stock of companies domiciled abroad or in Chile; or in equity rights of companies domiciled abroad which are owned by persons without domicile or residence in Chile, with any such stock or equity rights free of any lien, encumbrance or limitation.
6. Investments by the IPC outside Chile are regulated in detail in Section 41 D, Paragraph 6 of DL 824 under the form of capital contributions to and securities issued by companies which are formally established abroad but not in foreign countries or territories that are considered "tax havens" or that have preferential tax regimes ruled out by the OECD, and are regularly engaged in entrepreneurial activities.
7. Notwithstanding that the IPC has to be set up in accordance with the laws of Chile and be physically established in the country—and thus be considered as a Chilean tax payer taxable on its worldwide income—it shall be considered as not being domiciled or without residence in Chile solely for Chilean Income Tax purposes. Accordingly, any income derived in favor of the IPC from outside Chile is deemed to be "foreign source income" which is income tax exempt in Chile. As regards services, the IPC is subject to VAT.
8. The income tax regime applicable to foreign, non-Chilean shareholders of the IPC consists of total Chilean income tax exemption in respect of remittances from Chile of profits deriving from Chilean or foreign sources. Furthermore, a tax credit could be available to a non-Chilean resident shareholder of the IPC in the country of its tax domicile or residence in respect of any tax paid by the IPC in Chile on income of Chilean source distributed to a foreign investor.
9. No Chilean capital gains tax is imposed on any gain realized by the non-Chilean resident/foreign shareholder on the disposition of shares in

the IPC, except on that part of the gain attributable to investments by the IPC in Chilean assets, if any.

Other Legal Norms

1. The rules on bank secrecy with regard to deposits and investments, as established in Section 154 of the General Law on Banks contained in DFL No. 3 of 1997, of the Ministry of Finance, as amended, do not apply to IPCs. Accordingly, the Chilean Inland Revenue Service may have access to banking information as part of its tax avoidance control measures.
2. Recently issued rules on thin capitalization, as applicable to foreign investors, also apply to IPCs (DL 824, Section 59, Paragraph 1).
3. General rules on Income Tax Withholding apply to IPCs.
4. The general norms on Stamp Tax on lending documents apply to borrowings by IPCs.
5. Special and separate tax book-keeping rules apply in respect of investments by the IPC in and outside Chile and income deriving therefrom.
6. Also, special tax reporting rules apply to IPCs.
7. Tax benefits of all kinds available by application of treaties to avoid double taxation to which Chile is a party to are extended to IPCs and its shareholders.
8. Penalties and prosecution under the Chilean Tax Code (Decree Law 830 of 1974, as amended) apply to IPCs.
9. A special fine is imposed under new Section 41 D of DL 824, as established by the Law, consisting of up to 10% of the amount of investments made by the IPC for reporting incomplete or false information to the Chilean IRS.

There are indications that the international business community is appreciative of the benefits of the new law on platform investment companies and some have considered or may be considering establishing operations thereunder. Thus, as at March 2004, five foreign companies have decided to establish a platform investment or services company pursuant to Law 19,840 and have registered with the Chilean Internal Revenue Service.

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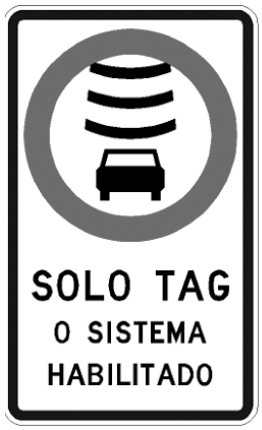
Electronic Toll Payment: Is the Chilean Legislation Adequate?

Since the return to democracy, the Chilean government has made the modernization of roads throughout the country a priority. Certainly the capital has not been the exception to this policy. Using the concession scheme applied in the rest of the country for interurban highways, four free-flow roads are currently under construction and refurbishment in the city of Santiago. The operation of a couple of these highways—or segments thereof—shall begin this year. By the end of 2006, the whole network will be in business. The network's technology for toll collection is state of the art: use is controlled *at highway* speed through the communication between roadside readers with electronic devices called "tags" or "transponders" which are permanently affixed to the windshield of vehicles. Under this third-generation system, vehicle owners are billed on a monthly basis.

Without cash lanes, the question with respect to the effectiveness of the legal framework to prevent unauthorized use becomes crucial. The Public Works Concessions Act enacted in the '90s had already established the right to collect payment against users who fail to pay tolls, establishing a penalty in favor of the concession holder equivalent to the greater of 40 times the amount of the unpaid tolls, duly adjusted, or two *unidades tributarias mensuales* (approximately US $100). In recent times, this right has been supplemented by new legislation enacted with the purpose of deterring unauthorized use of concession roads.

(image 1)

(a) On December 19, 2002, a new section was introduced in the Traffic Act making the use of free-flow toll roads without transponders or other auxiliary system enabling payment (i.e., a *day pass*) a traffic violation. The Department of Transportation of the Ministry of Public Works created a road sign alerting drivers of an upcoming free-flow toll road (image 1) and another road sign warning that use of the road is strictly reserved for vehicles holding a tag or day pass (image 2). The traffic violation—considered *gross* by the law—consists in



(image 2)

driving a motor vehicle in violation of the road sign. Offenders are subject to a fine of CH $30,600 (approximately US $50), for which the owner of the vehicle involved in the violation is strictly liable.

(b) Legal changes have also reached the procedural aspects involved in processing traffic violations by local police courts. On April 28, 2000, Law 19,676 introduced a new section 3 in the Local Police Court Proceedings Act ("LPCP Act") establishing that service of process of the violator is to be made at the address listed in the vehicle registration with the National Register of Motor Vehicles ("Register"). Service of process made at such address is valid, regardless of the fact that the owner of the vehicle changed domicile failing to report the change to the Register. The new rule prevents motions that dispute the validity of the fine imposed on the grounds that the violator did not receive service of process.

(c) In order to rule out evidence issues, Law 19,676 also introduced two new paragraphs in section 4 of the LPCP Act, authorizing police officers and state and municipal inspectors to use Ministry of Public Works-approved electronic equipment to control traffic violations and the admissibility in court of the records produced by such equipment, such as film, photographs or other forms of reproducing images and sounds.

(d) Finally, Law 19,676 created the Register of Unpaid Fines (the "RUF"). Every two months, local police court clerks must report vehicles involved in unpaid fines to the RUF. Once a vehicle is listed by the RUF, its owner may not renew the annual license required for circulation, unless the fines, duly adjusted, and processing fees are also paid. It should be noted that the law orders police officers and inspectors to withdraw from circulation any vehicle without a valid annual license and to turn it over to a municipal lot.

Of course the effectiveness of the rules as applied to the new urban free-flow roads has not been tested yet. Nevertheless, the interaction of the traffic violation with the impossibility of renewing the annual registration and its effects has been crafted in a way that should produce the desired effect of deterring unauthorized use. The workability of the scheme has been carefully analyzed, including by world-renowned MBIA Insurance Corporation, which acts as insurer of the bonds issued by at least two of the concession holders to finance the projects, resulting in the bonds being rated AAA. Finally, and perhaps most importantly, the fact that Chileans have a reputation for being law-abiding people provides a happy forecast for the system.

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The Intellectual Property Regulations in the U.S.-Chile Free Trade Agreement

On June 6, 2003, Chile and the U.S. signed a Free Trade Agreement (FTA), ending a two-year process and 14 rounds of talks that came to a conclusion in December 2002, when both countries reached a consensus on all of the commercial issues covered in the agreement. After its corresponding approval by the U.S. and the Chilean Congresses, the FTA entered into force on January 1, 2004.

Over the past 12 years Chile has negotiated trade agreements with most of its partners, among which are Latin American countries and Canada. In addition, an Association Agreement with the EU was subscribed, and negotiations with South Korea were completed, all of which makes Chile a solid investment platform thanks to this network of trade agreements comprising a market of more than 1 billion consumers.

General Aspects of the FTA

This agreement is the first ever signed by the U.S. with a South American nation. In addition to being the world's most powerful economy—with 22% of gross world product—the U.S. is also the first commercial partner and major foreign investor in Chile.

The FTA includes different issues, among which is the elimination of tariffs, customs procedures, sanitary measures, investments, competition policies, temporary entry of personnel, modern treatment of labor and environmental issues, as well as intellectual property regulations. Worth mentioning is also an expeditious and impartial mechanism for settling controversies and treatment of e-commerce, which will allow a more dynamic interaction in the new world economy.

As for tariff reduction for the trading of goods, the FTA provides that 90% of the goods imported by Chile from the U.S., and 95% of Chilean products imported by the U.S., will immediately become duty-free, whereas taxes on all other products will be phased out over a maximum period of 12 years. These conditions favoring access to the world's largest economy will constitute an attraction for leading international companies, American as well as European and Asian, without excluding opportunities that will also be available to Argentinean and Brazilian investors.

Regulations of Intellectual Property Within the FTA

FTA Chapter 17 is intended to regulate intellectual property rights, including special provisions to regulate the protection of encrypted program-carrying satellite signals and the limitations on liability for Internet service providers. On these matters, the FTA adjusts to modern standards, accounting for the latest technological advances. In general, it may be held that a substantial number of the regulations contained in this chapter have already been incorporated into Chilean legislation.

A relevant aspect of general application in Chapter 17 is the guarantee that each country will give to nationals of the other party non-discriminatory treatment as it would give to its own nationals regarding the protection and usufruct of intellectual property rights.

Acknowledgment of Treaties on Intellectual Property

Both countries acknowledge the convenience of relating to each other upon the basis established in existing international agreements in force in the field of intellectual property.

In this sense, the FTA provides that both countries should ratify or adhere to the Patent Cooperation Treaty (1984) before January 1, 2007, and that before January 1, 2009, they shall ratify or adhere to the International Convention for the Protection of New Varieties of Plants (1991), the Trademark Law Treaty (1994), and the Convention Relating to the Distribution of Programme-Carrying Signals Transmitted by Satellite (1974).

In addition, it provides that both countries will make reasonable efforts to ratify or adhere to the Patent Law Treaty (2000), the Hague Agreement Concerning the International Deposit of Industrial Designs (1999), and the Protocol Relating to the Madrid Agreement Concerning the International Registration of Marks (1989).

It also states that no FTA provision relating to intellectual property rights may be in detriment to the obligations and rights of a nation with respect to the other in virtue of the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) or multilateral agreements on intellectual property subscribed or operated under the auspices of the World Intellectual Property Organization (WIPO).

Trademarks

The FTA provides that trademarks shall include collective, certification and sound marks, and may include scent marks.

As for the protection of rights, the FTA provides that each party shall allow interested parties to oppose trademark registration applications, and recognizes the exclusive right of a holder of a registered mark to prevent third parties, without his or her consent, from using signs being identical or similar to his or hers on related goods or services when its use is likely to mislead consumers.

It is also acknowledged that Article 6 bis of the Paris Convention for the Protection of Industrial Property (1967) (Paris Convention) shall apply, the necessary changes having been made, to goods or services which are not similar to those identified by a well-known trademark, whether registered or not, provided the use of such a trademark indicates a connection among such products or services and the holder of the well-known trademark. Likewise, each country shall establish measures to prohibit or annul a trademark registration that is identical or similar to a well-known trademark, if the use of said trademark by a registration applicant could be confusing, misleading or deceitful, or if there is the risk of associating that trademark with the holder of the well-known trademark, or if it constitutes an unfair use of such trademark's reputation. In order to establish the reputation of a trademark, it will not be demanded that its reputation extend beyond the public sector that normally deals with the respective products or services.

The FTA also contains various regulations regarding the registration procedures of commercial trademarks, providing that each country should establish a system including information about the reasons to reject the registration, the time to reply to the authority, to disagree with an initial rejection and judicially disagree with any final rejection. Likewise, both countries undertake, to the greatest extent possible, to establish an electronic system for applying, processing, registering and maintaining trademarks.

Domain Names

Each party shall require that the management of its country-code top level domain (ccTLD) provide an appropriate procedure for the settlement of disputes, based on the principles established in the Uniform Domain Name Dispute Resolution Policy (UDRP), in order to address the trademark Internet piracy issue. Also, the management of their respective ccTLDs shall permit online public access to an accurate and reliable database, containing contact information for domain name registrants.

Geographical Indications

The U.S. and Chile undertake to reciprocally protect their geographical indications, further demanding of each other the publication of applications, the existence of an application objection procedure and registration annulment of geographic indications.

As of the date the FTA comes into force, only the protection or registration of a geographical indication will be rejected when it is confusingly similar to a pre-existing trademark application and carried out in good faith, or to a pre-existing registered trademark, or even to a pre-existing trademark whose rights have been acquired through use in good faith.

Patents

In this regard, the FTA provides that each party may reject or annul a patent only when reasons may justify the rejection of a patent.

Also, both countries undertake to adjust the term of a patent to compensate the unjustified delays that may occur when awarding it. To that effect, unjustified delay will be regarded as that which occurred when awarding the patent and which is higher than five years computed from the date the application is filed, or higher than three years from the date the application analysis has been requested, whichever occurs later.

An interesting aspect in this matter is that neither party will be able to a use public disclosure to bar patentability based upon a lack of novelty or inventive step if the public disclosure was made or authorized by the patent applicant and occurs within 12 months prior to the date of filing of the application.

As regards pharmaceutical products protected by a patent, each country shall grant a patent extension period to compensate the holder of the patent for the unjustified reduction of the patent period as a result of the marketing approval process, also having to provide the patent holder with the identity of any third party that requests the marketing approval in effect during the patent period, and deny the marketing approval to any third party before the expiration of the patent period, unless by consent or acquiescence of the patent owner.

Copyright and Related Rights

Among many other matters, the agreement establishes that both countries shall provide that authors of literary and artistic works are entitled to authorize and prohibit all reproduction of their works, in any manner or form, permanent or temporary, including temporary storage in electronic form. Also, notwithstanding what has been provided in the Berne Convention for the Protection of Literary and Artistic Works (1971) (Berne Convention), both parties will grant literary and artistic authors the right to authorize or prohibit the communication to the public of their work by wire or wireless means, provided that the disposal of their work to the public is done in such a way that they may be accessed from any place and at any time.

The FTA also assigns provisions regarding related rights, regulating the reproduction right, the authorization to dispose of the original and copy to the public, as well as the authorization or prohibition to broadcast.

It is also indicated that any person owning any economic right—not a moral right—may freely and separately transfer such right by contract. Each country may establish which contracts of employment underlying the creation of works or phonograms shall, in the absence of a written agreement, result in a transfer of economic rights by operation of law.

Enforcement of Intellectual Property Rights

To effectively penalize piracy and forgery, the FTA provides that both countries will provide civil and criminal procedures incorporating effective measures and remedies.

As regards civil procedures, it is provided that judicial authorities will have the authority to order the infringer to pay damages, the seizure of suspected infringing goods, and the destruction of the goods determined to be infringing goods. Any provisional measure filed without having heard the other party shall be acted upon expeditiously, being able to order the applicant to provide a security or assurance to prevent abuse, but without constituting an unjustified dissuasion of access to such procedures.

In the criminal field, the FTA states that both countries undertake to establish criminal procedures and penalties at least in cases of willful trademark counterfeiting or piracy, on a commercial scale, of works, performances or phonograms protected by copyright or related rights, including sentences of imprisonment and/or monetary fines that are sufficient to provide a deterrent to future infringements. Judicial authorities have the authority to order the seizure of suspected counterfeit or pirated goods, as well as to order the forfeiture and destruction of all counterfeit and pirated goods.

Border measures are also expressly regulated, establishing that any right holder will be entitled to initiate procedures for suspension by the customs authorities of the release of suspected counterfeit trademark or pirated copyright goods into free circulation.

Lastly, both regarding border measures and criminal procedures, the FTA provides that, in cases of copyright and related rights piracy and trademark counterfeiting, the competent authorities will be permitted to initiate measures or legal action *ex officio*—without the need for a formal complaint by a person or right holder.

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U.S.-Chile Free Trade Agreement: A Token for International Open Trade

1. Background

The U.S. is Chile's largest trading partner. In 2003, two-way goods and services trade totaled approximately US $5,900 million. The free trade agreement (FTA) between Chile and the U.S. was a long-sought-for objective which would crown Chile's open international trade policy implemented during the last three decades. The history of the FTA between Chile and the U.S. is one full of ups and downs. It was under President George H.W. Bush's administration that first steps were taken towards the implementation of a FTA. Notwithstanding the good intentions and commitment of both countries at that time, as a result of difficulties experienced in the U.S. Congress by President Clinton's trade agenda, only in December 2000 were Chile and the U.S. able to start formal FTA negotiations.

In August 2002, under the current Bush administration, the Trade Promotion Authority (TPA) was approved in the U.S. Congress. With the TPA negotiations speeded up it was possible to address the most sensitive trade issues such as labor, environment, investment and dispute settlement. Negotiations were neither an easy task nor a short-term effort. It took 14 rounds of negotiations during a term of two years before the text of the FTA was finally approved in 2002. The FTA entered into between Chile and the U.S. is a state-of-the-art international trade agreement which deals with international trade topics of an inherently complex nature such as agriculture, textile industry, labor, environmental protection and, for the first time, e-commerce. The Chilean Congress promulgated the FTA on December 31, 2003.

2. Why Chile?

Facts such as Chile's institutional stability, consistent open trade strategy, strong financial markets and highly competitive economy were essential characteristics which clearly turned Chile into an attractive partner for the U.S. to start the implementation of its free trade policy in the southern cone.

3. Why the U.S.?

It is not hard to realize what factors make the U.S. the ideal international trade partner. Just to mention a few: the U.S. economy represents 21.6% of world GDP; it has a stable, open economy; its internal market is huge; it is the most competitive economy on the globe, etc.

4. The Actual Agreement

The FTC entered into between Chile and the U.S. is the ultimate international trade agreement as far as the range of topics covered is concerned. It is made up of 24 chapters, of which we highlight those referring to market access, rules of origin, customs, sanitary and phytosanitary provisions, technical barriers to commerce, safeguards, government procurement, investment, services, financial services, telecommunications, e-commerce, competition policy, intellectual property rights, labor, environment, transparency and dispute settlement.

5. Most Important Highlights

(i) New market access for Chile and the U.S. All tariffs and quotas on all goods are eliminated immediately or after transition periods that run for up to 12 years, without exceptions.

(ii) Opportunity to export financial services. Chile will have the opportunity to become a potential exporter of financial services, as well as the business platform from which U.S. financial institutions will be able to render financial services to other markets in Latin America.

(iii) New opportunities for U.S. banks, insurance, securities and related services. The financial services chapter includes core obligations of non-discrimination, most-favored-nation treatment and additional market access obligations.

(iv) Investment. All forms of investment are protected under the FTA, such as enterprises, debt, concessions, contracts and intellectual property.

(v) Intellectual property rights ("IPR"). High level of IPR protection. Protection of copyrights, patents, trademarks and trade secrets is state-of-the-art, going beyond previous free-trade agreements. Enforcement of IPR is also enhanced under the FTA.

(vi) Dispute Settlement. All core obligations of the FTA, including labor and environmental provisions, are subject to the dispute settlement provisions of the FTA. An innovative enforcement mechanism includes monetary penalties to enforce commercial, labor, and environmental obligations of the agreement.

6. Major Accomplishment

The FTA between Chile and the U.S. will expand trade and investment between the world's largest economy and Latin America's most open economy. This FTA is the most comprehensive and thorough agreement negotiated by the U.S. as of this date and will become a benchmark for future free trade agreements currently under negotiation with other Latin American countries. The FTA reflects the U.S. and Chile's strong commitment to open international trade and it is expected that

it will introduce a significant push to the trade and relations between both countries.

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Leveraged Buyout in Chile

1. Introduction

Leveraged buyout ("LBO") is a mechanism used to acquire a controlling stake of a company (the "Target Company") being the financing of such acquisition secured by the Target Company. The Target Company can grant a personal guarantee (for instance, a *fianza*) or an assets guarantee (for instance, a pledge of assets, contractual rights, etc.) in order to secure said financing. Therefore, it is relevant to review whether this financial assistance provided by the Target Company to the buyer is valid under applicable laws.

The purpose of this article is to briefly review certain aspects that might be relevant regarding LBOs of a Chilean Target Company. We will make reference herein to certain provisions of Law 18,046 of Corporations (the "Chilean Corporations Law") regarding required corporate approvals, tender offer rules, purchase of its own shares by the Target Company, withdrawal rights of dissenting shareholders and duty of confidentiality of directors that are relevant for this matter.[1]

We will not review issues that would arise in a management buy-out transaction (i.e., when the buyer is a director, shareholder or officer of the Target Company). Therefore, we will not make reference herein to the provisions that would be applicable to such a transaction with related parties.

2. LBOs in Comparative Law

LBOs facilitate the transfer of shares since they help buyers to obtain the required financing. LBOs are normally used by private equity funds.

However, most European legislation forbids or restricts LBOs. For instance, Austrian law deems it an illegitimate benefit in favor of the buyer, since the Target Company compromises its own patrimony and reduces its financial capacity without any compensation or benefit. Therefore, it can only be valid and legal if the Target Company receives a profit *(fee)* for the granting of the security interest or has its own interest that justifies such security interest.

Likewise, section 161e of the Commercial Code of the Czech Republic forbids a company to finance or secure the financing of an acquisition of its own shares except if the company's workers or financial institutions make the acquisition. The same applies in Denmark, where the financing of acquisitions of its own shares or shares owned by the controlling shareholder has been forbidden since 1973.

In Canada, both federal and most provincial laws forbid financial assistance in the event of related-party transactions or acquisition of its own shares, unless it does not adversely affects the financial position of the company, which must be evidenced by means of solvency tests.

3. LBOs under Chilean Law

Chilean law does not regulate LBOs. Therefore, it is necessary to review general provisions of Chilean law that would be applicable to LBOs, especially certain corporate governance rules applicable to Chilean public corporations.

3.1. Tender Offer Rules

If the buyer will acquire control of the Target Company and the latter is a public corporation in Chile whose shares are traded in local stock exchanges, the acquisition must be done pursuant to the tender offer rules set forth in Articles 198 *et seq.* of Law 18,045 of Capital Markets (the "Chilean Securities Act"). There are certain exceptions to such rules, the most important one for this purpose being the rule stating that if the shares are "highly traded" and the price to be paid is lower than 10% over of the "market value," there is no obligation to purchase the shares through a tender offer process.[2]

Pursuant to the Chilean Securities Act, any person or group of persons with a shareholders agreement that holds shares directly or indirectly having (i) the capacity to ensure the majority of the voting rights in the shareholders meetings and to elect the majority of the board members or (ii) conclusive influence in the management of the company, is deemed as a "controller" of a corporation.[3]

In a tender offer process all the shareholders of the Target Company shall have the right to sell their shares. The Chilean Securities Act sets forth prorate and other requirements of the tender offer that we will not cover in this article, since it would be beyond its scope.[4]

3.2. Shareholders' and Directors' Obligations

Pursuant to the Chilean Corporations Law (i) shareholders cannot exercise their rights affecting the company's and other shareholders' rights; and, (ii) directors are subject to fiduciary duties, duty of care and duty to keep confidential any information related to the businesses of the company that has not been disclosed to the market, unless such disclosure benefits the company or it is related to a breach of its bylaws or the law.

Therefore, the delivery of certain information of the company (information that has not been disclosed to the market) by the controlling shareholders or the directors to the buyer is an important issue that should be carefully reviewed case by case.

In this regard it is important to note that there is currently a bill of law at Congress ("MK2 Bill of Law") providing that controlling shareholders and related persons to the company (i.e., officers, directors and shareholders holding more than 10% of shares of the company) will be allowed to disclose confidential information of the company, provided that the parties execute a confidentiality agreement.

3.3. Shareholders Approval

Since LBOs involve the granting of security interests or collateral by the Target Company, the approval thereof by an extraordinary shareholders meeting is required.[5] The shareholders cannot amend this provision in the bylaws of the company. However, if the principal obligor is an affiliate company the approval of the board of directors is sufficient.[6]

Unless the bylaws set forth otherwise, and with the exception mentioned below, the quorum required to have a valid shareholders meeting is the majority of all outstanding shares on the first call, and the number of shares that attend the meeting on the second call. Likewise, the quorum required to approve this matter is the majority of the shares present or duly represented at the meeting.[7]

3.4. Special Quorum if Guarantee Involves More Than 50% of the Assets

If the guarantee exceeds more than 50% of the assets of the Target Company it must be approved by 2/3 of all outstanding shares with voting rights. The shareholders cannot amend this provision in the bylaws of the company. However, if the principal obligor is an affiliate company the approval of the board of directors is sufficient.[8]

Please note that MK2 Bill of Law shall amend the above-mentioned norm, since the 50% figure will include not only the assets of the Target Company but also the affiliates'.

3.5. Withdrawal Right of Dissenting Shareholders

Should any shareholder vote against the approval of the granting of a guarantee that exceeds more than 50% of the assets of the Target Company and such a decision is approved by 2/3 of all outstanding shares as set forth above, the dissenting shareholder has the right to withdraw from the company, and the latter shall have the obligation to purchase such shares.[9] The price to be paid by the company to the shareholders shall be the book value in the case of public corporations whose shares are not "highly traded." If the shares are "highly traded," the price will be the average of the market price during the two months prior to the relevant shareholders meeting that approved the granting of the guarantee.[10]

The Target Company must sell in the market all shares it purchased from its shareholders as a consequence of the exercise of the mentioned withdrawal rights, within one year from the acquisition date. Otherwise its capital will be automatically reduced.

3.6. Purchase of Its Own Shares by the Target Company

Chilean law allows the purchase of its own shares by companies subject to the following requirements:[11]

(i) The shares must be "highly traded" and must be sold within 24 months of the acquisition date.

(ii) The purchase must be approved by 2/3 of all outstanding shares with voting rights, and the approval must set forth the maximum number of shares to be purchased, the maximum and minimum price and the term of the purchase program, which cannot exceed three years. However the shareholders can delegate the determination of the price to the Board of Directors.

(iii) If there are different types or series of shares, the offer must be made in proportion to the number of shares of each one that is "highly traded."

(iv) It cannot exceed 5% of the company's subscribed and paid shares. The excess must be sold within 90 days of the date of the acquisition that produced it.

(v) The purchase can only include shares that are fully paid and free of encumbrances, and must be made in stock exchanges on prorate basis or pursuant to the tender offer rules of Chilean Securities Act.

Please note that there are other exceptions and rules to this matter that are not discussed herein.

3.7. Need of a Cause

Pursuant to Chilean law, any act or contract must have a licit cause.[12] The majority of Doctrine understand that cause is the purpose of the parties to execute a contract; for instance, the price in a purchase and sale agreement or the non-profit intention (*mera liberalidad*) in a donation. However, the granting of a guarantee by the Target Company in LBOs cannot be a free contribution or a donation.[13]

Therefore, as in most foreign legislation, pursuant to Chilean law it is necessary to have a valid interest or benefit by the Target Company in order to grant the mentioned security. If there is a lack of such an interest the validity of said guarantee could be contested.

4. Conclusion

Although Chilean law does not regulate LBOs, it is possible to structure LBOs with respect to a Chilean Target Company, subject to restrictions and requirements imposed by Chilean law, as explained above.

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Endnotes

1. This article is a summary of certain aspects that are relevant for the discussions of the validity of LBOs pursuant to Chilean law. However, if a person plans to do an LBO with respect to a Chilean Target Company it shall be necessary to review the situation on a case-by-case basis.
2. *See* Article 198 *et seq.* of the Chilean Securities Act.
3. *See* Article 97 of the Chilean Securities Act. To have "conclusive influence" is defined in Article 99 of the Chilean Securities Act.
4. *See* note 2 above.
5. Article 57 No. 5 of Chilean Corporations Act. The provision includes any kind of collateral, security interest or guarantee.
6. Pursuant to Article 86 of the Chilean Corporations Act, an affiliate (*filial*) is any company whose parent company (*matriz*) owns directly or indirectly more than 50% of the shares with voting rights or can elect or appoint the majority of the affiliate's directors or managers.
7. *See* Article 61 of the Chilean Corporations Act.
8. *See* note 6 above.
9. *See* Article 69 number 4 of the Chilean Corporations Act.
10. *See* Article 79 of Decree 587 Regulations to the Chilean Corporation Act.
11. *See* Article 27A and B of the Chilean Corporations Act.
12. *See* Article 1467 of the Civil Code.
13. *See* Article 1397 of the Civil Code.

European Union

Clean-up "EU" Act

Background

It is estimated that there are currently circa 300,000 polluted sites in the European Union ("EU"). Current clean-up costs are estimated at 106 billion euros. The EU will soon expand from 15 to 25 Member States. This expansion may significantly add to the number of EU polluted sites. Against this backdrop, EU governments have recently agreed on legislation in the form of the Directive on Environmental Liability ("Directive") to compel polluting companies to cover the full costs of environmental clean-ups. The adoption of this Directive on 10 March 2004 marked a significant departure from pre-existing legal norms in Europe, where polluters are not liable at an EU or Member State level for the full costs of pollution damage to water, soil and biodiversity.

As the Directive must be implemented in national legislation in all EU Member States within three years from adoption, international counsel and companies operating in the EU should be aware of the new regime in order to gauge and minimize costs of (non) compliance.

This article examines the Directive's objectives, scope of liability, enforcement procedure and exemptions.

Objectives

The fundamental principle of the Directive is that a company or individual ("operator") whose activity has caused environmental damage or an imminent threat of such damage, is to be held financially liable. This is in order to induce operators to adopt measures and develop practices to minimize the risks of environmental damage so that their exposure to financial liabilities is reduced. According to this "polluter-pays" principle, an offending operator will bear the cost of the necessary preventive or remedial cleanup measures, unless valid exemptions or defenses apply.[1]

The Directive establishes an EU liability regime which allows Member States to hold parties liable for environmental damages they have caused, but does not establish a comprehensive clean-up plan. There is no Directive-mandated commitment to cleaning up sites if the courts do not rule in favor of the plaintiffs.[2]

Scope of Liability

The emphasis of the scope of liability in the Directive is on the operator in control of the activity that caused the damage.

The operators of the dangerous or potentially dangerous activities listed in Annex III of the Directive may be held strictly liable under the Directive for the costs of preventing or remedying environmental damage. These include, *inter alia*, releasing restricted substances into surface/ground water or into the air, operation of installations producing dangerous chemicals, operation of waste management facilities, operation of landfill sites and incineration plants.[3]

Operators of activities outside Annex III may also be liable, under the Directive, for the costs of preventing or remedying biodiversity damage, but only in the

event they are found to be negligent or otherwise at fault.[4]

Whether liability under the Directive will be proportional or joint and several is unclear. It is up to the Member States to establish national rules covering cost allocation in cases of multiple party causation. Member States are also to take into account, in particular, the specific situation of users of products who might be responsible for environmental damage under the same conditions as those producing such products. In this case, apportionment of liability will be determined in accordance with national law. Member States may provide for flat rate calculation of administrative, legal, enforcement and other general costs to be recovered.[5]

It is also noteworthy that the Directive does not prevent Member States from maintaining or enacting more stringent provisions in relation to the prevention and remedying of environmental damage; nor does it prevent the adoption by Member States of appropriate measures in relation to situations where double recovery of costs could occur as a result of concurrent action by a competent authority under this Directive and by a person whose property is affected by the environmental damage.[6] Accordingly, national legislation must always be consulted.

Enforcement Procedure

The Member State governments will have primary responsibility in bringing cases to court. If the governments are negligent in fulfilling this responsibility, qualified public entities (public interest groups, including NGOs) and persons who have a sufficient interest (i.e., who have suffered a damage) may request the competent authority to take action and challenge the competent authority's action or inaction.[7]

When environmental damages occur, the relevant Member State government ("competent authority") is in charge of assessing the significance of the damage and determining which remedial measures should be taken in co-operation, as much as possible, with the operator responsible for the damage.

The competent authority may require the operator to take the necessary preventive or remedial measures, in which case the operator will finance such measures. Alternatively, the competent authority may implement the measures itself or have them implemented by a third party. The operators will also ultimately bear the cost of assessing environmental damage and, as the case may be, assessing an imminent threat of such damage occurring.[8]

In the event the restoration or prevention is implemented by the competent authority or by a third party on its behalf, in the place of a responsible operator, that authority will then recover the cost incurred by it from the operator within a reasonable period of time from the date on which those measures were completed.[9]

Exemptions

The Directive does provide noteworthy exemptions and defenses to liability claims of competent authorities.

The Directive, once implemented in the Member States, will have no retroactive effect.[10] Damage caused before the expiration of the deadline for implementation of this Directive will not be covered by its provisions.

Activities and emissions which are believed to be safe for the environment, according to the state of scientific and technical knowledge at the time of occurrence, are exempt. Furthermore, in the event the potential for damage could not have been known when the event or emission took place, there will be no liability. Emissions that have been authorized by the relevant EU government will not be actionable.[11] The Directive also will not apply to activities the main purpose of which is to serve national defense or international security.[12]

The Directive does not apply to cases of personal injury, to damage to private property or to any economic loss.[13] However, the Directive does not take away any rights of compensation for traditional damage granted under any relevant laws or international agreement regulating civil liability.[14]

The following prerequisites must be in place to establish a prima facie case against an operator: (a) one or more polluters must be identifiable, (b) the damage should be concrete and quantifiable, and (c) a causal link must be established between the damage and the identified polluter(s).[15]

Defenses to liability claims primarily include force majeure, contribution to the damage, or consent, by the plaintiff, and intervention by a third party. Any costs incurred by the operator who is able to invoke any such defenses successfully are recoverable from the Member State involved.[16]

Insolvency per se is not a defense to liability, but it may hinder cost recovery. Member States are encouraged by the Directive to allow for insurance and proper financial security arrangements during the Directive implementation process to minimize the impact of insolvency. Such measures are to be voluntary for at least six years, when the EU will again consider a mandatory scheme.[17]

Conclusion

It is possible that a strict liability standard for damage to health and environment caused by inherently dangerous occupational activities, and fault-based liability for damage to biodiversity caused by non-dangerous activity, may cause confusion and available exemptions and defenses may lower the number of cases ruled in favor of plaintiffs. However, it may be the case that the inclusion of damages caused by non-hazardous substances could lead to a higher number of cases than if the Directive covered only damages caused by hazardous substances.

Whether the availability of the Directive will serve as a useful deterrent to would-be environmental polluters and/or will instigate a wave of litigation is not yet determinable. However, arguing against such a wave is (a) the probability that litigation costs for plaintiffs will be high in the EU and (b) the example of Germany which already has a similar, but not identical, environmental liability regime under which very few cases have been brought.[18]

Counsel to companies operating in the EU should in any event advise clients to (a) implement pollution prevention measures to obviate the need for concern about untold liability and (b) carry appropriate insurance to cover the cost of unexpected clean-up bills.

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Endnotes

1. *See* Environmental Liability Directive, EU Council and Parliament approved joint text, 10 March 2004, p. 2.
2. *See* Janet Stone McGuigan at request of EU Commission, *Potential Economic Impact of Environmental Liability: The American and European Contexts* ("McGuigan"), December 2000, p. 23.
3. Directive, p. 4, para. (8) and Annex III.
4. Directive, p. 5, para. (9).
5. Directive, p. 7, para. (19); p. 8, para. (22).
6. Directive, p. 10, para. (29).
7. Directive, p. 9, paras. (24), (25) and (26).
8. Directive, p. 7, para (18).
9. Directive, p. 7, para. (18), p. 8, para. (23).
10. Directive, p. 10, para. (30).
11. Directive, p. 24, 4(a) and (b).
12. Directive p. 19, Article 4.
13. Directive, p. 6, para. (14), p. 17, 3.
14. Directive, p. 6, para. (12).
15. Directive, p. 6, para. (13).
16. Directive, p. 8, para. (20), p. 23, 3.
17. Directive, p. 6, para. (27).
18. Janet Stone McGuigan at request of EU Commission, *Potential Economic Impact of Environmental Liability: The American and European Contexts,* December 2000, p. 25.

Italy

The Italian Labor Market Reform: Old Problems and New Opportunities

1. Introduction

During 2003, a significant reform of the Italian labor market occurred, which should radically transform the framework within which companies and employees operate. The reform offers numerous advantages and opportunities and some new liabilities for companies operating in Italy.

This article addresses the main changes in the Italian labor law—following the entry into force of Legislative Decree No. 276, the so-called "Biagi[1] Law" on October 24, 2003 (the "Reform"). Its full implementation is subject to both the Ministry of Labour and National Collective Bargaining delegation. Accordingly, the full picture will only emerge after the next few months.

2. The Framework of the Reform

The Reform covers a wide range of topics and is intended to lead to a more structured and better coordinated employment system. The Reform will apply only in the private sector. The main innovations introduced by the Reform are as follows:

- end of the public monopoly on job placement services: private employment agencies will be allowed for these services;
- greater ability for companies to enter into staff leasing agreements for a definite or indefinite term (both conditioned to certain requirements);
- regulation of employee secondment and more flexibility for companies with respect to business transfer and outsourcing;
- introduction of new forms of employment contracts, such as job on call and job sharing;
- greater flexibility in part-time jobs;
- new regulation of the self-employment agreements.

Private Employment Agencies

Public employment structures (the so called Employment Centers) will now be assisted by Private Employment Agencies, which shall provide the following services: staff leasing both for an indefinite and a definite term, recruitment, assistance in personnel replacement and training.

Such agencies shall operate on the basis of a sole ministerial authorization (conditioned on certain economic requirements) and shall be distinguished as follows: (i) staff supply agencies, either general (i.e.,

authorized to deal with all types of definite and indefinite-term staff supply contracts) or special (i.e., authorized to exclusively deal with a specific type of indefinite-term staff supply contract); (ii) labor intermediation agencies; (iii) recruitment agencies; (iv) outplacement agencies. The current obligation for employment agencies to have a corporate purpose exclusively focusing on the single activity actually performed shall no longer exist, with a view to encouraging the establishment of multi-functional agencies.

The Reform also introduced an information technology system (literally, "Labor Exchange") able to contribute to matching labor demand and supply, thus favoring entrance to the market and recruitment by companies.

Staff Leasing

Companies are now allowed to lease staff both for a definite and indefinite term. In particular,

(a) indefinite term agreements are now allowed in 15 different situations specifically identified in the Reform, including—among others—cleaning service, management consultancy, personal management, recruitment and management of call centers;

(b) indefinite term agreements are permitted for technical, productive, organizational or substitution reasons.

The prohibition of replacing employees on strike or in productive units where collective dismissals took place in the last six months is still in force, while the prohibition to contract out personnel has been eliminated.

Finally, the Reform has introduced a distinction between service contracts and staff leasing, under his control.

Secondment

For the first time in Italy the secondment of employees is regulated by a statutory provision. The definition set out by the Reform confirms the three conditions stated by case law in order to have a lawful secondment, i.e.:

(c) the employer must have a significant interest in the employee performing his duties in favor of another entity;

(d) the assignment must be for a definite term;

(e) the seconding employer remains responsible for the employment relationship with the secondee.

Business Transfer

In line with the provisions set forth by recent EU legislation (relating to the safeguarding of employee rights in the event of transfers of businesses or parts of it), additional amendments have been made to the definition of business transfer (art. 2112 of the Italian Civil Code). In particular,

(f) as far as a transfer of part of a business is concerned, transferor and transferee shall identify the part of business itself in the relevant transfer agreement (with respect to previous legal provisions, more flexibility is granted to the parties since it is no longer required that the part of business pre-exist to the transfer);

(g) the transferor and the transferee shall be jointly liable for the labor concerns if the part of business transferred is used by the transferee in order to perform a contract entered into with the transferor (i.e., if it is "outsourcing").

Moreover, in order to simplify fulfillment of the obligations set out by payroll, social security and welfare regulations, companies belonging to groups of undertakings shall be allowed to entrust the parent company with the fulfillment of such obligations also with respect to employees of other companies of the Group.

New Types of "Flexible" Employment Agreements

The following new forms of employment agreements have also been introduced to provide greater flexibility:

(a) Job on call, pursuant to which an employee makes himself available to the employer, who may use his occasional performance (within the limits to be set out in the national collective agreements). The agreement shall set out—among other things—duration, place of work and according to which conditions the employee shall be available (there is a minimum work notice of one working day). The economic and regulatory treatment granted to the employee has to be adjusted with respect to the activities actually carried out and the relevant availability indemnity.

Finally, job on call agreements may be entered into for a definite or an indefinite term, and the employee may be contractually obliged to be available in case of call.

(b) Job sharing. Under this agreement (only) two employees jointly undertake to fulfill a work

obligation, for which each employee shall remain personally and directly liable. The job sharers can decide how to replace one another, at any time and at their own discretion.

Replacement by third parties is instead forbidden, unless it has been agreed with the employer. Moreover, resignation by or dismissal of one of the jointly liable employees shall cause the termination of the whole; on the contrary, should one of the two employees be willing (subject to the employer's consent) to perform the obligation in full (or partially), the agreement shall become an ordinary employment agreement.

(c) Placement agreements. These are particular types of agreements aimed at placing or replacing certain categories of employees on the labor market (i.e., young people between 18 and 29 years of age, long-term unemployed, employees over 45 without any job, women residing in areas having low female employment rates, disabled, etc.).

Except for the short term (between nine and 18 months), it is interesting to notice that the employee can be categorized two levels below the category of an employee performing corresponding duties, and employees who have been employed according to a placement agreement shall not be taken into account in the calculation of the limits set out by the law and national collective agreements for the purposes of applying particular rules.

Part-time Work

The rules governing part-time work have been substantially modified. Most importantly, for the first time

(i) pursuant to horizontal part-time agreements, employees can be required to work overtime (i.e., beyond the working hours set forth in the agreement) upon the application of the same terms and conditions applied to full-time employees: an employee's refusal to work overtime does not constitute a justified ground for dismissal (as well as in case of refusal to convert a part-time agreement to a full-time agreement and vice versa).

(ii) with respect to vertical and mixed part-time jobs only, it is now possible to provide flexible clauses concerning an increase in the work period. The terms and procedures to introduce such clauses will be set out by the National Collective Bargaining.

Moreover, the following existing obligations of the employer have been eliminated:

(i) hiring part-time employees who have asked to convert their agreements to a full-time agreement, before hiring new full-time personnel;

(ii) where requested, to "adequately provide the reasons" underlying the refusal to convert a part-time agreement into a full-time agreement in case of new hiring.

Consultant Agreements

In general, ongoing consultancy relationships will be permitted only when related to the execution of one or more specific projects or work programs or stages thereof. These must be autonomously managed by the collaborator who will be required to achieve a specific result.

Consultancy agreements focusing on a specific project shall be entered into in writing and shall specify, among other things, the duration of the relationship (either determined or determinable), the criteria to be adopted for the determination of the remuneration and the relevant amount (which shall be in proportion to the quantity and quality of the work performed), the expiration dates and terms of payment, and the rules governing the refund of expenses.

In the absence of the above requirements, the consultants shall be considered subordinate employees on an open-term basis, effective from the beginning of the relationship, apart from the following activities that are considered as—occasional—consultancies:

(a) occasional work, i.e., work executed for a term not exceeding thirty days during a calendar year, for the same employer, except in the event that the remuneration obtained in the same calendar year exceeds Euro 5,000 (in such case the provisions concerning project work shall apply);

(b) occasional work of an accessory nature carried out by particular individuals. Such activities are merely of an occasional nature (petty housework, private lessons, petty gardening, etc.) and are carried out by particular individuals (unemployed, housewives, students, pensioners, disabled, etc.).

Finally, with respect to Registered Professionals and to members of Boards of Directors (or Sole Directors), their activities shall continue to be considered as self-employees with a consultancy agreement: as a consequence they shall not be subject to the new provisions concerning project works.

3. Conclusions

The Reform has introduced several innovations in Italian labor law, which will now amend employment

relations significantly. The aim of the government is to give a solution to a twofold problem: the intricate structure of Italian labor law (which has led to a low rate of employment, a high level of long-term unemployment and the spread of the underground economy) and, on the other hand, the ideological and political suspicions related to the way in which the legal framework must change (overall, the strong reserves of the unions and confederations).

The introduction of a high degree of flexibility in labor organization should help solve such problems, as it addresses a number of the most important issues relating to doing business in Italy: making the Italian market far more attractive from a labor law perspective.

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Endnote

1. Marco Biagi, an Italian labor law and industrial relations expert and government consultant, was murdered in Bologna by terrorists on March 19, 2002. He was one of the group responsible for drafting the government's controversial White Paper on labor market reform, which contains most of the innovations set out by the Reform.

Italian Corporate Law Reform and the Role of Directors in Italian Limited Liability Companies

The deep innovations brought by the Italian corporate reform entered into force in January 2004 have been greeted with a common feeling that new and more flexible rules were finally introduced, with a view toward increasing the harmonization of Italy's rules with those of the U.S. and the other countries of the European Union, as well as encouraging foreign investments in the Italian market.

This article intends to focus on the role of the directors in Italian limited liability companies, as modified (or enhanced, if you wish) by the reform, and attempts to make some analogies with the classic dynamics of a board of a U.S. corporation, with respect to their duties and their independence.

1. The Central Role of the Board of Directors

The reform has undoubtedly revitalized the role of the board. Many novelties have been introduced; whereas a complete summary thereof would be out of the scope of this article, we would like to sketch out below an overview of the most "intriguing" news (for the two main types of Italian limited liability companies), sufficient however to give an idea of how Italian corporate law has been reorganized on the point as a consequence of the long-awaited reform. As a preliminary remark, it must be noted that the two main types of Italian limited liability companies are *societa' a responsabilita' limitata* and *societa' per azioni*. Very broadly, the main difference between the two is that the *societa' a responsabilita' limitata* is generally used for smaller businesses and by a smaller number of shareholders in search of a particularly sensible corporate vehicle, while the *societa' per azioni*, is generally used for greater businesses and a larger base of shareholders.

Firstly, it is probably worth mentioning that, as of this year, the *societa' per azioni* can have new models for the directors' management of the company. They may leave the regular scheme of having a sole director or board of directors (along, of course, with the board of statutory auditors), to land in a modern "monistic" model, where the board is supported by an internal committee deputed to the control of the management, or even to a "dualistic" model, where a surveillance committee and a management committee can be added to the board.

It is also interesting to note how the reform (new article 2381 of the civil code) finally takes into consideration the different role of the *amministratore delegato* in the *societa' per azioni* (i.e., a managing director of the company, who is chosen among the members of the board and who is generally entrusted with broad managing powers) and the other members of the board, including the chairman, by providing for definite roles for each of those bodies.

The chairman of a *societa' per azioni* does not have managing powers, being instead in charge of the correct functioning of the board (i.e., calling of the board meetings, defining the meetings' agendas, coordinating the works and making sure that all the members of the board have the information necessary on the items on the agenda).

The "big player" in the *societa' per azioni* will be the *amministratore delegato*, who finally sees his role recognized also by the law: he will have to (i) manage the company, in the limits provided by the delegation of powers of the members of the board; (ii) set up an efficient organization of the business under any profile (its competences depending, however, on the model of management which the company chooses); (iii) periodically refer to the board and the statutory auditors and at least once every six months.

The board of a *societa' per azioni* will resolve the most important matters relating to the management, which cannot be delegated or have not been delegated; in addition, it can give binding directions to the *ammin-*

istratore delegato and decide to resolve on matters which had been delegated to the *amministratore delegato*.

Directors (of both a *societa' per azioni* and a *societa' a responsabilita' limitata*) are also granted with the power (unless the company's bylaws otherwise provide) to issue company bonds, which, previously to the reform, was a task strictly reserved to the shareholders.[1] Bonds issued by a *societa' a responsabilita' limitata* can, however, be subscribed only by professional investors (e.g., banks, insurance companies, pension funds).

The board of directors of either a *societa' per azioni* or a *societa' a responsabilita' limitata*, if the company's bylaws so provide, may even resolve upon the mergers in those cases where the incorporating company owns at least 90% of the corporate capital of the company to be incorporated. Directors can resolve on the creation or cancellation of secondary offices of the company. They may decide on what directors will have the representation of the company. They will be able to decide on the reduction of the corporate capital of the company in case of withdrawal of a shareholder, as well as on the transfer of the registered office of the company (within Italy).

The directors of a *societa' a responsabilita' limitata*, provided that the company's bylaws expressly set forth the hypotheses of exclusion of the shareholders from the company's ownership, may resolve upon the exclusion of same shareholder, when such circumstances actually occur.

With the above probably the most important innovations as far as the rules on the board of directors are concerned, it is now important to verify what kind of liability regime is ancillary to the role of a director of an Italian corporation.

2. The Regime of Directors' Liability

Italian law did not nominally set forth the obligations of the directors of a limited liability company, nor it does now, notwithstanding the reform. This is so because the legislators did not deem it convenient to list them, as this would probably have the effect of narrowing somehow directors' possible liability. We examine in this paragraph the discipline for the *societa' per azioni*, which is more articulated in this respect than the one set forth for the *societa' a responsabilita' limitata*.

Article 2392 of the civil code (which survived, at least partially, to the reform) makes generic reference to the duties deriving from law and the incorporation deed.[2]

The source for directors' liability is the failure to comply with the above mentioned obligations with the necessary diligence, provided that the company has suffered from an actual damage as a result of such failure. However, Article 2392 of the civil code introduces a new parameter: the diligence applied by the directors is not anymore the generic diligence to be applied by the *mandatario* (a sort of agent), as provided before the reform; it is a new and enhanced, and even more rigid, degree of diligence, as it is the diligence "*required by the nature of the task and by the directors' specific skillfulness.*"

Also, the last paragraph of article 2381 of the Italian civil code, as reformed, finally contains these specific words: "*the directors have to act in an informed way.*"

Such new wording added by the reform to substantiate the care to be exercised by the directors in doing their job resembles, now more closely, the standard of care with which directors of U.S. corporations have to comply as well. Information must be at the basis of the decision-making process of a U.S. corporation's director, as well as it must be for Italian companies' directors. As mentioned, the "Italian" standard of care has been upgraded as well, being similar now to the standard of care provided by the Model Business Corporations Act, where reference is made to the "*care that a person in a like position would reasonably believe appropriate under similar circumstances.*" The background and the qualifications of a director may be relevant in verifying his compliance with the standard of care.

Analogies between the two legislations exist also with respect to the duty of loyalty imposed on U.S. corporations' directors. Duty of loyalty essentially means that a director must demonstrate unyielding loyalty to the company and the company's shareholders: this basically translates into prohibition of self-dealing, penalizing transactions carried out in conflict of interest.

The conflict of interest situation is also very much taken into consideration by Italian law. Article 2390 sets forth that the directors cannot be shareholders with unlimited liability in companies in competition with the company of which they are directors, nor carry out (on their behalf or on behalf of third parties) an activity in competition with that of the company, nor be directors or *direttori generali* (sort of general managers) in such companies. On the other side, article 2391 of the Italian civil code sets forth a procedure aimed at regulating situations in which actual conflict arises. Pursuant to this provision, the director has to inform the other directors and the board of statutory auditors of any interest which he or she has (even on behalf of third parties) in a given company's transaction, specifying the nature of the interest itself, its terms, origin and extension. If the director in conflict of interest is the *amministratore delegato*, he has to refrain from carrying out such transaction, by referring to the board. Failure to comply with such provision results in the personal liability of the

director for the damages suffered by the company as a result of such failure; by the same token, the director will be liable for the damages suffered by the company as a result of the use to his or her own advantage of the data, news or business opportunities of which he or she became aware while exercising his or her functions as a director.[3]

However, directors have their "business judgment rule" under Italian practice, too. According to solid case law, the court which has to examine the possible grounds of a liability action against a director cannot judge on the basis of criteria based on the opportunity or convenience, as in this way it would substitute its "ex post" judgment to that expressed by the board; the only verification the court has to carry out is whether the directors are in breach of their obligations. As it happens in the US, therefore, Italian law does not impose on the director the obligation of managing the company without making mistakes, but only to comply with certain standards.

No standard requires the director to be "independent," but this is becoming an issue in Italy, particularly with reference to large public companies. Below is a summary of where Italian law stands in this connection.

3. The Requisite of Independence

Although a controversial issue,[4] many consider an independent director a better director.

The reform has introduced certain provisions regarding the independence of the directors in a company. Article 2387 (applicable to *societa' per azioni*), as modified by the reform, provides the possibility for a limited liability company (not necessarily public) to subordinate the "*hiring*" of a director to the possession of special requisites of honorability, professionalism and independence, even by referring to the requisites "ad hoc" provided, for instance, by the Corporate Governance Code of the *Borsa Italiana*. This is a collection of guidance rules set forth by *Borsa Italiana* and applicable only to listed companies, provides that (article 3.1) "*an adequate number of non-executive directors shall be independent*" and (article 3.2) "*directors' independence shall be periodically assessed by the board of directors. . . . The results of the assessment shall be communicated to the market.*" The Corporate Governance Code is not of mandatory application for listed companies, but it is a *best practice model* that can be adopted by them.

Furthermore, article 2409—*septiesdecies* (with specific reference to the new case of the monistic model of the *societa' per azioni*) provides that at least one-third of the members of the board of directors has to be "*independent*," in accordance with the criteria set forth by article 2399 with respect to the members of the board of statutory auditors.[5] It also provides that, if so provided by the company's by-laws, the directors shall have the requisites of independence provided by the Corporate Governance Code or similar code.[6]

Curiously enough, it seems that the same tendency is present in the United States. A recent IRRC study on board structure and practices found that only 7% of the 1,200 U.S. public companies surveyed had a truly independent chairman who was not a current or former employee or otherwise affiliated with the company. Moreover, many shareholders are of the opinion that U.S. companies would benefit most from two separate individuals holding, respectively, the CEO and chairman positions. And, recent legislative and regulatory changes (including the Sarbanes-Oxley Act of 2002) are aimed at increasing the authority and independence of a company's board.

4. Considerations

The Italian reform seems to be in line with most of the expectations that the law operators had, in order to enjoy a more flexible and versatile corporate legislation. The novelties exposed with reference to the board of directors combine with other very interesting modifications in corporate law, among which, it may be worth to mention the possibility for *societa' per azioni* to issue tracking stocks, the new discipline on shareholders' agreement, the broadest powers of self-regulation granted to the shareholders of the *societa' a responsabilita' limitata* and many others. The new corporate law also matches the reform of Italian labor law which, modifying substantially the legal framework then existing, now gives the employers the opportunity to hire employees under a high number of different schemes and not only through the indefinite term contract. Another effort of the Italian legislator has been represented by the passing of the national tax reform, essentially aimed at creating in Italy a tax environment competitive with those existing in other EU countries. In other words, a serious and complete attempt to render Italy more aggressive in that difficult market represented by the countries in which investing today is worthy.

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Endnotes

1. Unless in case the company's bylaws expressly provided that the board was granted with the power of issuing bonds, for a period, however, not exceeding five years and leaving to the shareholders the determination of the maximum amount of leverage.
2. The Italian civil code does list some of the directors' obligations, but it is not exhaustive.
3. The relevant board resolution is also subject to challenge, subject to certain conditions.
4. J.D. Westphal, in *Second Thoughts on Board Independence: Why do so many demand board independence when it does so little good?*, stated that "Nearly two decades of research find little evidence that

board independence enhances board effectiveness. Studies have, however, found a negative effect."

5. Such requisites prevent the appointment of, among others, the spouse, the relatives and the relatives-in-law of the directors of the company; those who are related to the company or to the subsidiaries of the company or its controlled companies, due to an employment relationship or a consultancy relationship, or through other relationships for a consideration which may jeopardize the independence of the same directors.
6. The provision of article 2409—*septiesdecies* is justified by the circumstance that, in the monistic model, the board of directors appoints the committee on the control of the management within its members; as the committee (whose tasks are similar to the board of statutory auditors) has to be composed by independent members only, this explains why the provision on the independence applies to the board of directors.

Monaco

Lack of Income Taxation in Monaco and Implications with International Tax Evasion and Money Laundering

The Principality of Monaco ("Monaco" or the "Principality" or the "Country") has not enacted any legislation that requires the filing of a declaration of assets.

The local tax system does not impose any direct taxation on an individual's wealth, whether Monegasque or foreign, who lives in the Principality.

However under the bilateral Tax Convention signed between France and Monaco on December 23, 1951, and May 18, 1963, French nationals resident in the Principality are considered as having their fiscal domicile in France and consequently are subject to the French fiscal legislation. This agreement does not apply to French citizens who became a resident before January 1, 1957.

Since Monaco has not signed tax conventions with countries other than France, each country can reserve the right to apply its tax legislation and filing requirements for assets located abroad. However, these declarations would not be filed with the Monegasque tax authorities but with the Monaco resident's home country.

On the other hand, Monaco authorities are aware of the developments concerning the issue of tax evasion and fraud. In fact, the Country has been taking steps to prevent the use of its territory as a haven for funds derived from criminal activities and money laundering. As a consequence, the Principality has reinforced its collaboration with other countries and increased its efforts to comply with the directives of the *Groupe d'Action Financière Internationale* (Financial Action International Group), or GAFI.

Money laundering, tax fraud, tax evasion, and financing of terrorism are just variants of the same problem. The Organization for Economic Co-Operation and Developments ("OECD") currently lists Monaco as a non-cooperative country regarding the exchange of information relating to fiscal questions. Monaco has, nevertheless, undertaken a series of measures to respond to the international standards: developing its campaign against money laundering; fighting the financing of terrorism; strengthening its control over banks to guarantee the security of transactions throughout the Euro Zone; and signing an agreement with the French securities regulators ("COB") to strengthen the exchange of information related to insider trading offenses.

In 1994, the Principality also saw the creation of the specialized service *Service d'Information de Contrôle des Circuits Financiers*, or Department of Information and Control of Financial Trading (SICCFIN), which controls the transfers of suspicious funds and to which financial establishments must make disclosures, should they have any doubts about the legitimacy of funds.

Indeed, co-operation in economic and financial matters between the judicial authorities of Monaco and foreign judicial authorities is frequent and attested by the numerous International Rogatory Letters ("IRL") that the Principality receives every year.

Generally, the investigative demands are executed with reasonable promptness, because Monaco treats these inquiries with the highest level of importance. There is no bank or professional secrecy when economic and financial offenses are involved. The State Prosecutor ("le Parquet") processes the IRL, with the assistance of the courts and the financial sector of the Monaco Police (Brigade Financière de la Sûreté Publique).

The Principality of Monaco has enacted a broad spectrum of legislation, rules, and regulations, established several regulatory bodies to regulate financial activities, and entered into a number of multilateral and bilateral relationships directed to guarantee regularity in financial transactions.

The purpose of these measures is in large part to control money laundering and to prevent insider trading. We believe the purpose of these measures is similar to that of the United States securities laws, namely, to assure integrity in financial markets and prevent financial fraud and abuse. More specifically, these measures Monaco has adopted include:

1. Law 1144 of July 26, 1991, that regulates economic activities;
2. Law 1161 of July 7, 1993, that makes knowingly acquiring funds of illegal origins, participating or attempting to participate in the laundering of such funds a crime;
3. Law 1162 of July 7, 1993, that imposes a number of obligations on banks, brokerage firms, insurance companies, and others that engage in finan-

cial transactions to "know their customer," the source of the funds involved, and to report suspicious transactions, and provides criminal sanctions for failure to do so;

4. Law 1194 of July 9, 1997, that regulates the provision of financial services and which has created the *Commission de Contrôle de la Gestion de Portefeuilles et des Activités Boursières Assimilées* (Commission to Oversee Portfolio Management and Related Stock Exchange Activities);

5. Law 1241 of July 3, 2001, that makes knowingly engaging in insider trading a crime.

More recently, Monaco has also taken numerous diplomatic steps to assure the integrity of financial transactions that take place in the Principality, as follows:

1. On April 8, 2002, Monaco ratified the International Treaty Against Financing of Terrorism;

2. On October 8, 2003, Monaco established a cooperation agreement with the French Banking Commission to reinforce the transparency of banking transactions;

3. On November 3, 2003, Monaco ratified the United States convention against the transnational criminality and its protocols related to the illicit traffic of immigrants.

Another major aspiration of the Principality is to reinforce its collaboration with other countries to prevent investment of funds resulting from illegal transactions or frauds.

In such a perspective the Country has signed numerous bilateral agreements with various European countries—among which are Belgium, Great Britain, Spain, and Portugal—to establish cooperation in tracking money laundering.

On May 4, 2004, the Minister of State signed a further cooperation agreement, which reinforces the cooperation between Monaco and the state of Andorra. This agreement is the product of the successful negotiations between the SICCFIN and the UPB (*Unitat de Prevenció del Blanqueig*).

It is evident that Monaco wishes to present itself as a modern state that is vitally concerned about preventing unlawful financial activities within its borders. Monaco does not want to be a haven where a person can safely hold funds in its banks if those funds result from fraud, insider trading, or other illegal transactions.

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Netherlands

Debt Restructurings Through Parallel Bankruptcy Protection Proceedings in the Netherlands and the U.S.: Convergence of Applicable Rules

I. Introduction

Recent global economic hardship has compelled several Netherlands-based international telecommunication companies to restructure their debts substantially. Bankruptcy protection proceedings have increasingly been used to facilitate these restructurings, with the objective to convert debt into equity in order to reduce interest costs. The international nature of these companies and their investor bases have caused some of these companies to initiate parallel proceedings in the Netherlands and in the United States. In the Netherlands, the Netherlands Bankruptcy Act provides bankruptcy protection through a "suspension of payments" procedure (*surseance van betaling*). In the U.S., Chapter 11 of the United States Bankruptcy Code provides bankruptcy protection.[1]

Bankruptcy protection proceedings require cooperation by the creditors of the company. Generally bondholders are seen as creditors, although nowadays they often do not possess bearer bonds. Instead, the bonds are being held by a common depository.[2] Typically one or more "global notes" are issued to a "global note holder," and individual bondholders are registered with the global note holder. A trustee will be appointed to exercise certain rights connected to the notes. The agreement underlying the global notes is referred to as the "indenture"; the trustee is usually referred to as the "indenture trustee."[3] In this structure the indenture trustee holds a title to the bonds, but the bondholders are the beneficial owners of the bonds. Pursuant to Dutch law, the bondholder should only be regarded as an *economic* beneficiary, which is not the same as beneficial ownership under U.S. law.[4]

The fact that the Netherlands Bankruptcy Act does not explicitly recognize the concept of beneficial ownership, as does U.S. law, can impede the mirroring of U.S. Chapter 11 bankruptcy protection proceedings. In particular, this conceptual difference may cause a different outcome as to who is entitled to vote on the "plan of composition," the agreement by which creditors approve of the renewed terms of their claims. This article discusses the complications that may arise from the differences between the Dutch and U.S. bankruptcy regimes, and focuses on the solutions that have been applied by the Amsterdam District Court in this respect.

First, we will offer a brief introduction to the Dutch suspension of payments procedure pursuant to the Netherlands Bankruptcy Act. We will then proceed to highlight some significant differences between the Dutch suspension of payments procedure and Chapter 11 of the U.S. Bankruptcy Code and analyze the complications that may arise when combining these two procedures. Subsequently, we will provide an overview of some recent debt restructurings in the Netherlands and the solutions that have been applied by the Amsterdam District Court.

II. "Fast Track" Suspension of Payments in the Netherlands

In order to have a plan of composition adopted within the shortest period possible, a debtor in possession will typically initiate a "fast track" suspension of payments procedure. A fast track procedure under the Netherlands Bankruptcy Act usually takes place along the following lines.[5] First, restructuring agreements need to be negotiated among the debtor and its bondholders. Such agreements usually consist of a commitment by the bondholders that they will vote in favor of the future plan of composition.[6] In doing so, they may explicitly consent to a debt-for-equity swap, depending on the purpose of the restructuring. In addition, restructuring agreements may stipulate modifications of the indentures in order to eliminate certain specific default provisions and facilitate the restructuring, and may further contain detailed provisions regarding the future position of shareholders.[7]

Once the restructuring agreements have been entered into, the debtor files a petition for suspension of payments at the District Court and at the same time submits a draft plan of composition that is in conformity with the restructuring agreements.[8] In this fast-track procedure, the District Court will instantly grant provisional suspension of payments and schedule a meeting of the creditors in which the plan of composition shall be put to a vote.[9] The Netherlands Bankruptcy Act requires that approval of the plan of composition be given by at least two-thirds of the creditors that submitted their claims, representing at least three-fourths of the net worth of the admitted claims.[10]

Upon approval by the creditors, the plan of composition will have to be ratified by the Court (*homologatie*). The Court will refuse to ratify the plan in any of the following circumstances: (i) if the value of the assets of the estate considerably exceeds the amount that was offered in the plan of composition; (ii) if performance of the plan of composition is not sufficiently guaranteed by the terms of the plan of composition; (iii) if the plan of composition was achieved by fraud or the preferential treatment of one or more creditors or by any other unfair means, whether or not the debtor or any other person participated therein; and (iv) if fees and expenses of experts and of the administrator have not been paid to the administrator, nor security has been issued therefor.[11] Ratification may also be refused on any other grounds as well as *ex officio*.[12] Ratification of the plan of composition, once the issue is closed to appeals, terminates the suspension of payments procedure and provides a title of enforcement for the creditors.[13]

III. Dutch Suspension of Payments Procedures in Relation to Chapter 11 of the U.S. Bankruptcy Code

The Dutch suspension of payments procedure described in the previous paragraph is to a certain extent comparable to bankruptcy protection under Chapter 11 of the U.S. Bankruptcy Code.[14] The objective of both regulations is to facilitate financial restructuring and reorganization of the company.[15] However, some significant differences exist. The following discussion offers an overview of the major differences.

Pursuant to section 215 of the Netherlands Bankruptcy Act, the Court appoints an administrator who is entitled to conduct the business of the debtor jointly with the debtor, commonly referred to as the "debtor in possession."[16] Mutual consent is required to perform acts of administration or to dispose of assets of the estate, and consequently a certain degree of supervision is created in order to protect the interest of the creditors. Under Chapter 11 of the U.S. Bankruptcy Code, the debtor in possession retains full powers to act in the ordinary course of business.[17] In addition, the U.S. Bankruptcy Code provides for an automatic stay on actions against the estate.[18] Under the Netherlands Bankruptcy Act, a period of an automatic stay can also be ordered, but this is restricted to a period of one month with an optional extension of one month.[19] During this period, creditors that have a claim that is secured by a mortgage, pledge or any other privileged right cannot execute this right. It should be noted that the Netherlands Bankruptcy Act does not require the debtor in possession to make any disclosure statements regarding the business, whereas the U.S. Bankruptcy Code does impose such requirements.[20]

Whereas the Dutch suspension of payments rules have been designed to redefine creditors' interests, Chapter 11 provides for an opportunity to take equity interests into account.[21] Suspension of payments under Dutch law only applies to non-preferential or ordinary creditors that do not have a claim that is secured by a mortgage, pledge or any other privileged right, and therefore has a limited scope.[22] Under Chapter 11, different classes of creditors and interests may be designated, and each class will have to vote in favor of the plan of composition, unless the Court decides to "cram down" the plan.[23]

In light of the financing structure described earlier, one difference that is particularly interesting is that the Netherlands Bankruptcy Act does not explicitly recognize the concept of beneficial ownership, as does U.S. law. This conceptual difference can impede the mirroring of Chapter 11 procedures, in particular with regard to the acceptance of the plan of composition. The next paragraph discusses these impediments and the solutions that have been applied by the Dutch courts in several recent cases.

IV. The Voting on the Plan of Composition

Pursuant to the Netherlands Bankruptcy Act, the indenture trustee in his capacity as the legal owner of the global note is normally, depending on the terms of the indenture, to be seen as a creditor of the debtor in possession.[24] As a consequence, the indenture trustee is exclusively entitled to submit a claim and to vote on the plan of composition.[25] Bondholders, although recognized as *economic* beneficiaries, do not have any rights in this respect. However, the indenture trustee will generally be contractually prohibited from voting on the plan of composition. Under the Netherlands Bankruptcy Act, abstention will be regarded as a negative vote, and thus, by not voting, the trustee may in effect renounce the plan of composition. But even if the indenture trustee would not be contractually prohibited from voting, its vote would only be recognized as one single vote instead of the amount of votes represented by the bonds entrusted to the indenture trustee. Clearly, this situation would not correspond to economic reality and would be highly undesirable from a practical perspective.

As far as Chapter 11 procedures are concerned, the concept of beneficial ownership enables the bondholders to validly cast their votes. Clearing organizations distribute ballots to the bondholders who can subsequently submit their ballots to a clearing organization or a bank. The clearing organization or bank will then submit the "master" ballot to a ballot agent appointed by Court order. A voting record date is set by the Court, thus enabling continuation of trade in the period between the voting record date and the confirmation hearing.

In parallel proceedings in the U.S. and the Netherlands, for reasons of efficiency and consistency it is desirable that the voting process can be synchronized and that each bondholder is entitled to cast its vote on the plan of composition in a transparent manner.[26] The Amsterdam District Court has recognized this need in a series of three restructurings that are discussed here. The first time that this issue was explicitly addressed by the Amsterdam District Court was in 2002 with the restructuring of Global TeleSystems Europe B.V. ("GTS Europe"), a fully owned indirect subsidiary of Global TeleSystems Inc.[27] The objective of this restructuring was to convert bonds issued by GTS Europe into bonds issued by KPNQwest N.V., the company that was to acquire GTS Europe as a part of the greater Global TeleSystems Inc. restructuring.

In the GTS restructuring, parallel proceedings in the U.S. and the Netherlands had been initiated on November 14, 2001. Upon acceptance of the plan of composition in the U.S. by an overwhelming majority of the creditors, the Amsterdam District Court was requested to adopt the results of the voting since they were supposed to accurately represent the opinion of the creditors. Pursuant to section 225 of the Netherlands Bankruptcy Act, the Court has the power to set out specific rules with regard to a suspension of payments procedure, if that would be required in the interest of creditors.[28] Such rules may deviate from the standard procedure prescribed in the Netherlands Bankruptcy Act. In its judgment, the Amsterdam District Court contemplated that "*it would be contrary to economic reality to qualify the legal owner as the sole creditor instead of the truly interested parties, the beneficial owners.*"[29] Accordingly the Amsterdam District Court, using the power granted by section 225 of the Netherlands Bankruptcy Act, held that applying the voting results of the U.S. plan of composition would indeed correspond with the rationale of the Netherlands Bankruptcy Act. Therefore, the U.S. voting results would be accepted in the Dutch proceeding.[30] In this landmark case the Amsterdam District Court first recognized the concept of beneficial ownership and applied the concept within the framework of the Netherlands Bankruptcy Act, in order to find a practical solution to the complications that arise when combining a Dutch suspension of payments procedure with a U.S. Chapter 11 procedure.

Another recent restructuring combining a Dutch suspension of payments procedure with a U.S. Chapter 11 procedure is the restructuring of Versatel Telecom International N.V. ('Versatel').[31] This restructuring aimed at converting all of Versatel's outstanding high yield convertible bonds and loans (to the amount of approximately EUR 1.7 billion) into a combination of equity (approximately 365.4 million new ordinary shares, representing an 80% interest in Versatel) and cash (approximately EUR 343 million).

In the Versatel restructuring, a request was filed with the Amsterdam District Court simultaneously with the initial request for suspension of payments to allow bondholders to submit their claims on the U.S. voting record date, consequently entitling these bondholders to vote on the Dutch plan of composition. The Amsterdam District Court granted this request and decided accordingly, consistent with its authority deriving from section 225 of the Netherlands Bankruptcy Act. In doing so, the Amsterdam District Court reconfirmed the concept of beneficial ownership and showed its willingness

to grant the beneficial owners the right to submit their claim and to vote on a voting record date. The difference here was that the Amsterdam District Court did not, as in the GTS restructuring, apply the voting results of the U.S. procedure directly on the Dutch procedure. Instead, the bondholders were entitled to vote separately on the Dutch plan of composition.

Finally, a third restructuring combining a Dutch suspension of payment procedure with a Chapter 11 procedure is the restructuring of United Pan-Europe Communications N.V. ("UPC").[32] In this restructuring, a significant part of UPC's outstanding consolidated debt was to be eliminated by converting UPC's "Belmarken" notes (with an accrued value of EUR 925 million) and UPC notes (with an accrued value of EUR 4.3 billion) into new common stock.

In the UPC Dutch suspension of payment procedure, again, a request was filed with the Amsterdam District Court to allow bondholders to submit their claims on the U.S. voting record date and to vote on the Dutch plan of composition. This time, the Amsterdam District Court determined that the beneficial owners of the notes at the voting record date, as determined by the U.S. Court, would be *exclusively* entitled to submit their claims with the administrator and to vote on the Dutch plan of composition. Thus, the indenture trustee, although regarded as legal owner pursuant to this ruling, did not have a right to vote as a creditor of the debtor in possession. Previously, qualification of the indenture trustee as the legal owner had led to a situation in which the indenture trustee was regarded as a single creditor legally permitted to cast only one vote on the Dutch plan of composition. Now, upon authorization by the bondholders, the indenture trustee could be entitled to represent the total amount of votes in favor of the plan of composition that were submitted by the bondholders, on behalf of those bondholders. On August 26, 2003, the Dutch Supreme Court confirmed the validity of the use by the District Court of section 225 of the Netherlands Bankruptcy Act to allow beneficial owners to vote on the plan of composition and to set a voting record date, in the interest of the creditors.[33] According to the Supreme Court, the specific circumstances surrounding this case, notably the fact that the indenture was governed by New York law, and that pursuant to both the indenture as well as New York law the bondholders had been exclusively entitled to vote on the plan of composition in the parallel U.S. Chapter 11 procedure, justified the entitlement of the beneficial owners to vote on the Dutch plan of composition.[34] With regard to the voting record date, the Supreme Court stated that the Netherlands Bankruptcy Act does not prohibit the use of a voting record date if this is required for practical reasons.[35] The Supreme Court noted, however, that the period between the voting record date and the voting on the plan of composition should not be too long.[36]

V. Conclusion

Over the past few years, significant debt restructurings have taken place through parallel bankruptcy protection proceedings in the Netherlands and the U.S. Parallel proceedings require a synchronized and consistent voting process in order for both the U.S. and the Dutch plans of composition to be accepted at the same time. Although the concept of beneficial ownership is not explicitly recognized in the Netherlands Bankruptcy Act, the Amsterdam District Court has recognized bondholders as beneficial owners and set a voting record date in a series of decisions, by the use of a special provision in the Netherlands Bankruptcy Act. The Dutch Supreme Court has confirmed that under specific circumstances the use by the District Court of such measures may be justified. Pursuant to these decisions, upon request bondholders can now be found exclusively entitled to submit a claim and to vote on the Dutch plan of composition in case of parallel bankruptcy protection proceedings in the Netherlands and the U.S.

In the Versatel and UPC restructurings discussed in this article, the company that filed for suspension of payments requested the Amsterdam District Court to determine that the beneficial owners were entitled to submit claims and to vote on the plan of composition. The Amsterdam District Court concluded accordingly and subsequently a voting record date was set on the same day as the voting record date in the U.S. Chapter 11 procedure. Because restructuring agreements had been negotiated among the debtor in possession and its bondholders, the plan of composition was swiftly accepted and the debt restructuring could proceed according to the business reorganization plan. With the approval by the Dutch Supreme Court of the solutions applied by the Amsterdam District Court, Dutch law can now adequately facilitate future debt restructurings through parallel proceedings in the Netherlands and the U.S., consistent with the needs of modern financing practice.

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Endnotes

1. 11 U.S.C. §§ 1101 *et seq.* The authors wish to express that this article is written from a Dutch legal perspective and does not claim to provide an in-depth analysis of the United States Bankruptcy Code in this respect.
2. In practice, clearing organizations such as Euroclear, Clearstream and DTC are normally used as common depositories.
3. The indenture is typically governed by the laws of the state of New York.

4. C.M. Harmsen, *Van GTS tot Versatel; de Surseance van Betaling als Instrument voor Internationale Herstructurering*, Jurisprudentie Onderneming & Recht *plus*, 2003, (hereinafter Harmsen: Van GTS tot Versatel) at 27.
5. Netherlands Bankruptcy Act §§ 213 to 283.
6. Mr. P.R.W. Schaink, *Surseance als Vehikel voor Debt-for-Equity Swaps*, Ondernemingsrecht 2003-5 (2003) (hereinafter Schaink: Surseance als Vehikel) at 173.
7. *Id.*
8. Netherlands Bankruptcy Act § 214, subsection 2.
9. *Id*. § 255.
10. *Id*. § 268.
11. *Id*. § 272, subsection 2. *See also* Peter J.M. Declerq, Netherlands Insolvency Law: The Netherlands Bankruptcy Act and the Most Important Legal Concepts (T.M.C. Asser Press, 2002) (hereinafter Declerq: Netherlands Insolvency Law) at 49.
12. *Id*. § 272, subsection 3.
13. *Id*. §§ 276, 274.
14. 11 U.S.C. §§ 1101 *et seq.*
15. Michael A. Gerber, Business Reorganizations (2nd ed. Lexis Publishing 2000) (hereinafter Gerber: Business Reorganizations) at 6; Declerq: Netherlands Insolvency Law, *supra* note 11, at 34.
16. Netherlands Bankruptcy Act §§ 215 *et seq.*
17. 11 U.S.C. §§ 1107, 1108.
18. 11 U.S.C. § 362.
19. Netherlands Bankruptcy Act § 241a.
20. 11 U.S.C. §§ 521, 1106.
21. *See* 11 U.S.C. §§ 1121 *et seq.*, and *e.g.*, *In re Lionel Corp.*, 722 F.2d 1063 (2d Cir. 1983). *See also* Gerber: Business Reorganizations *supra* note 15, at 597.
22. Netherlands Bankruptcy Act § 232. In light of a project designed to enhance the reorganizational ability of the Netherlands Bankruptcy Act (*Modernisering Faillissementswet*, commonly referred to as the "MDW"-project), several proposals have been made to expand the scope of the suspension of payment procedure. Two bills are currently before parliament but it remains uncertain if and when the current Act will be amended. See, for a more detailed analysis of the MDW-project, Declerq: Netherlands Insolvency Law, *supra* note 11, at 50 and R.J. Botter, *Herstructurering van door Nederlandse Uitgevende Instellingen Uitgegeven Obligaties*, in Een Bewezen Bestaansrecht, Lustrumbundel 2002 Vereniging Effectenrecht (Kluwer 2002), at 42.
23. Pursuant to 11 U.S.C. § 1126(c), a class of claims has accepted a plan if such plan has been accepted by creditors that hold at least two-thirds in amount and more than one-half in number of the allowed claims of such class held by creditors. In addition, the court may decide to confirm a plan that has not been accepted by all classes if "*the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan*." 11 U.S.C. § 1129(b).
24. For an explanation of the definition of a creditor in light of the Netherlands Bankruptcy Act, see N.J. Polak and C.E. Polak, *Faillissementsrecht* (8th ed. Kluwer 1999), at 2.
25. Netherlands Bankruptcy Act §§ 257, 268.
26. With regard to bankruptcy (-protection) proceedings with an international aspect some initiatives have been taken on a supranational level, notably the European Council Regulation nr. 1346/2000 of 29 May 2000 on insolvency proceedings, *available at* http://www.europa.eu.int (last visited on June 9, 2003) and the *Model Law on cross-border Insolvency with Guide to Enactment*, of the United Nations Commission on International Trade Law, available at www.uncitral.org (last visited on June 9, 2003).
27. GTS, Amsterdam District Court, February 21, 2002, *JOR* 2002/107 (hereinafter Amsterdam District Court, February 21, 2002).
28. Netherlands Bankruptcy Act § 225.
29. GTS, Amsterdam District Court February 21, 2002, *supra* note 27, r.o. 15.
30. In *GTS*, based upon section 225 the Court decided to equally apply the rationale of an exception rule for bearer bonds, as set forth in section 260, subsection 2 in conjunction with section 134 of the Netherlands Bankruptcy Act. According to this rule, on the provisional list of creditors, every verified bearer claim is treated as a claim from a separate creditor. For a more detailed analysis of the filed request and the Amsterdam District Court decision, see Schaink: Surseance als Vehikel, *supra* note 6, at 173; Harmsen: Van *GTS* tot Versatel, *supra* note 4, at 28; A.P.K. Luttikhuis, *Rb. Amsterdam 21 februari 2002 (GTS-KPNQuest)*, TvI 2002/5 at 245 and GTS, Amsterdam District Court, February 21, 2002, *supra* note 27, r.o. 10.
31. *Versatel*, ratification of the plan of composition by the Amsterdam District Court on September 18, 2002. This restructuring was preceded by the restructuring of Completel (ratification of the plan of composition by Amsterdam District Court September 4, 2002). In *Completel*, the Amsterdam District Court further developed its reasoning that would ultimately result in the *Versatel*-doctrine. The Completel restructuring is not discussed here because it did not deal with a parallel U.S./Dutch debt procedure. The Versatel restructuring was followed by the restructuring of Netia (ratification of the plan of composition by Amsterdam District Court November 16, 2002), not discussed here for the same reason.
32. *UPC*, ratification of the plan of composition by the Amsterdam District Court on March 13, 2003. The ratification of the plan of composition by the Amsterdam District Court has been appealed by one creditor. The appeal was rejected by the Dutch Court of Appeals on April 15, 2003. (Hof Amsterdam 15 april 2003, JOR 2003/157) Subsequently this decision was appealed to the Dutch Supreme Court. The Dutch Supreme Court rejected this appeal (Dutch Supreme Court, case nr. RO3/049HR). (See below.)
33. Dutch Supreme Court, case nr. RO3/049HR. One interesting aspect of the approval of this specific use of section 225 of the Netherlands Bankruptcy Act is that measures taken by the District Court pursuant to the authority that derives from section 225 can not be appealed (see section 282). This contributes to a swift execution of the plan of composition.
34. Dutch Supreme Court, case nr. RO3/049HR, r.o. 3.8.3.
35. Dutch Supreme Court, case nr. RO3/049HR, r.o. 3.8.5.
36. *Id.* It is not further specified what may be a reasonable period of time.

Spain

The New Spanish Insolvency Regime

On September 1, 2004, a new Insolvency Act enacted on July 9, 2003 will come into force in Spain. This Act, in combination with Organic Law 8/2003 enacted on the same date, will substantially modify the rules governing the insolvency process in Spain in issues such as the ranking of credits, the rights of certain privi-

leged creditors, the so-called "retroactive date" of insolvency proceedings, and the enforceability of contractual early termination clauses based on the declaration of insolvency of one of the parties.

This article summarizes some of the most relevant issues modified by the Act, emphasizing those aspects that affect foreign investors holding a credit against, or otherwise an interest in a Spanish company.

Single Procedure

The two types of insolvency proceedings applicable for corporations—namely, insolvency (*quiebra*) and suspension of payments (*suspensión de pagos*)—have now been replaced by a single procedure (*concurso*). This procedure will apply to individuals and corporations (other than insurance companies, credit institutions or investment undertakings, which are subject to their own special regulations).

The insolvency proceedings will be universal and the insolvency judge will have exclusive jurisdiction over any matter affecting the debtor's estate, including labor-related matters.

Ranking of Creditors

Credits are divided into three categories: privileged, ordinary and subordinated credits. Privileged creditors include (a) secured creditors who have a "special" privilege over specific assets of the debtor, as a result of an *in rem* right created over such asset, and (b) creditors who have a "general" privilege over all assets of the debtor, mainly the employees of the debtor within certain limits, the Spanish Tax and Social Security authorities, credits arising out of tort and 25% of the credit of the creditor who called the insolvency proceedings. Creditors with a general privilege rank junior to specially privileged creditors.

However, the enforcement of secured credits is delayed until the earlier of: (i) the date of approval of the agreement between the debtor and its creditors; or (ii) one year from the declaration of insolvency if the liquidation process of the company has not been initiated, unless the affected asset is not a core asset of the debtor's daily business.

Notarized unsecured creditors that under the previous statutory regimes ranked senior to ordinary creditors and creditors whose right was notarized on a subsequent date are now treated as ordinary creditors.

Certain categories of credits are automatically subordinated by operation of law. As a consequence thereof, in addition to ranking junior to privileged and ordinary creditors, any guarantee of any kind granted to secure those credits is automatically cancelled. In particular, the following categories of credits are legally subordinated: debts that were not claimed on time; contractually subordinated debts; debts arising from interests; debts arising from fines; and debts owing to persons with a special relationship with the debtor ("related parties"). In the case of corporations, the following are considered "related parties": (i) partners with unlimited liability and shareholders holding a stake in excess of 10% of the share capital or 5% if the company is listed; (ii) legal or *de facto* directors, insolvency trustees and nominees holding general powers to bind the bankrupt, and also those who held any of these positions during the two years preceding the insolvency; and (iii) any company belonging to the debtor's group, and their respective shareholders. The concept of de facto directors is not defined under Spanish law and may raise some legitimate concerns as to whether it will be broadly interpreted by the judges to include lenders that have made use of stringent contractual covenants enabling them to monitor the debtor's operations.

Additionally, if the credit is assigned to an unrelated third party within the two years preceding the initiation of the insolvency proceedings, the assignees of these credits will also be held to be related parties for the purposes of the insolvency proceedings if the credit was assigned, although this presumption may be upheld.

It is also noteworthy that the Act will also apply to credits executed before its enactment.

Insolvency Act rules apply only to the ranking of credit rights within insolvency proceedings, while pre-insolvency insolvency situations will continue to be governed by the general provisions of the Spanish Civil Code.

Effects of the Insolvency Proceedings Over Contractual Arrangements

Early termination clauses based on the declaration of insolvency of the debtor or premonitory situations that evidence the debtor's financial distress have become standard in Spanish banking practice. These contractual provisions give the lenders the right to request immediate repayment of amounts withdrawn and even enforce the guarantees securing the loan or credit before the formal insolvency proceedings begin, in order to avoid the effects of insolvency proceedings.

Under Article 61.3 of the Insolvency Act, early termination clauses will be regarded as if they had not been established in the contract. Since the Act literally refers to the declaration of insolvency, it may be argued that this statutory provision may be avoided by including in the contract other early termination provisions that enable the calling of early maturity on the basis of certain events that may take place before or after the initiation of insolvency proceedings and result in a breach of contract.

The above notwithstanding, the scope that the Spanish insolvency judges will give to this provision as regards more general premonitory situations affecting the financial situation of the creditor is still uncertain.

In addition to the foregoing, the Act also enables the insolvency judge to reactivate loan agreements that were early terminated during the three months preceding the declaration of insolvency proceedings due to non-payment by the debtor.

Retroactivity Period

The new regime suppresses the so-called "retroactive period" of the insolvency, which allowed the insolvency judge to establish a date prior to the formal declaration of the insolvency and back-date the effects of the insolvency, causing the automatic nullity of all acts and transactions —including the creation of a security interest—carried out by the bankrupt after the retroactive date.

This notwithstanding, the Act contemplates the possibility of rescinding certain acts carried out by the bankrupt during the previous two years that are considered harmful to its financial situation; in particular, the granting of a security interest to secure pre-existing obligations is presumed to be harmful and therefore subject to rescission, although this presumption may be upheld. This provision will discourage financial institutions from refinancing their debtor's obligations, which will in turn hasten the debtor's financial distress.

Insolvency Procedures Involving a Foreign Element

In line with the European Regulation on cross-border intra-European insolvency proceedings, the Insolvency Act introduces certain International Private Law rules that extend its scope to other jurisdictions.

If the debtor's main place of interest is located in Spain, the insolvency proceedings held in Spain before the Spanish insolvency courts will have universal effects over all of the debtor's assets, irrespective of where they are located. In the case of companies, the registered address is also considered to be the main place of interest.

If the debtor's main place of interest is located outside Spain but it holds an establishment in Spain, insolvency proceedings may be held in Spain with a limited effect affecting only those of the debtor's assets located in Spain. In particular, in the event that insolvency proceedings are initiated in the U.S. in respect of a U.S. company that holds an interest in Spain, the insolvency proceedings held in Spain will only affect the Spanish-based establishment.

The Insolvency Act also contains certain rules of international coordination in the event that an insolvency proceeding is initiated outside Spain in connection with the debtor's assets located outside Spain.

Conclusions

The new Bankruptcy Act introduces significant legal certainty to the existing insolvency regime, establishing an appropriate procedure to deal with financially-distressed companies in a more rapid and predictable manner, and as such, has been received well by specialists and market players alike. However, certain specific features of the Act such as those outlined above should be carefully considered by lenders when extending credit to Spanish business concerns and adequately addressed when structuring the transaction, since they may have a significant impact on the ability of the creditors to recover the full value of their investment.

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United States

U.S. Tax Opinions and Practices

The U.S. Treasury recently proposed changes to Circular 230, which incorporates regulations that govern practice before the IRS. These changes prescribe best practices for all tax advisers, combine and modify standards for marketed and "more likely than not" tax shelter opinions, revise procedures for ensuring compliance with standards of practice, and provide for advisory committees to the Office of Professional Responsibility. The proposals hope to restore, promote, and maintain the public's confidence in the honesty and integrity of professionals who provide tax advice.

Best practices must be observed by all tax advisers for oral and written advice: (1) communicate clearly with the client regarding the terms of the engagement and the form and scope of the advice or assistance to be rendered; (2) establish the relevant facts and evaluate the reasonableness of any assumptions or representations; (3) relate the applicable law, including potentially applicable judicial doctrines, to the relevant facts; (4) arrive at a conclusion supported by the law and the facts; (5) advise the client regarding the significance of the conclusions reached; (6) act fairly and with integrity in practice before the IRS. All tax advisers must follow best practices and comply with certain tax shelter opinion requirements; managing tax partners must also ensure that the procedures are in place to enable advisers to do so. Devising adequate procedures to comply with the regs will require creativity to balance the clients' needs for timely responses.

Key definitions are modified for tax shelter opinions. A "tax shelter" includes any partnership or other entity or any investment plan, other plan, or arrangement with a significant purpose of avoidance or evasion of any tax imposed by the Code. Tax avoidance generally refers to a strategy to minimize tax and includes an essentially unlimited range of personal, financial, and business transactions. A "tax shelter opinion" is written advice by a practitioner concerning federal tax aspects of any federal tax issue related to a tax shelter item or items (for example, income, gain, loss, deduction, or credit: the existence or absence of a taxable transfer of property; and the value of property), including a financial forecast or projection, predicated on assumptions regarding federal tax aspects of the investment or tax risks portion of offering materials.

Current exclusions for municipal bonds, annuities, family trusts, individual retirement accounts, stock option plans, and certain other specific transactions are eliminated. Written advice may range from a short e-mail response to a client inquiry to an extensive formal opinion letter, challenging managing tax partners to develop practical compliance procedures. A practitioner must determine whether an opinion is a tax shelter opinion, for which there are additional compliance requirements.

A "more likely than not" tax shelter opinion reaches a conclusion at a confidence level greater than 50 percent that one or more federal tax issues will be resolved in the taxpayer's favor. A "marketed tax shelter opinion" exists if a practitioner knows or has reason to know that it will be used by others in promoting or recommending the tax shelter to one or more taxpayers. If either type of opinion exists, the adviser must, *inter alia*, identify and consider all relevant facts and must not rely on any unreasonable factual assumptions or representations; relate the applicable law to the relevant facts and not rely on any unreasonable legal assumptions, representations, or conclusions; reach a conclusion, supported by the facts and the law, with respect to each material federal tax issue; and provide an overall conclusion about the federal tax treatment of the tax shelter item or items and the reasons therefor. If a practitioner cannot reach a conclusion or an overall conclusion, the opinion must state the issues and reasons for failure to reach a conclusion and make certain disclosures; limited-scope opinions are allowed only for non-marketed opinions.

A practitioner must disclose any compensation arrangement or any referral agreement with any person (other than the client) with respect to promoting, marketing, or recommending a tax shelter. A marketed opinion must disclose that it may not be sufficient for a taxpayer to use for the purpose of avoiding penalties and that the taxpayer should seek advice from his or her own tax adviser. A limited-scope opinion must state that additional issues may exist that may affect the federal tax treatment of the tax shelter under discussion. If an opinion fails to reach the confidence level of at least "more likely than not" with respect to one or more material federal tax issues, it must disclose that fact and that it was not written, and cannot be used by the recipient, for the purpose of avoiding penalties with respect to such issues. One objective of the proposed regulations is to ensure that a client is informed explicitly about what protection an opinion provides to him or her.

This article was first published by the Canadian Tax Foundation in 2004, volume 12, number 3, *Canadian Tax Highlights*.

Update since original publication: In April 2004, the IRS announced that, in final regulations, the definition of tax shelter opinion for these purposes will not apply, if at all, to written advice concerning municipal bonds rendered less than 120 days after the publication of final regulations.

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Request for Contributions

Contributions to the *New York International Chapter News* are welcomed and greatly appreciated. Please let us know about your recent publications, speeches, future events, firm news, country news, and member news.

Oliver J. Armas
Richard A. Scott

Firm News

Ex-WCO Director Becomes "Of Counsel" to Meeks & Sheppard

Meeks & Sheppard, an international trade and customs law firm with offices in New York, California and Connecticut, is pleased to announce that Holm Kappler has recently become affiliated with the firm in an "Of Counsel" capacity.

Mr. Kappler was most recently the Director of Tariff & Trade Affairs at the World Customs Organization (WCO) in Brussels, Belgium. He was elected to this position by the Customs Directors General at the June 1998 WCO Council Sessions in Marrakech, Morocco. Mr. Kappler's Directorate was responsible for tariff nomenclature (Harmonized System), customs valuation, and rules of origin issues.

In prior positions, Mr. Kappler was Chief of Staff to the Commissioner of the U.S. Customs Service (now U.S. Customs and Border Protection). In that capacity, in addition to managing the activities and staff of the Office of the Commissioner, he served as a senior advisor and counsellor to the Commissioner with regard to all aspects of customs work.

Mr. Kappler has an extensive background in tariff and trade policy, having worked as a customs and trade attorney for both the U.S. Customs Service and the U.S. International Trade Commission and as a trade negotiator for the Office of the U.S. Trade Representative in Geneva.

Mr. Kappler has a Juris Doctor degree from the University of San Francisco and is a member of the California State Bar.

Four Hodgson Russ Partners Participate in Canadian Corporate Counsel Association's National Spring Conference

C.J. Erickson Featured Panelist

Hodgson Russ LLP partners Pamela Davis Heilman, C.J. Erickson, George J. Eydt, and Kenneth N. Frankel participated in the 2004 National Spring Conference of the Canadian Corporate Counsel Association (CCCA), "Navigating Corporate Shoals: Corporate Counsel, Think or Swim!," April 18 through 20, Halifax, Nova Scotia. Hodgson Russ was a conference sponsor.

Mr. Erickson, a member of Hodgson Russ's Customs, Trade & Transportation and FDA Practice Groups, resident in the firm's New York City office, took part in the panel discussion "Steering the Right Course: Cross-Border and International Shipping, Exporting Issues, and More." Mr. Erickson's presentation was "Trading with the U.S. Post 9/11."

Ms. Heilman, the lead attorney for Hodgson Russ's CCCA involvement, said, "Hodgson Russ is delighted to have sponsored and taken part in a conference of such exceptional caliber, with representatives from industry, government, and the private sector addressing the increasing challenges faced by in-house counsel in meeting corporate expectations, an area in which Hodgson Russ attorneys are eminently able to offer assistance."

The conference program included an essay by Gary M. Schober, Hodgson Russ's Intellectual Property & Technology Practice Group leader, "Who Owns the Copyright? What Do You Mean I Paid for It but Don't Own It?"

Ms. Heilman practices in the areas of international commercial transactions, nonprofit corporations, professional corporations, and mergers and acquisitions. She is vice president of the Business Division at Hodgson Russ and a member of the firm's Corporate & Securities and Canada Practice Groups. As one of the lead lawyers in the cross-border Canada/U.S. practice, Ms. Heilman regularly counsels Canadian organizations and businesses considering expansion into the United States. Ms. Heilman also has extensive experience counseling nonprofit organizations and closely held businesses.

Mr. Erickson concentrates his practice in all areas of customs and trade law including the representation of domestic and multinational corporations before various government agencies, including the U.S. Customs Service, the Food and Drug Administration, and the Fish and Wildlife Service, as well as congressional subcommittees in connection with pending and proposed trade legislation.

Mr. Eydt, a member of Hodgson Russ's Corporate & Securities and International/Cross-Border Practice Groups, is the managing partner of the firm's Toronto office. He concentrates in the areas of franchise and distribution law, corporate law, mergers and acquisitions, and international commercial transactions.

Mr. Frankel, a partner in the firm's Toronto office, has more than 20 years of experience managing transactions in North America, South America, Europe, and Asia, with particular expertise in joint venture and consortium projects in telecom, rail transportation, and outsourcing.

Hodgson Russ Vice President Pamela Davis Heilman Receives 15th Annual ATHENA Award

Pamela Davis Heilman, Esq. was honored with the 15th annual ATHENA Award at a luncheon presentation ceremony April 29 at the Hyatt Regency, Buffalo. Ms. Heilman is the vice president of the Business Division of Hodgson Russ LLP.

The ATHENA Award honors an individual who has attained and personifies the highest level of professional excellence, demonstrates dedication to leadership opportunities for women professionals, and provides significant assistance on their behalf. The ATHENA award program is administered by the nonprofit ATHENA Foundation, which supports programs in more than 350 cities worldwide. Proceeds from the event benefit the WNY Women's Fund, which supports innovative solutions to the issues and needs of women and girls in the Buffalo-Niagara region.

In addition to serving as one of Hodgson Russ's two vice presidents, Ms. Heilman is a member of the firm's Corporate & Securities and International/Cross-Border Practice Groups, concentrating her practice in the areas of international commercial transactions for nonprofit and professional corporations, including mergers and acquisitions. She is one of the lead lawyers in Hodgson Russ's cross-border Canada/US practice and regularly counsels Canadian organizations and businesses considering expansion into the United States.

Ms. Heilman has devoted substantial time to the promotion of women in international business and the development of cross-border business relationships. In 1997 she served as an advisor to the Business Women's Team Canada Trade Mission to Washington, D.C., and was panel chairperson at the annual APEC Women Leader's Network Conference held in Ottawa. Since its inception, she has served on the bi-national panel of judges for the Canadian American Business Achievement Award. She represented Hodgson Russ as a sponsor of the Canada-U.S.A. Business Women's Trade Summit in Toronto in 1999, which was attended by 150 women-owned businesses each from Canada and the United States.

Ms. Heilman's many business and community affiliations include serving since 1995 as a member of the board of directors and secretary of SJL Communications LP, which owns and manages network television broadcast stations throughout the United States. She was recently elected to the board of the Canadian American Business Council. Ms. Heilman is a member of the board of directors of Financial Institutions, Inc., the oldest bank holding company in New York State, and chairman of its Management Development and Compensation Committee.

Ms. Heilman received a J.D. with honors from University at Buffalo Law School, State University of New York and an A.B. with honors from Vassar College.

Chapter Chair News

Madrid

The Madrid Chapter reports continued activity in their periodic "dinner-colloquiums" involving informal presentations/debates featuring speakers of interest to internationally oriented practitioners based in the Madrid area.

A June 23rd dinner featured Xavier Ruiz of McDermott, Will & Emery (New York office) and formerly of Baker & McKenzie, and Juan Manuel de Remedios, of Latham & Watkins (London office) and formerly with Banco Santander and Rogers & Wells (New York office). Their topic involved globalization of legal practice as seen by dual-qualified Spanish lawyers practicing in or with foreign and particularly U.S. firms outside of Spain.

An October dinner is on the drawing board to feature Paul Silverman of Alston & Bird and to focus on comparative bankruptcy law and practice. This is a particularly timely topic since this fall a new Spanish bankruptcy law, to some extent inspired by comparative and U.S. bankruptcy and Chapter 11 approaches and representing a substantial overhaul of the country's rather archaic existing rules, will take effect.

The Chapter is open to scheduling dinners of this sort on the occasion of visits to Madrid of people who might be willing and able to address our group of internationally oriented, mostly Spanish, of course, practitioners. We invite potentially interested speakers thinking of a Madrid visit in late 2004 or early 2005 to contact Calvin Hamilton or Cliff Hendel to set something up if appropriate.

Committee News

ILPS Executive Committee Retreat

The Executive Committee Retreat this year had a distinct Quebec influence. Not only was the Retreat itself held in Montreal (at the Ritz-Carlton Hotel on Friday and Saturday, June 4th and 5th), but a delegation of Section members presented a program on recent developments in several areas of U.S. law at the Annual Meeting of the Barreau du Quebec on Friday (June 5th) in Quebec City.

The primary purpose of the Retreat is to allow the officers of the Section and members of the Executive Committee to spend more time than the quarterly meetings allow in addressing the current issues and programs of the Section and in planning its future activities in the years ahead. The principal reason for holding the meeting in Montreal was to strengthen the Section's ties with Canadian law firms with offices in New York. That goal was achieved by the active participation by a number of lawyers from the Montreal and Toronto offices of four firms which sponsored receptions, luncheons or dinners of the Retreat weekend. The Executive Committee is grateful to the firm of Fasken Martineau & Du Moulin LLP and Stikeman Elliott LLP for the sponsorship, respectively, of a reception at Fasken Martineau's offices and dinner at Altitude 737 on Friday evening and to Blake, Cassels & Graydon LLP and to Fraser Milgrain & Casner, LLP for their sponsorship, respectively, of the working lunch and later a reception and dinner at the University Club on Saturday.

The Section members speaking in Quebec City were Nava Bat-

Avraham, Kenneth A. Schultz, Allan E. Kaye, Michael W. Galligan, Lawrence E. Shoenthal and Phillip M. Berkowitz, as well as John Beardwood of the Fasken, Martineau office in Toronto. Assisting in organizing the event was Louise Martin-Valiquette, who is the Barreau du Quebec's liaison to the IL&PS of the NYSBA.

Also while in Montreal for the Retreat, the Chair, Paul M. Frank, was interviewed on the "Report on Business" nightly television program, which was arranged by the Fraser, Milgrain, Casner firm.

International Privacy Law Committee

Invitation

Please look for the announcement of the International Privacy Law Committee's future meeting. This meeting will consist of a two-hour lecture series on Privacy and Ethics. We are planning to have this seminar meet the MCLE Requirements of NYSBA Committee Meetings so we may offer two credit-hours of ethics. The meeting will be open to International Privacy Law Committee participants and New York State Bar Association members. The meeting will be free of charge.

Event News

Mayor of Toronto, David Miller, Addresses Business Leaders in New York City

On June 3, 2004, the New York office of Fraser Milner Casgrain LLP had the honor of hosting a luncheon for Toronto Mayor David Miller, on behalf of the City of Toronto, to address leaders of the New York business, financial and legal community, during the Mayor's economic development campaign in New York City.

The program, held at the historic Union League Club, was originally designed as a Business Roundtable Luncheon. As word-of-mouth spread amongst the business community, the luncheon quickly snowballed into an event for well over 100, resulting in the Mayor delivering an address to his guests and opening a dialogue between the two cities. Attending the lunch were organizations from financial and business sectors such as CIBC World Markets Corp., Citigroup, JP Morgan, Deloitte & Touche, Credit Suisse First Boston, Marsh, Morgan Stanley, Kodak Polychrome Graphics and PepsiCo International. Also on hand was representation from the Office of the Mayor of New York, the Canadian Consulate General, the United Nations Procurement Division and many members from top-tier law firms including Allen & Overy; Clifford Chance US LLP; Debevoise & Plimpton; Fulbright & Jaworski LLP; King & Spalding LLP; Lovells; Proskauer Rose; Paul, Weiss, Rifkind, Wharton & Garrison; Simpson Thacher & Bartlett LLP; and Winston & Strawn LLP.

Following an introduction by Fraser Milner Casgrain Chair Jeff Barnes, Mayor Miller outlined for his audience the exciting opportunities Canada's largest and most vibrant city has to offer; including its key competitive positioning of being North America's third-largest banking center as well as having the third-largest information and communications technology sector. Highlighting another competitive edge, Mayor Miller went on to explain that Toronto is one of the most livable cities in the world, with a highly educated labor force, safe and clean streets, and a vibrant artistic and cultural scene.

Touching on his dedicated efforts to strive for the best quality of life Toronto can offer, Mayor Miller also spoke of one of his most significant projects: to revitalize the waterfront area and turn it into an environmentally and residentially stable community with parks, recreational activities, businesses and a waterfront promenade.

Fraser Milner Casgrain is frequently involved with presenting events to the New York business and legal communities that promote doing business in Canada.

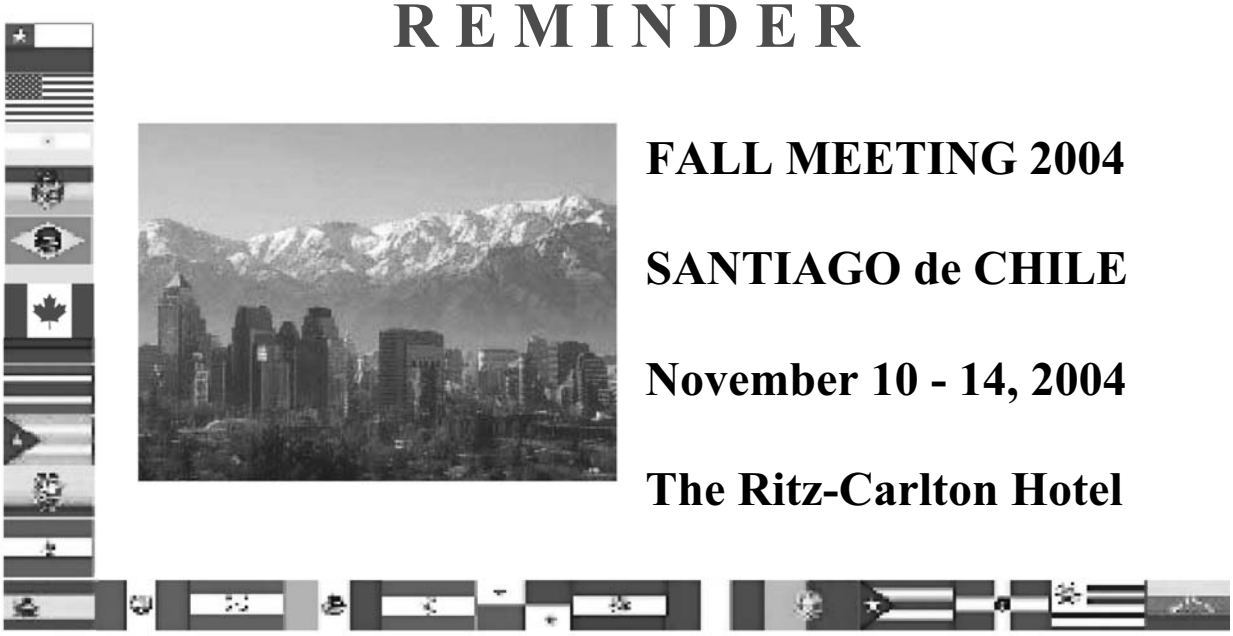
INTERNATIONAL LAW AND PRACTICE SECTION MEETING

The International Law & Practice Section has been one of the fastest growing sections in the New York State Bar Association. We welcome you to join us for the 2004 Fall Meeting in Santiago!

NEW YORK STATE BAR ASSOCIATION

INTERNATIONAL LAW AND PRACTICE SECTION

REMINDER



FALL MEETING 2004

SANTIAGO de CHILE

November 10 - 14, 2004

The Ritz-Carlton Hotel

The 2004 Fall Meeting of the NYSBA's International Law and Practice Section will be held in Santiago, Chile, from Wednesday, November 10 through Sunday, November 14, 2004. The meeting is designed to go beyond national boundaries and aims at being a true **Latin American Summit**. The main theme will be "Free Trade And Beyond: Legal Challenges for the Americas." In various panels, leading lawyers from Latin America, the U.S. and Europe will address related key legal issues.

The meeting will be held at the new Ritz-Carlton Hotel in the Las Condes/El Golf section of Santiago. The hotel features everything you would expect from a Ritz-Carlton, and is located within a few blocks of leading Chilean law firms active in the international practice of law. The El Golf area also offers shopping, restaurants, etc. A subway station is close to the hotel.

Locations for social events include the U.S. Embassy, the Los Leones Golf Club, the Palacio Cousiño, and the Club Hípico race track. Spousal and guest trips are also being offered, *e.g.* to the coastal city of Valparaiso. A brunch at an art gallery concludes the program. Possible locations for pre- and post-meeting trips include Cuzco / Machu Picchu (Peru), the Galapagos Islands as well as Chile's Lake District and Tierra del Fuego.

Sponsorship opportunities for the meeting are currently available. To request further information, please use the attached form or check out our website at **www.nysba.org/santiago2004**. Thank you.

Oliver J. Armas
Meeting Chair

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