In spite of its relative success in deploying its available powers under articles 85 and 86, EEC, in the control of concentrations, however, the Commission still feels the urgent need, which it has felt ever since the *Continental Can* judgment,[41] for a specific regulation in this field empowering it to act still more flexibly in the public interest, for example, by exempting technical abuses under article 86, or restrictions falling outside article 85(3), which might nevertheless be considered desirable on other grounds. It is increasingly aggrieved that the Council has not yet seen fit to enact such a regulation, probably through reluctance to increase the Commission's discretion in what is frequently a politically sensitive field. The Commission has recently, therefore, forwarded to the Council yet another draft of such a regulation for the Council to consider for enactment,[42] and there are some signs that the Council is at last willing to move on this matter.[43]

*Prepared by Peter Bentley and Yuk Tong Cheung of Baker & McKenzie, Chicago, Illinois, in cooperation with the firm's offices in the Pacific Basin.

41. *Supra* note 33.

42. Commission Working Paper COM(88)97.

43. Information Memo (1988) P-22.

Pacific Basin*

I. Australia

A. Inquiry into Mergers, Takeovers, and Monopolies

The Australian House of Representatives Committee on Legal and Constitutional Affairs announced in February 1988 that it would conduct an inquiry into the adequacy of Australia's regulation of mergers, takeovers, and monopolies, and make recommendations for future policy. The outgoing Trade Practices Commission chairman had publicly expressed the view that the merger provision of the existing Trade Practices Act (TPA) could lead to monopolies in some markets.

The Committee intends to structure its "broad-ranging" inquiry by examining the extent of control needed to protect the public interest, the adequacy of current legislation, and the role and effectiveness of the Trade Practices Commission in applying the TPA's provisions on mergers and misuse of market power. The Committee expects to pay particular attention to the TPA in connection with mergers that result in dominance of a market, and will also review associated legislation on takeovers.

The committee, whose members include representatives of the legal, business, and economic sectors, expects to present a report in 1989.

B. Thin Capitalization by Nonresidents

A new Division 16F of the 1936 Income Tax Assessment Act (the Act), in effect as of July 1, 1987, has introduced thin capitalization rules. These rules apply to foreign investors as well as to resident companies or groups of companies, trusts, and partnerships.

The new legislation limits tax deductions for interest paid on debt (foreign debt) to related foreign creditors. If a taxpayer's foreign debt exceeds a certain ratio of foreign debt to foreign equity, interest on the debt in excess of the prescribed level is not deductible. Current prescribed ratios of foreign debt to foreign equity are 6:1 for banks and other financial intermediaries and 3:1 for all other taxpayers.

The rules apply only to the class of taxpayers subject to Division 16F, and do not apply if an Australian owned nonresident company is the nonresident "controller." They do not apply to debt that is interest-free or guaranteed by a parent corporation, or to loans from an unrelated lender.

The rules apply to all foreign investments made after June 30, 1987, and any earlier investments for which the Foreign Investment Review Board required an undertaking not to exceed a prescribed foreign debt to equity ratio. Other financing arrangements not subject to such undertakings will not have to comply with the prescribed ratio until either the date the debt is refinanced or June 30, 1988, whichever comes first.

II. Hong Kong

A. Futures Market Collapse; Legality of Futures Deals

A number of lawsuits have resulted from the crisis in the Hang Seng Index futures contracts market that occurred during the October 1987 crash in world stock markets. The Hong Kong Stock and Futures Exchange closed for a week between the two "Black Mondays" (October 19 and 26, 1987). As the market reopened, I.C.C.H., the clearing house for the futures market, required additional margin and deposits from members with net long positions. Noncomplying brokers were suspended from the Futures Exchange and served with writs claiming the amounts concerned, and I.C.C.H. liquidated their net positions over the following week at the then prevailing low index levels. Most of the defendants and other brokers have commenced proceedings against their losing customers for the money due.

The futures contracts and the circumstances of the cases raise several interesting issues. The main defense, according to press reports, is the argument that the suspensions of the Stock and Futures Exchanges were illegal and frustrated all contracts. There is also a question as to whether brokers are principals or merely agents of nonhouse accounts. In addition, several technical issues may arise:

- that I.C.C.H.'s liquidation of net positions breached section 46 of the Commodities Trading Ordinance;
- that the Hong Kong Futures Guarantee Corporation is an unlicensed insurance company and the relevant contracts are not enforceable;
- that all Hang Seng Index futures contracts are illegal and void as wagers under the Gaming Act of 1710.

The High Court of Hong Kong recently held that the Futures Exchange contracts might be illegal under the Hong Kong Gambling Ordinance. A firm of brokers took legal proceedings against two customers, futures index investors, for money due. In response to the plaintiff's motion for summary judgment, the defendants argued that the contracts were illegal and therefore void under the Gaming Act of 1710 as amended in 1835. The master's denial of summary judgment was upheld by the High Court, which said that futures exchange contracts appeared to be illegal, as they were clearly contracts for differences (gambling).

The High Court Judge distinguished contracts for *differences,* Futures Index contracts, from contracts for *tangibles,* e.g., the commodities traded under the 1976 Commodities Trading Ordinance (cotton, gold, soybeans, and sugar). The Judge saw an element of gambling in the trading of contracts, and thought that it should be examined to see whether it came under the Gambling Ordinance. He cited an 1899 English case that held that contracts for differences were contracts of gambling and wagering.

The strength of this defense has not yet been tested in court. Many brokers, however, have put actions against their customers on hold, while waiting for results of the test cases.

B. Localization of the Judiciary; End of Appeals to Privy Council

Under the joint declaration made by the United Kingdom and People's Republic of China Governments, Hong Kong's Supreme Court authority is to be established locally after Hong Kong is handed over to China. The handover date is July 1, 1997, but the judiciary would prefer to have this Final Court of Appeal established well before then, to give it time to be accepted by the legal and business communities.

The Hong Kong Government's Executive Council approved an outline of plans, still being discussed with the Chinese Government, to end appeals to the Privy Council in London by 1992. A new Final Court of Appeal in Hong Kong would replace the Privy Council. This new court would convene two to three times a year, and would include two foreign judges. The court would have three local judges, one of whom would be the Chief Justice of Hong Kong, but justices from the court of appeal would not be permitted to take the other two local seats.

The Executive Council also decided that by 1995 half of Hong Kong's judges and magistrates should be Chinese. There are now fewer than forty Chinese out of a total of 150 judicial officers in Hong Kong.

III. Indonesia

A. Deregulation

The Indonesian Government issued new deregulation provisions in December 1987. This is the sixth such deregulation reform during the past three years.

- Measures to promote nonoil exports include the following: Foreign shareholders of a foreign joint venture company (called PMA), now have fifteen years (previously ten) to reduce their equity participation to 49 percent.
- Certain PMA companies—those established with capital greater than U.S. $10 million, located in certain remote areas, or exporting at least 65 percent of their production—may now be established with 95 percent foreign shareholding (previously 80 percent). This foreign shareholding must be reduced to 80 percent within ten years, and to 49 percent within fifteen years.
- Foreign shareholders of PMA companies located in bonded zones and exporting 100 percent of production may maintain a 95 percent equity participation indefinitely.
- An exporter, or a manufacturer that is also an exporter, may obtain a refund of value added tax or sales tax on luxury goods when the tax has been paid on goods and materials purchased for the production of export goods. Contractors for certain government projects are exempt from import duties and may be able to postpone value added tax and sales tax on luxury goods.

Selective import liberalization has also taken place. The number of products that must be imported through sole agents has been reduced significantly, and foreign companies may now distribute products through a number of nonexclusive distributors.

The listing requirements of the existing Stock Exchange have been simplified. The government has also published basic regulations for a proposed over-the-counter market.

B. Business Visas

Foreigners visiting Indonesia on business may now receive a four-month multiple entry business visa that can be extended for two more months without leaving the country. Previously, a business visa was valid for two months with a possible one-month extension. Visitors should be aware that there are still significant Indonesian tax risks for regular or lengthy visits.

IV. Japan

A. Changes to Leveraged Leasing Rules

In September 1987 the Japanese National Tax Administration (NTA) began to publicize its opposition to cross-border leveraged leases through which Japanese investors in assets used outside Japan could fully depreciate those assets for Japanese tax purposes. In some situations, so-called double dipping was possible: the non-Japanese lessee could also fully depreciate the assets in its country. In December the NTA began several adverse audits of investors in such leases and, as a result, the Japanese equity market for any similar international investments was effectively frozen.

After discussion with the Japanese Lease Association (JLA), the NTA issued in April and May 1988 two circulars that establish new guidelines for such transactions. These guidelines are expected to allow new transactions to proceed, albeit at a reduced level of tax benefits to the Japanese lessors and a reduced financial benefit to the lessees. Transactions completed prior to March 31, 1988, were "grandfathered" into favorable treatment, except for only a very limited number of transactions considered to have been particularly abusive.

Under the new rules, if the lease term of a transaction is longer than 120 percent of the asset's statutory useful tax life, and the transaction does not meet any one of four criteria, it should qualify for favorable tax treatment. If all four such criteria are present in such a transaction, however, the transaction will be treated for Japanese tax purposes as a sale or finance transaction, thereby denying all depreciation to the lessor.

The four criteria are:

- the lessee has selected and arranged the purchase of the asset, or has first acquired the asset and sold it to the lessor;
- total rentals equal substantially (at least 90 percent of) the entire cost of acquisition (including interest expenses and other ancillary costs) of the asset to the lessor;
- early termination of the lease is not permitted, or if it is, the lessee must pay substantially all of the remaining rental payments for the unexpired lease term; and
- the lease does not specify that the lessee will acquire the asset at fair market value.

Many aspects of these new rules remain to be tested and clarified in the context of actual transactions. In June 1988 the market for such Japanese cross-border leveraged leases had already begun to show signs of very active revival within the framework of these new guidelines. This market should remain very active at least through 1989 and into 1990 before any additional changes or adjustments (if any) are imposed by the Japanese NTA.

V. Malaysia

A. Easing of Foreign Investment Rules

One of the objectives of Malaysia's New Economic Policy of 1970 was to restructure ownership of Malaysian companies so that foreigners would eventually own only 30 percent of their shares on a sector-by-sector basis. Accordingly, Foreign Investment Committee (FIC) approval is required for the following activities:

- foreign acquisition of substantial fixed assets in Malaysia;
- acquisition of assets or interests, mergers and takeovers of companies, as a result of which ownership or control passes to foreign interests;
- acquisition of 15 percent or more of the voting power of a Malaysian company by any one foreign interest, or acquisition by foreign interests in the aggregate of 30 percent or more of such voting power;
- control of Malaysian companies through joint-venture, management, and technical assistance agreements, or other arrangements;
- a merger or takeover, by Malaysian or foreign interests, of a company in Malaysia; and
- any acquisition of assets or interests with a value greater than MR $5 million.

By the end of 1987, although the value of shares held by foreigners in Malaysian companies had increased, the percentage of such shares had decreased to 24 percent. Concerned about a lack of interest by foreign investors, the Malaysian Government appears to be taking steps to attract them. The FIC now meets twice rather than once each month, and FIC approval is not normally required for incorporation of a Malaysian company by foreigners. However, such a company is still required to obtain FIC approval for any of the activities listed above.

The Malaysian Industrial Development Authority has speeded up the process of application for tax incentives under the 1986 Malaysian Promotion of Investments Act. An applicant can expect a response to an application within four to six weeks, and projects that receive the Authority's approval will not require FIC approval. The Authority is also willing to consider investors' evaluations of whether a proposed product or activity can be added to the list of products or activities for which tax incentives are available under the 1986 Act.

VI. People's Republic of China

A. Changes to the Ninety-Day Rule

On January 21, 1988, the PRC Ministry of Finance issued a notice amending the ninety-day rule, under which an individual who resides in China for more than ninety days is subject to Chinese individual income tax. The amendment, effective retroactively to January 1, 1988, makes three changes to the rule.

First, the ninety-day period is now calculated on a calendar year basis. An individual who resides in China for ninety days or less in a single calendar year is exempt from PRC individual income tax on wages and salary from an overseas employer.

Second, only the days that an individual is actually present in China are counted. Under the old rule, an absence from China of thirty days or less was deemed to be part of the ninety-day residence period, but an absence of more than thirty days began a new count for a new ninety-day period. Therefore, PRC taxes were easily avoided by staying away from China for more than thirty days between visits. Under the new rule, a new ninety-day period will not begin after an absence of more than thirty days.

Third, individuals who reside in China for more than ninety days in a calendar year will be subject to income tax only for the actual number of days present. Under the old rule, once individuals reached the ninety-day threshold, all income from the period of deemed residence, including absences of thirty days or less, was subject to PRC income tax.

VII. Singapore

A. Representative Offices

Foreign companies may establish a representative/liaison office in Singapore, with approval from the Trade Development Board. The office must operate according to strict guidelines, and is essentially restricted to liaison and promotional activities. An office that complies with these guidelines is not viewed as having a corporate presence in Singapore and is not required to register or fulfill any corporate filing requirements under the Companies Act. Normally, as the representative office does not conduct business and has no profit, it is not taxed.

The Board is apparently developing a new policy on representative offices. New registrations are being given for an initial one-year period, subject to renewal either for one year or possibly for three years (the renewal period is still under review). The new policy may reflect the view that, if a company's representative office is successful, the company should establish a more permanent presence. There is no indication whether the new rules will apply to representative offices that have been registered before the new policy becomes fully effective.

VIII. Taiwan

A. Object Code Licensing

Software licensing in Taiwan is an area of uncertainty. Taiwan's Copyright Law contains no provisions about licensing of copyright, so it remains purely a matter of contract. In order to guard the confidentiality of their source code, many foreign licensors grant licenses in Taiwan for software only if it is in object code, or machine-readable form. The validity of such licenses in Taiwan is not clear.

The Copyright Law does recognize translation rights in copyrightable works, so a licensor may grant separate licenses for different language translations of a book. It is not clear whether a licensor may grant separate licenses for source code and object code versions of a computer program. Computer technology presents other related problems under the Copyright Law. For instance, it is uncertain what the original "language" of a program is; whether computer languages are analogous to human ones; whether programs can be "translated"; whether object code (which only machines can read) is a language; and to what extent a computer language must be intelligible to people before it is considered a language subject to "translation."

In 1986 the Ministry of the Interior issued "Draft Guidelines on Copyright Infringement of Computer Software," which began to address some of these questions. The Guidelines treated source code and object code versions of a program as "transformations" rather than translations, suggesting that different transformations could not be licensed separately. However, the Guidelines, which were poorly drafted, were withdrawn a few weeks after being released, and there is now no official guidance at all on the question.

The Copyright Law presents a further problem as it does not grant copyright protection of translation rights to non-Republic of China nationals. This suggests that even if source code and object code versions of a computer program were considered translations, a foreign program would not enjoy copyright protection of translation rights.

B. Trademark Law—Revised Classifications

In October 1987 Taiwan amended its classification system for trademarks and servicemarks, which differs significantly from the international classification system. The number of classes has been reduced to ninetyfive, and various goods that were formerly separate classes are now combined into one class. Thus ice and ice cream, which were formerly in two separate classes, are now covered by the same class because of their common characteristic of coldness; furthermore, tea and coffee, which were formerly in a third class, are now in the same class as ice and ice cream, on the basis that ice cream, tea, and coffee are generally available at the same locations.

This combination of products into the same class may increase the chances that a trademark application will be rejected on the grounds that it is confusingly similar to an existing registration for another product within the same class.