May 2012

The International Dispatch

Akin Gump
Strauss Hauer & Feld LLP

IN THIS EDITION

Welcome to *The International Dispatch*. This edition looks at two broad themes: emerging market investing and multi-jurisdictional regulation and enforcement.

Investor confidence in China and Africa over the past year has continued to rise, and investors are looking for ways to maximize growth opportunities in these key regions. This edition includes editorial pieces that take a broad look at structuring investments into Africa, as well as practical ways to efficiently extract returns from Chinese investments.

Equally as prevalent in the mind of those within the funds industry is the current regulatory climate and what the future may hold. This edition brings to light developing regulation in the EU with a summary of recent legislative developments, as well as an in-depth review of the UK's insider dealing regime.

We are proud to advise clients who operate in diverse global markets. By analyzing recent developments in specific markets and geographies and placing them into a wider global context, we are able to provide our clients with comprehensive global-data to help them place current trends in context and plan for their future success.

We hope that you enjoy this edition of *The International Dispatch*, and we welcome any feedback, comments and suggestions for future editorial pieces.

contents

The Scramble for Africa

Structuring Investment in Emerging Africa

By Jonathan Ivinson, Partner
Andrew Callaghan, Associate

Historically, political and macroeconomic concerns have deterred many international investors from investing in African assets. However, the once overlooked region is now receiving mounting interest from investors seeking highly profitable returns, particularly in natural resources through mining and similar investments.

As with any investment, it is important to get the tax structuring right. Given the opacity of some African tax regimes, the political instability in certain regions, the shortage of qualified personnel on the ground and the general rates of withholding taxes on payments of interest, dividends and royalties to foreign companies, most international investors opt to invest indirectly into Africa through a holding company in another jurisdiction. In light of recent reforms to the U.K.'s controlled foreign companies regime and the breadth of the U.K.'s double tax treaty network, the U.K. may offer a favorable location for such a holding company.

This article sets out a brief summary of some of the domestic African tax issues that should be considered when making African investments, some of the key tax benefits of investing in Africa through a U.K. holding company and a very high-level overview of how a U.S. investor investing into African assets might expect to be taxed on a direct investment compared to an indirect investment through a U.K. holding company.

African Domestic Taxes

The tax rules, rates and administration are different for each African nation. Specific investments should, therefore, be considered on a case-by-case basis. Broadly, the general rates of corporation tax in the key African jurisdictions range from around 15 percent to 40 percent, but most gravitate around the 25 percent mark. Taxes on certain streams of revenue can, however, be much higher (such as the petroleum income taxes of up to 85 percent in Nigeria, for example). As a general rule, reasonable expenditure that is incurred wholly and exclusively for the purposes of the production of a company's income is likely to be deductible for tax purposes. In this way, where there are genuine operations on the ground (which there should be when investing into natural resources, for example) tax leakage at the local operational company level can often be kept to a minimum.

Tools such as debt financing and the payment of reasonable management service fees to other group entities can also sometimes help to erode the local tax base, and consequently the quantum of local tax payable.

Tax Incentives

With the goal of attracting local and foreign investment, a number of African countries offer sector-specific tax incentives. Such incentives often take the form of "tax

holidays" where the relevant company is exempted from tax. Some African countries, for example, offer tax-incentives for pioneer companies (being a company engaged in the rendering of certain services or the production of certain products), certain manufacturing companies, certain agricultural companies and companies in the oil, gas and mining sectors. The availability of local tax incentives can make a substantial difference to the tax leakage suffered in an investment and should be explored in the context of each African investment.

Government Partners

Investment into Africa, particularly into natural resources, can sometimes take the form of a joint venture with a local government or state. When entering into substantial projects with African governments it has been known for certain tax concessions to be negotiated. In some cases investors have sought a full exemption from capital gains taxes on a sale of shares in local companies, an exemption from local corporate taxes and from any withholding taxes on outbound payments of dividends and interest.

Outbound Withholding Taxes

Profits arising from investments held in African companies will usually flow up a chain of companies to non-resident ultimate beneficiaries, normally by way of dividends or interest on shareholder loans. The repatriation of income to the ultimate beneficiaries will either require income to pass from the relevant African country to the ultimate investors directly, or from the relevant African country to a holding/intermediate company in another jurisdiction and then to the ultimate beneficiaries (i.e., an indirect investment).

Each African jurisdiction has its own withholding tax rules. Some do not levy a withholding tax on payments of interest or dividends at all (such as Libya); however, the domestic law of most African countries will impose a withholding tax between 10-15 percent on payments to nonresidents.

It is a general concept of international taxation that domestic withholding tax rates imposed on payments from one jurisdiction to another may be reduced (sometimes to 0 percent) under a double tax treaty between two countries. Most of the key African jurisdictions have a limited network of double tax treaties, thus, international investors will rarely benefit from a reduced rate of withholding tax if they invest directly. This is one of the key tax reasons why international investors may choose to invest in Africa through an offshore holding company that is located in a jurisdiction that has a beneficial tax treaty with the relevant African jurisdiction.

The U.K. has one of the widest and most developed networks of double tax treaties in the world, having entered into agreements with over 100 different countries, including with many African countries. Therefore, a U.K. holding company structure can often be utilized by international investors from jurisdictions that do not have a beneficial double tax treaty with the relevant African jurisdiction. A summary of the tax treatment of a U.K. holding company, and some of the other benefits of a U.K. holding company, are discussed in the next section. The rates of withholding tax applied under a relevant treaty should be considered on a case-by-case basis, as the reduction of the withholding tax rate applied is sometimes only minimal when compared with the normal domestic rate that is applied to payments to non-treaty jurisdictions. For some investors it may be the case that, on balance, the tax saving is outweighed by the other costs involved in making an indirect investment.

U.K. Holding Company

Minimal U.K. Taxation

As a general rule, a U.K. holding company in an African investment structure should be subject to minimal U.K. taxation, on the basis that—

- a U.K. holding company should be able to receive dividends from an African subsidiary without a charge to U.K. corporation tax (as one of the U.K.'s domestic exemptions should be available in most cases);
- withholding taxes on inbound payments can be reduced in some cases where the U.K. has a double tax treaty with the relevant African jurisdiction. The extent to which a double tax treaty assists in reducing or eliminating an inbound withholding tax burden should be considered on a case-by-case basis;
- subject to some specific exceptions, the U.K. does not impose outbound withholding tax in respect of dividends paid to its shareholders. Income repatriated to the shareholders of a U.K. company should not, therefore, suffer tax leakage at the U.K. holding company level;
- subject to certain anti-avoidance and transfer pricing provisions, the U.K. has generous rules on the deductibility of interest payable by a U.K. taxable company in calculating its taxable profit. Thus, in certain circumstances, loans from shareholders or third parties, (including debt used to acquire an interest in a subsidiary) can be effective in reducing the tax burden of a U.K. company;

- on an exit, the sale by a U.K. holding company of its shares in its operating company subsidiaries (whether U.K. or non-U.K.) will, provided certain conditions are met, most often benefit from a specific exemption from U.K. corporation tax on capital gains. However, consideration should be given to local taxes on capital gains that may be imposed in the relevant African jurisdiction. An example where an African jurisdiction has sought to impose such a charge is the recent case of Cove Energy, in which the Mozambique tax authorities sought to impose a charge to Mozambique tax on the sale of Cove by virtue of it holding a stake in Mozambique assets, even though Cove itself is not resident in the jurisdiction; and
- non-U.K. resident companies (that do not have a permanent establishment in the U.K.) and non-U.K. resident individuals are not within the charge to U.K. corporation tax or U.K. capital gains tax (as applicable). Non-U.K. resident shareholders in a U.K. holding company will, therefore, be able to sell their shares in the U.K. holding company without suffering a charge to U.K. capital gains tax.

Controlled Foreign Companies (CFCs)

In some circumstances U.K. tax may become chargeable on U.K. resident companies in respect of the income of certain companies, over which they have a sufficient level of control. The U.K. provisions under which such a charge could be imposed are referred to as the CFC rules. The aim of the CFC rules is to deter U.K. companies from exploiting low tax territories or other favorable overseas tax regimes to reduce their U.K. tax liabilities. The rules achieve this goal by bringing profits of CFCs within the U.K. tax net, which have been intentionally (and artificially) diverted from the U.K.

Historically the CFC rules have unintentionally acted as a deterrent for international groups wishing to use U.K. holding companies. However, following increased political pressure to make the U.K. a more attractive place for multinational organizations, the CFC rules are in the process of complete reform, with further draft legislation recently published in the U.K. Finance Bill 2012. The aim of the reform is to move towards a more territorial tax system, such that the rules should tax only those profits that are economically derived from U.K. activity, rather than from worldwide business.

In light of the available exemptions set out in the recent reforms, and the general emphasis towards making the U.K. a more attractive place to do business, the CFC rules should no longer be as prohibitive to multinational organizations that seek to create holding companies in the U.K. in order to make African investments, provided such African companies have genuine operations on the ground and income is not artificially diverted from the U.K.

U.S. Investor – a High-level Example

Direct Investment

A U.S. company that invests in African assets directly will need to consider the tax treatment at the following levels—

- corporation tax at the local African company level;
- withholding tax on payments from the African company to the U.S. investor;
- U.S. tax on receipt of income from its African subsidiary; and
- U.S. tax on an exit/disposal of the African subsidiary.

As set out above, the tax levied at the local company level will depend on the African jurisdiction in which the

U.S. company wants to invest. Generally the headline tax rates are between 15 percent and 40 percent for most of the key African jurisdictions. Certain deductible expenses can be taken into account to reduce the overall tax burden at the local company level.

The African countries that have entered into double tax treaties with the U.S. are Morocco, South Africa and Tunisia. Interest and/or dividends received by a U.S. company from any other African jurisdiction will, therefore, be subject to the full amount of withholding tax imposed by the relevant country, with no scope for reduction under a tax treaty.

A U.S. company is subject to U.S. corporate tax upon its receipt of dividends from its African subsidiary. However, subject to certain complex rules and limitations, the U.S. company may be able to claim a credit against its corporate tax liability for foreign taxes paid by it or its foreign subsidiaries.

To the extent that the shares of its African subsidiary have risen in value, a disposal should give rise to a chargeable gain for U.S. tax purposes.

In summary, a U.S. investor that chooses to invest in Africa directly should, very broadly and without further structuring, expect tax leakage on its investment at the local level in the form of corporation tax on the income of the African company, through withholding tax on income paid to the U.S. investor, and on any profit made on the eventual disposal of the investment. In addition, a U.S. direct investor would also need to consider the impact of the U.S. tax rules on foreign subsidiaries as these may result in further tax leakage.

Indirect Investment

An indirect investment through a U.K. holding company will result in some tax leakage at the African company level in the same way as a direct investment from the U.S. However, the imposition of a U.K. holding company may in some cases help to reduce the overall tax leakage for a U.S. investor wishing to invest in Africa through minimizing the overall withholding tax in the structure.

The U.K. has a much wider network of double tax treaties with African countries compared to the U.S., having entered into agreements with Botswana, Egypt, Gambia, Ghana, Ivory Coast, Kenya, Lesotho, Libya, Malawi, Morocco, Namibia, Nigeria, Sierra Leone, South Africa, Sudan, Swaziland, Uganda, Zambia and Zimbabwe. Each treaty should be considered on a case-by-case basis, but on the face of it there is scope under many of the treaties to minimize withholding tax leakage on payments routed through a U.K. company as compared to direct payment to a U.S. company. The U.K. company will be required to have sufficient substance in the U.K. in order to not fall foul of anti-treaty abuse laws.

The U.K. does not levy a withholding tax on payments of dividends to foreign entities. Therefore, the repatriation of income to the U.S. from a U.K. holding company should result in minimal tax leakage at the U.K. holding company level (i.e., on the small amount of any profit made by the U.K. company).

The sale of shares in a U.K. company by a U.S. shareholder would be outside the scope of U.K. capital gains tax. Therefore, on exit, a U.S. company could sell its shares in the U.K. holding company without incurring a charge to U.K. capital gains tax. The U.S. tax treatment of such a disposal would, however, need to be considered.

As discussed above, the now favorable U.K. CFC rules mean that, provided the correct structuring is in place, there should be no U.K. tax leakage through the imposition of a charge to U.K. tax on the income received by the underlying African subsidiary company.

In summary, it may be worthwhile for a U.S. investor to consider making its investment into Africa indirectly through a U.K. holding company. Such a structure might, in some cases, reduce the outbound withholding tax for an ultimate U.S. investor. In addition, the U.K.'s historically prohibitive CFC rules should no longer apply to impose a charge to U.K. tax on the profits of the African subsidiary. There could also be benefits of "pooling" investments into different African countries under the same U.K. holding company, especially where all of the underlying investments are in countries that have a double tax treaty with the U.K.

A Summary of

Key EU Legislation for U.S. Investment Advisors in 2012

By Simon Thomas, Partner
Samuel T. Brooks, Associate

MiFID II AIFMD EMIR FTT Solvency II MAD II

Broadly, key EU legislative initiatives currently in progress, from the perspective of an investment advisor, can be categorized as relating either to financial infrastructure or to operational issues (with some legislation relating to both). Legislation relating primarily to financial infrastructure includes—

- the replacement for the Markets in Financial Instruments Directive (**MiFID II**);
- the European Market Infrastructure Regulation (**EMIR**); and
- the proposed Financial Transactions Tax (the **FTT**).

Legislation primarily relating to operational issues includes—

- the Alternative Investment Fund Managers Directive (**AIFMD**);
- the replacement for the Market Abuse Directive (**MAD II**);
- the Regulation on Short Selling and certain aspects of Credit Default Swaps (**Short Selling Regulation**); and
- the Solvency II Directive (**Solvency II**).

Financial Infrastructure

MiFID II

MiFID II is in fact both a directive and a regulation (MiFIR), collectively intended to replace the EU Markets in Financial Instruments Directive, which has regulated investment services in financial instruments and the operation of regulated markets within the European Union since 2007. MiFID II is primarily concerned with the infrastructure of the financial industry, particularly the trading of over-the-counter (OTC) derivatives and commodity derivatives. However, it also contains new operational rules, most significantly with regards to "algorithmic" trading, governance and "dealing commissions." The EU Commission's initial draft proposals were issued in October 2011, and a revised draft, incorporating industry comments, is expected in the next few months. As currently envisaged, political agreement may be reached in the first quarter of 2013, with application of the new rules taking effect from 2015.

EMIR

EMIR will introduce new obligations on financial and certain nonfinancial counterparties to clear specified OTC derivatives contracts with central counterparties and report the details of all derivatives transactions to trade repositories. It will also introduce new authorization and ongoing requirements on such central counterparties and trade repositories. The final text of EMIR was agreed upon by the European Council, Parliament and Commission in February 2012, and is expected to be formally adopted by the European Parliament in mid-March 2012. EMIR is expected to be in force beginning January 1, 2013.

The FTT

The FTT currently remains at the proposal stage, but if enacted in its current form could become effective on January 1, 2014. The FTT would be payable on all transactions of equities and bonds at 0.1 percent of value and on all derivatives transactions (both exchange-traded and OTC) at 0.01 percent of value calculated on the basis of the derivative's notional underlying value. The proposals remain extremely controversial, with a study by the Alternative Investment Management Association (AIMA) suggesting that it could lead to a significant decrease in cross-border trading and the European Commission admitting it would likely reduce GDP growth as well as possibly aggregate tax revenues. Some EU Member States, including the U.K., have indicated that they believe the FTT should only be adopted if comparable measures are taken in other jurisdictions–particularly in the United States.

Operational Issues

Alternative Investment Fund Managers Directive

The AIFMD has been enacted, and EU Member States are required to transpose its provisions into national law by July 22, 2013. The AIFMD is intended to provide a harmonized EU-wide framework for the regulation of managers of all investment funds other than Undertakings for Collective Investment in Transferable Securities (UCITS)–the European equivalent of a U.S. mutual fund. U.S. investment advisors wishing to market non-EU funds in the European Union will be subject to registration and reporting requirements.

MAD II

In October 2010, the European Commission adopted proposals for a revised Market Abuse Directive (MAD II) and a new Regulation (MAR). The proposals are intended to establish a harmonized market abuse regime across the European Union, in order to reduce the possibility of regulatory arbitrage. Under the new regime, market abuse relating to financial instruments traded over the counter, as well as commodity derivatives, will be brought into scope and aligned more closely with the rules relating to securities markets. A new offense of "attempted market manipulation" will also be introduced. It is envisaged that the MAD II consultation and legislative process will generally run in parallel with MiFID II.

Short Selling Regulation

The Short Selling Regulation will come into effect on November 1, 2012, and will introduce restrictions and disclosure requirements on persons short selling EU shares and sovereign bonds, as well as prohibiting naked or uncovered credit default swaps (CDSs) relating to EU sovereign debt. The Short Selling Regulation will also provide Member States' regulatory authorities with significant emergency powers to, among other things, prohibit or restrict short sales and limit sovereign CDS transactions. Such powers may be exercised on a temporary basis for up to a three month period and may be extended by further periods up to three months if grounds continue. Authorities may also impose a restriction on short selling any financial instrument that has suffered a significant fall in price in a single day. This may be extended up to an additional two days if there is an additional significant fall in price.

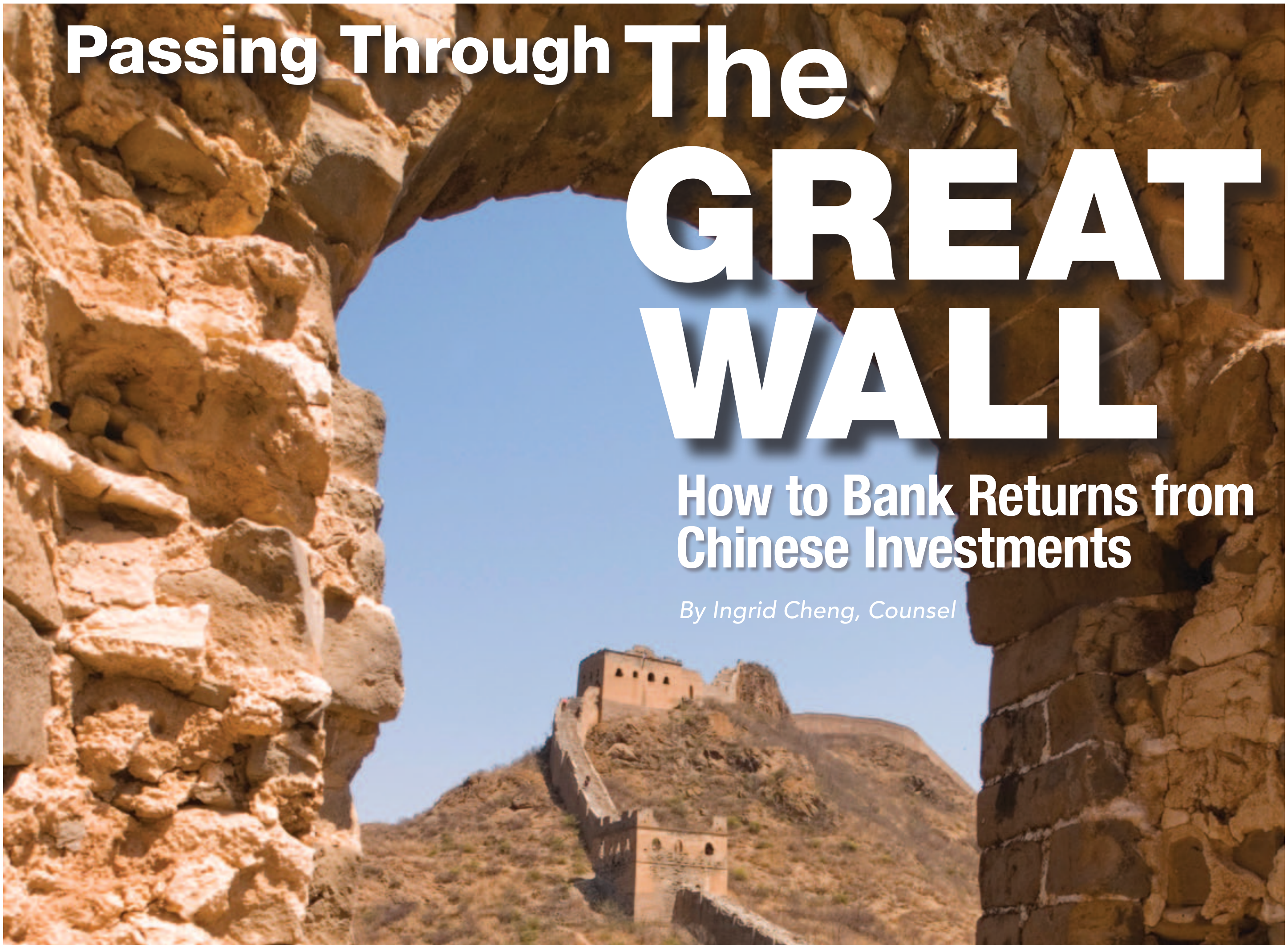
Solvency II

Although Solvency II is primarily significant to insurance companies, it will also be important for investment advisers, whose funds insurance companies invest in. Solvency II imposes substantial capital requirements on insurance companies as well as extensive reporting obligations. These reporting requirements will require significant input on balance sheet assets from funds in which insurance companies invest. Solvency II was published in the *Official Journal of the European Union* in December 2009, and implementation across the EU Member States is expected from January 1, 2014.

Passing Through The GREAT WALL

How to Bank Returns from Chinese Investments

By Ingrid Cheng, Counsel



With China's economy still booming, opportunities abound for foreign direct investment (FDI). Foreign exchange regulations in China are considerably tighter than in many other countries; however, foreign investors have complained that it is far more difficult to transfer capital out of China than it is to make the investment in China in the first place. Chinese regulators have taken note, and there has been a marked loosening of the regime related to "current account" foreign exchange (FX). So long as specified procedures are closely followed, repatriation of dividends and other capital is possible. This article summarizes some of the most important considerations with respect to Chinese FX issues, particularly the repatriation of capital from China under the foreign direct investment (FDI) regime.

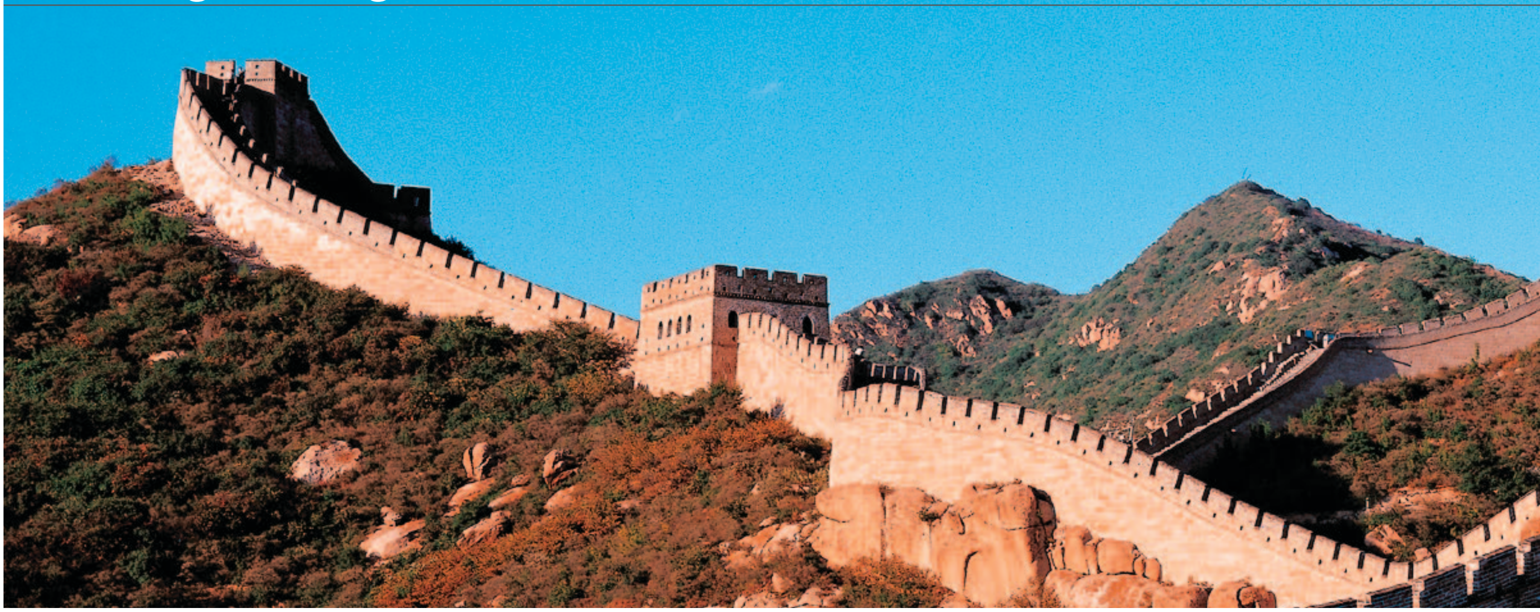
Key Regulators

China employs currency controls that are designed to prevent large withdrawals of capital from the country. The system functions through the following authorities:

1. PEOPLE'S BANK OF CHINA (PBOC)
   As the central bank of China, PBOC sets monetary policies, monitors FX market fluctuations and determines FX rates.
2. STATE ADMINISTRATION OF FOREIGN EXCHANGE (SAFE)
   SAFE manages and controls foreign currencies in China. It monitors FX bank accounts, approves FX transactions and registers all foreign debts.
3. DESIGNATED FX BANKS (DFXB)
   Authorized by the PBOC, DFXBs are the channel for FX to flow in and out of China. DFXBs follow SAFE's rules in processing FX wire transfers, periodically report to SAFE and share a synchronized database of FX transactions with SAFE.

Current Account and Capital Account

The FX accounts of a foreign invested enterprise (FIE) are divided into two categories: current account and capital account. While transactions involving



current account items have largely been liberalized, those involving capital account items remain restricted.

1. CURRENT ACCOUNT ITEMS
   Current account items are funds that occur in the ordinary course of business, including transactional funds such as payments to and receipts from international trading of goods and/or services and funds for daily operations. An FIE may freely purchase and sell current account FX at a DFXB without obtaining prior approval from SAFE; although, the FIE is still required to submit relevant documents upon the making of a cross-border payment or the receipt of funds, respectively, evidencing the truthfulness of the underlying foreign trade transaction for the DFXB to verify pursuant to the SAFE's requirements (e.g., the import/export contract, invoice, shipping documents, bill of lading and customs forms), invoices and tax clearance certificates in relation to the underlying transaction to such DFXB for verification.

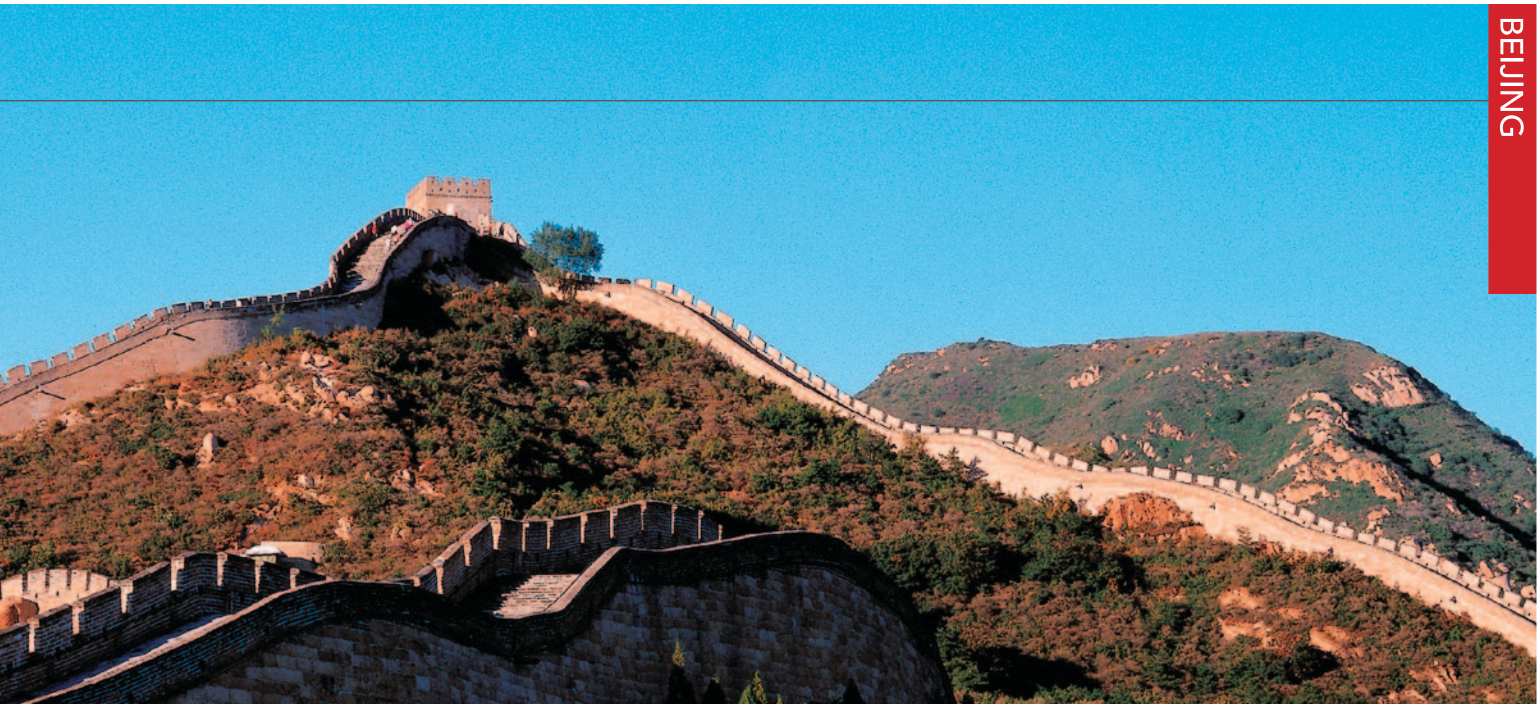
2. CAPITAL ACCOUNT ITEMS
   Capital account items are funds intended for use in FDI in the form of capital contributions, foreign loans and real estate purchases. Such transactions are subject to examinations and approvals by SAFE or its local branches, and SAFE will require approval documents issued by the Ministry of Commerce (the MOFCOM), the department in charge of FDI in China, or its local branches.

Repatriation of Dividends

Dividends are considered a current account item and can be remitted upon the satisfaction of the following requirements—

- the registered capital of the FIE has been fully paid;
- the FIE's cumulative losses carried forward from earlier years have been set off;
- any tax payable by the FIE has been cleared; and
- a minimum deduction of 10 percent of after-tax profits has been reserved for employee bonuses and welfare, enterprise expansion and reserve funds. This reservation may be capped when the cumulative amount of the mandatory reservations reaches 50 percent of the FIE's registered capital.

Assuming these requirements are met, the FIE may remit dividends abroad by submitting supporting documents to its DFXB, including a verification certificate of capital injection issued by a qualified accounting firm, certificates of tax clearance (from the local and state tax offices), its most recent audited financial report, a board resolution, its original FX registration certificate (issued by SAFE) and other required ancillary documents, which can generally be completed "on the spot" at the DFXB's counter and enable cleared dividends to be paid in either RMB or an FX to the designated offshore account.



Repatriation of Capital

An FIE may repatriate capital under three scenarios: capital reduction, equity transfer or dissolution. Each case is subject to specific regulations and governmental approvals; none of which can be completed "on-the-spot" at a DFXB counter.

1. CAPITAL REDUCTION
   Generally, an FIE may not reduce its registered capital during the term of its operation. In order to alter the total investment or production scale, the FIE must first submit a capital reduction application to the MOFCOM or its authorized local branch that initially approved the investment project. The reduction may not result in a lower capital amount than the minimum registered capital threshold applicable to that type of FIE required by law. Another requirement is that there is no pending litigation regarding the FIE at the time of application for the reduction.

   The FIE is required to submit its most recent balance sheet, an asset checklist, a list of creditors verified by a qualified accounting firm and a statement of debts arrangement (repayments or provision of guarantees to the creditors) to the MOFCOM. In addition, the FIE must directly notify its creditors or issue a public announcement of the capital reduction plan in a qualified newspaper. Within 30 days of receipt of such notice, or within 45 days of the public announcement, the FIE's creditors may require it to clear its debts or provide appropriate guarantees in order to proceed with the reduction. If the FIE's creditors complain, the MOFCOM may reject the capital reduction application. The MOFCOM will not approve a reduction if the debt issues cannot be settled properly. If the application for the reduction in capital is approved, the FIE will be required to make corresponding changes to the company registration information at the Administration for Industry and Commerce (AIC), China's enterprise registration authority.

   Upon completion of the procedures referenced above and receipt of an approval letter from the MOFCOM, the FIE may then request approval from SAFE for repatriation of the capital reduction, and make the remittance with its DFXB. This process may take two to six months. The FIE needs to obtain the MOFCOM approval of capital reduction, then SAFE approval on conversion and remittance of the reduced capital amount and lastly submit the MOFCOM and SAFE approvals to the DFXB to convert and wire the funds.

2. EQUITY TRANSFER
   In order to transfer an equity interest in a joint venture or a wholly foreign owned enterprise, the registered capital must be paid in full. All shareholders must consent to the transfer of any shares

to a third party, and shareholders' preemptive rights will apply. If any shareholders are opposed to the transfer, they are required to purchase the shares in question. If the dissenting shareholders do not purchase those shares, they will be deemed to have agreed to the proposed transfer. In addition, the transfer may not cause the foreign stake in the FIE to fall under 25 percent of its registered capital (unless the transfer results in the withdrawal of 100 percent of the foreign shares), and the purchaser must be a legal entity (i.e., not an individual). The parties must also look into the Foreign Investment Industrial Guidance Catalogue (the Catalogue), a long-standing tool used by the Chinese government to guide foreign investment in China, to ensure the proposed transfer complies with China's FDI policies. For example, if the proposed transaction involves limitation on foreign stake, the investor should ensure that the transaction does not cause the foreign equity percentage to exceed the equity share limitation.

Subject to the forgoing, the FIE may submit the equity transfer agreement to the MOFCOM and then proceed to submit it to the competent state and local tax offices, AIC and SAFE for their respective approval of the equity transfer, tax clearance, company change registration, FX conversion and remittance in order to remit the proceeds outside China. Assuming the equity transfer agreement is in place, the approval procedures generally take three to four months.

3. DISSOLUTION

Dissolution of an FIE may take place upon the expiration of its term as specified in the FIE's organization documents, by shareholders resolution, upon the revocation of a business license, by a mandated winding-up, merger or division, serious losses, as specified in the organizational documents, force majeure, a court petition initiated by shareholders representing at least 10 percent of the voting rights, upon default in capital contributions and upon other circumstances specified in its articles of association and/or shareholders agreement.

The FIE must apply for an approval from the MOFCOM for any proposed dissolution. Once granted, a liquidation committee will be formed and if the liquidation committee cannot be set up within 15 days after the occurrence of one of the stated dissolution facts, the People's Court will appoint the members of the liquidation committee, usually from the supervisory authorities of the FIE, such as accounting and legal professionals, to carry out the liquidation process. Any dissolution proceeds will be distributed, in order of priority to cover liquidation expenses, employee wages and social insurance, outstanding taxes, and debts and liabilities. Any remaining proceeds will then be distributed to the investors on a pro rata basis. When remitting residual sums (if any), the relevant DFXB will examine and verify the MOFCOM's approval, the final dissolution report provided by the liquidation committee and approved by the board of directors or shareholders, the tax clearance certificate, the AIC record and SAFE's approval.

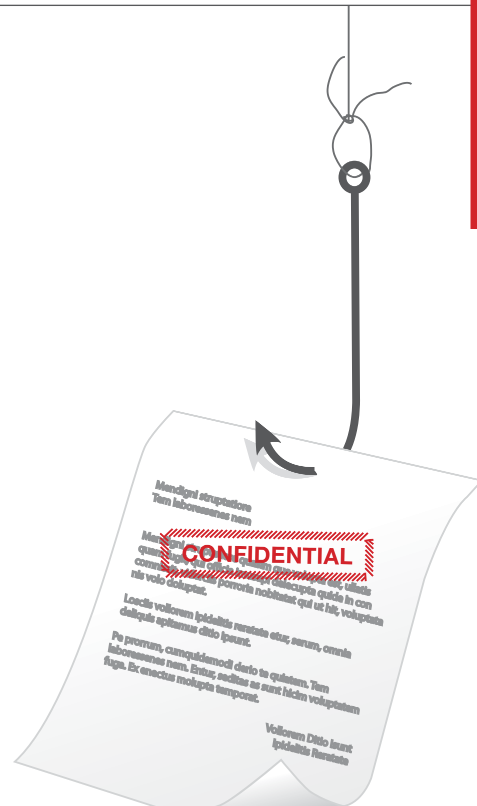
If at any time the FIE is found to be insolvent, a judicial bankruptcy proceeding will be triggered and a competent People's Court will be installed to carry out the distribution per the principles described above.

Withholding Tax

In addition to any taxation applicable to the FIE, foreign investors are subject to a withholding tax (WT) when receiving capital returns from China. A general 10 percent WT rate will apply if there is no applicable bilateral tax treaty specifying a particular rate. It is noteworthy that under the Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA), a Hong Kong resident holding company would enjoy more favorable WT tax rates compared to those of other jurisdictions, subject to the review and verification of China's tax authorities. The tax rate for dividends is 5 percent if the Hong Kong resident investor holds more than a 25 percent equity interest in the PRC subsidiary and 10 percent if the Hong Kong investor's equity interest is less than 25 percent. The tax rate for the transfer of equity or for dissolution proceeds will either be 0 percent or 10 percent, depending on whether the major real properties of the subsidiary are located in China. If no real properties are involved, a 10 percent WT will be attached if the Hong Kong transferor holds more than a 25 percent equity interest in the PRC subsidiary for a consecutive 12-month period prior to the transfer.

Traps for the Unwary

What Every International Investor Should Know About INSIDER Dealing Law In The U.K.



By Douglas A. Rappaport, Partner
Simon Thomas, Partner
Patrick M. Mott, Associate

Introduction

Over the last three years, the U.K.'s Financial Services Authority (the FSA) has emerged as one of the world's most aggressive regulators of insider trading or "insider dealing," as the offence is known in the U.K. Despite not securing a single insider dealing conviction during the first nine years of its mandate, the FSA has successfully obtained the insider dealing convictions of 13 individuals since 2009. The FSA shows no signs of slowing down this effort to deter insider dealing on U.K. markets, a total of 10 individuals are currently on trial in the U.K. for insider dealing and four more individuals are awaiting trial on insider dealing charges.

In light of this trend toward more active insider dealing enforcement, it is important for U.K. market participants to understand the broad range of conduct covered by the U.K. insider dealing regime. Those accustomed to analyzing the regulatory risk of executing specific trades under the fraud-based insider trading regime in place in the U.S. may be surprised to find that some time-honored techniques for insulating oneself from liability in the U.S. may be ineffective in the U.K. This article highlights some of the areas in which the insider dealing laws in force in the U.K. diverge from U.S. insider trading laws and discusses the impact of those divergences on investors seeking to adapt their compliance policies to address comprehensively the regulatory risks associated with trading in the U.K.

Background: The FSA and the U.K. Insider Dealing Regime

The FSA oversees enforcement of the U.K.'s two overlapping insider dealing laws. The Criminal Justice Act 1993 (the CJA) provides for the criminal prosecution of "insiders" who deal in price-affected securities on the basis of "inside information," encourage others to deal in price-affected securities on the basis of inside information or disclose inside information otherwise than in the proper performance of their employment, office or profession.

The Financial Services and Markets Act 2000 (the FSMA) provides for the imposition of civil penalties for various forms of "market abuse," including conduct that would constitute insider dealing or improper disclosure under the CJA. The insider dealing provisions of the FSMA cover conduct occurring within the U.K. as well as any conduct relating to "qualifying investments" on markets situated, operating or regulated in the U.K. The term "qualifying investment" includes shares in companies, bonds and other forms of negotiable securitized debt, derivatives on commodities, financial-futures contracts, forward interest-rate agreements, money-market instruments, interest-based swaps, currency swaps, equity swaps and options on any of the above instruments. Although the ranges of

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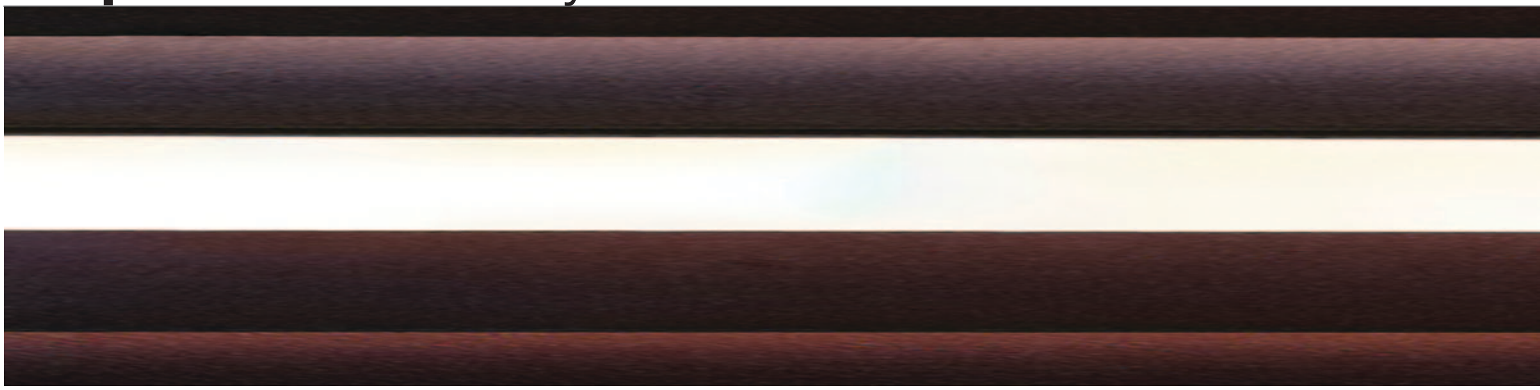

conduct covered by the insider dealing and improper disclosure prohibitions of the CJA and the FSMA are relatively similar, there are some slight differences of terminology. In this article, we will use the terminology from the FSMA, which covers a slightly broader range of conduct.

What Is Inside Information?

Under the FSMA, information is "inside information" if it is: (1) precise, (2) not generally available, (3) related to one or more issuers or qualifying investments and (4) likely to have a significant effect on the price of a qualifying investment or another instrument related to a qualifying investment. Information is "precise" if it is specific enough to enable a conclusion to be drawn as to the possible effect of an event or set of circumstances. Information is likely to have a "significant effect" on price if it is of a type that a reasonable investor would be likely to use in making an investment decision.

Who Is an Insider?

A person is an "insider" if he has inside information as a result of: (1) membership of an administrative, management or supervisory body of an issuer; (2) holding shares of an issuer; (3) having access to the information through the exercise of his employment, profession or duties or (4) criminal activities. In addition, a person may also be an "insider" if he has acquired the inside information by any other means as long as he could reasonably be expected to know that it is inside information. The importance of this last point for those accustomed to U.S. insider trading law cannot be overstated. Any person who acquires inside information by any means may be liable for dealing in the U.K. on the basis of that information.

What Constitutes Improper Disclosure and Encouragement?

An insider may be liable for disclosing inside information "otherwise than in the proper course of the exercise of the insider's employment, profession or duties." Importantly, and in contrast to U.S. law, the recipient of the disclosed information need not provide a personal benefit to the insider in order for the insider to be liable for improper disclosure. Likewise, taking or refraining from taking any action that has encouraged another person to engage in insider dealing or improper disclosure may also result in civil or criminal liability. Liability may be incurred even if the person being encouraged does not actually carry out the improper dealing or disclosure.

Lessons for Issuers and Investors

- *Beware of channel checks and other research techniques that could lead to the acquisition of inside information*

Under U.S. insider trading law, regulators typically must allege a breach of a duty of trust or confidence by either the person trading on the information or someone who provided the information to the trader directly or indirectly. As a result, through a research method known as "channel checking," investors may, in certain circumstances, legally trade on potentially material nonpublic information regarding a U.S. issuer if there is no breach of duty implicated in the disclosure of the information. Fund managers should exercise extreme caution before trading whenever they believe they are in possession of material nonpublic information, regardless of whether they are trading on a U.S. or a U.K. exchange. U.S. legal rules regarding breach of duty can be applied in

unpredictable ways, and the prudent course is generally to refrain from trading whenever a party comes into possession of material nonpublic information. Under the FSMA, however, any person who acquires inside information by any means–regardless of whether a duty was breached–may be held liable for dealing on the basis of the information. Those who wish to trade in U.K. markets must take responsibility for ensuring that any information acquired through channel checks, whether performed directly by the investor or indirectly by a consultant or third-party research provider, does not constitute "inside information" under the FSMA or the CJA.

- *Refusal to sign a nondisclosure agreement does not mean you are free to trade*

In the U.S., an investor may often be able to retain its ability to legally trade on information it obtains if there isn't a nondisclosure agreement (NDA) or other agreement to treat the information as confidential. In the U.K., however, an insider who receives inside information may need to refrain from dealing regardless of whether or not it entered into an NDA.

- *If you receive inside information, do not disclose it other than in the exercise of your professional duties*

In the U.S., a purchase or sale of securities is required before the government may assert a violation of the securities fraud laws, so no insider trading liability attaches if no one actually trades while in possession of material nonpublic information. While Regulation FD provides civil liability for issuers who selectively disclose inside information, it does not cover situations in which an employee of a private company improperly discloses inside information. In the U.K., however, improper disclosure of inside information may result in criminal or civil liability even if no trade occurs. Moreover, employees of private companies, including investment managers, could be liable for improper disclosures of information that could potentially affect the price of a qualifying investment even if no trade occurs.

- *Do not pressure issuers to disclose inside information*

Under the FSMA, an investor who encourages an employee of an issuer to provide inside information could be liable for encouraging another person to engage in market abuse. In theory, the employee of the issuer wouldn't even have to provide the information for the investor to be held liable. As a result, U.K. market participants should be extremely careful to phrase questions to issuers in a way that does not appear to be intended to elicit inside information.

Conclusion

The FSMA and the CJA provide the FSA with powerful tools to regulate a relatively broad range of market activity that may be legal if conducted in the United States. Investors looking to expand their trading activities into the U.K. must closely examine their compliance policies to ensure that they are up to the task of addressing the full scope of research, trading and investment management activities that could attract the attention of an increasingly aggressive FSA.

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