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Cloud Computing Continues to Loom Large on the International Data Privacy Agenda

By Daniel Cooper, Erin Egan, Henriette Tielemans and Mark Young
(Covington & Burling LLP)

While we wait for the next steps of the European Commission, Federal Trade Commission and Department of Commerce on the current consultations on European and U.S. data privacy laws, the shift to cloud computing continues to loom large on the international data privacy agenda. Government agencies on both sides of the Atlantic have begun to provide guidance to public sector bodies on moving to the cloud, and industry and policymakers continue to focus on the need to reflect this technological shift in today's legal frameworks. This article summarizes relevant reports and speeches on cloud computing from the past few weeks.

ENISA Reports on Data Breach Notification and Governmental Cloud in the EU

January was a busy month for the EU's "cyber security" agency, ENISA. First, it issued a report on January

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13 on data breach notifications in the EU. This is in response to the 2009 amendments to the ePrivacy Directive requiring telecom and internet service providers to issue notifications for personal data breaches, which Member States must transpose into national legislation by May 2011. The report reviews best practices in countries where data breaches already are required or are expected to be notified (e.g., Germany, Spain and Ireland), highlights concerns of providers and regulatory authorities regarding the new EU-wide mandatory notification regime, and identifies areas where further EU level or local guidance is needed.

Government agencies on both sides of the Atlantic have begun to provide guidance to public sector bodies on moving to the cloud, and industry and policymakers continue to focus on the need to reflect this technological shift in today's legal frameworks.

ENISA followed up the data breach paper with a report on January 17 on cloud computing in government. (To date there have been few such reports, other than draft German guidelines that were released in September 2010 on information security issues relating to the cloud.) The ENISA report is targeted at senior managers of public bodies who are considering cloud computing platforms and services. It summarizes relevant legal and regulatory considerations and highlights the pros and cons of different cloud models regarding information security and resilience. While ENISA acknowledges that cloud computing has the potential to offer public administrations substantial benefits and improvements over current IT provisioning, overall it urges European governments to adopt a staged approach in integrating cloud computing into their operations.

National Institute of Standards and Technology Draft Guidelines on Security and Privacy in Public Cloud

In the U.S., the National Institute of Standards and Technology (NIST) issued draft guidelines on security and privacy in public cloud computing. (<http://www.nist.gov/SP800-144>)

Cloud Computing Continues, continued on page 4

Cloud Computing Continues *(from page 4)*

Technology (“NIST”) issued drafts guidelines on February 2 for managing security and privacy in the cloud (SP 800-145). The document provides an overview of the security and privacy challenges for public cloud computing and presents recommendations that organizations should consider when outsourcing data, applications and infrastructure to a public cloud environment. Aside from the obvious suggestion to plan the security and privacy aspects of cloud computing solutions before engaging them, NIST encourages federal departments and agencies to ensure that any selected public cloud computing solution is configured, deployed, and managed to meet their security, privacy, and other requirements; emphasizes the importance of maintaining security in the client-side environment (e.g., over mobile devices, browsers, plug-ins and applications that are used to access cloud services); and stresses the need to maintain accountability over the privacy and security of data through strong management practices. Similar to the ENISA report, NIST emphasizes that cloud computing should be approached carefully with due consideration to the sensitivity of data, and addresses the issue of negotiating service agreements with public cloud providers. NIST invites comments on the guidelines by February 28. Complementing the guidelines, NIST also has published “The NIST definition of cloud computing” (SP 800-145), which is intended to enhance and inform the public debate on cloud computing.

Microsoft’s General Counsel Discusses the Policy Challenges and Opportunities for Cloud Computing at the French Assemblée Nationale in Paris

Building on a speech and white paper that was released last January, Brad Smith gave a speech on January 24 at the French Assemblée Nationale about the trends and possibilities of cloud computing, and what needs to be done in the way of better laws and improved industry and government cooperation to get ready for this technological shift. Microsoft has identified several regulatory reforms to enable Europe to maximize the economic and social benefits of the cloud, including harmonizing the EU’s data governance rules, applying a single law to cloud

providers operating in multiple Member States, facilitating international transfers, establishing clear and consistent data retention rules, and bolstering security in the cloud. Microsoft set out more detail about these topics in a new white paper and summary of “Steps Europe Can Take to Promote the Cloud” that it published to accompany Brad Smith’s speech.

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Commissioner Neelie Kroes outlines a European Cloud Computing Strategy at Davos

Finally, following on from ENISA’s report on cloud computing in government, Commissioner Neelie Kroes set out some further thoughts on a European Cloud Computing Strategy at Davos on January 27. In an encouraging sign for cloud providers and European industry more broadly, Commissioner Kroes spoke positively about the need to ensure that effective data protection and the EU’s Single Market do not clash with cloud computing, and her wish to make Europe “not just ‘cloud-friendly’ but ‘cloud-active.’” To help achieve these goals, Commissioner Kroes indicated that her strategy would cover three broad areas: the legal framework regarding data protection and privacy; technical and commercial fundamentals, including research, security and technical standards; and the market, e.g., support for pilot projects aiming at cloud deployment. Commissioner Kroes will be inviting cloud providers and cloud users to Brussels “for a series of intense consultations” in the spring. □

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EU Suspends Carbon Trading After Almost \$38 Million Stolen

By Brandon H. Barnes and Susan M. Cooke (McDermott Will & Emery LLP)

The most recent theft of almost \$38 million in EU Emission Trading System carbon credits may shift political support in favor of centralization and abolition of national registries.

On January 20, 2011, the European Commission, the executive arm of the European Union (EU) in charge of overseeing the Emission Trading System (ETS), suspended all spot-trading activity on the carbon emissions market after determining US\$37.7 million worth of credits may have been stolen. The EU suspects the fraud occurred because of insufficient network security on the national carbon registries for Austria, the Czech Republic, Estonia, Greece and Poland. Maria Kokkonen, spokeswoman for the EU's Climate Action Commissioner, announced that spot-trading will be suspended until all countries participating in the ETS provide the commission with independent reports confirming network security system upgrades.

The ETS is the oldest and largest of the greenhouse gas trading markets established to reduce carbon emissions from stationary sources through market-based incentives. The trading system places a "cap" on annual carbon dioxide emissions and allows entities whose carbon emissions are below their allowable cap to sell surplus emission credits to other entities that require additional credits to cover their carbon emissions. The total value of ETS credits traded in 2010 was almost \$120 billion, with spot trading accounting for 10 to 20 percent of those trades. The ETS derivatives and futures markets that comprise the rest of the trading are not affected by the suspension.

The recent theft is the latest in a string of trading issues involving ETS and the national registries. In November 2010, hackers stole almost \$33 million worth of allowances from Holcim Ltd., a Swiss cement company, which held credits with the Romanian National Registry for Greenhouse Gases. There have been similar reports of fraudulent transfers in the Dutch and German registries.

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Currently, each of the countries participating in the ETS operates an independent national carbon registry to track carbon credit ownership within that country. Unlike a bond or stock trade that is settled through a clearinghouse, the national registries cannot verify ownership before moving the credits into an account. The credits are traded through independent emissions exchanges; however, since the credits only exist online, they can then be sold in multiple transactions before the owners are aware that they have been stolen.

While a 2013 deadline for centralizing ETS trading into one clearinghouse in Brussels is fast approaching, earlier political opposition to such centralization appears to be waning as a result of pressure from the trading community.

While catching the thieves is a primary concern, the speed of emission credit trading also raises complex legal questions over ownership and what entity suffers the loss in the event of theft. Depending on which country's law applies, the "owner" can be the original owner, one of the entities that bought the credits, the exchanges where the credits were traded or the defrauded national registries.

ETS has suffered the setbacks characteristic of an immature financial market, namely, volatility, booms, busts, and fraud and abuse. When it was established in 2005, centralization of the trading market and abolition of national registries were discussed but never implemented, due to lack of political support from individual countries. While a 2013 deadline for centralizing ETS trading into one clearinghouse in Brussels is fast approaching, earlier political opposition to such centralization appears to be waning as a result of pressure from the trading community.

Based upon the lessons learned in EU ETS design, it can be expected that the new clearinghouse will incorporate centralized registry and exchange mechanisms like those adopted in China and California. This in turn will increase the security of the credits, thereby increasing investor confidence and bolstering public opinion in the efficacy of a cap-and-trade program. □

European Truck Industry Cartel Investigations and Rewards for Information Highlight Enforcement Tools

By Frances Murphy and Natasha Hall (Jones Day)

New investigations into possible cartel activity among European truck manufacturers have highlighted the tools available to some antitrust enforcement agencies. In separate investigations both the European Commission (EC) and the UK's Office of Fair Trading (OFT) have conducted on-site investigations of the offices of truck manufacturers, and the OFT has gone a step further and offered a reward to individuals who come forward with additional information about the alleged cartel. This may be designed to support a more robust criminal prosecution of cartel activity by the UK.

In September 2010, the OFT opened investigations into suspected price-fixing and market-allocation by truck manufacturers. The OFT carried out an unannounced inspection at the UK premises of Mercedes-Benz and reportedly requested information from several other manufacturers. It also used its criminal powers to arrest the managing director of Mercedes-Benz's UK commercial vehicle operations.

The OFT is pursuing parallel civil and criminal investigations under the Competition Act 1998 and the Enterprise Act 2002, respectively, which it commenced after receiving information on suspected cartel activity, possibly provided by a whistleblower or a third party making a complaint.

In January 2011, the EC also conducted on-site investigations at the premises of several truck manufacturing companies in a number of Member States. The EC said it had reason to believe that the companies may have infringed EU antitrust rules on cartels and restrictive business practices or the abuse of a dominant market position (Articles 101 and 102 TFEU).

The UK Investigation

In late January, the EC investigations were followed by the OFT appealing for further information in its civil and criminal investigations, offering the possibility of rewards

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of up to £100,000 for those individuals that came forward. The OFT is seeking information that may be relevant to its investigations, in particular relating to suspected contacts between individuals from competing vehicle manufacturers operating in the UK. The OFT also highlighted the possible availability of leniency.

This is unprecedented action by the OFT. The OFT has never before appealed for information with the offer of a financial reward. In addition, the OFT has never before made a payment to an individual under its reward scheme, which was introduced in 2008.

In late January, the EC investigations were followed by the OFT appealing for further information in its civil and criminal investigations, offering the possibility of rewards of up to £100,000 for those individuals that came forward. The OFT has never before appealed for information with the offer of a financial reward.

The UK's Informant Reward Scheme

Under the informant reward scheme, an individual may receive up to £100,000 for providing information on a cartel to the OFT. The amount of the reward actually given will depend on the effort and risk taken by the informant, the value of the new information, and the harm to the economy and consumers from the conduct. The UK is one of only a handful of jurisdictions to offer informant rewards to individuals, along with Hungary, South Korea and Pakistan.

The OFT stated that individuals directly involved in an alleged cartel ordinarily may not claim a reward. Instead the OFT expects them to apply for immunity from criminal sanctions under its leniency policy (described below). Nonetheless, the OFT may consider a reward in addition to leniency, where the person's role in the cartel was peripheral, such as an employee occasionally directed by his superiors to attend a cartel meeting, but not asked to take an active part in the cartel.

The UK reward is intended to encourage people with

“inside” knowledge to come forward, to increase the chances of detecting cartels and improve the possibility of criminal convictions. In civil investigations the OFT very often finds the existence of a cartel on the basis of circumstantial evidence. However, circumstantial evidence would unlikely be sufficient to secure a conviction in the criminal courts. The OFT’s active use of the scheme perhaps signals that it is intending to get even tougher on sanctioning cartel activity, including pursuing both civil and criminal sanctions where at all possible.

The UK’s Leniency Program

In addition to its reward scheme, the OFT operates a leniency program, whereby an individual or a company may receive immunity from criminal prosecution and financial sanctions, respectively. The goal is to increase detection of cartels, which are secretive by nature. In order to gain complete immunity, certain conditions must be satisfied, as set out below.

For individuals, they must admit participation in the criminal offence, provide all information and cooperate fully with the OFT, refrain from further participation in the cartel, and not have taken steps to coerce another undertaking to take part in the cartel. In addition, the OFT must not believe that it already has, or is in the course of gathering, sufficient information to bring a successful prosecution of that individual.

For a company, it must provide all information and cooperate fully with the OFT, refrain from further participation in the cartel, be the first to report and confess involvement in the cartel, and not have taken steps to coerce another undertaking to take part in the cartel activity. The OFT must not have had any pre-existing investigation into the cartel.

In the trucking investigation, since the OFT already has commenced civil and criminal investigations into suspected cartel activity in the sector, both individuals and companies will now struggle to obtain immunity from criminal penalties and fines. However, if a company has succeeded already in obtaining full civil immunity, then its past and present employees will enjoy automatic immunity from criminal investigation. The OFT may also be willing to grant immunity to employees of any company that has succeeded in obtaining partial immunity.

The European Commission Investigation

The EC also is conducting a civil investigation of suspected competition law infringements in the truck manufacturing industry. The EC started its investigation aggressively with simultaneous dawn raids, in a number of Member States including reportedly Sweden, the Netherlands, Italy, Belgium, Luxembourg and Germany.

Less is known about the current status of this investigation, and there is no legal deadline by which the EC must complete its inquiries. Like the OFT in the UK,

the EC operates a leniency policy for companies, applying similar conditions to those in the UK. However, the EC does not offer individual rewards and does not have the jurisdiction to carry out criminal investigations.

The OFT’s position is that there is no link between the two investigations, which it says are being conducted separately and are different in scope. However, the OFT has also confirmed that it is cooperating closely with the EC .

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Conclusions

Both investigations are in their early stages. Therefore it will likely be some months before further information about the investigations becomes public. In the meantime, the investigations and the OFT’s highly publicized use of its rewards scheme will serve as a stark reminder of the risks of cartel activity by a corporation or its employees. Involvement may be uncovered by a fellow cartel member blowing the whistle or by employees who are aware of the conduct. Civil and criminal sanctions will be pursued with vigor, even if that means the government must make substantial payments to obtain necessary information. □

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European Food Safety Authority Releases Initial Guidance on Risk Assessment of Food and Feed Applications of Nanotechnologies

By Dr. Anna Gergely and Erik Janus (Step toe & Johnson LLP)

On January 5, 2011, the European Food Safety Authority (EFSA) endorsed for public consultation its draft guidance on risk assessment concerning potential risks from applications of nanoscience and nanotechnologies to food and animal feed. Stakeholders and interested parties have the opportunity to comment on the guidance until February 25, 2011.

Building on EFSA's previous scientific opinion of February 2009 on the potential risks associated with nanoscience and nanotechnology in food and feed applications, the purpose of the present guidance is to provide risk assessors, regulators and other stakeholders with practical advice on a risk assessment methodology for engineered nanomaterials used in food and feed.

The draft document represents the first regulatory guidance on risk assessment of engineered nanomaterials used in food and animal feed, and covers all potential applications, including food additives, enzymes, flavorings, food contact materials, novel foods, feed additives and pesticides. The EFSA guidance distinguishes between risk assessment of nanomaterials concerning (i) products/applications intended for consumption by humans or animals, (ii) agrochemicals used in plant production, and (iii) products coming into contact with food/feed.

For the assessment of a nanoscale material used in food and feed applications, where the non-nanoform (i.e., 'bulk form') of the substance is approved for the same intended use, the guidance outlines the additional data needed to address potential intrinsic hazards that may arise from the nanoform. The supplementary data criteria include in vitro genotoxicity tests; information on absorption, distribution, metabolism and excretion ('mechanistic studies'); and a 90-day oral rodent toxicity

study. Additional in vivo data requirements may be triggered 'depending on the outcome of these studies and on the comparison with data on the non-nanoform.' One such criterion is for an additional toxicity study with an animal species that is phylogenetically different from a rodent (e.g., rabbit, dog, pig, non-human primate), which is similar to the data requirements under the US Environmental Protection Agency's Federal Insecticide, Fungicide and

Using these testing guidelines and risk assessment strategies as a baseline allows for greater regulatory certainty; however, the decision-making agencies will continue to rely on industry to provide high-quality information for risk assessment (some of which will be considered confidential).

Rodenticide Act (FIFRA). To register an active ingredient in an antimicrobial product for food uses, FIFRA requires two 90-day animal studies with a rodent and non-rodent species. Depending on the results of these Tier 1 studies, FIFRA may also require a one-year non-rodent oral toxicity study. Despite animal welfare concerns, there are several compelling scientific reasons (in addition to regulatory requirements) to rely on in vivo studies to assess the potential toxicity of nanoscale materials.

In the case where the engineered nanomaterial in question 'persists in the food/feed matrix and in gastrointestinal fluids and has no approved non-nanoform application', then relevant EFSA testing guidelines for its intended application should be used following certain modifications as outlined in the guidance. The issue of test modifications is largely one of kinetics and the appropriate adjustments to measurement and testing protocols to ensure the most relevant and useful information is collected. This is reflected in the EFSA statement: 'Some test models and standard testing protocols used for non-nanoform substances may not necessarily be appropriate or optimal.'

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The guidance appears to be an initial reasoned approach that takes many thoughtful areas into consideration, such as the need to explore alternative dose metrics, the local interaction between material properties and chemical properties at the target site and the resultant kinetics, a focus on non-soluble and non-biodegradable materials, bioavailability issues specific to the food/feed matrix and route of exposure, and the confounding effects often found at very high testing doses. EFSA points out that existing conventional risk assessment paradigms should be sufficient in most cases, and states: 'A loss of nano-specific properties will move the risk assessment into

a conventional risk assessment and the nano-specific risk assessment procedure will no longer apply.'

Using these testing guidelines and risk assessment strategies as a baseline allows for greater regulatory certainty; however, the decision-making agencies will continue to rely on industry to provide high-quality information for risk assessment (some of which will be considered confidential). Collectively, these decisions require much thought and attention up front to identify the most relevant concerns and how best to address them without sacrificing one's competitive position in the market. □

Leveraged Landscape for 2011

By Neil Caddy (Mayer Brown LLP)

The signs for the leveraged finance market in 2011 are mixed. Questions remain as to whether this year will see a fresh spate of restructurings and/or continued growth in primary issuance. While data compiled by Fitch Ratings has shown that European PE backed company default rates slowed in 2010 (and premier league spending during the January transfer window topped £225 million compared with £30 million last year), the primary leveraged finance market has started slowly this year.

The European leveraged finance market improved during 2010 with a trend away from small club deals to larger and widely syndicated deals signaling a return in market confidence. Oversubscriptions have been reported on recent deals such as Vue Entertainment, Britax, Picard Surgeles and Convatec showing a healthy appetite for well structured and priced LBO deals. However the leveraged finance market still remains depressed compared with historical levels.

There are a number of recurring themes and factors that will continue to inform the debate as to what the year holds in store and impact on how the year will unfold.

Macro Situation

Macro-economic conditions remain on a knife edge. Austerity measures being implemented by a

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number of European governments may, at least in the short term, lead to reduced consumer spending and unemployment. The UK economy shrank by 0.5% in the fourth quarter of 2010 and fears of creeping inflation and therefore potential interest rate rises could stifle the prospects of growth. The well documented

The European leveraged finance market improved during 2010 with a trend away from small club deals to larger and widely syndicated deals signaling a return in market confidence.

and continuing sovereign crises in Portugal, Ireland, Italy, Greece and Spain may well trigger difficulties for leveraged credits with high dependency on the economies of those countries. For example, lenders to the Greek casino group Regency Entertainment are already anticipating covenant breaches. Other leveraged credits in those countries and elsewhere may find that their covenants come under pressure as required levels become tighter and underlying performance remains, at best, flat. Some believe that there have not been as many LBO restructurings as might have been expected given the parlous state of the world economy in recent years, so we may see a correction of that.

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Leveraged Landscape *(from page 9)*

Bond Market

The European high yield market performed strongly in 2010. Analysts estimate that 2011 will see around EUR 45bn high yield issuance in Europe. Much of the issuance in 2010 was used to refinance impending maturities and many market participants expect this to continue. However there has been a rise in the number of LBOs where “senior secured” high-yield bonds have provided all of the term debt and the loan market a working capital facility. Loan participants are becoming more comfortable with this structure where the bonds share in the same security and guarantee package and rank *pari passu* with the loans (albeit that the working capital line is afforded “super senior” status in a default scenario).

Due to the increased liquidity in the high-yield bond market the headline cost is very competitive when compared with the loan market (and may well become more so with the advent of additional costs that banks may pass on in relation to Basel III – see below).

With all of that said however, the high yield bond market is notoriously fragile and does have a propensity to close very suddenly.

CLO Position

Many CLOs are still in their re-investment periods and many will continue to run for the next year or two. This fuels loan market capacity since CLO managers are incentivized to reinvest any repayments or pre-payments they receive due to their cheap cost of funds relative to the margins available on today’s loans. This will continue to be the case in the near term particularly if high yield bonds continue to refinance existing CLO debt holdings. However, some reinvestment periods do look set to close during 2011 and it is estimated that around 70% of CLOs’ reinvestment periods will end before 2014. If CLO supply does dry up and new CLO funds (as it would appear likely) cannot fill the void this could impact primary LBO activity and hinder refinancing/amend and extend efforts.

Refinancing Wall/Cliff

A number of credits have already refinanced/cleaned up their capital structure, in a lot of cases, by tapping the bond market. While refinancing/maturity extension does still remain a focus for many borrowers some companies may also postpone refinancing either due to the cost of doing so (since loan financing will now be on average around twice as expensive as the loan financing it replaces) or because better credits hoover up what supply there is. In any event 2011 is unlikely to be a pinch point for maturity triggered restructurings since the bulk of the refinancing cliff is unlikely to hit until 2013/14.

Basel III

Although full implementation is a way off, now that the final text of the Basel III package of capital and liquidity reforms has been issued, it seems likely that prudent banks will now begin to observe how their activities would be regarded under Basel III. For many banks this will begin to affect behavior now so that banks do not need implement all changes that they need to make all in one hit and from a standing start. While the full effect on the loan and bank market is still to be seen as the detail is digested and considered, there are already a number of effects that can be postulated:

In any event 2011 is unlikely to be a pinch point for maturity triggered restructurings since the bulk of the refinancing cliff is unlikely to hit until 2013/14.

Increased capital and liquidity requirements and restriction on overall leverage may well result in higher costs to the banks and therefore for borrowers

Increased risk weighting for exposure to financial institutions may increase appetite to lend to corporates instead but at the same time may restrict banks that rely heavily on the interbank market for funding

The imposition of a leverage ratio (i.e. an overall cap on capital: total assets) may mean an overall reduction on bank funded liquidity in the market. Since the assets in the ratio calculation receive no risk weighting, this may also mean that there is an increased demand for leveraged, high yielding credits to generate a higher return on a bank’s smaller asset base

The liquidity coverage ratio requires that banks have a sufficient pool of liquid assets to cover potential cash outflows over a 30 day period. Banks would therefore need to have the entirety of any revolving credit facility commitments covered by liquid assets. This may well become relevant to revolving credit facilities proposed from now on since revolving credit facilities entered into with the customary 6 year availability period will still theoretically be in place in 2015 when it is projected that banks will have to be compliant with the liquidity coverage ratio

The net stable funding ratio (which effectively requires long term assets to be matched by long term funding) may mean that banks are less willing to commit to the long term 6 year maturity leveraged finance loans (although in theory for loans granted this year

even if they remained on their books until maturity they would mature prior to 2018 when the net stable funding ratio is due to be implemented)

Bonds are regarded as liquid assets for the purposes of the net stable funding ratio so they are not required to be match funded (whereas loans are) meaning that perhaps banks will have more incentive to recommend to their clients that they issue bonds rather than loans

Heightened Scrutiny

Those new deals that do get done will remain subject to the greater scrutiny that has characterized the market in the last couple of years. As a result of this secondary/tertiary buyouts have been more readily "bankable" than new credits coming to market. Higher yields will still be required to get deals done with margins still up around 4.50-5.00% with OIDs and LIBOR/EURIBOR floors likely to remain a feature in the market.

Despite healthy competition for assets as a result of the "dry powder" currently available, sponsors must also be analyzing potential acquisitions more closely.

Factors such as (i) more risk averse lenders; (ii) lenders requiring more "skin in the game" so that sponsors take less risks from a strategy / operational perspective; (iii)

Despite healthy competition for assets as a result of the "dry powder" currently available, sponsors must also be analyzing potential acquisitions more closely.

less debt available generally; and (iv) the greater cost of funds putting pressure on target debt capacity, all mean that sponsors need to write greater equity cheques and therefore need to have a more compelling equity story to justify investments. □

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Roundup

By Reuters

EU Stability Watchdog May Pinpoint Countries, Favors Stress-test Publishing

Europe's new super-watchdog, the European System Risk Board, will single out problems bubbling in individual countries if they pose a risk to the wider system, said new body leader, Jean-Claude Trichet.

Trichet, who is also president of the European Central Bank, said at a hearing at the Economic and Monetary Affairs Committee of the European Parliament that the ESRB was also looking at how best to design its warnings.

Later, European Central Bank Governing Council Member Ewald Nowotny said most members of the board support publishing the results of commercial bank stress tests. Nowotny, a member of the risk board, said during a panel discussion that there appeared to be a political majority in favor of comprehensive publication.

EU to Present Draft Law Curbing Auditors in November

Auditing firms in the European Union face more competition and curbs on their activities to restore their "tarnished" image, the bloc's financial services chief said.

EU Internal Market Commissioner Michel Barnier told a hearing on auditing in Brussels that he intended to make proposals on the industry in November. Lawmakers worry the sector is too concentrated and if one of the big four auditors collapsed it could destabilize markets. Policymakers also ask why auditors gave banks a clean bill of health when many of them had to be rescued by taxpayers as the financial crisis unfolded.

Barnier said record feedback from a public consultation on the future of auditing in the EU showed some support for putting ceilings on the total market share of the bigger auditors for listed companies. He also mentioned the possibility of "joint auditing" in which two firms, including one outside the big four, would take part. Auditors could have a "European passport" to operate across borders and there could also be a "two-speed" set of rules, with a lighter touch for smaller auditors to help them grow.

Steven Maijoor, chair of the new European Securities and Markets Authority, said better quality auditing is needed to create a single market for an auditing passport system.

Barnier said the role of auditors should also be "clarified" to see whether they should go beyond endorsing accounts and give an opinion on the state of health of the company.

Separately, the Bank of England and the Financial Services Authority published a draft code for consultation to require auditors to tell regulators about concerns over clients.

Paris and Berlin -- the driving forces behind euro zone policy -- set out a wish-list of measures they want euro zone and the wider EU to adopt to improve competitiveness and help tackle the year-long debt crisis.

EU Mulls Penalties to Control Derivatives Trade

The European Union's executive is examining penalties on derivative trading to force controls on the opaque sector that has been blamed for spiraling grain prices.

Michel Barnier, the top EU official in charge of changing the rules of finance, announced possible penalties to force traders to keep extra capital if they do not route their business through central clearing houses, which connect traders, record their activity and step in if a deal breaks down.

Officials believe this makes the financial system safer because clearing houses provide a safety net in the event of a collapse like that of Lehman Brothers. They also keep a paper trail, making it easier for regulators to enforce order. Barnier also wants more power for regulators to intervene when speculative positions in commodity-linked derivatives send grain or energy prices spiraling.

The EU Commission plans to push traders to disclose positions and is also considering imposing so-called position limits to stop mega-trades that could upset markets.

As in the past, however, Berlin and Paris are likely to face opposition from London to any new regulations, presenting an obstacle that could force them to water down their proposals.

Irish Government Says Has No Mandate for Recapitalizing

Ireland's outgoing government has shelved plans to inject up to 10 billion euros into local banks until after an election, throwing down a challenge to opposition parties who want bondholders to shoulder some of the cost.

Under an EU/IMF bailout, Dublin had agreed to boost the capital in Bank of Ireland, AIB and EBS Building Society by the end of February, but Finance Minister Brian Lenihan told a news conference he lacked authority to proceed after the collapse of the governing coalition late last month.

Just two hours earlier, the IMF had warned that with an election looming on February 25, Ireland's politicians could hold up the agreed overhaul of the banking sector, which triggered the rescue package amid mounting loan losses and a flood of deposit withdrawals. Lenihan said he told the IMF and the EU of his decision and stressed that the banks, which have already received 11.5 billion euros in state funds, were adequately capitalized.

Lenihan's surprise move means the main opposition parties, expected to form a new coalition government, will be faced with an immediate decision on whether to follow through with their tough line on banks' bondholders.

Paris, Berlin Reach Deal on Stronger Eurozone, Others Frustrated

Germany and France tried to win backing for a pact to strengthen the euro zone economy, but many other EU states were angered by what they saw as a 'fait accompli' and the measures contained in it.

Paris and Berlin -- the driving forces behind euro zone policy -- set out a wish-list of measures they want euro zone and the wider EU to adopt to improve competitiveness and help tackle the year-long debt crisis. The proposals included limits on debt levels written into national laws, a higher retirement age, the abolition of wages indexed to inflation, unified bank crisis-resolution mechanisms, and a minimum corporate tax rate

But there was almost immediate pushback against the proposals, with large and small EU states, from Belgium and Austria to Ireland, Spain, Portugal, Poland and Luxembourg expressing aggravation at France and Germany's methods, as well as the substance of the six-point proposal. The issue is likely to be taken up again at an extra summit after March 9, Germany said, with the aim still to try to forge an agreement by the end of next month.

Google, EU in Antitrust Resolution Talks

Google and European Union regulators are in early talks to resolve an antitrust probe against the Internet's dominant search engine, a source familiar with the case said. A deal could avert a lengthy battle and possible fine for the U.S.-based company.

The European Commission opened an investigation into Google last November after three complainants accused it of abusing its position by demoting rival sites in search results and giving preference to its own services.

A decision on whether the tentative talks could lead to a settlement could take months. A Commission spokeswoman said the EU executive was not in discussions with Google at the moment and was still reviewing the case.

Google Chief Executive Eric Schmidt told Britain's Sunday Telegraph in an interview that the company was keen to avoid a lengthy legal battle.

Auditing firms in the European Union face more competition and curbs on their activities to restore their "tarnished" image, the bloc's financial services chief said.

EU Seen Pushing Ahead on Radical Contract Law Plans

The European Union's executive is expected to present plans for common legal safeguards for Internet shoppers later this year, despite deep skepticism among member states, an EU official indicated.

EU Justice Commissioner Viviane Reding unveiled preliminary plans last July for some form of European contract law -- giving common rights of redress if goods do not arrive for instance -- in a bid to better exploit a single market of 500 million consumers by encouraging cross-border shopping and competition.

Reding is expected to propose reform by year end.

Andres Stein, one of Reding's officials, acknowledged that a single European contract law imposed on EU states to replace national rules had been ruled out given the degree of opposition.

Despite a "great deal of skepticism" among consumer groups, businesses and EU states over the need for change, a public consultation showed support for two less radical measures.

Some states backed a "toolbox" of common approaches to future consumer law, though this could take years to make an impact. Others, including online retailers, supported a "28th" law that would give consumers the right to opt-in using a pan-EU contract law -- a reference to a regime running alongside national law in the 27-country EU. That is the step Reding is widely expected to propose. □

The Bribery Act: Are the Reports of its Death Greatly Exaggerated?

By Richard Kelly, Jo Rickard, Philip Urofsky and Danforth Newcomb
(Shearman & Sterling LLP)

There has been a flurry of recent stories about the implementation of the UK Bribery Act being delayed, with a leading business group describing it as “not fit for purpose” and some newspapers calling for it to be dropped altogether. All of this has generated a great deal of uncertainty on when – and perhaps even whether – the Act will now come into force. Our view is that the political damage of failing to implement the Act would be so great that it is still more likely than not that the Act will come into force later this year.

Delayed Implementation

The Act was passed in April 2010 after many years of international criticism, particularly from the OECD, of the adequacy of the UK’s anti-corruption laws. Despite the UK’s signature of the OECD Convention in 1997 and regular criticism from the OECD Working Group on Bribery from 2000 onwards, it took a further 10 years before Parliament finally enacted a comprehensive reform of the U.K.’s anti-corruption laws during the final days of the Labour Government. The Act requires the Secretary of State to issue guidance on the measures, which companies can put in place to prevent people associated with them from paying bribes. Originally that

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guidance was expected in the summer of 2010, with the Act then going live in October 2010. However, in July 2010 the new Government announced, apparently in response to widespread concern about the Act’s stringent standards and its uncertain breadth, that there would be a short consultation on the content of the guidance, with the finalized guidance to be released early in 2011 and the Act coming into force in April 2011.

Our view is that the political damage of failing to implement the Bribery Act would be so great that it is still more likely than not that the Act will come into force later this year.

That was the plan. However, January has now passed without the finalized guidance being issued. Furthermore, the Ministry of Justice has said that the Act will not come into force until three months after the finalized guidance is published. As such, May is now the earliest time that the Act could be implemented. In addition, the Act is now being examined again in the context of the UK Growth Review, which is concerned with identifying and removing impediments to growth of the UK’s private sector.

This further delay has caused something of a furor. Mark Pieth, Chair of the OECD’s Working Group on Bribery, has described it as “very disappointing.” Equally, Transparency International has accused the UK government of “back pedaling” on the Act, saying that this further delay is “disastrous news” and that it “raises serious doubts about the credibility of the Government’s commitment to the [Act]....”

Against the background of the sustained international criticism of the UK’s existing anti-bribery laws and prosecutorial record, the scale of political damage which would be caused by significant delay or amendment to the Act most likely rules out either option now. The US experience with the FCPA is apposite here. For ten years after its initial enactment in 1977, critics of the

statute sought to exploit a change in the political climate in Washington during the Reagan administration and brought very considerable pressure on the Congress to repeal the FCPA. In the end, however, Congress was not willing to be viewed as endorsing corruption, and it instead merely enacted minor amendments in 1988 that clarified and codified existing enforcement practices.

Similarly, we expect the Act to go live without major amendment later this year, but with some additional materials (for what they are worth, as discussed below) on how the Act is intended to operate in practice.

The anti-bribery guidance The recent delay will hopefully at least allow the guidance to be improved from the short very general and high level draft version released last year. The draft version identified the following six principles of bribery prevention and provided a short summary of each of them: (1) risk assessment; (2) top level commitment; (3) due diligence; (4) clear, practical and accessible policies and procedures; (5) effective implementation; and (6) monitoring and review. The guidance did not seek to set out what will constitute an adequate policy on any of these matters, recognizing instead that "there is a huge variety of circumstances" with which different companies of greatly varying size engaged in different businesses around the

world will need to contend. It was therefore expressly said to be neither prescriptive nor exhaustive.

Many organizations and commentators criticized the draft guidance on the basis that it did not resolve many of the perceived problems with the Act, such as the uncertainty surrounding the limits of acceptable corporate hospitality and the jurisdictional reach of the Act. Our view is that shortcomings of this sort are issues with the Act itself, and as such they cannot be resolved through guidance on anti-bribery procedures, however detailed. However, in the current climate, we still expect the finalized guidance to be more detailed and prescriptive than its draft predecessor.

There is also prosecutorial guidance currently being drawn up for the Act. One of the most unsatisfactory issues surrounding the Act is the idea that any problems arising out of vague or uncertain aspects of the Act can be resolved by way of sensible use of prosecutorial discretion. This approach provides no prospective certainty for those subject to the Act and makes it far harder for businesses to understand what actually remains permissible. It was similar concerns about the FCPA that lead to the adoption of procedures in the US for the provision of administrative guidance on the FCPA. Anything that the UK prosecutorial guidance

The Bribery Act, continued on page 16

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The Bribery Act *(from page 15)*

can do to mitigate such issues with the UK Act would be gratefully received by the business community and perhaps, like the US, would reduce the outcry for wholesale amendment to the Act.

The Serious Fraud Office For its part, and no doubt to try and meet concerns about the Act putting UK businesses at a disadvantage, the SFO is now seeking to emphasize the advantages for UK businesses of having the Act. The Director of the SFO Richard Alderman recently gave the example of where a UK based company and a US based company are competing in a third country. If the US company makes facilitation payments to get its operations there up and running more quickly, Alderman has said that he would consider prosecuting it for making those payments if it conducted any business in the UK, because otherwise the UK company would be at a competitive disadvantage. However, he acknowledged that the SFO's assertion of jurisdiction over foreign companies under the Bribery Act will be subject to the review of the UK courts.

More generally, these are uncertain times for the SFO. The Government had originally stated that a new Economic Crime Agency would take over the work of tackling serious economic crime that is currently carried out by the SFO. Possibly as a consequence, a number of the SFO's senior team have recently left, including

the SFO's head of anti-corruption who only joined it in 2009. However, the Government has now announced that it will be consulting in the spring on whether the SFO should instead be part of a new National Crime Agency.

Despite the current uncertainties about the Act, we still expect that it will go live later this year and any changes to its operation will be at the margins.

Conclusions Despite the current uncertainties about the Act, we still expect that it will go live later this year and any changes to its operation will be at the margins. Many companies which carry on business in the UK are already fully engaged in reviewing their anti-corruption programmes using the OECD compliance guidance and similar existing materials. For those who have not yet started this process, now is a good time to do so instead of waiting in the hope for major substantive changes to the Act. □

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