A Financial Stability Board (FSB) official and a Deutsche Bank in-house counsel have clashed over the Board’s plan to ban contingent convertible instruments (CoCos) from being used in global systemically important financial institution (G-Sifi) buffers.

Speaking at yesterday’s session ‘Recapitalising financial institutions in distress – can it really work?’, and ahead of an official announcement on Friday after the G-20 summit in Cannes, Eva Hüpkes of the FSB said that they had considered the pros of allowing CoCos in the G-Sifi buffer, the shareholder discipline effect and lower costs.

“But at the end, those who pointed to the risks associated with these instruments prevailed, so the requirement will be common equity tier one only,” said Hüpkes.

Trigger failure was one reason cited by Hüpkes, as the complexity of the instruments will actually prevent the definition of the trigger. The trigger instruments will also be effectively in a gone concern scenario, she said, as the death spiral effect will precipitate reactions, adverse signaling and reverse maintenance effects on shareholders and dilution.

Hüpkes also confirmed that there will be a new 3.5% bucket (the highest so far is 2.5%) for banks which may become even more systemically important, but for now that bucket is empty.

However Mathias Otto, deputy general counsel of Deutsche Bank for Germany and Central and Eastern Europe, said this approach reveals inconsistencies in the approach to the Sifi debate. “You seem a little bit confused at the moment,” he said.

On one side there is an implied assumption that Sifis won’t be resolved, therefore more high quality capital is simply added to make an accident less likely, he said. There are also concerns about CoCos not being similar enough to common equity.

“But when they agree consensually to a conversion, at least they say that one size fits all and require a higher capital charge regardless of what the resolution plan tells us.”

If a capital requirement is a consequence of a bank’s own planning and structuring and it can see the benefits of taking harsh measures of adjusting corporate structures and streamline businesses, he said, it can immediately yield on that.

Supply shortage

Otto also noted that there is an overall agreement that the banking sector should operate with a broader capital base and with capital of better quality, but the question is where would that come from?

Hybrid capital is key to diversifying the investor base, he said. If the Council of the EU raises its core tier one requirements to 9%, banks will be driven to the equity market.

However a sector facing increased costs from regulatory burdens, a move towards product simplicity and a shift to central market infrastructures means the ability to earn wide margins is limited.

“Translate that into an equity story for investors, and banks are not that appealing a sector to put money into,” said Otto.

“I am a little concerned that there won’t be a sufficient supply to meet the demand of the sector.”

A false market?

But while the arguments for and against CoCos are relatively clear, do investors actually want to buy it?

Hendrik Hagg of Hengeler Mueller said that when he speaks to investors they often can’t understand the instrument. It doesn’t fit into their infrastructure, as it’s very difficult to divide them between equity, debt and convertibles.

It may be hard to find people who are interested as the risk profile isn’t very attractive, he said.

Randall Guynn of Davis Polk & Wardwell said he’s been in meetings with institutional investors who in some cases can buy debt but not equity. If they’re buying debt and the company goes into receivership and they receiving equity, that’s something they can live with as that can happen with corporate debt.

“But when they agree consensually to a conversion, at least when I’ve been in meetings with investors they’ve struggled as to whether they can actually do that,” said Guynn.
UK family law revision expected

The UK’s Supreme Court is set to “water down” a much-criticised 2001 Court of Appeal judgment, according to a retired UK High Court judge.

The precedent-setting Payne v Payne case is perceived by many to be outdated and overly adversarial. It is argued the judgement placed undue weight on the wishes and feelings of the relocating mother involved and was formulated on unproven assumptions concerning the so-called distress argument.

Speaking at yesterday’s session, “International relocation of children (non-Hague Convention countries),” Justice Singer said family practitioners in the UK were waiting for the Supreme Court to be presented with an opportunity to clarify their position on this.

“When a suitable case gets to Supreme Court, I expect they will water down the original judgement,” he said.

The Family Court of Australia’s Justice Michelle May said Australian law was “not Payne v Payne.” But she acknowledged women were placed in a very difficult position in family law proceedings involving relocation.

“It is very hard for a mother involved in such proceedings to make decisions on how to manage the case,” she said.

Greater emphasis needed to be placed on the importance of practicality in any family law judgments, she said.

“Judgments that are impractical cause the most trouble,” she said.

Family law in Australia had been amended with that in mind, she said.

Law Institute Victoria president Caroline Counsel added that the provision under Australian law that families undergo mediation proceedings prior to any court appearances had also proved very effective. It presents parents with the opportunity to both digest what is going on and to understand the impact of their behaviour on the children at the centre of the case, she said.

“The power of the educative role played by the family consultant in these proceedings should not be underestimated,” she said.
The IBA’s new man

Akira Kawamura speaks to Tom Young about his priorities for the presidency, the IBA’s role in an age of economic uncertainty and his must-see sessions this week

In the climate of economic uncertainty, how do you think the IBA and the rule of law generally can help avoid future crises?

It is extremely difficult to know exactly how to avoid future crises. These are challenging times and the issues involved are complex.

The global financial crisis has caused much examination of the laws and regulations that govern many sectors of business, in all jurisdictions. The introspection has been widespread and the actors and stakeholders involved are numerous – including business leaders, financial analysts, government officials, law enforcement agencies, and economists, to name a few, and of course also much of the legal profession. However, the IBA provides forums necessary for these international actors to congregate and discuss divergent opinions and approaches to regulation and law.

Through IBA specialist conferences, the latest thinking and trends in relation to a number of fiscal issues, including trade, tax, private equity, capital markets, and intellectual property are debated and shared. This sharing of information and dialogue may help to reduce instances of future crises. We all know that the requirement for international coordination and cooperation of sovereign nations to work towards harmonising laws has never been greater than it is now with cross-border transactions higher in number than ever. It follows that, better regulations and enforcement measures are essential. Here, the legal expertise of the IBA is invaluable.

Further, the IBA Presidential Task Force on the Financial Crisis is making significant contributions to the search for efficient and lasting solutions to the problems confronting the world’s financial markets.

The IBA has also partnered with the OECD and the UN Office on Drugs and Crime (UNODC) on a project to raise awareness among legal professionals of issues in relation to international corruption. With bribery and corruption widely acknowledged as significant contributors to the financial crisis the ‘Anti-Corruption Strategy for the Legal Profession’ project is an important initiative in the context of international regulatory framework gradually reducing the avenues used to accommodate corruption.

The financial crisis is being tackled on many fronts. With the rule of law largely accepted as an important component in the long term stability of a nation, the IBA will continue its work of promoting and strengthening the rule of law across the globe for the general well-being of all of humankind.

What practice areas/working groups within the IBA do you believe are of most importance in the current climate and why?

There are so many excellent IBA specialist committees and working groups dedicated to important issues that it is difficult to choose one above another. However, the rule of law and human rights are of particular importance to me. Strengthening the rule of law globally brings stability to world markets, which in turn stimulates economic development, reduces poverty and raises the living standards of the world’s poorest citizens. Coupled with the protection and advancement of human rights this work improves the lives of many, which makes for a better world.

Also, with the increase in prominence of cross-border legal practices the IBA is set to establish a committee to address related issues. This is an important initiative because such business activity affects us all.

The Global Financial Crisis Task Force continues very important work for the IBA and will increase its focus on the well-being of people badly affected by the global financial crisis.

What are your key objectives for your presidency at the IBA?

The key objectives of my presidency are: to bring about peace and the well-being of people through law by emphasising corporate social responsibility and collaborating on rule of law projects with other international and regional organisations such as the United Nations, World Trade Organisation, International Criminal Court, European Union and the World Bank. I also aim to meet the challenges arising from the increased globalisation of the legal profession, promote the rule of law widely and strengthen relationships between law firms in the Middle East and across the globe.

How will your presidency differ from that of your predecessor, Fernando Pelaez-Piera?

Fernando Pelaez-Piera was an incredibly energetic IBA President. He dedicated enormous amounts of energy and time to promoting the good works of the IBA throughout the world. During my presidency I aim to follow his example and build on his legacy. In addition, I aim to further raise the public profile of the IBA and strengthen the public service of the legal profession globally.

Your mission is to use “international legal services [to] help the development of Japanese society” – how will you do this?

Wherever possible I encourage young Japanese lawyers and professionals to be more active in the international community, to participate as speakers in international legal conferences and to go overseas to work. In addition I emphasise the importance of establishing links with their peers in different nations. I believe that Japanese society must be more open to the world. The traditional domestic Japanese law firm is now keenly aware of its responsibilities to better serve its clients by going abroad and developing its international contacts. My own firm, Anderson Moni & Tomosuke in Tokyo, has been successful in developing its own global professional network through such international activities and I believe that the IBA’s annual conference remains the pre-eminent event in the calendar of the legal profession for all lawyers, including those in Asia to build their business network.

You were the first chair of the IBA Bar Issues Commission – what did that involve?

It was an honour to be appointed the first chair of the Bar Issues Commission (BIC) in 2005. Through the various bar associations and law societies that are members of the IBA, I was afforded the opportunity through roundtables and seminars to understand the important issues of the day facing the legal profession globally. We created working groups to develop guidelines and resources for fledgling bar associations; practical initiatives with tangible results.

How, if at all, did it prepare you for the larger role of IBA president?

Being Chair of the BIC placed me in good stead for my current position of IBA President because I have a very deep appreciation of what can be achieved through cooperation and of the work involved in advising the IBA Council on resolutions and statements.

What sessions are you most looking forward to this year?

As always the working sessions of the IBA Annual Conference cover a wide number of topics. There are more than 180 to choose from, which means that I am looking forward to a great number! However, the showcase sessions are all covering topical issues which will be very interesting; the showcase of the International Bar Association’s Human Rights Institute will examine the implications for human rights in the context of political changes in the Middle East; the IBA showcase will focus on how new media is affecting government control of information; the Legal Practice Division showcase will report on the issue of legal privilege with a particular focus on the recent decision handed down in the AkzoNobel case by the European Court of Justice; the Public and Professional Interest Division showcase will discuss the independence of the judiciary; and the Rule of Law Symposium will consider the issue of financial growth at the expense of the rule of law and democracy, and also debate the unequal status of women and the rule of law.

Will you have time to look round Dubai? If so, what are you most looking forward to doing?

There are so many wonderful sites and places of interest and excitement unique to Dubai. Ideally, I would like to visit the tallest man-made structure ever built, the Burj Khalifa; spend a few days on some of Dubai’s glorious beaches; relax in some of the magnificent hotels like the Burj Al Arab, the Desert Palm Retreat, the Armani Hotel and the Jumeirah Beach Hotel; watch some camel racing; go shopping in any of the expansive malls; visit the Old Bastakiya District and the Dubai Museum in Al Fahidi Fort; and then fast-forward myself to a time when the Dynamic Tower has been completed! Unfortunately, it seems unlikely that I will be able to find the time to indulge myself. However, through some of the social events, like the IBA welcome and closing parties, I am looking forward to experiencing some of the wonders of Dubai.
HEAR FROM HADEF & PARTNERS AT THE IBA CONFERENCE TOMORROW

FRIDAY, 4 NOVEMBER 2011
9.30am – 17.30pm

BRENT BALDWIN
From desert to dessert: leisure development in MENA nations and beyond
Leisure Industries Committee and Real Estate Committee

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The pioneers

Part three of our run down on the world’s most innovative bankers’ counsel

I

n this poll, published first in International Financial Law Review in September, our team of journalists and editors acknowledge the world’s most influential in-house bank lawyers in their own right, and let them discuss what they think are the biggest concerns in their industry.

INTEGRATING LEGAL WITH BUSINESS AT UBS

Markus Diethelm

UBS

Aside from his undoubtedly seniority, Markus Diethelm’s position on our list was secured by his involvement in high profile cases such as the 2007 World Trade Centre litigation. This case saw him successfully negotiate a multi-billion dollar settlement between a group of insurers and a developer of the World Trade Centre.

What do you view as the single biggest regulatory burden to UBS?

The industry faces some real retention issues. It’s losing talent because people are wondering how they can make money. There’s a risk that they will go into different industries and do different things.

It’s this uncertainty that makes it very hard to manage the 65,000 employees that we have with confidence because there’s a question mark around every corner. This will be with us for some time, and all we can do is set the right course, live the right culture and lead the way as top management.

Do you agree with Switzerland’s higher regulatory capital requirements compared to those in the rest of Europe?

Switzerland almost lost its biggest bank, so it is understandable that the regulators need to take decisive action.

The financial sector is an important engine of growth in Switzerland. It’s sensible and necessary for the banks to have higher capital requirements. These requirements should also be somewhat stricter in Switzerland than in other countries.

Governments look closely at what Switzerland and other countries do and take these steps into their considerations. We should all know: if you shrink the banks you will shrink the economy. This is definitely not something the regulators should want, especially in the current economic situation. I don’t think the discussion is over.

Do you agree that these capital requirements could limit the ability of Swiss banks to compete with other banks internationally?

We need to stay coordinated and competitive. And a well-integrated and diverse global financial system can withstand any blow much better than individual locally capitalised undertakings. Therefore, the current strong push toward subsidiarisation may not be the final state of play.

Do you think Cocos should count as regulatory capital?

At UBS we don’t think it’s a great instrument simply because the market will always behave according to directional signals that it receives. If you put a trigger at 7% everyone will get out of the stock at around 10% and then it becomes meaningless. At UBS we will retain earnings and we don’t pay out dividends to earn the necessary capital. We believe this is a much better way to go about it.

PROTECTING GOLDMAN’S REPUTATION IN EUROPE

Laura Holleman

Goldman Sachs

As general counsel of Goldman Sachs’ investment banking division since 2007, Laura Holleman has helped steer the bank through one of the most challenging economic crisis of the last century.

One of the most difficult aspects of her role has been striking a balance between the commercial imperative and protecting the bank from litigation and reputational damage.

The commercial pressure has become stronger over the years as new players create more competition in the market. “The pressure has increased to do things faster, cheaper, and to some extent with what we would consider lower standards,” says Holleman.

“We’ve needed to develop ways to be competitive and at the same time protect our reputation and protect ourselves from liability.”

With business increasingly focused on growth markets, many with well-known issues with corruption and accounting fraud, this pressure is only going to rise.

She admits that people intent on committing fraud are generally able to commit it. So the best they can do is put a structure in place to identify any wrongdoing.

Holleman is adamant, however, that Goldman isn’t willing to play by the rules that some local competitors play by.

“We consider it our job to improve the market practice wherever we can do that,” she says. “We have to be willing to push back and say no, and to shape what comes out of our new markets, not simply blindly chase whatever business is available.”

An understanding of what the real risks are, as opposed to the theoretical risks that something bad might happen, is also crucial.

“What helps me is to say I think the right answer is X – does that help you accomplish your goals?” she says. “And then we work to accomplish those goals instead of saying ‘here’s some law that I know’, which is not particularly helpful.”

While as a manager it’s impossible to be too hands-on, Holleman believes that she can’t be relevant without a close enough connection with the business to know what’s going on.

“You need to review underwriting agreements in order to keep current? No, but you have to know why things are happening in the way that they are; whether the English or American models are winning, what model is being imported into China or south east Asia and so on,” she says.

With much of the Goldman’s growth projected to come from countries with a developing regulatory framework, this understanding is more integral than ever.

THE DEALMAKER

Kit Wilson

JP Morgan

It takes time to learn how to manage the financial services industry functions, time to learn how to navigate one’s own institution and time to gain enough trust with internal clients that they can contextualise and better accept a ‘no’.

As JP Morgan’s managing director and associate general counsel, Christopher (Kit) Wilson has invested that time.

Today, whether by personal lobbying or ensuring that the appropriate business or control groups are involved, he is able to balance the tensions between short-term deal revenue and long-term shareholder value.

Put simply, he helps make transactions better. But if he recognises the influence he wields, he is modest as to the reasons why.

“As Woody Allen said, eighty percent of life is just showing up,” he says. “I wish I could say that any influence I have derives from a brilliant legal mind, but I think the truth is more prosaic.”

Joining JP Morgan in 2004 from Simpson Thacher & Bartlett, his decision to move in-house was prompted by a desire to work more closely with a business.

He wanted a role where technical skills are required, but where the real added value lies in the ability to help guide clients through decisions that frequently involve a mix of legal, commercial and reputational issues, he says.

He wasn’t disappointed. “We can face enormous pressure in-house to be commercial on issues, and the pace at which we are often required to make decisions based on imperfect information can be daunting,” he says.

“But it’s liberating to be able to devote more time and focus to certain key issues than would otherwise make economic sense.”

THE DEFENCE-FIRST IN-HOUSE

Chul Chung

UBS

The new general counsel of UBS’s investment bank, Chul Chung, has certainly hit the ground running.

Already, Chung has begun implementing his ideas on how legal departments should service internal clients. Judging by the reaction of his peers, his efforts have not gone unnoticed.

Like many successful in-house counsel, Chung believes in a stronger distinction between compliance and control responsibilities and business facilitation and execution functions – with the former taking priority for the department.

The legal department should have a defence first mentality, he says.

Chung is also focused on reshaping how the investment

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IBA Daily News – Thursday November 3 2011

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I’m not sleeping very much because I also use the quiet hours Whampoa.

 projects in Canada, Edith Shih is always immediately identi- 

fied with the market over many cycles and from the standpoint of a regu- 

larly put forth by counsel just over a year ago, Slatter took the role during a time of the continuing internationalisation of debt markets has seen the rise of competing securities regimes, but Fishman’s work with JP Morgan Chase has not wavered from its home country’s standards. “The Securities Act establishes a pretty vigorous liability regime, and because of that we try to hold ourselves to those standards when conducting due diligence whether the deal is done in the US or elsewhere.”

THE AMERICAS PROJECTS EXPERT

Kathryn Hoff-Patino

US Export Import Bank

Kathryn Hoff-Patino has been a key figure in structuring some of Export Import Bank of the United States’ (Ex-Im Bank) most complex and award-winning deals. She led the bank on the 2009 Papua New Guinea LNG project, a development that’s transforming the host country.

Ex-Im Bank’s $3 billion of commitments was its largest ever and made it the biggest single provider on the $18 billion deal. Despite closing in the financial crisis, and with five other export credit agencies and 17 commercial banks, deal documents were signed within 12 months of the financing’s kick-off. “For a deal of this complexity, that was impressive,” Hoff-Patino says.

And even that old stalwart the FSA will soon be broken up, under the tripartite system expected next year. But despite the market niches where commercial financing is not available – has taken on a new dimension. Exporters have relied on the bank like never before and new strategies have been developed to assist. One example which Hoff-Patino has been involved in is supply chain financing, a product to help finance small businesses that are suppliers to major exporters. While Ex-Im Bank would like to see the commercial banks return, Hoff-Patino says they stand ready for as long as the market needs them. The banks increased activity over the past two-and-a-half years had exposed one of its biggest challenges:

Hutchison Whampoa organises its own in-house seminars so colleagues can have the opportunity to fulfill professional education requirements. “I serve as a teacher everyday to my colleagues on their work and family issues – it’s a matter of being able to understand other people’s problems and helping them overcome that,” she says.

Being a teacher is second nature to Shih, who spent the earlier years of her life studying education and applied linguistics in order to teach English to speakers of other languages.

But having dabbled in languages and music, she believes that rejecting an MBA program for law school and subsequently joining Mayer Brown JSM in Hong Kong was a very good decision in hindsight.

“I could always be in business, which I am in many ways even now, without going to business school,” says Shih, with no intention whatsoever of belittling a business school education.

“But I could never have my career supported by a legal back- ground without going to law school.”

Always up for a challenge, Shih declined partnership and ventured to an investment bank of the Cheung Kong group to experience life from the other side of the table. It was there that her abilities caught Folks’ eye and she was transferred over to Hutchison Whampoa for strategic planning and business development after a two-year stint at the bank.

When Folks subsequently asked Shih to head the legal depart- ment, she was unimpressed.

“I told him I came to Hutchison Whampoa to get away from being a lawyer,” says Shih. But he argued Shih would not only deal with legal work. He was right. “We take personal responsibility not just for the legal documentation but for the good health and growth of the business we run,” Shih explains.

In her 18 years as group general counsel and 14 years as company secretary of Hutchison Whampoa, her work on trans- actions involving Orange’s 2G business in Europe have been the most memorable.

Hutchison Whampoa was originally pressured to sell off the operating unit, but it persevered and led Orange from very difficult times to a profitable FTSE 100 business that sold for $14.6 billion, with an additional $6.4 billion on resale to Voda- fone – the largest transaction in history at the time.

Hutchinson also recently listed the business trust of the Hutchison group’s Hong Kong and Guangdong container ports businesses in Singapore – a move which sparked calls for Hong Kong regulators to make such listings possible in the city-state.

“We when first consulted the Singapore and Hong Kong lawyers who advised on this listing – it was at Christmas last year and everyone had to cancel their holidays,” recalls Shih.

“They said we were not needed in it three. They said that was absolutely impossible, but we proved them wrong.” Hard work is basic, she explains. And learning is a life-

long process.

Making the most out of opportunities that cross her path has become her defining ethos.

THE TEACHER

Edith Shih

Hutchison Whampoa

Whether attending to an enquiry in Europe or overseeing projects in Canada, Edith Shih is always immediately identi- 

fied as the first point of contact. It is because she doesn’t sleep, according Canning Fok, group managing director of Hutchison Whampoa.

“As well as tending our overseas businesses, the reason why I’m not sleeping very much is because I also use the quiet hours of the night to attend to work generated by external appoint- 

ments and volunteer services,” says Shih. “I am at the stage of my career where I think it’s time to give back to society.”

As the chairman of the Education Committee and vice-

chairman of the Hong Kong Institute of Chartered Secretaries and a government-appointed council member of the Hong Kong Institute of Certified Public Accountants, Shih is a teacher both on a professional and personal level.

“I give seminars and lectures to legal, accounting and company secretary practitioners on topics of importance and concern, such as internal control and risk management, direc- 

tors and shareholders meetings,” she says.

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long process.

Making the most out of opportunities that cross her path has become her defining ethos.

THE VETERAN

Stuart Fishman

JP Morgan

With nearly thirty years experience, Stuart Fishman is one of North America’s most respected bankers’ counsel. He’s watched the market over many cycles and from the standpoint of a regu- 

lator, a law firm and in-house.

Within JP Morgan Chase, he’s sat on the issuer’s side representing corporate functions including corporate treasury and capital planning, then worked on high grade debt private placements, and since 2002 has picked up the bank’s high yield business.

He’s purely a securities lawyer, and having worked on each facet of an issuance, has an unvarnished perspective of the industry. Rather than taking primary responsibility for any one deal, Fishman now oversees the outside counsel working on the bank’s transactions, addressing issues as they arise. “I’m talking to my lawyers on my deals every day, sometimes multiple times a day,” he says.

Many of these relationships have developed over many years. His input can range from negotiating underwriting agreements, preparing prospectuses, to addressing diligence and disclosure issues through his role on the bank’s debt underwriting com-

mitments committee. Through Sifma, Fishman has contributed to industry dialogue on the removal of ratings in offering docu-

ments. But Dodd-Frank has had only tangential effects on his focus areas.

“Unlike derivatives where the regulatory regime is undergo- ing wholesale changes, in securities offerings we are still work-

ing with the same basic disclosure regime since the adoption of the Securities Act of 1933,” he says.

The continuing internationalisation of debt markets has seen the rise of competing securities regimes, but Fishman’s work with JP Morgan Chase has not wavered from its home country’s standards. “The Securities Act establishes a pretty rigorous liability regime, and because of that we try to hold ourselves to those standards when conducting due diligence whether the deal is done in the US or elsewhere.”

### THE MOTIVATOR

Emma Slater

Deutsche Bank

It’s a tough time for most senior in-house counsel. But Emma Slater, general counsel for UK and western Europe at Deutsche Bank, has had a particularly bumpy ride. Appointed as general counsel just over a year ago, Slater took the role during a time of huge cost cutting for the bank.

It’s just a shame this coincided with the start of the biggest regulatory overhaul in decades.

Slatter remains upbeat: “We are under a great deal of pres- sure but it’s exciting, even though we are doing more with less.”

How did she keep a tired, stretched group of lawyers happy?

“The only way was to take my team with me. When you have bright, enthusiastic people, you have to involve them, and also be completely honest about the fact that it is tough and it’s go- 

ing to remain tough for a while,” says Slater.

“You have to bear in mind that a lot of younger lawyers have never experienced a severe economic downturn before,” she adds. It’s not just the sheer weight of regulatory change, but dealing with new inquisitors which poses problems. “We have always worked with the Financial Services Authority, BaFin and our local regulators, but we now receive requests from EC and the US Department of Justice that haven’t previously been so focused on our markets,” says Slater.

And even that old stalwart the FSA will soon be broken up, under the tripartite system expected next year. But despite many fearing the body won’t be able to fill its senior roles with the relatively meagre pay on offer, Slater thinks otherwise.

“It is challenging when there is competition from financial institutions also recruiting in the sector. But I don’t think this is all about money. We shouldn’t underestimate the appeal of a sense of public service and a change of viewpoint.”
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So why look further?

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Paul Koster, chief executive of the Dubai Financial Services Authority, discusses the priorities and challenges of the region’s key financial hub

Lucas Becker sat down with the chief executive of the Dubai Financial Services Authority (DFSA), Paul Koster, at an interesting time in the Dubai International Financial Centre (DIFC)’s development.

The centre was a key hub during the boom years, but suffered from a downturn in the real estate market that was its very foundation. More recently, political unrest and a u-turn by Qatar on the shariah compliance of international banks offering Islamic banking has cast a shadow over Dubai that is hard to avoid.

The fate of property developer Dubai World are inexorably linked with the DIFC. As the company emerges from its insolvency proceedings, the DIFC is attempting to reassert itself as a regulatory leader in the UAE and around the region. As the regulatory cliché goes: never waste a good crisis.

Here, Koster lays out his priorities and names his challenges, and gives his position on the future of the Islamic sector, the need for insolvency reform and the importance of regional and international regulatory cooperation.

How do you compare the DIFC’s regulatory regime to its regional rivals such as Qatar? Qatar is doing a good job. I always favour competition. It keeps you on your toes. It’s very clear that Abu Dhabi and Qatar are all trying to make sure they have standards that are recognised worldwide.

But really, it is about enforcement. Are you taking the right steps in enforcement, do you communicate to the world that if you do something wrong you will be held accountable? While as regulators we’re not competing, we are not commercially unaware, and that’s why we participate in all these international bodies.

Given the Qatar Central Bank’s recent decision to roll back the Islamic banking sector, how do you see the future of the sector in Dubai? It is a very small industry if you compare it to the total financial market. I’m guessing it would not be more than 2%. So the growth potential is enormous. But one of the critical elements that need to be addressed is how we set standards? For instance how do the International Financial Reporting Standards match with some Islamic requirements? All those issues need to be addressed. That’s not easy and that’s going to take some time.

At the same time it is about providing opportunities — General Electric issued a sukuk bond for example — however the nature of investing in sukuk is different than it is in the western bond market. So you have to realise that some of these developments will need their own momentum that is different than what you can expect in conventional finance.

I’m cautiously optimistic. I wouldn’t say it’s going to be a free home run. We do participate with some of the standard setting bodies, so we have to wait and see how it’s going to be establishing itself over time. It’s interesting but it’s not exaggerated, the size of it is still small.

What regulatory challenges do you foresee over the next 12 months? We need to avoid incidents as much as we can. With the financial crisis and the serious attempts of regulators worldwide to address them, we tend to over-emphasise the regulatory rules. To me, supervision, and strong supervision, is probably the most critical element in avoiding a future crisis.

History has proven it’s very difficult to predict crises, but I’m relatively optimistic that if we fine tune and focus more on the supervisory side then we might be able to spot some of the issues earlier on. One of the key elements is cooperation among regulators. Mark McGinness [DFSA’s director of international relations] has just taken a critical initiative within Isco, to look at regional MOUs [memoranda of understanding]. This is in the early stages, but it is one example where, as a region, you will probably have a better understanding of each other’s commitment and willingness to share information.

When there is a problem regulators would like to have a good exchange of information. This will allow them to take steps that are appropriate without hindering what is happening in the home country. These supervisory colleges need to be developed. We are participating in a number of them, with the UK Financial Services Authority (FSA), the Netherlands and Switzerland authorities.

We also need to be careful about some of the steps being taken with regard to raising the capital requirements. This industry is pretty good at responding to changes and challenges. We, as regulators, need to fully understand and comprehend the response from industry.

We should not try to hinder the innovation of this industry too much. But, at the same time, we should participate earlier with them and understand the developments.

The United Arab Emirates (UAE) is smaller, so it’s much easier for us than for the UK, US, China or Japan where they have a large pool of firms. We still have a significant size, over 250, but nevertheless it’s still manageable. But incidents always happen; that’s how the industry is. And we will not be able to stop incidents from happening, but you can try to contain them earlier on in the process.

The educational aspect is critical. We have recently had Sir Callum McCarthy [former UK FSA chairman] review our supervisory process. Following his study one of the issues that came up is that the board need to spend time on the risk profile — that is, working out a firm’s risk appetite and what we as a regulator are willing to accept.

We completed the whole circle of risk assessment, impact probability issues and looked at the scenarios of what could happen. You can look at risks and say you could take mitigating steps to control the risk, but that is costly.

One of the issues that came up in the report is that we sometimes baptise some of the smaller firms when their impact is not significant. And the probability of these firms having problems is quite high because they don’t have the systems and controls, the audit committees, or the auditors and a board being that much involved.

But the risk of them going under and us being affected is smaller than if one of the big firms had an issue. So what we try to do is spend our time in the areas where risks are really the highest. The probability might be inaccurate but we still want to avoid them.

We have created a system by which we allow all firms to enter that meet all the requirements. But, by looking at their setup, the maturity of your business, the business model, the traction that needs to be developed, we tell them that we will spend more time with them in the beginning if this is required.

We’re at a place where we pretty much know how we will respond to a certain mix of probability and impact. Our board has said ‘these are the kind of controls we expect, and if you take those controls and those steps then we’re willing to accept that risk’. And then the board can hold us as regulators accountable for those steps.

What are the DFSA’s priorities over the next 12 months? The priority for a regulator is constant, and that is to avoid incidents in the market. But, we do have a number of issues that I think warrant our attention.

One of our key priorities is that we will stay closely involved in the trends of the new entrants coming from countries such as Turkey and India, and be very closely involved in their day-to-day business.

We have seen about 40 firms leave the DIFC, but we’ve seen some 40 plus firms come in, and I think overall the nature and the underlying models of these new entrants are quite promising.

Another key area is money laundering; we need to be aware of those issues. The DFSC needs to report suspicious transactions to the Central Bank of the UAE, which falls under its jurisdiction.

We noticed a suspicious transaction we report it. The collaboration and cooperation with the Central Bank has increased significantly, so we undertake mutual training programmes on money laundering, and we do exchange a lot of information in helping us to combat this issue.

Thirdly, we try to participate in all critical standard-setting bodies — that is the Basel Committee, Isco [International Organisation of Securities Commissions], IAFS [International Association of Insurance Supervisors] and the Asian Oceanic Standard Setters Group.

The fourth area is auditors. Auditors in the region will see an increased level of attention towards their business activities, not only from us but from the Ministry of Economy and we shall closely collaborate in discussing these issues within the UAE. Within the DFSC we have auditor oversight and we’re looking at making auditor oversight applicable to the listed firms. This is quite critical as they are also sometimes subject to very difficult decisions and auditors are prone to not always taking the right decision.
How shareholder activism has changed

Shareholder passivity, executive compensation and the role of the media emerged as the topics to watch in yesterday morning’s session ‘Shareholder activism: how shareholders drive change and how boards and advisers respond’. Shareholder activism over the first nine months of 2011 was up 90% from the same period last year, putting the issue firmly back on corporates’ agendas. The panel of M&A partners from around the world compared and contrasted how the pick-up has manifested itself in their jurisdictions, and the changes urged by market players. Ironically, institutional shareholders’ inactivity has attracted much attention.

“The counter to shareholder activism is shareholder passivity. In Switzerland this has been as important over the last couple of years as shareholder activism,” said panelist Dieter Gericke from Homburger in Zurich.

“We have as much of a shareholder passivist discussion as a shareholder activist discussion,” he added. Big shareholders such as pension funds, for example, are expected to become less passive.

The UK is in a similar position. Last year its Financial Reporting Council introduced the Stewardship Code with the goal of putting more pressure on institutional investors to more actively drive change within the company and become more involved in governance, said Slaughter and May partner Craig Cleaver.

This was a response to the “fairly calamitous series of events during the crisis where potentially imprudent transactions obtained shareholder approval.”

“Some institutional investors in Australia are playing a larger role in shareholder class actions – an entrenched part of the country’s shareholder litigation landscape but dominated by non-institutional investors, said Mallesons Stephens Jaques partner Sharon Henrick.

Another area tipped to watch in Australia is shareholder votes on executive compensation. Like the US and Sweden, it’s in its first year of mandatory, advisory votes on board members’ pay packages.

Under the two-strike rule, a board will be forced to stand for re-election if its pay proposal is rejected by 25% or more shareholder votes in two consecutive years. The legislation has been controversial at home, and bewildered some panelists.

“So if the say-on-pay vote fails two years in a row, the board has to resign. That struck me as particularly cutting edge there,” said session chair Jeffrey Lloyd from Canadian firm Blake Cassels & Graydon, garnering some laughs from the panel and audience.

“Doesn’t it fundamentally shift the balance in terms of who is running the corporation, from directors to shareholders? That is a very big change in corporate governance,” commented panellist David Rockwell from Sullivan & Cromwell in London.

The very low threshold of 25% was the most surprising aspect. “The minority rules,” said one speaker. In recent weeks two well-known companies have exceeded that level: NewsCorp’s pay proposal was rejected by 54% and Crown Casinos by 76%.

The media has become a more prominent channel for activists. “I’m sure in all of your jurisdictions one of the most effective ways to try putting pressure on boards is through the press,” said Cleaver.

A question from the audience started a lively debate on the possibility of rewarding long-term shareholders. The audience member asked for the panel’s thoughts on boards countering the powers of activist shareholders by imposing benefits for long-term shareholders such as through extra dividends or more voting rights.

Rockwell said “it’s a very intriguing question,” but that there’s been no discussion in the US and that there would be enormous cultural and intellectual obstacles before anything like it would take hold. Fellow panelist Pablo Artagaveytia from Marval O’Farrill agreed that in Argentina it would not be a possibility.

But the benefits of giving more rights to loyal shareholders have been discussed in the UK and Switzerland. There here has been noise in the UK about this, but deciding how to distinguish between long and short term investments has proven difficult.

In the last revision of Swiss corporate law there was discussion on whether shareholders would have to gain certain rights, such as the right to call shareholder meetings, based on their track record, said Gericke.
VOX POP

QUESTION: What have been your favourite moments of this year’s conference?

A B Mahmoud
Dikko & Mahmoud
Nigeria

I have many favourite moments from the conference this year. I found the arbitration law session especially useful. The panelists discussed many hot topics and current issues. For example, issues relating to third party funding. All the speakers at the session were fantastic and took different angles.

Felipe Cousiño
Alessandri & Compañía
Chile

I particularly enjoyed the sessions organised by the investment funds committee. There were some very interesting discussions in relation to Sharia-compliant funds as well as the emergence of new fund domiciles and the importance of sovereign wealth funds. The sessions relating to antitrust issues were also very good.

Ashwin Trikamjee
Garlicke & Bousfield
South Africa regional forum

I thought that the opening ceremony, although it was a bit too long, ended with a fantastic keynote speaker. I particularly enjoyed the interactive question and answers session. Interactive sessions are always the best because they are provocative. The venue is also very good and easy to access.

Shoeb Saher
Habib Al Mulla
Dubai

I practice in Dubai so it’s very nice to see the area so full of energy and to meet lots of interesting people. This is my first IBA and I think it’s been excellently managed. It has certainly encouraged me to go to future IBA conferences.

Ali Abdulla Al Aradi
Bahrain Chamber for dispute resolution
Bahrain

The most important thing is that this event is happening in Dubai. It’s the first time an IBA annual conference has been held in the Middle East and it has provided a great opportunity for people to get a taste of what the region is able to provide.

Omar Al Heloo
Hadeef & Partners
Dubai

I enjoy the sessions and meeting new people. I particularly liked the construction committee session on Monday. I have also enjoyed the social activities such as the antitrust law lunch yesterday. This field is still new in our region and the UAE, Oman and Bahrain have no antitrust law.

Dr Ogugua Ipeze
Ipeze & Ipeze chambers
Nigeria

I particularly enjoyed the family law sessions and the surrogacy discussion. The surrogacy issue is very interesting for my culture because in the past the relatives of people unable to have children tried to assist them by encouraging them to have children with their husband.

Özge Atilgan Karakulak
Mehmet Gün & partners
Turkey

My favourite moment has been getting together with people I met from Madrid and Vancouver at previous IBAs. This is my third IBA. I believe it isn’t just about what you can get from one annual meeting, but the continuance of a relationship; that’s how you develop your business.

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To find out more, please contact
Roxanne Speight at Tel: +44 207 779 8380
Email: rspeight@euromoneyplc.com

www.iflr.com

Europe:
Claudia Tan
Tel: +44 (0) 20 7779 8637
Fax: +44 (0) 20 7779 8520
Email: ctan@iflr.com

Asia, Australia, North America,
Middle East and Africa:
Denny Squibb
Tel: +852 2842 6945
Fax: +852 2521 8900
Email: dsquibb@alphk.com

Latin America:
Roberto Miranda
Tel: +44 (0) 20 7779 8435
Fax: +44 (0) 20 7779 7894
Email: rmiranda@iflr.com

China and Taiwan:
Bryce Leung
Tel: +852 6126 3601
Fax: +852 2521 8900
Email: bryceleung@euromoneyasia.com
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