K&L Gates Global Government Solutions℠ 2011: Annual Outlook

January 2011

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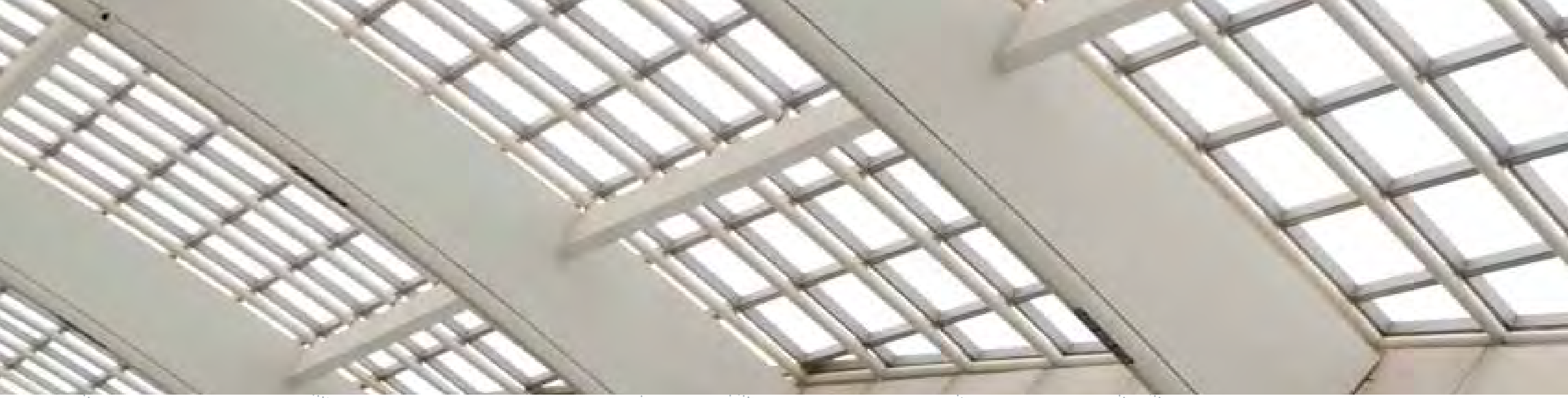
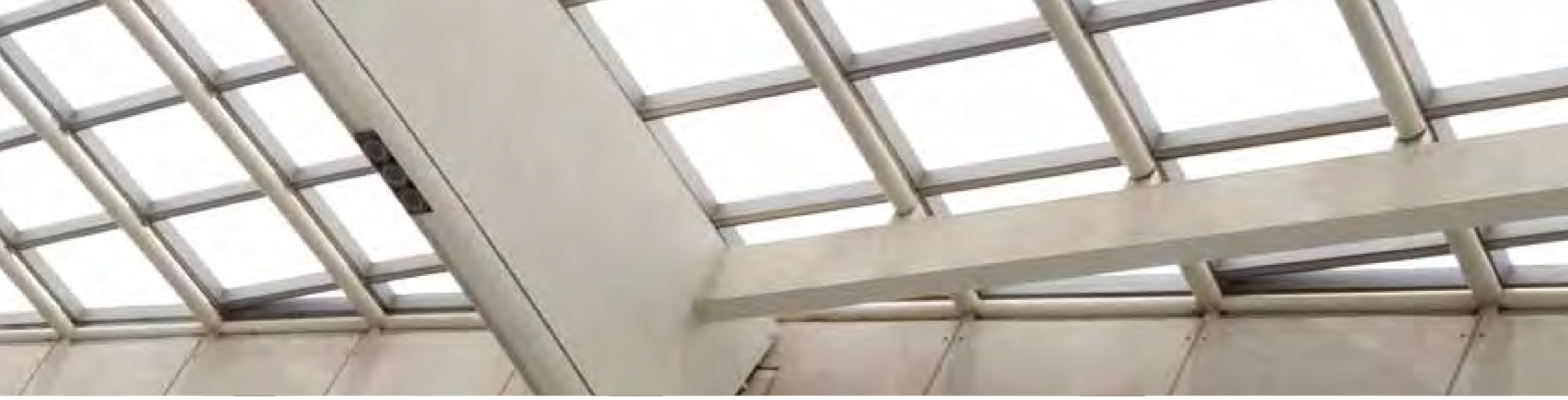


With more than 30 policy and regulatory practice disciplines and more than 400 alumni of government agencies on three continents, K&L Gates can assist clients in dealing with virtually any legal issue involving government.



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Last year, members of this initiative published *2010: The Year Ahead* and *2010: Mid-Year Outlook*. These two reports analyzed anticipated government actions and priorities on a broad spectrum of topics. Since the publication of those reports, the trend of government activism has continued to accelerate, and the relationship between business and government has continued to evolve.

This 2011 Annual Outlook contains concise articles on some of the most consequential government developments that we anticipate in 2011. Among the topics covered are the implementation of the Dodd-Frank financial reform law and the Basel III accords on international financial regulation, the global convergence of competition law, changes in the health care industry and related regulations, environmental and energy policies, aggressive regulatory and law enforcement efforts, and changes in the political landscape. We hope that you will find our perspectives to be valuable and provocative.

If you have questions about any of the articles or if you wish to obtain further information, you may contact the authors directly, or send an e-mail to governmentsolutions@klgates.com.

Best Wishes for a successful 2011.

Peter J. Kalis

Chairman and Global Managing Partner

Key U.S. Policy Issues for the Financial Services Industry

There will be two key issues driving financial services policy in the 112th Congress – implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") and the reform of Government-Sponsored Enterprises ("GSEs"), Fannie Mae and Freddie Mac. The new political dynamics, with Republicans taking control of the House and realizing significant gains in the Senate, will impact the policy direction on both of these issues.

Political Dynamics Generally

As a result of the 2010 mid-term elections, the committees with jurisdiction over the financial services industry in both the House and the Senate will have new chairmen. With the retirement of Senator Chris Dodd (D-CT), Senator Tim Johnson (D-SD) will serve as the new Senate Banking Committee chairman; Ranking Member Richard Shelby (R-AL) will remain in that role. For the House Financial Services Committee, Congressman Spencer Bachus (R-AL) will be the new chairman, and former Chairman Barney Frank (D-MA) will be the Ranking Member.

The Dodd-Frank Act

Signed into law by President Obama on July 21, 2010, the Dodd-Frank Act is the most dramatic and wide-reaching financial reform legislation since the Great Depression. However, enactment is by no means an end point to the reform process, and the 112th Congress will undoubtedly continue work on issues implicated by the Dodd-Frank Act.

This work will come in several forms. First, on many of the most contentious and complex issues, Congress "punted" responsibility to the regulators. The legislation contains 315 rulemaking requirements and 145 study and reporting provisions. Congress will have a vested interest in the outcome of these provisions and will exercise this interest in a variety of ways, most importantly through oversight. Second, given the magnitude of the bill (over 2,000 pages) and the relative speed in which it was considered (one year), there will be a need for technical corrections legislation. Third, Congress may pursue substantive changes to the legislation.

The outcome of the mid-term elections will affect the way in which Congress will undertake each of these three functions – oversight, technical corrections legislation, and substantive legislation. First, both the Republican-controlled House and the Democratic-controlled Senate will aggressively engage in oversight, but to different ends. The House will focus on mitigating the impact of some of the more controversial provisions by influencing the implementation process, while Senate oversight will be held in an effort to ensure that the implementation of the Dodd-Frank Act is proceeding consistent with enacted Congressional intent. In addition, the House may pursue substantive legislation to roll back all or portions of the Dodd-Frank Act. One possible target is the Consumer Financial Protection Bureau, the new consumer financial protection entity with broad rulemaking, examination, and enforcement powers. However, the success of these efforts is likely to be limited, since the Democratic Senate and

Policymakers—both Democrats and Republicans—have agreed that there is a need for GSE reform.

administration are unlikely to act on any such bills that emerge. However, there may be a technical corrections bill and possibly a substantive legislation bill, to the extent there is bipartisan agreement on discrete issues that need to be addressed.

GSE Reform

Policymakers – both Democrats and Republicans – have agreed that there is a need for GSE reform. There is general agreement that the role of government involvement in the GSEs must be reduced, providing an opportunity for more involvement by private industry in the mortgage and housing market. However, Democrats and Republicans are likely to disagree, among other matters, on the relative degree of government versus private industry involvement and the pace at which such reforms should be implemented. Moreover, the continued fragility of the U.S. housing market will add a layer of complexity as policymakers consider reducing the primary source of finance for residential housing in the United States. Despite significant debate and deliberation, neither Democrats nor Republicans have put forth a proposal. As a result, whether and when the GSE debate moves beyond political rhetoric to substantive legislation remains to be seen.

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Banks Face “Extremely Demanding” Capital Standards Under Basel III

In 2011, bank regulators across the globe are expected to begin implementing new capital and liquidity standards issued by the Basel Committee on Banking Supervision, commonly known as “Basel III.” Following unprecedented government intervention to shore up the global banking system during the 2008-2009 credit crisis, the heads of state representing the Group of Twenty (“G-20”) endorsed Basel III’s general outline at their September 2009 meeting in Pittsburgh. It was an ambitious plan designed to prevent the need for future government rescues of banks holding inadequate capital reserves and insufficient liquid assets. Now more fully developed, these standards will require banks and their holding companies in all participating countries to increase both the quality of their capital and the amount of capital held. In the words of Nout Wellink, the chairman of the committee developing Basel III, it will be “extremely demanding” for banks to meet the new standards.

Among other items, Basel III will:

- Require banks to increase their common equity, the highest form of loss absorbing capital, from a global minimum of 2 percent under Basel II to 7 percent of risk-weighted assets, which includes a minimum common equity level of 4.5 percent and an individual capital conservation buffer of 2.5 percent;
- In periods of “excess aggregate credit growth,” require banks to have total capital as high as 13 percent of risk-weighted assets, 9.5 percent of which would be common equity (the 7 percent mentioned above, plus a 2.5 percent countercyclical capital buffer);
- Increase the quality of capital held by excluding certain mortgage servicing rights and other instruments from the definition of common equity;
- Require banks to hold significantly more liquid assets;
- Likely slow economic growth by limiting cash available for lending;
- Likely slow, if not extinguish, markets for hybrid capital instruments and subordinated debt; and
- Likely pressure banks to raise capital to levels above Basel III’s already significant increases.

The chart on the next page illustrates how these capital increases will be phased in between now and 2019.

Capital Buffers

New “capital buffers” will effectively require banks to maintain capital in the form of common equity above the increased minimum. These capital buffers will allow banks to absorb losses without falling below minimum capital levels. If a bank were to deplete its capital buffer, general bank operations would not be affected, but dividends, subordinated debt payments, and employee bonuses would be restricted. Thus, although capital buffers are not technically part of the required minimum capital, investors interested in receiving dividends will likely treat capital buffers as required capital.

The “countercyclical capital buffer” will apply only during periods of rapid credit growth, shoring up capital during good times in anticipation of expected losses when the credit markets decline. Critics object to the countercyclical capital buffer because it converts capital levels into a macroeconomic tool, and they doubt that, as the economy approaches a period of economic stress bank regulators will tell banks to begin depleting their capital reserves.

Increased Capital Quality

Under current capital standards, the key measure of a bank's financial strength is Tier 1 capital, also known as core capital. Basel III will require additional Tier 1 capital, but will also shift the primary focus to common equity by requiring most Tier 1 capital to qualify as common equity. While banks face the need to raise more capital, some existing instruments will cease to qualify as regulatory capital.

The portion of Tier 1 capital that qualifies as common equity will have to be at least 4.5 percent of risk-weighted assets, and generally will be limited to common stock and retained earnings. Mortgage servicing rights, deferred tax assets, and minority investments in subsidiaries will generally be excluded from common equity, although a limited exception will permit their partial treatment as common equity. At the urging of the United States, mortgage servicing rights will be allowed to be counted in an amount of up to 10 percent of common equity.

Banks will have to increase their capital that counts as Tier 1, which currently must be at least 4 percent, to 6 percent of risk-weighted assets. In addition, there will be a new leverage measure, based on total (not risk-weighted) assets and off-balance sheet exposures, requiring Tier 1 capital equal to 3 percent of such assets and exposures.

Cumulative preferred stock, subordinated debt, and hybrid instruments will generally qualify as Tier 2 capital, the least favored form of capital, but only if they have an original maturity of at least five years, which is likely to limit their attractiveness in the marketplace.

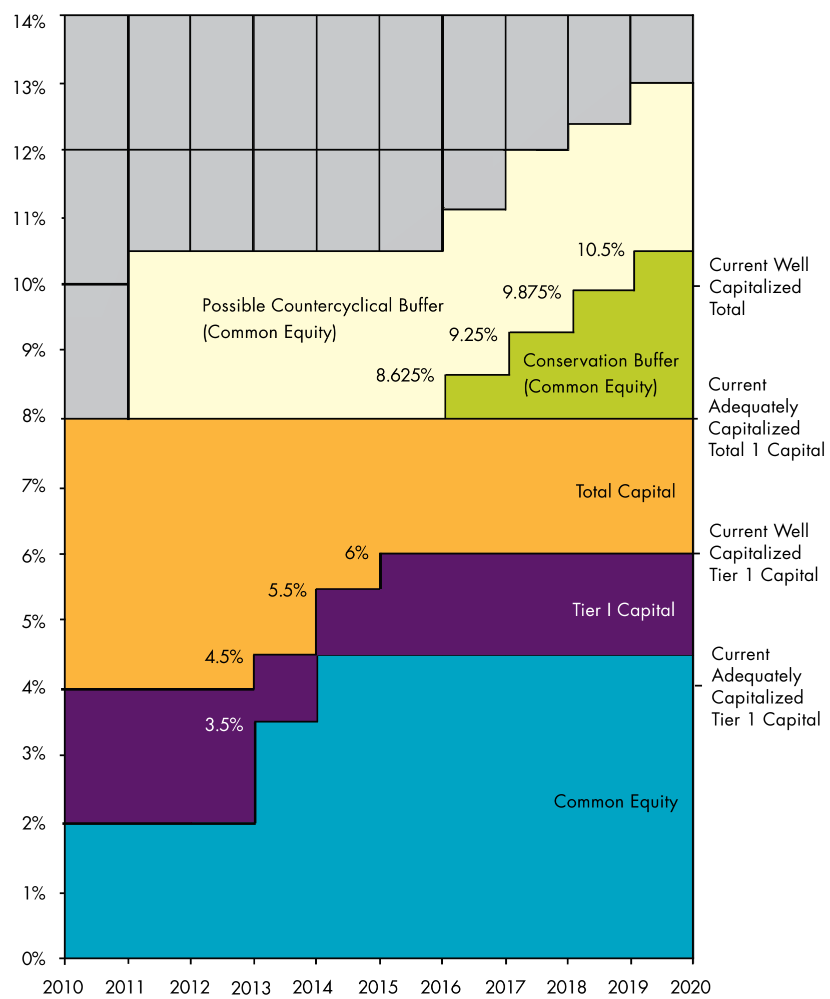
The treatment for a bank's allowance for loan and lease losses ("ALLL") has not been explicitly addressed, but it is expected that in the United States it will continue to count as Tier 2 capital, at least initially.

Liquidity

Basel III also introduces two minimum liquidity standards—the Liquidity Coverage Ratio and the Net Stable Funding Ratio. The Liquidity Coverage Ratio will require banks to maintain enough liquid assets to meet their net cash outflow over 30 days. Net cash outflow is determined by taking into account the likely stability of different types of funding and favors banks with a large core deposit base over banks with brokered funds or wholesale funding sources. Responding to concerns that short-term creditors withdrew their support of troubled financial institutions during the height of the financial crisis, the Net Stable Funding Ratio will require banks to maintain stable sources of funding relative to illiquid assets and contingent obligations over a one-year period, again favoring banks with stable deposits and less reliance on wholesale funding.

As regulators refine new liquidity concepts, one example of potential controversy in the United States will be distinguishing between "stable" and "less stable" deposits. Regulators may even reconsider their treatment of "core" and "brokered" deposits because those categories do not precisely match the Basel III concepts.

Basel III Minimum Captial Ratios



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Implementation

The G-20 nations have endorsed Basel III and committed to implement its capital increases before January1, 2013, after which minimum capital levels will increase each year through 2019. U.S. bank regulators support Basel III, and are expected to fully implement the reforms through regulation. Given the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act, no additional legislative authority is expected or needed.

A looming question for many banks is whether regulators or market forces will require capital levels above Basel III's significant increases. In Switzerland, regulators have endorsed a so-called "Swiss Finish" that would go beyond the Basel III minimum. In the United States, current regulations set the minimum capital ratio at 8 percent, yet regulators have used their ratings systems to effectively raise the minimum requirements to 10 percent or higher. Other countries may take similar approaches.

While certain components of Basel III may be manageable, the complete package of reforms will be a significant challenge for banking organizations globally. With the worldwide banking industry seeking to increase the amount of capital held, while also replacing many existing capital instruments with common equity, banks will likely find it frustrating to simultaneously build reserves of liquid, and low-yielding, assets. The strongest banks will probably adapt to the new standards with relative ease, especially given the long phase-in period, but many significant banks, especially many European banks and certain U.S. banks, may have difficulty raising sufficient capital and maintaining adequate liquidity.

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Dodd-Frank's Derivatives Mandates May Become Subject to Review, Amendment and Possible Challenges in 2011

As key leadership posts changed in the U.S. Congress, the year 2011 began with the prospect of members of Congress amending the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), enacted in 2010, or possibly interrupting funding for key regulators to carry out the mandates of Dodd-Frank.

President Obama signed Dodd-Frank into law on July 21, 2010. Dodd-Frank requires more than 300 regulations – one-third of them on the subject of derivatives – to carry out the historic reform of the U.S. financial system. The Commodity Futures Trading Commission ("CFTC"), Securities and Exchange Commission ("SEC") and other important federal bodies such as the U.S. Treasury Department have begun the process of reshaping the $300 trillion derivatives market in the United States.

Among other historic requirements within Dodd-Frank, Title VII prohibits the trading of any derivative over-the-counter ("OTC") if the SEC or CFTC requires the derivative to be centrally cleared (and thereby collateralized). The prospect of properly clearing and arranging for margin to support volumes of derivatives previously traded OTC is daunting to many.

However, Rep. Barney Frank (the Act's namesake) has stated that he expects that a bill in early 2011 will be necessary not only to make technical corrections to Dodd-Frank but also to make more substantive changes to clarify the end-user exception. Given the prospect of a corrections bill and comments in the media by the new Republican leadership in the House of Representatives, the implementation of the mandates of Dodd-Frank may be challenged this year.

Reconsideration of the End-User Exception and Clearing Mandate

The end-user exception is an important exception to the mandate by the CFTC and the SEC that certain derivatives be centrally cleared and not traded OTC. The exception is available for derivative transactions in which one of the counterparties is a commercial end-user (not a dealer of derivatives) that uses the derivative to hedge or manage commercial risk. Qualifying end-users must not be "financial entities" and must notify the regulatory agency having jurisdiction over that end-user and explain how the end-user intends to meet its financial obligations with respect to the derivative.

The mandate within Title VII of Dodd-Frank, that derivatives be centrally cleared if so mandated by the SEC or CFTC, was so controversial that Senate leaders released a letter clarifying the amendment and the end-user exception, despite the absence of any obligation to do so. Senators Christopher Dodd (D-CT) and Blanche Lincoln (D-AR) wrote to the House leadership, stating that the intent of the end-user exception (and the scope of the definition of the most active derivative users, major swap participants) is to permit users of derivatives that do not speculate with these instruments to continue to use them to hedge risk.

Given Rep. Frank's statement in favor of a corrections bill during the televised committee meeting on June 29, 2010 as well as the new Republican leadership in the House of Representatives, there may well be momentum to at least reconsider, if not amend, the scope of the end-user exception to enlarge that exception to the derivatives clearing requirement.

Key members of the House of Representatives have begun the effort to reconsider the clearing mandate and end-user exception. Representative Spencer Bachus (R-AL), the Chairman of the House Financial Services Committee, and Rep. Frank Lucas (R-OK), the Agriculture Committee Chairman, sent a letter on

December 16 to regulators warning that the economy could be hurt if end-users are not fully protected from margin, clearing and exchange trading requirements as Congress intended under the end-user exemptions in the reform law.

> [I]t is crucially important that the commercial end-user exemption from the requirements of Title VII be implemented in a manner that is consistent with congressional intent. "…As our economy slowly recovers, we have serious concerns that Dodd-Frank will force American companies which did not cause nor contribute to the financial crisis to move billions of dollars in capital onto the sidelines to comply with the law. Requiring end-users to post margin will delay or prevent businesses from expanding and will limit the creation of badly needed jobs … creating a prohibitively expensive and rigid climate for the use and trading of derivatives in the United States and could shift this market overseas."

An Early Amendment to Dodd-Frank

Dodd-Frank has already been subject to amendment. Representative John Sarbanes (D-MD) and Rep. Luis Gutierrez (D-IL) co-sponsored in late 2010 H.R. 6398, an act that amends the Federal Deposit Insurance Act ("FDIC"), which was amended by Dodd-Frank, to treat interest on a Lawyers Trust Account as a noninterest-bearing transaction account that is fully insurable by the FDIC. This act, passed by both houses of Congress, was signed by the president on December 29, 2010 as one of the earliest pieces of legislation to adjust a part of Dodd-Frank. While H.R. 6398 raised far fewer controversial issues than an amendment to the clearing or end-user exception would if introduced, the leadership and political makeup of the Congress in 2011 differ in many important respects and there is no assurance that further amendment to Dodd-Frank will not take place.

While it is unlikely that Dodd-Frank will be subject to a substantial amendment at this stage, Congress after the midterm election in November 2010 will likely consider budgetary proposals and a corrections bill for certain more technical parts of Title VII of Dodd-Frank. Those developments, along with the majority of the 300 rules mandated by Dodd-Frank, promise an eventful 2011 for participants in the U.S. derivatives market.

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CFTC's Dodd-Frank Rulemaking on Protections for Customer Funds For Cleared Swaps Confronts Significant Market Structure Issues

The Commodity Futures Trading Commission ("CFTC") considers one of its highest priorities to be the protection of the funds that customers deposit with their futures commission merchants ("FCMs") for their futures contracts. The current regulatory framework for protection of futures customer margin deposits has been in place for decades. As a result of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), however, the CFTC is now grappling with whether it should adopt a fundamentally different regime for the protection of customer funds deposited as collateral for the new trading in cleared swaps.

A different regime could establish significantly greater protection for swap customer funds in the event of a commodity broker bankruptcy, but might also impose significantly higher costs for both swap customers and FCMs. The outcome will affect all parties to those swaps that Dodd-Frank requires to be cleared, such as swaps involving pension plans and other financial entities. The CFTC issued an Advance Notice of Proposed Rulemaking seeking comment on various approaches to this issue; the comment period closed on January 18, 2011. Following review of those comments, the CFTC is expected to formulate proposed regulations by the end of the first quarter of 2011, and to publish those for further comment.

The existing framework applicable to customer funds for futures trading mutualizes the risk of any customer default on a futures contract across all customers of the FCM. Each futures clearinghouse—or, as they are referred to by statute, "derivatives clearing organization" ("DCO")—establishes the minimum levels of futures margin that an FCM must collect from its customers and post with the DCO. Section 4d(b) of the Commodity Exchange Act ("CEA") permits an FCM to maintain those customer margin funds in the FCM's omnibus customer account at the DCO. If a futures customer defaults on a futures contract and the FCM carrying that customer's account cannot cover the defaulting customer's obligations on its futures contracts, the DCO may use any or all of the collateral in the FCM's customer omnibus account—including the assets of the FCM's other customers—to meet the defaulting customer's obligations. This regime obviously puts the funds of non-defaulting customers in jeopardy, and is sometimes referred to as "fellow-customer risk."

Some opponents of a futures-style mutualization of risk for swap customer collateral have argued that Section 724 of Dodd-Frank, which added new CEA Section 4d(f)(6), does not permit it. Section 4d(f)(6) is identical to CEA Section 4d(b) except for the absence of one letter "s". Section 4d(b) makes it unlawful for a DCO to treat the funds of futures customers "as belonging to the depositing [FCM] or any person other than the *customers* of the [FCM]." (Emphasis added.) New Section 4d(f)(6) is the same for swaps except that the term "swaps customer" (in the singular) is used instead of "customers." Opponents of fellow-customer risk for swaps contend that use of the singular prohibits one customer's funds from being treated as belonging to any other person, including any other customer. The scant legislative history on the subject is not definitive.

Acknowledging arguments on all sides, the CFTC's Advance Notice posits four alternative schemes for the protection of customer funds. The first is "full physical segregation" of each swap customer's funds at the FCM, the DCO and any other depository, which would eliminate fellow-customer risk. A second alternative,

referred to as "legal segregation with commingling," would require collateral requirements for each swap customer to be calculated on an individual basis, but the DCO could maintain the collateral in a customer omnibus account. Both of these alternatives would prohibit a DCO from using the collateral of a non-defaulting customer to satisfy the obligations of a defaulting customer. The third alternative, described as "moving customers to the back of the waterfall," would be similar to the second alternative, except that the DCO could use the collateral attributable to a non-defaulting customer in case of a default, but only after it first used its own capital and the assets in the DCO's guarantee fund established from contributions of its clearing members. The last alternative, referred to as the "baseline model," is the current framework for futures.

The CFTC has requested comments on the costs and operational procedures related to each of these models. One DCO has estimated that margin requirements for clearing members could increase by 60 percent if swaps are treated differently from futures, with these increased costs being passed on to customers. The CFTC also requested comment on the moral hazard that may be associated with providing greater protection for swap customer funds and thereby lessening the concern a customer may have with the risk management practices of the FCM it chooses. This leads to questions of whether and how a swap customer could even assess the risk posed by fellow customers and the efficacy of an FCM's risk management practices.

There is at least a concern that the resolution of these issues could affect futures customers as well. The director of the CFTC's Division of Clearing and Intermediary Oversight stated that, if a system for swaps were permitted that differed from the baseline model, the futures system might need to be conformed because it would not be feasible to operate differing systems for swaps and futures. CFTC Chairman Gensler, however, has questioned whether that would be the case.

Requiring the clearing of standardized swaps through a central counterparty is one of the hallmarks of Dodd-Frank, which is intended to reduce systemic risk in the U.S. financial markets and banking system. However, centralized clearing of swaps also introduces the potential of fellow-customer risk, and a fundamental and controversial policy issue for the CFTC. Given the potential impact of the CFTC's ultimate decision, continued intense debate and scrutiny undoubtedly will continue before the issue is resolved.

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Developments in the Investment Management Industry

Implementation of the regulatory agenda set in motion by the voluminous Dodd-Frank Wall Street Reform and Consumer Protection Act, passed by a Democratic-dominated Congress in July 2010, is well underway. Designated government agencies continue to pump out rulemakings under an ambitious schedule mandated by statute. By some estimates, about 20 percent of the regulatory initiatives called for by the statute have been put into place, with the remaining 80 percent to be implemented on a timeline extending several more years.

Securities and Exchange Commission

The lion's share of this burden rests with the SEC, which is responsible for more than 100 rulemakings and about two dozen studies or reports. So far, the SEC is keeping up with the rapid pace required by the Dodd-Frank statute. Some of the key issues addressed to date include the following:

Swaps. The SEC, jointly with the CFTC, has made significant headway proposing rules defining key terms related to the security-based swaps market, including "swap dealer," "security-based swap dealer," "major swap participant," "major security-based swap participant" and "eligible contract participant," as well as considering issues related to clearing organization and execution facility governance and conflicts. Both agencies have also proposed implementing rules related to conflicts of interest, reporting, registration, fraud prevention and other basic rules of the road in the security-based (in the case of the SEC) and non-security-based (in the case of the CFTC) swaps markets going forward.

Hedge Funds and Other Private Funds. Implementation of the investment adviser registration requirement of Dodd-Frank is not mandated until July 2011. As it works on developing those proposed rules, expected as this publication goes to print, the SEC has busily published related proposals implementing the exemptions from registration for advisers to venture capital firms and for certain advisers to other private funds and to "family offices." It also has proposed rules to implement the transition of mid-sized investment advisers (between $25 and $100 million in assets under management) from SEC to state regulation.

Whistleblower Rules. In November, after issuing its initial annual report to Congress related to the Securities Whistleblower Incentives and Protection program, the SEC proposed whistleblower rules to reward individuals who provide the agency with high-quality tips that lead to successful enforcement actions. The SEC's proposed rules sought to counterbalance the potential that these financial incentives might undercut corporate compliance efforts by encouraging whistleblowers to side-step reporting through internal channels, but many commenters criticize these efforts as woefully inadequate. It is not clear whether the final rule will reflect any major changes in this regard. The SEC staff also announced the formation of an Office of Market Intelligence within the Enforcement Division to implement the whistleblower program.

Potpourri. The SEC's website lists more than 40 rulemaking and administrative actions it has taken under Dodd-Frank since its passage, including proposed governance rules regarding shareholder votes on executive compensation and related disclosure by institutional investment managers of votes on executive compensation; proposed disclosure rules in the asset-backed securities market; and steps taken to improve SEC organization, operations, and efficiency. The SEC has also released its study of the appropriate fiduciary standards for brokers, dealers, and investment advisers.

Enforcement. In the meantime, the SEC has also announced an aggressive enforcement agenda. The director of the Division of Enforcement, Robert Khuzami, in testimony before Congress in September, identified an ambitious program of internal reform in the division and targeted new initiatives to identify securities fraud. Among these new initiatives is a newly designated Asset Management Unit, intended to focus on mutual funds, private funds, and investment advisers. So far, the unit has (i) developed "risk analytics" that identify "red flags" for further investigation of disclosure and valuation issues in mutual fund bond portfolios; (ii) instituted a program for detecting "problem investment advisers" based on their representations about their education, experience, and past performance; and (iii) developed "analytics" for reviewing whether mutual fund advisers charge retail investors "excessive" fees, with the ultimate objective of targeting investment advisers and fund boards of directors.

Financial Stability Oversight Council (FSOC) Actions

The FSOC, established by Dodd-Frank as the oversight body for monitoring systemic risk and resolving jurisdictional questions among the financial service regulators, has conducted its initial organizational meetings with little fanfare. At its inaugural meeting in October, the FSOC, among other matters, sought input on proposed factors for designating nonbank financial companies for heightened supervision. It also solicited comments in connection with its study of the Volcker Rule, which prohibits proprietary trading and certain private fund investments by financial institutions, and made recommendations to inform coordinated rulemaking among relevant agencies. In November 2010, the FSOC sought input on the criteria and analytical framework for designating financial market utilities (other than clearing and settlement activities of financial institutions) as systemically important.

Money Market Funds (MMFs)

The FSOC is expected to tackle the regulatory status of MMFs, as requested by the President's Working Group in its Money Market Fund Report issued in October 2010. Options proposed by that report include the adoption of floating net asset values, redemptions in kind by larger funds (either of which could be implemented by the SEC), and the introduction of a private emergency liquidity facility and insurance for MMFs. The FSOC will also consider whether to require the conversion of MMFs to special-purpose banks, or to allow a two-tier system of MMFs that might combine different features. These latter actions could require the involvement of banking or other regulators in addition to the SEC.

On the Horizon

With a Republican majority now taking control of the House of Representatives and a Republican congressman chairing the SEC's oversight committee, Dodd-Frank implementation may well take a new turn. Congressional feuding over spending has already frozen budgets at last year's levels under continuing resolutions lasting through March 4, 2011, and these freezes could well become indefinite. As a result, the SEC has stopped its post-Dodd-Frank hiring spree, and the agency has announced it has deferred several Dodd-Frank initiatives due to "budget uncertainty." Among the initiatives on hold are the creation of investor advisory and investor advocacy offices, as well as an office of credit ratings rulemaking, although existing staff in other offices appear to be handling the activities proposed for these new entities.

The SEC has also announced delays or cutbacks in enforcement and market oversight efforts and has noted that the longer it is required to operate under significant budgetary restrictions, the greater impact this will have on its mission. The ambitious enforcement agenda announced in September may already be diminishing in light of these reductions and related travel restrictions, and enforcement cases may need to be staffed more thinly and timelines extended.

The SEC still has on its plate many significant issues, including rulemakings regarding oversight of credit rating agencies; critical issues involving CFTC coordination regarding derivatives and swaps; issues involving asset-backed securities and short sales; revisions to the "accredited investor" standard and other issues impacting hedge fund management and marketing; and corporate governance and related disclosure matters.

With 2011 just beginning, the SEC is quickly finding itself between a rock – Dodd-Frank mandated agency actions – and a hard place – Congressional impasse on spending authorizations. Although the SEC's regulatory agenda for the next several years seems set by Dodd-Frank, the agency may need to creatively exercise discretion in assessing how much of Dodd-Frank it can realistically implement, and determining how to effect the requirements of the law within its budgetary constraints and its own significant enforcement agenda.

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Accountable Care Organizations: A New Frontier in Provider Integration

President Obama signed the Patient Protection and Affordable Care Act into law on March 23, 2010 and the corresponding reconciliation bill on March 30, 2010 (collectively, the "Health Care Reform Bill"). While the individual mandate and other provisions have garnered greater mass media attention in recent months, the Health Care Reform Bill also contains a number of provisions directed towards instituting and developing new Medicare and Medicaid value-based payment initiatives that may have an equally revolutionary impact on the American health care industry. Such initiatives attempt to reward value, rather than volume, and therefore seek to pave the way for a transformation in how providers are reimbursed.

The Congressional Budget Office has estimated that one of the principal initiatives – the Medicare Shared Savings Program, which encourages the formation of Accountable Care Organizations ("ACOs") – could be responsible for $4.9 billion in Medicare savings through 2019.[1] Since March 2010, providers and industry stakeholders have attempted to determine what exactly an ACO is and how to form one without running afoul of existing federal fraud and abuse and antitrust laws. The answers have remained elusive to date. However, after soliciting feedback from key stakeholders through teleconferences, requests for written comments, and a face-to-face task force meeting in October, the government is expected to issue additional guidance on how an ACO can avoid liability under antitrust and fraud and abuse laws.

ACOs: What We Know

The Health Care Reform Bill requires the Secretary of the Department of Health and Human Services to establish the Medicare Shared Savings Program by January 1, 2012. ACOs must have accepted responsibility for the overall care of at least 5,000 Medicare beneficiaries, although each beneficiary retains the ability to choose any provider of his or her choice either within or outside of the ACO. Physicians may form an ACO on their own or in partnership with hospitals. The leadership structure must have clinical and administrative systems to facilitate integration. ACOs must have defined processes to promote evidence-based medicine, report the necessary data to evaluate quality and cost measures, and coordinate care.[2] Finally, an ACO must be able to demonstrate patient-centeredness.

Providers in an ACO will continue to be paid under the Medicare fee-for-service model; however, the ACO will be eligible for additional payments if certain quality metrics and cost savings are achieved, relative to a benchmark amount per Medicare enrollee. Accordingly, the ACO must have a formal legal structure to receive and distribute such shared savings. The Centers for Medicare and Medicaid Services ("CMS") are also authorized to pay ACOs under alternative payment models, including partial capitation in which providers are partially paid a defined fee per beneficiary per month.

To be workable, an ACO cannot simply be used as a vehicle for collective contracting, such as a Medicare "physician-hospital organization" ("PHO"). These organizations in many instances failed to accomplish change in the health care delivery system because they focused primarily on payment issues – as opposed to streamlining and improving care through clinical integration. Instead, an ACO will need to embody genuine commitment among the participants to work to form a new type of delivery system where the ACO is the provider with various integrated components collectively meeting the patient's needs, rather than merely a framework for separately practicing providers to distribute payment.

Challenges under the Existing Fraud and Abuse and Antitrust Framework

Such a shared savings program among providers raises regulatory issues by implicating the federal Anti-Kickback Statute (which prohibits any remuneration between entities intended to direct or induce referrals or generate federal health care program business), the federal Stark Law (which prohibits any financial relationship between a physician and an entity, such as a hospital, to which the physician refers designated health services, unless such relationship fits within an enumerated exception), and the federal Civil Monetary Penalties law (which prohibits the payment of anything to a physician to reduce or limit services to a Medicare beneficiary under his or her direct care).

While hospitals could theoretically employ physicians to form an ACO and potentially avoid many of these regulatory issues, the government appears to be attempting to encourage new, innovative ways for providers to affiliate. For example, in a November 17 request for comments, CMS states that it is "seeking to advance ACO structures that are organized in ways that…foster participation of physicians and other clinicians who are in solo or small practices."

Given existing fraud and abuse laws, the notion of an ACO raises questions such as: how can an ACO distribute shared savings payments? How can an ACO provide incentives for providers to refer, or for patients to choose providers, within the ACO? Can an ACO reduce services to beneficiaries in order to provide more efficient and cost-effective care? Can hospitals incur the startup costs associated with forming an ACO that also benefits referring physicians?

In addition, ACOs raise significant issues under federal and state antitrust provisions if they are also to collectively negotiate prices with private payors, which many believe is necessary to justify the costs of ACO development. Like PHOs and independent practice associations that have been subject to significant federal regulatory action and comment, ACOs must demonstrate substantial financial and/or clinical integration sufficient to justify the potentially anti-competitive effects of allowing independent providers to collectively bargain with payors. Even fully integrated ACOs may still face antitrust scrutiny based on their market share in a given geographic market.

In order to help address these issues, the Health Care Reform Bill gives the secretary the authority to waive certain fraud and abuse laws in order to achieve the goals of the ACO initiative. Part of the current debate involves how such waivers should be structured: should they be one-off waivers based on the particular arrangement, or should the government create specific exceptions under each applicable law, so that entities can structure their arrangements to comply? While not explicitly authorized by the Health Care Reform Bill, antitrust regulators are similarly considering various options for new or expanded safe harbors for qualifying ACOs, such as deeming qualifying ACOs as integrated for purposes of antitrust review, expanding relevant geographic service areas for purposes of determining market share, or adjusting the treatment of exclusive networks (*i.e.,* those that prohibit providers from participating in more than one network).

The government has solicited comments from industry groups on a number of occasions. In June, CMS held a teleconference in which it solicited questions and concerns related to ACOs. On October 5, 2010, the Federal Trade Commission, CMS, and the Office of Inspector General of the Department of Health and Human Services ("DHHS") held a public workshop regarding ACOs and implications regarding antitrust, Stark, Anti-Kickback, and Civil Monetary Penalty laws. The inspector general of DHHS stated that the goal is to ensure that ACOs "are not unduly inhibited by existing laws" and that "fresh thinking" is needed about program integrity.[3] In addition to this conference, a number of

The government has solicited comments from industry groups on a number of occasions.

industry groups, including the American Hospital Association, the American Medical Association, and the American Health Lawyers Association, have provided comments to the government regarding ACOs in the last few months. For the most part, such comments have focused on the concerns of the particular industry group. Aside from the need for further guidance from the government, no prevailing consensus has emerged. Most recently, on December 1, the chief of staff of the Justice Department's Antitrust Division told a House judiciary committee that it would provide an expedited review of ACOs under the federal antitrust laws. Additional guidance is expected to be forthcoming in 2011.

Conclusion

While providers will need to navigate and avoid the potential legal pitfalls associated with ACOs, the ultimate success of an ACO is likely to be measured by whether the provider members focus on effecting a legitimate change in the delivery system or whether they only seek to comply superficially with the ACO requirements in order to attempt to receive increased reimbursement. A radical departure in how providers think about care is needed. In the end, the ACO project likely offers a glimpse into the future of reimbursed models and in turn the delivery of care.

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1 March 20, 2010 Letter to Ms. Pelosi, Speaker of the House, from D. Elmendorf, Director of Congressional Budget Office, Table 5.

2 CMS, Preliminary Questions and Answers, Medicare "Accountable Care Organizations," available at: www.cms.gov/OfficeofLegislation/Downloads/AccountableCareOrganization.pdf

3 Text of Remarks by D. Levinson, October 2, 2010, located at: http://www.ftc.gov/opp/workshops/aco/index.shtml

Recent U.S. Actions on Greenhouse Gas Regulations

Efforts in the United States to regulate greenhouse gas ("GHG") emissions date back to 1998, when the former general counsel of the U.S. Environmental Protection Agency ("EPA") concluded that GHG emissions were pollutants under the Clean Air Act and could be regulated. A year later, a group of organizations petitioned EPA to regulate GHG emissions from new motor vehicles. In 2003, EPA denied the petition, which was challenged by Massachusetts, among others, in litigation that ultimately was decided by the U.S. Supreme Court.

In 2007, the U.S. Supreme Court found that the EPA had the authority under the Clean Air Act to regulate GHG emissions. In 2009, the EPA issued an "endangerment finding" under the Clean Air Act that GHG emissions from new motor vehicles may endanger public health or welfare. This finding required EPA to issue GHG emissions standards for light-duty motor vehicles, and it also triggered the need for other regulations, including GHG permitting standards, the installation of Best Available Control Technology ("BACT") for controlling GHG from new or modified stationary sources, and New Source Performance Standards ("NSPS") for GHG emissions.

As the 112th Congress kicks off and the new House majority is set to begin intensive oversight of EPA rules, EPA recently took two significant actions that will affect the schedule for issuing GHG regulations. These actions also will ultimately affect the level of GHG emissions controls that will be required at power plants and other large stationary sources.

The first action went into effect on January 2, 2011, requiring that permits issued under the Clean Air Act for large stationary sources begin to address GHG emissions, as well as require BACT to control these emissions. To prepare for this requirement, the EPA issued a series of rules on December 23, 2010 to (1) narrow the permitting requirement so that facilities with GHG emissions below the levels set in the tailoring rule do not need permits and (2) give EPA authority to issue GHG permits in states that need to revise their permitting regulations to cover GHG emissions.

Second, on January 12, 2011, EPA waived GHG permits for the next three years for utilities, boilers and other industrial facilities using biomass. EPA is expected to continue to study the effects of biomass, and before the end of the three-year deferral, issue a rule clarifying the GHG permitting requirements for biomass.

Beginning on January 2, 2011, permits issued for large stationary sources will have to address GHG emissions.

Third, EPA announced a schedule for issuing regulations controlling GHG emissions from electric generating units and petroleum refineries. According to this schedule, EPA will propose standards for natural gas, oil and coal-fired electric generating units by July 26, 2011 and for refineries by December 10, 2011, and issue final standards by May 26, 2012, and by November 10, 2012, respectively. EPA agreed to this schedule as part of a settlement with several states, local governments and environmental organizations that had sued EPA over its failure to update emissions standards for power plants and refineries as required by Section 111 of the Clean Air Act. Section 111 requires EPA to issue NSPS that set emissions limits for new facilities and address emissions from existing facilities.

Implications

These two actions, along with EPA's endangerment finding, have set the stage for the regulation of GHG emissions from stationary sources over the next two years. These actions are extremely controversial. EPA's endangerment finding has been challenged in court, and there is some bipartisan support in Congress to use the Congressional Review Act to limit or overturn EPA's GHG rulemaking. If Congress fails to overturn or delay these actions (a likely outcome since it would require the president's approval), EPA's actions will likely be challenged in court. At a minimum, EPA's permitting and NSPS rules will have significant implications for utilities and refineries, among others.

Permitting Requirements

Beginning on January 2, 2011, permits issued for large stationary sources will have to address GHG emissions. However, because these permit requirements are being phased in, and initially no facility will be required to get a new permit solely due to its GHG emissions, the burden to industry should be somewhat reduced, at least through the middle of this year. Beginning this July, however, all new sources with GHG emissions of 100,000 tons per year or modified sources with GHG emissions of 75,000 tons per year will be required to get a permit. This will rapidly increase the burden on industry and state permitting agencies.

One big unresolved question is how state permitting agencies ultimately will define BACT; in guidance issued late last year, EPA essentially passed this responsibility to states by providing only general recommendations that states should use when making BACT decisions. These determinations will prove controversial since a facility will have to use BACT to obtain a permit. In EPA's BACT guidance to state agencies, EPA placed an emphasis on BACT options that improve energy efficiency, and it identified carbon capture as a promising but expensive technology that should be considered. At the same time, EPA also recognized that certain biomass fuels by themselves may be considered BACT, and in early January went so far as to waive permit requirements for three years for facilities using biomass. The availability of options to industry and the ultimate costs will depend on the flexibility of the state permitting agencies in determining BACT.

New Source Performance Standards

Implementing the agreement that EPA reached in December with states and environmental groups, on the EPA's schedule for issuing GHG NSPS for new and modified electric generating units and refineries, will likely be contentious. Once these standards are issued, these two industries will be subject to maximum limits for GHG emissions. The EPA administrator will determine whether the industry has adequately demonstrated the application of the best system of emissions reductions.

The Clean Air Act gives EPA the flexibility in setting these standards to consider several factors, including the cost of achieving such reductions, any non-air quality health and environmental impacts, and energy requirements. To establish such emissions standards, EPA will need to undertake an extensive review of existing technology and its costs, and ultimately will establish specific numeric standards for emissions of carbon dioxide, sulfur oxides, particulates, and nitrogen oxides that will vary by industry.

It is likely that EPA will establish tight controls and emissions limits on carbon dioxide emissions from power plants and petroleum refineries, thereby creating an incentive for them to reduce their GHG emissions, either directly by changing feed stocks, or by diverting the emissions for beneficial reuse.

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Photovoltaic Energy in France: A Transitional Year Ahead

As France continues to develop its renewable energy industry and struggles to recover from the global economic crisis, we expect to see a number of trends in 2011 affecting both businesses and investments in this sector.

Since the 2007 *"Grenelle de l'environnement"* conference, France has adopted an ambitious strategy for developing renewable energies. The conference brought together representatives of the central government, local authorities, trade unions, businesses and nonprofit organizations for the purpose of developing a concrete action plan to tackle environmental issues. The conference participants recognized that renewable energies (such as wind and solar power) were underdeveloped in France and called for the French government to stimulate this sector.

Following the conference, the French government has established a common framework to encourage the generation of energy from renewable sources, with the objective that energy from renewable sources should represent 23 percent of total energy production in France by 2020. This is consistent with the target established by the European Union in Directive 2009/28/EC. France has implemented financial and tax incentives to encourage homeowners and businesses to achieve this target. Electricity from renewable sources is also being promoted through a feed-in tariff system by which Electricité de France (the largest supplier of electricity in France) is guaranteeing to producers a fixed price for the purchase of power generated from renewable sources for a duration of 20 years.

France's photovoltaic market is considered to be the fourth largest in Europe, and significant growth is anticipated. The French government's plan calls for the installed capacity of photovoltaic power to increase more than 15 times, from 349 MW on March 31, 2010 to 5,400 MW by 2020. French photovoltaic capacity has already more than doubled over the course of this year, to approximately 850 MW.

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The government's target is likely to be achieved before 2020, primarily due to the attractiveness of the feed-in tariffs. Currently, feed-in tariffs for electricity produced by photovoltaic panels range between 0.352 €/KWh and 0.580 €/KWh (compared to an average of 0.110 €/KWh charged to energy consumers) depending on criteria such as the level of power generated by the panels, the geographic region in which the panels are located, whether they are located on the ground or on a building, and whether the panels are integrated into any such building. These tariffs are among the highest in Europe, and both investors and homeowners have taken advantage of this situation.

However, this explosion of capacity means that the subsidization of photovoltaic energy may become a significant burden. The French government is evaluating measures, including the potential adjustment of feed-in tariffs, to reduce the risk of speculation and to prevent the development of a "solar bubble," although room to maneuver will be limited given the need to maintain a system sufficiently attractive for the market to reach the target of 5,400 MW installed by 2020.

The French government has set a deadline of March 2011 for determining a new, rebalanced approach on feed-in tariffs, and in the meantime is holding extensive consultations with the industry players. On December 9, 2010, a decree was enacted withholding until March 2011 the registration of new projects generating more than 3 KW.

In this context, we believe that the French government may attempt to slightly decrease the current feed-in tariffs for new generating capacity (former tariffs will continue to apply to installed equipment) and/or to set a "soft" annual cap, limiting new installations up to 500 MW per year. Under such a soft cap, power would be purchased from photovoltaic installations at the feed-in tariffs currently in force until a 500 MW annual threshold is reached, and the feed-in tariffs would then decline significantly for additional installations.

If the feed-in tariffs are not decreased and/or if a soft cap solution is not implemented, the government may instead opt to amend the feed-in tariffs in a way that small installations (such as homeowners' installations) could continue to benefit from a favorable tariff compared to larger installations (those generating more than 250 KW for instance), with those tariffs to be based on a sliding scale.

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Prospects for Passage of Pending Bilateral Free Trade Agreements

During the 2008 presidential campaign, then-candidate Obama expressed considerable disaffection for the North American Free Trade Agreement ("NAFTA"), asserting that it had resulted in a loss of U.S. jobs, particularly in the former industrial heartland states. At the outset of his administration, President Obama also showed little interest in concluding any of the pending bilateral trade agreements, including those with South Korea, Colombia, and Panama. Due to the state of the economy, however, the political and trade policy winds have shifted, and the administration is now keen to be perceived as pursuing every available mechanism to promote job growth, including through trade policy-related initiatives. For example, the administration has announced a new initiative to streamline export controls, in part to better facilitate exports. The cornerstone of these efforts, however, has been a push to finalize the bilateral trade agreements pending at the beginning of this administration, which have languished for several years. There are three such agreements.

South Korea

In early December 2010, U.S. and South Korean trade negotiators reached agreement on the long-delayed U.S.-South Korean Free Trade Agreement ("KORUS FTA"), which had been signed initially in 2007. Upon approval by Congress, the KORUS FTA would be the second largest such arrangement, in terms of volume of trade, in which the United States participates, second only to NAFTA. According to President Obama, the KORUS FTA will boost annual exports of automobiles, agricultural products, and other goods and services by US $11 billion and support approximately 70,000 jobs in the United States. Access to the South Korean market for U.S.-manufactured automobiles had been the primary sticking point between the parties. The revised agreement maintains the current 2.5 percent U.S. tariff on South Korean automobile imports until the fifth year of implementation, while South Korea's 8 percent tariff on U.S. automobile imports will be cut in half immediately. However, the revised deal does not address U.S. concerns regarding restrictions imposed by South Korea on imports of U.S. beef, which had been imposed in response to the discovery of "mad cow" disease in U.S. cattle a number of years ago.

Because the United States negotiated, concluded, and entered into the KORUS FTA within the parameters of Trade Promotion Authority ("TPA") under the Bipartisan Trade Promotion Act of 2002 (Pub. L. 107-210), any implementing legislation should be subject to expedited procedures, that is, mandatory congressional consideration, limited debate, no amendments, and an up-or-down vote.

Colombia

The U.S.-Colombian Free Trade Agreement ("CFTA") was signed on November 22, 2006 and, like the KORUS FTA, was negotiated and entered into under TPA. However, although implementing legislation for the CFTA was submitted to Congress in April 2008, due to alleged procedural deficiencies the House voted to make the so-called "fast track" protocol inapplicable to the implementing legislation. Democrats in Congress have balked at approving the agreement until Colombia takes positive steps to address a number of lingering issues, most notably anti-union violence. By contrast, some policymakers and members of Congress have touted the progress that Colombia has made in recent years to curb violence, and have suggested that the failure to finalize the agreement with a crucial ally in Latin America could lead to further violence in the region.

Panama

The free trade agreement between the United States and Panama was signed on June 28, 2007, in time for the agreement to be considered under TPA

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before such authority expired on July 1, 2007. By contrast to the agreements with South Korea and Colombia, the Panama agreement is considerably less controversial, although, at the behest of Congress, it does contain provisions relating to enforceable labor standards, adherence to multilateral environmental agreements, and easier access by developing countries to generic pharmaceuticals that extend beyond those found in existing bilateral free trade agreements. Two additional concerns relate to Panama's labor statute, which some members of Congress would like to see amended to reflect International Labor Organization guidelines relating to the formation of unions, as well as to Panama's status as a tax haven. The first of these lingering issues has yet to be resolved, but on November 30, 2010, the United States and Panama entered into a tax information exchange agreement designed to enable the United States to more effectively enforce its tax laws, including by being able to obtain information relating to bank accounts in Panama.

Timetables/Steps for Completing the Agreements.

The Office of the United States Trade Representative stated in mid-December 2010 that the Obama administration intends to finalize the legal text of a supplemental agreement for the KORUS FTA by late January or early February 2011. However, there remains no indication as to when the President might submit the necessary implementing legislation to Congress, although some administration officials reportedly expect that this could occur by the end of February 2011. Formal submission of the legislation to the House would trigger the "fast track" timeline, which requires a House vote within 60 legislative days, although there is some question as to whether the supplemental agreement itself would qualify for TPA.

In response to assertions by the incoming House GOP leadership that the agreements should be addressed simultaneously by Congress, or in "tight sequence," the administration has stated that there is not yet any timeline for moving the Colombia and Panama agreements. House Speaker John Boehner (R-OH), for example, has stated that he desires to approve all three pending trade agreements at about the same time in 2011, although Rep. Kevin Brady (R-TX), who was announced on January 6, 2011 as the House Ways and Means Trade Subcommittee chairman, supports passage of all three agreements in the first half of 2011. On January 7, 2011, it was reported that the Republicans serving on the House Ways and Means Committee intend to hold a full committee hearing on the three pending free trade agreements at the end of January or in early February 2011, at which U.S. Trade Representative Ron Kirk likely will be asked to testify.

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European Union Competition and Antitrust Law: Key Issues for 2011

Global Convergence of Competition Law

The watchword for EU competition law in 2011 will be "convergence." EU Competition Commissioner Joaquín Almunia emphasized in a speech at the International Competition Network in December that it does not make sense to confine competition enforcement within national boundaries. He made the point that while some diversity of approach is required, the cross-border nature of today's business enterprises and transactions work necessitates a reduction in the number of conflicting rules between different jurisdictions.

The ultimate elimination of these conflicts would reduce compliance costs and create transparency and legal certainty to the benefit of business, competition authorities and consumers, although he noted that convergence should not rest on the lowest common denominator. Almunia did acknowledge that to aim for full convergence would be unrealistic and that it would be better to aim for a global balance between under- and over-enforcement. However, he has yet to articulate substantively how he will initiate a movement towards convergence.

State Aid

The 2008 State Aid General Block Exemption Regulations ("the Regulations") of the European Commission ("the Commission"), which were instituted as a result of the global financial crisis, will be applied into 2011, with some modifications. The EU state aid rules essentially prohibit member states from granting aid (in whatever form) where this will distort competition by favouring certain companies or industries and will affect trade between member states. As such, specific legislation (in the form of the Regulations) was required in order to permit member states lawfully to provide financial support in the current economic crisis. The availability of this support has been a vital safety net for member states' financial systems. The Commission will continue its gradual phasing-out of the measures. From January 1, 2011, all banks receiving support in the form of capital or impaired asset measures, regardless of size, will be required to submit a restructuring plan. The Commission's message is that banks must prepare to return to a world of normal market conditions without state support.

State aid for the real economy under the Temporary Framework ("TF") (which was published in 2009 and permits member states to provide direct financial support to small, medium and large companies) comes with the same message. The Risk Capital Guidelines (first issued in 2006 and intended to provide guidance to member states on assessing risk capital investments in such a way as not to hinder investment by private investors) have been modified to increase from €1.5 million to €2.5 million the maximum amount of finance that a member state can invest in a startup company. These guidelines are set until the end of 2013. The Commission has further simplified the procedure for short-term export credit insurance. However, firms in difficulty will now be examined under the normal Rescue and Restructuring Guidelines ("the Guidelines") when they receive state support, rather than the TF. The Guidelines were published in 2004 and give general guidance to member states on when and how they may rely on the exemption under EU law for providing state aid to firms in financial difficulty. The Guidelines set out a highly stringent regime for the granting of aid in such circumstances. The Commission launched a consultation on a revised version of the Guidelines in December 2010. Furthermore, subsidized working capital loans and guarantees for large firms are now also excluded from the TF, and the maximum aid a company can receive is being reduced from €500,000 to the standard *de minimis* €200,000. The Commission expects to return to the normal application of state aid rules by January 2012.

Cartels and Inability to Pay

The Commission will continue its war on cartels in 2011. It took action against seven cartels in 2010 and in total imposed fines of over €3 billion in that year. There is an ongoing debate about "inability to pay" claims that will continue as a regulatory issue in 2011. There is a fine balance to be drawn between imposing large punitive fines to function as a deterrent and putting smaller companies under severe financial strain or out of business, which may have a counterproductive effect of reducing competition in that market.

The Commission argues that companies' financial troubles are their own doing, often caused by factors predating the fine. For this reason, poverty pleas are regularly ignored. Many criticize the Commission for wasting a disproportionate amount of its scarce resources chasing companies to recover fines that have been imposed, often not recovering anything because the company goes into liquidation. With Almunia's arrival at the Commission, the approach appears to have softened, as nine out of the eleven pleas granted since 2005 (out of 54 requests in total) came in 2010. This was certainly influenced in part by the global recession. We expect to see a continuation and development of this balanced approach in 2011.

Google and Article 102 Abuse of Dominance

The Commission has recently opened an antitrust investigation into Google, with a particular focus on the way in which its search results are set out. The investigation is likely to continue through most of 2011. Search service providers have complained that their services receive unfavourable treatment in Google's unpaid and sponsored search results and that Google's own services are preferentially placed. Almunia stresses that this investigation does not indicate that there is definitely a violation, but rather that there are grounds for an enquiry. The Commission will continue to pursue the aim of limiting (where possible) barriers to entry across all business sectors throughout 2011 and beyond, but we may see particular emphasis on the information and communications technologies sector because, as Almunia notes, maintaining the industry's dynamism will benefit the whole economy.

Collective Redress

Almunia has announced a public consultation for the beginning of 2011 to address the need for an antitrust-specific directive on private follow-on damages actions, which in practice are very difficult to pursue in most EU member states. He said in a speech in October that although Europe needs to avoid the "excesses" of a U.S.-style class action model, access to the right to collective redress is at present inadequate in many member states, and the cost and time inefficiencies of the current system suggest that collective action at the national level would be a pragmatic solution. He anticipates agreement on a general legal framework for collective redress in the Spring, which will be used to launch specific legislative initiatives to address representative actions. A proposal for an antitrust-specific directive is expected in the second half of 2011.

Horizontal Agreements

Finally, the Commission adopted new guidelines on horizontal cooperation in December 2010, with only very minor changes from the draft document released earlier in the year. The changes mainly concern standard-setting and information exchange, with the aim of promoting fairness and transparency and to better serve customers.

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2011: Changes to the UK Employment and Immigration Law Landscape

2011 will see some significant changes to the UK's employment law regime resulting from a series of government initiatives.

The first is the elimination of the default retirement age of 65 with effect from April 2011. From this time, any enforced retirement of an employee at any age will constitute age discrimination unless that retirement can be objectively justified by the employer. This is a fundamental change to working relationships in the UK, where retirement has been a feature for many years. Employers are now faced with difficult policy decisions that will have to be resolved in early 2011. Do they persist with a retirement age that they will have to objectively justify in the event of challenge? If so, now is the time for the employer to be gathering evidence of the business needs and objectives served by maintaining a retirement age. Or, do they abandon the whole concept of retirement, and instead face up to the cultural difficulties inherent in managing older employees in what may be difficult or sensitive circumstances?

Second, from October 2011, agency workers – that is, workers engaged by an employment agency to provide services for an end user – will be entitled to a host of new rights. UK business is one of the highest users of agency workers in the EU, and these new protections are designed to combat perceived abuse by employers of a group which, until now, has had very little in the way of employment rights. Under the new regime, once an agency worker has worked for the same end-user for 12 weeks, he or she will be entitled to the same pay and other conditions as the end user's own permanent employees. This will inevitably increase the cost of using agency workers, which may lead to a decline in their use, a cause for concern for both employment agencies and the end users of these workers.

Finally, in November 2010, the government confirmed that it was considering whether to make it more difficult for employees to claim unfair dismissal against their former employers. Currently, only employees with at least one year of service can claim unfair dismissal. The government is considering whether to increase that to two years' service. There is historical precedent for this. Before the Labour government came to power in 1997, the service requirement stood at two years but was reduced to one by the Labour government. A potential consequence of such a change, however, is that employers may face more claims for which no period of service is required, such as discrimination (under the new Equality Act 2010) and claims arising out of an act of whistleblowing.

The UK government has also set its sights on the immigration system. As part of its attempts to combat unemployment, the government has announced significant curbs on the ability of nationals of countries outside the European Economic Area to obtain visas allowing them to work in the UK. The Tier 1 (General) category of visa, which allows highly skilled migrants to obtain visas without a specific offer of employment, will be closed from April 2011, and replaced with a new visa for "persons of exceptional talent," intended to cover migrants who "have won international recognition in scientific and cultural

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Do they persist with a retirement age that they will have to objectively justify in the event of challenge?

fields," or who are likely to do so. This is a much higher threshold and in addition is subject to an annual limit of 1,000 visas.

The Tier 1 (General) category is already subject to monthly limits, which are currently being met within the first 10 days of each month. It is therefore likely that some applicants who have already submitted their application for this category of visa will not have their application processed in time before the category is closed. The Tier 1 (General) visa has been a very effective way of enabling highly skilled individuals to enter the UK to work or to look for work on a flexible basis, and its abolition is going to have a significant impact on those individuals.

Also with effect from April 2011, the number of visas which can be granted to individuals who are already in receipt of a job offer in the UK will be limited to 20,700 for 2011/12, a reduction on previous years. Intra-company transfers have, however, been excluded from this limit.

Finally, UK regulators are also starting to flex their muscles. The Information Commissioner ("IC"), who is responsible for the enforcement of the Data Protection Act 1998, recently fined Hertfordshire County Council £100,000 following two serious incidents where council employees faxed highly sensitive personal information to the wrong recipients. This followed another fine of £60,000 issued to an employment services company, one of whose employees lost an unencrypted laptop which contained personal information relating to 24,000 people who had used community legal advice centres in Hull and Leicester. The IC has the power to impose fines of up to £500,000, and 2011 may well see more such action being taken to ensure compliance with the UK's data protection legislation.

The combination of these reforms is likely to mean that employers will be kept very busy in 2011 ensuring that they keep abreast of changes to the law. It is not all bad news, however, since the government has also announced that Friday, April 29, 2011 will be a public holiday in recognition of the Royal Wedding!

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UK Election Law: Campaign Falsehoods by Incumbent Void Election

Election campaigns in the UK may become more civil as a result of the recent voiding of the result in a contest in which one candidate was found to have published falsehoods about his opponent.

In the final days prior to the May 2010 parliamentary election, the incumbent in the constituency of Oldham East & Saddleworth, former government minister and Labour MP Phil Woolas, published allegations that, amongst other things, his Liberal Democrat opponent, Elwyn Watkins, associated with extremist Muslims who advocated violence. Woolas also alleged that Watkins pandered to these extremists in an effort to secure their votes. Woolas won the seat by 103 votes.

Watkins subsequently challenged the result, making use of a rarely used process known as an election petition. This is the only means for challenging the result in a parliamentary election, and this was only the fifth substantial challenge since 1910. Watkins based his challenge on a statute originally enacted in 1868, and the grounds were last used in 1911, providing that no person may make a false statement about the personal character or conduct of another candidate in an attempt to affect the result of the election unless he believes it to be true and has reasonable grounds for doing so. K&L Gates advised Watkins on his challenge.

It is a curiosity of English law that an election petition is heard by two High Court judges sitting together as an Election Court within the constituency. This derives from Parliament's anxiety in the 19th century not to allow too much authority to the judges (originally Parliament used to hear these petitions itself), and Parliament was extremely keen to ensure that these petitions were conducted with the utmost speed and adjudicated very quickly.

A court was established in a small civic center in the town of Uppermill, outside Oldham in the North West of England, to hear the petition in the week beginning September 13, 2010. The High Court in London took control of the procedure, and this small civic center had to be converted into a court for the week. With security issues being a very live concern, an enormous amount of preparatory work had to be done. The advantage was that local people—which is what the Act always intended—were able to see the challenge in process, and to hear their (then) MP being cross-examined. He was cross-examined for almost a day.

The judgement of the Election Court was handed down—back in Uppermill again—on November 5th. That was an ironic choice of date, being Bonfire Night (the day on which the British celebrate Guy Fawkes' unsuccessful attempt to blow up the House of Commons). The court ruled that Mr. Woolas had committed a number of the illegal practices complained of and that his election was therefore void. He was barred from standing for elective office for three years and also lost the franchise (a token but important gesture), *i.e.* the right to vote, for the same period. Woolas was also suspended immediately from the Labour Party, and, to make matters even worse, the House of Commons authorities demanded the return of all salary and expenses paid to him since May.

The legislation under which this challenge took place does not allow for an appeal, but Woolas sought judicial review of the decision, with the support of a large number of back-bench Labour MPs, who were appalled and angry at the courts' attempt to interfere with their process. This attempt failed, and three judges of the Administrative Court in London ruled on December 3rd that the election remained void and that Woolas remained barred from elective office.

A by-election was held on January 13, 2011 and Labour retained the seat. This was the first by-election of the new Parliament, and was seen as a test of the popularity of the new coalition. Watkins stood again (Woolas was disqualified from doing so) and again he came in second. One of the key differences for him was that when he first stood, the Liberal Democrats were in opposition and now they are in government.

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Public-Private Partnership in the Russian Federation

Public-private partnerships ("PPP") have been declared a key element for economic development in the Russian Federation's Program for Social and Economic Development, which runs through the year 2020. Relevant federal agencies have provided guidance on key aspects of the program, special economic zones, investment funds and concession agreements. In addition, certain administrative regions in Russia are considering regional laws related to PPP.

Two initiatives are particularly noteworthy: (a) a state investment fund for financing infrastructure projects, and (b) the creation of special economic zones in the Russian Federation.

Investment Fund

The Investment Fund of the Russian Federation (the "Fund") was created to promote cooperation between the Russian state and private business and to facilitate the participation of the private sector in large-scale projects, both on a national and regional level. The Fund is not a separate legal entity, but rather is a part of the Russian state budget that is specially allocated for financing projects of great significance for infrastructure development. The Fund was created by the Russian Federation in 2005, and regulations governing its activities were issued in 2008 and 2010.

The Fund, which was designed to finance both national and regional projects, has financed more than 30 projects to date, including the construction of roads, railroads, factories, plants, and various projects in housing and community services. In order to qualify for the receipt of funds from the Fund, a national project's value must be a minimum of five billion rubles (approximately $163 million), and the value of a regional project must be at least five hundred million rubles (or approximately $16.3 million). The participation of private investors is required in any project in which the Fund invests. Private investors must finance at least 25 percent of national projects and 50 percent of regional projects. All projects must receive the positive endorsement of the investment advisor.

Special Economic Zones

Another PPP-related measure is the creation of special economic zones, which provide business activities conducted in those zones with certain benefits, including exemption from customs duties, VAT, and excise duties. Currently, there are four types of special economic zones:

- Special economic zones for industrial production;
- Special economic zones for technology development;
- Special economic zones for tourism and recreation; and
- Special economic zones for ports.

These zones are designated by the Russian government through a tender process and are generally created for a term of 20 years, although economic zones for ports are created for 49 years. Users of the special economic zones enter into agreements for their activities and are guaranteed to be exempt from unfavorable changes in the law within the terms of such agreements.

Further development of special economic zones is planned for 2011. Plans include:

- A special economic port zone in the Petropavlovsk-Kamchatskiy region, which is expected to become an important hub in the region, taking advantage of the Northern Sea Route as an international transit corridor.
- A new tourism and recreation special economic zone named "Hvalynskiye Kholmy" is planned in the Saratov region, which is expected to result in a significant influx of tourists.
- An industrial special economic zone known as "Titanic Valley" is expected to be created in the Sverdlovsk region. Financing in the amount of 10 billion rubles (approximately $326 million) will be provided exclusively by regional authorities and private investors.

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Localism in the UK?

Localism is a political doctrine central to the manifesto of the Conservative Party prior to the May 2010 general election. Now that the Conservatives are in power (albeit in coalition with the Liberal Democrats), we will get to see how this doctrine will filter down into practical policies and legislative changes. The Localism Bill published December 13, 2010 and due to become law before the end of 2011 gives the first solid insights into how the manifesto pledges will become reality.

Before looking in detail at the Localism Bill, it is also noteworthy that it is the first major piece of legislation to be produced by the ConLib coalition. However, many of the core concepts behind "localism" also feature in the Liberal Democrat ethos of decisions being made at the lowest possible level within government, and which they have been practicing in local government where they have had powerful roles for many years. Hence localism is not a topic that was likely to throw up rifts between the coalition partners, and hence this bill does not tell us too much about the state of the coalition, or about how it will function in the tougher tests that it is set to face in the future.

The Localism Bill is wide-ranging and covers many topics, some of which could be considered to be uneasy bedfellows. Commentators suggest that much of the bill has been made up "on the hoof" and that the final list of matters covered was determined as much by the practicalities of what could be drafted and what were considered "easy wins" as by an effort to comprehensively address ideological objectives.

The bill is broken down into eight parts as follows:

1. Local Government
2. EU Fines
3. Non-domestic Rates
4. Assets of Community Value
5. Planning
6. Housing
7. London
8. General

Parts 1-4 contain many items that will be of interest to local activists as well as much of the substance to the Conservatives' objection to "Big Government." Part 1 grants to local governmental bodies a general power of competence, the intention of which is that these bodies will be empowered (except where specifically prohibited) to do anything that a private individual may do. This is expected to result in great innovation in the delivery of public services and the running of local government; however, it may also result in legal and practical problems and much litigation in cases where public bodies get out of their depth or inadvertently cause problems which local political accountability is unable to address, such as long-term financial commitments.

Communities will be granted new powers to designate certain government property as a "community asset" and then to seek to acquire it, as well as new powers to challenge public bodies to let them take over and run certain public services. Important local

Before looking in detail at the Localism Bill, it is also noteworthy that it is the first major piece of legislation to be produced by the ConLib coalition.

issues can be made subject to a local referendum, which although non-binding must be taken into account by decision makers. These are all radical and untested concepts in the UK.

Tied in with these changes will be changes to the governance of local authorities. Potentially there could be more local committees, with the intention of getting more local councillors involved in decision taking. Twelve cities will have the opportunity to elect a mayor; currently only London has a directly elected mayor with significant powers more than a ceremonial role.

Current rules on predetermination and bias in decision-making (which apply where a councillor is directly affected by a decision, for instance because of where he or she lives, or where they have spoken out in public on a matter in advance of a decision formally being taken through due process) are to be abolished. The Standards Board for England, which previously has monitored the behaviour of councillors, is to be abolished, to be replaced by accountability at a local level only, reinforced by new criminal sanctions for wrongdoing in office. Sceptics may say that there is the potential for an explosion of cronyism and local corruption, which (apart from a few notable exceptions) has not been a significant feature of the system for many years. In addition, there are unanswered questions as to whether the populace has the appetite or skills to take on roles that have previously been left to local bureaucrats to administer and whether local councillors and staff at local councils have the capacity, acumen and enthusiasm to exercise the new powers in the way envisaged by the government. Some undoubtedly do, but others may find themselves unsuited to a role so different from that in which they have previously found themselves.

"Open Source Planning" was the Conservatives' pre-election policy booklet, explaining how the town-and-country planning system was "broken" and needed to be "rebooted." The bill is the second manifestation of the government's vision for how that reform is to take place. The first was the announcement by the planning minister that the regional tier of planning was to be abolished. This action was subject to a successful legal challenge and was followed by a further announcement, also subject to successful legal challenge.

It could be argued that both challenges succeeded on a technicality – that the regional tier of planning was introduced in primary legislation and hence needed primary legislation to remove it, and could not be removed by ministerial statement alone, as such a statement can only be one of policy and does not itself have force of law. However, it does not build confidence that the ministerial team in charge of planning has mastered the detail and legal niceties around which the current system of town-and-country planning in Britain operates.

Also, whilst removing the regional tier of planning is intended to simplify and make more locally accountable the planning decisions that affect everyday lives of citizens, a new top-level national planning statement would appear at first to be a step backwards for localism. When coupled with a new neighbourhood level of planning, decisions may not be streamlined or simplified. Further complications will come because many plans are likely to be written by local residents with NIMBY (Not In My Back Yard) inclinations and no formal planning training. Whilst it may streamline decisions that are refusals, it likely will not deliver on national planning challenges such as the delivery of new housing or waste treatment facilities – the two sectors most affected by the abolition of regional planning, since the binding regional targets for delivery of housing and waste treatment facilities were key elements of the regional plans.

Developers looking to the planning system to deliver quick and easy success for their projects could be sorely disappointed, since in many areas the forward planning system is likely to be in a state of stasis for a couple of years, as many authorities decide to deploy resources elsewhere and wait and see how the new system will develop.

On the other hand, a new "Community Right to Build" will mean that certain types of development will be allowed to proceed without planning permission at all, subject to certain safeguards such as a 50 percent vote in a local referendum.

There is also to be radical reform to the system of affordable housing in the UK, which is truly innovative and takes the sector down a completely different route than that traveled under the previous government. It is very ambitious and will

Twelve cities will have the opportunity to elect a mayor; currently only London has a directly elected mayor with significant powers more than a ceremonial role.

completely change the way that new social housing stock is delivered and existing housing stock is managed, since financial decisions and priorities are to be set at a local level.

Finally, the mayor of London will have generous new powers, taking over roles previously performed by the Homes and Communities Agency and the Development Corporations, both central government-organized quangos (quasi-non-governmental organisations), as well as new powers to form further Development Corporations, including organizations to capitalize on the legacy of London's hosting the 2012 Summer Olympic Games.

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Introduction to New Rules for Mainland Investment in Taiwan

Recently, with the increasingly closer economic and trade exchanges between Mainland China and Taiwan, more and more mainland enterprises have chosen to make direct investments in Taiwan. In June 2010, the Economic Cooperation Framework Agreement (the "ECFA") between the two sides of the Taiwan Strait was successfully executed. As a result, the PRC National Development and Reform Commission (the "NDRC"), the Ministry of Commerce (the "MOFCOM") and the Taiwan Affairs Office of the State Council (the "Taiwan Affairs Office") jointly released the Measures for Administration of Investment in Taiwan by Mainland Enterprises (the "New Measures") on November 23, 2010. The New Measures, with the purpose of further encouraging, guiding and regulating mainland investments and improving the prosperous economic relations between the two sides of the Taiwan Strait, effectively integrate previous regulations and rules, minimize their discrepancies, and enhance the governmental support of mainland investments in Taiwan.

Requirements for the Mainland Investor

Under the New Measures, the requirements for mainland investors to invest in Taiwan are:

1. Be an enterprise legally registered and operating on the mainland;
2. Have enough capital, technical, and management capabilities in the relevant industry; and
3. Promote the peaceful development of cross-strait relations and impose no threat to national security and reunification.

Examination and Approval of Mainland Investment in Taiwan

The New Measures require that all investment projects in Taiwan be examined and approved by the NDRC in accordance with the Interim Administrative Measures for the Examination and Approval of Overseas Investment Projects (2004) (the "Examination and Approval Measures").

Local enterprises will have to file applications with the NDRC's offices at the provincial level. After a preliminary examination, NDRC's local offices shall submit the proposed projects to the NDRC for approval based on a number of criteria, including the capability of the investor and the impact of the investment on national security.

State-owned enterprises directly managed by the central government ("central enterprises") are required to apply to the NDRC for their proposed projects to be examined and approved by the NDRC directly. The NDRC will consult with the Taiwan Affairs Office during the course of the examination.

For those enterprises that intend to establish a for-profit enterprise or a non-profit entity in Taiwan, approval from the MOFCOM is required pursuant to the Administrative Measures for Overseas Investment (2009) (the "Administrative Measures").

Local enterprises are required to submit to preliminary examinations at a local department of the MOFCOM before they can obtain final approval from the MOFCOM itself. Central enterprises are required to apply to the MOFCOM directly. In the course of examination, the MOFCOM will consult with the Taiwan Affairs Office. However, for those projects that have already been reviewed by the Taiwan Affairs Office through the NDRC process, the MOFCOM will make decisions directly. Upon approval, a Certificate of Overseas Investment will be issued.

Preference Policies

The New Measures explicitly indicate that mainland enterprises, which qualify for certain conditions in accordance with the ECFA (effective on Sept. 12, 2010) and its appendices, will enjoy the benefits of the preference policies under the ECFA. The primary elements of these policies include commitments to open areas for investment such as conference

In June 2010, the Economic Cooperation Framework Agreement between the two sides of the Taiwan Strait was successfully executed.

and exhibition services, special commodity design services, movie reproduction services, broker services, sports and entertainment, computerized aerial positioning systems, and banking and other financial services (except for securities, futures and insurance) in Taiwan.

Governmental Support

The New Measures also emphasize the role of the NDRC, the MOFCOM and the Taiwan Affairs Office in supporting mainland investment in Taiwan. The three regulatory bodies will provide guidance to enterprises through various channels, including overseas investment consulting service systems and investment guidelines. The New Measures also provide for enhanced training regarding Taiwan investments for mainland investors, which will be provided by government agencies and industry associations.

Overview of Relevant Regulations on the Taiwan Side

In addition to the New Measures, Taiwan has been drafting and amending related rules since 2003 in order to respond to the closer economic and trade ties between the two sides of the Taiwan Strait. Taiwan has issued regulations to specify industry categories in which mainland enterprises are permitted to invest, as well as approval procedures for setting up a subsidiary, branch or representative office in Taiwan. The competent approving authority is the Investment Examining Commission under the Department of Economic Affairs of Taiwan (the "Investment Commission").

If mainland investments fall within any industry category permitted by the Department of Economic Affairs of Taiwan, a letter of approval will be granted by the Investment Commission. The mainland investor will be permitted to proceed to the registration procedures with the Department of Commerce under the Department of Economic Affairs or the local authority governing commercial matters with the Letter of Permission. (The permitted categories are defined in the Listing of Mainland Residents' Permitted Investment in Taiwan. Please visit the website http://www.moeaic.gov.tw/ for information regarding the Listing. The Listing is in Chinese only; no English version is available.) The industries which mainland enterprises are permitted to invest in include: (i) the manufacturing industry, for example, the textile industry and the manufacturing of electronic parts; (ii) the service industry, for example, the restaurant industry, e-commerce and web portal sites; and (iii) public infrastructure projects in which investment is permitted, for example, designated civilian airport terminal projects and designated tourism and recreation facilities. With the development of cross-strait trade and the effectiveness of the ECFA, the list of categories is expected to be extended soon.

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Telecommunications, Media, and Technology

The telecommunications, media and technology sector enters 2011 with significant regulatory uncertainty surrounding key industry segments, including broadband Internet and online privacy and advertising. The Federal Communications Commission ("FCC") faces an uphill battle in 2011 on many signature regulatory initiatives of its Democratic chairman, as the new Republican-controlled U.S. House of Representatives has promised vigorous oversight of the FCC, and traditional Democratic supporters urge the FCC to stand firm for stricter oversight of the industry.

Net Neutrality

The Obama administration and FCC Chairman Genachowski have targeted "net neutrality" and what the FCC refers to as the "open Internet" as a key policy initiative. Net neutrality refers generally to a series of requirements on broadband Internet service providers (*e.g.*, cable, telephone company and wireless broadband access providers), addressing, among other matters, nondiscriminatory handling of lawful online content, applications, and services; customer transparency; and reasonable network management. In general, Internet content and application providers and their public interest group allies favor strong net neutrality rules, while broadband access providers and more ideologically conservative interests argue that federal net neutrality rules are unnecessary and unlawful.

In October 2009, the FCC initiated a rulemaking proceeding to codify six open Internet policy principles. However, an April 2010 federal appellate court decision, *Comcast v. FCC*, cast significant doubt on the FCC's jurisdiction to regulate broadband Internet services and access providers given the current regulatory classification of Internet access. Over the remainder of 2010, the FCC, Congress, industry stakeholders, and public interest groups engaged in intense debate over the merits of net neutrality and the FCC's jurisdiction to implement such rules absent legislative action.

At year end, over the vocal objection of the incoming House Republican leadership and the dissent of the FCC's two Republican members, the FCC adopted a net neutrality order that codified certain open Internet policies and sought to address the jurisdictional questions raised by the Comcast decision. The FCC distinguishes between fixed and mobile broadband providers, and grants certain concessions to mobile broadband, reasoning that mobile broadband is an earlier-stage platform than fixed broadband and has more operational restraints.

While the FCC appears to have threaded a needle and made concessions to gain the tenuous support of industry stakeholders on each side, House Republicans have indicated that they will increase Congressional scrutiny and oversight of FCC actions, and will potentially block consensus communications legislation necessary to initiatives of the FCC chairman. Republicans in House Commerce Committee leadership positions, Rep. Fred Upton (R-Mich.), Rep. Greg Walden (R-Or.), and Rep. Lee Terry (R-Neb.), pledged to rely on the little-used Congressional Review Act to fight the FCC order, and at least one Republican House Commerce Committee staffer has suggested that a joint resolution disapproving the net neutrality order would have a good chance of passing in 2011 (although it seems unlikely that the President would sign it). Moreover, in light of the likely questions surrounding the jurisdictional basis for the new order in the face of the Comcast decision, appeals of the new rules have already been filed.

Comcast-NBC Merger

On January 18, 2011, the FCC and the U.S. Department of Justice's Antitrust Division approved the acquisition by Comcast, the largest U.S. cable television company, of a controlling interest in NBC Universal ("NBCU"), valued at $30 billion. NBCU owns and operates television broadcast stations, the NBC television network, various video programming and online properties, and Universal Studios. The deal includes conditions by the FCC and Antitrust Division, which will last for seven years, designed largely to prevent potential harms of the Comcast-NBCU combination. The conditions include, notably, (1) net neutrality requirements for Comcast's broadband Internet access service provided by its set top boxes (*i.e.,* Comcast-NBCU must not prioritize its own Internet content over unaffiliated Internet content), (2) a requirement that once an online video distributor ("OVD"), such as Hulu, Netflix or Google TV, enters into a distribution agreement with a peer of Comcast-NBCU, then Comcast-NBC must share NBCU's comparable programming with that OVD under economically comparable terms, (3) Comcast must provide stand-alone (*i.e.,* unbundled) broadband access service at reasonable prices, and (4) at least half of NBC's owned and operated television stations must enter into cooperative agreements with locally focused non-profit news organizations in the same markets of such stations. While the conditions are transaction-specific, as opposed to rules of general application, the conditions could significantly shape the wider media landscape, including by fostering the continued rise of an established OVD market.

Internet Privacy

In December 2010, the Federal Trade Commission ("FTC") released a report on improving online consumer privacy, recommending the implementation of a "do-not-track" system that would allow consumers to opt out of being tracked by companies and advertisers while browsing the Internet. Websites often track consumers that visit their sites, and many Internet business models are currently based on providing targeted ads based on consumers' Internet activities.

While consumers on the national "do-not-call" registry sign up to opt out of receiving telemarketing telephone calls, the FTC's proposed "do-not-track" system would consist of a "persistent setting" on the consumer's Internet browser that signals the consumer's choices about being tracked and receiving targeted advertisements. The FTC report also recommended that websites more clearly explain to consumers how they collect and use their personal information and provide consumers with options on how much information they divulge.

The FTC intended the report as a regulatory and legislative guide, and legislation may be required to provide the FTC with explicit rulemaking authority to implement the privacy recommendations. Sen. John Kerry (D-Mass.) plans to introduce a privacy bill in 2011 that would delegate to the FTC such jurisdiction, while Rep. Ed Markey (D-Mass.) and Rep. Bobby Rush (D-Ill.) are also expected to introduce "do-not-track" legislation in 2011. Republicans, including Rep. Joe Barton (R-Tex.) and Rep. Cliff Stearns (R-Fla.), have also voiced support for Internet privacy legislation, and the topic could garner bipartisan support in 2011.

Additional FCC Initiatives

There remain a number of important FCC initiatives that are expected to get continued focus in 2011. On media issues, there has been heated debate between broadcasters and cable operators over retransmission consent negotiations, which have resulted in several disputes where broadcasters have temporarily pulled their stations from cable systems pending agreement on carriage terms. Recently, FCC staff indicated that the FCC would open a rulemaking on retransmission consent negotiations in early 2011, although there is some question as to the FCC's authority to adopt specific remedies in the area.

The FCC is also commencing a series of rulemakings implementing the 21st Century Communications and Video Accessibility Act, a new law which expands various disability access requirements to a vast range of Internet, TV and telecom services and devices. In addition, it is expected that Universal Service Fund ("USF") reform will continue to get significant focus in 2011, including efforts by the FCC to convert the USF from its telephone-centric model to one that subsidizes broadband. Here, too, last year's Comcast decision cast a shadow over the FCC's jurisdiction to implement these objectives.

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Patent Strategies: The New Normal in 2011

The patent industry, like many other things in the world today, is experiencing such extended change that it could be said to be entering a "New Normal" condition. Features of the New Normal for patents in 2011 may include the following developments.

More Funding for Innovation

As the economy continues to rise out of the worst recession in 80 years, and the stock market continues its upward trend in 2011, there will likely be more funding for innovation of all types. As a result, companies will fund more products. There will be more equity financing of technology companies. More patent applications will be filed, and more patents will be litigated.

Some Industries and Technologies will be Funded and Innovate More than Others

There will be disproportionate growth of patent activity in certain industries. Software, business method and computer-related patent applications will increase in volume. (These technologies already represent more than half of the new patent applications at the U.S. Patent Office.) Biotech applications will also grow rapidly in volume. Selected niche technologies, such as nano-technology, will also boom. Traditional, more mature technologies – such as the mechanical, chemical, electrical, and pharmaceutical arts – will have more modest growth or maintain past levels of new patent applications.

Hot industries for patent growth will include software, Internet, mobile telecom and wireless, Internet security, e-commerce, genetic engineering, energy exploration and production, solar, nano-technology, bio-pharma, and batteries, among others. Also, as the financial industry enjoys better economic results, it will return to more intense patent strategies and innovation.

More Intense Intellectual Property Due Diligence in Equity Financing

Increased interest in patent due diligence by financial institutions, investors, and buyers in M&A will increase the intensity of IP due diligence and its impact on price and terms in equity transactions. IP due diligence will start earlier in deals, be more detailed, and take more time and budget. The perceived and realized value of IP will increase as a result. Patent owners will activate patent development programs earlier to better prepare a pro-active IP story for the next equity deal. IP lawyers will be called on to better explain the IP world to the corporate bar, and to participate as transactional attorneys in equity deals. Corporate tax planning for patent strategies will be increasingly important, especially for international businesses.

IP due diligence will also increase in intensity for the purchase of large technology projects (such as computer systems), because users of technology share exposure to potential patent infringement issues.

Patent Case Law will Continue its Evolutionary Change in Select Areas

Patent case law will continue its evolutionary, not revolutionary, development this year. In 2011, we may see U.S. Supreme Court decisions on topics including: (1) the standard

Patent case law will continue its evolutionary, not revolutionary, development this year.

of proof for patent invalidity, (2) the extra-territorial effect of U.S. patents, (3) the state of mind needed for induced infringement, (4) more on the patentability of medical diagnostic methods, (5) the extent of university ownership rights in federally funded inventions, (6) the standard for indefiniteness that is necessary to invalidate a patent, and (7) the standard for inequitable conduct, among others.

We may also see Federal Circuit decisions regarding (1) the standard for inequitable conduct, (2) the patentability of DNA sequences in product and method claims, (3) prosecution laches, and (4) the patentability of diagnostic methods, among other issues.

We may also see the development of trends in the district courts in the application of recent Supreme Court cases on obviousness, and the standards for patentability for software and business methods, among other issues.

No Extensive Patent Reform Act in 2011

The probability of extensive patent reform legislation will continue to wane, and there will be less speculation that such an act might pass than there was in the period 2005—2010.

New Patent Litigation will Increase as the Economy Strengthens

The annual rate of new patent litigation dropped about 10 percent during the recession but is approaching and may exceed pre-recession highs.

More Patents in the U.S.

In 2010, the U.S. Patent Office issued about 30 percent more patents than it did in 2009. This unprecedented increase in output at the Patent Office, in just one year, comes after at least a decade of increasing backlog and delay in processing applications.

This increase in production at the Patent Office will continue, and the office will continue to reduce the backlog in applications and reduce the delay in examining patents. This will yield patents faster from the Patent Office. Faster patents tend to cost less, and be worth more. This will increase the importance of patents for business and increase the growth in new patent applications. This will stimulate the growth and finance of innovative business.

More China Patent Action in the United States

As of 2009, China has been the most active patent office in the world (in terms of new WIPO patent applications filed). The Chinese government's 10-year patent plan targets a doubling of the number of new China patents by 2015 and targets a larger effort to pursue foreign counterpart patents.

As a result, the volume of China-origin patent applications in the United States will increase dramatically. Furthermore, Chinese buyers will become increasingly active M&A players in the United States. Favored technologies and industries will include wireless telecom, Internet infrastructure, automobiles and auto parts, batteries, solar energy, wind energy, and natural resources exploration and production.

Each of these developments represents opportunities and dangers for the business and market capitalization of the patent owners and other players in the patent and IP industries. Those who embrace and exploit change will prosper.

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Employers Face Scrutiny in 2011: Systemic Litigation and Fair Labor Standards

With the Obama administration's legislative agenda on labor and employment law largely stalled, enforcement efforts under existing statutes are expected to expand and accelerate in 2011. The Equal Employment Opportunity Commission ("EEOC" or "Commission") and the U.S. Department of Labor ("Department" or "USDOL") have both announced aggressive enforcement and litigation goals for which employers should be prepared.

At the EEOC, Chairman Jacqueline Berrien has vowed to reduce the Commission's backlog in charge processing and to reinvigorate its Systemic Litigation Initiative. With increased funding and 383 new employees, including 41 attorneys, the agency is poised to do both. According to the Commission's report for fiscal year 2010, which ended on September 30, systemic litigation will be a top priority. It points to 20 such suits filed in the past fiscal year. Even more telling for the year to come, it discloses that 465 systemic investigations were in process at year-end.

Of particular import for employers is the Commission's stated intent to focus systemic litigation on "policies and procedures, employment actions, or practices in particular industries that may have a significant or adverse impact on protected groups." The emphasis on adverse impact claims can be particularly difficult for employers, because those claims do not involve discrimination in the traditional sense of intentionally treating employees differently because of a protected characteristic, such as race, sex or national origin. Rather, disparate impact claims attack facially neutral – and often well-intended and longstanding – policies because they may affect protected employees disproportionately. Among the facially-neutral policies identified by the EEOC as possible targets of disparate impact suits are the use of credit reports in hiring or other employment decisions, the use of arrest or conviction records, employment tests, subjective decision making, and exclusions based on names, zip codes or geographic areas.

The use of credit reports is a particular target of the Commission in litigation and was addressed in a recent public meeting. Although various employer representatives presented arguments in support of the use of credit checks, the position of the Commission appears clear. According to Chairwoman Berrien, the practice fails as a matter of law and policy. She cites it as unfair to individuals whose credit slipped after layoff during the economic downturn. She cites it as potentially illegal because it may impact protected groups such as African Americans, Hispanics, women and the disabled disproportionately. The chairwoman's willingness to address whether certain employment practices are fair (and not just whether they comply with the statutes she is charged to enforce), along with the suggestion that "subjective decision-making" may be a target of agency litigation, is a clear signal to the business community of the current EEOC's perception of the scope of its role.

Any doubt as to the EEOC's intent to litigate is dispelled by a note in connection with its E-RACE initiative (Eradicating Race And Colorism from Employment). In what could be interpreted as pressure to compel regional offices to file suit, the Commission states that regional offices will be reviewed to determine whether the number of cases filed is "reasonable" when compared with the number of meritorious charges processed.

Like the EEOC, the USDOL under the Obama administration has adopted an operational approach that should cause great concern for employers. The USDOL is engaging in a publicity campaign focused on alleged "wage theft" and the wrongs suffered by low-wage workers. It has abandoned its historic role of providing fact-specific guidance to employers on how to comply with the Fair Labor Standards Act ("FLSA"); it is hiring a broad range of new investigators; and it has promised an aggressive litigation-first approach to enforcement. Although it is uncertain whether the USDOL's approach will increase compliance with the FLSA, there can be no doubt that every employer will face greater scrutiny from the department and the plaintiffs' bar in an effort to identify wage violations.

Spurred on by a 2009 GAO Report that concluded that the Bush administration "left thousands of actual victims of wage theft … with nowhere to turn" and a 2009 National Employment Law Project study that indicated 68 percent of the low wage workers surveyed reported that they were denied minimum wage or overtime, Secretary of Labor Hilda Solis has repeatedly committed to address "wage theft" issues. Thus, in April 2010, USDOL launched its "We Can Help" initiative. This initiative involves a public outreach program for low wage workers, especially illegal aliens, and is aimed at encouraging employees and community groups to report "suspected" wage violations. One of the cornerstones of the initiative is a commitment that complaining employees will not suffer retaliation, which seemingly includes a

commitment that the USDOL will not take any action to report or deport illegal aliens for whom it seeks wages.

At the same time that the USDOL is encouraging complaints about non-compliance, it has dramatically reduced the avenues through which employers may obtain compliance assistance. The department historically provided detailed opinion letters in response to inquiries from employers and other interested parties that addressed difficult compliance issues based on the specific facts presented by the requesting party. Thus, an employer that wanted to comply with the law could outline an approach or issue and obtain a determination from the USDOL as to whether the approach complied with the law. Unfortunately, in March 2010, the USDOL announced that it would no longer issue such opinion letters. The department indicated that responding to compliance inquiries absorbed too many resources that could otherwise be redirected to investigations and enforcement activities.

With additional appropriations as well as the funds that the USDOL has saved by minimizing its compliance guidance, the department is in the process of hiring hundreds of new investigators. A large group of these investigators is tasked with addressing contract compliance issues under the Davis-Bacon Act, which covers public works and construction projects, and the Service Contract Act, which covers services contractors who receive federal funds. Other new investigators are focusing on the perceived misclassification of employees as independent contractors, and still others are focusing on USDOL-designated high-risk industries, such as construction, health care, transportation, janitorial, and personal services.

In light of these steps by the USDOL, it should be no surprise that Labor Solicitor M. Patricia Smith has emphasized that the department intends to achieve legal compliance through use of a big stick. In a recent speech, she argued that "a few well-placed criminal cases are the best deterrent we can have" and explained that her goal is to make USDOL enforcement "more aggressive, creative, and effective." Although it is difficult to assess the impact of such attitudes both within and outside of the Department, a review of federal court dockets suggests that there has been more than a 10 percent increase in FLSA lawsuits filed when comparing 2010 with 2009. There are now an average of 33 such matters filed every day. As new USDOL investigations move forward and as plaintiffs' counsel continue to be emboldened, those numbers are certain to increase further.

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It's Not Your Grandfather's FDA Anymore

The U.S. Food and Drug Administration ("FDA") has continued the aggressive oversight and enforcement promised by Commissioner Hamburg in August 2009. A number of significant recent developments warrant the attention of FDA-regulated industries. As the examples below attest, FDA is more willing than ever to extend its responsibilities beyond traditional products (food, drugs, medical devices, cosmetics) and regulate "new" items that some may have thought were outside of FDA's jurisdiction.

Caffeinated Alcoholic Malt Beverages

Over the last several years, a new market emerged in the United States for caffeinated alcoholic malt beverages, containing an alcoholic content in the 10 percent range and sweet and fruity flavors attractive to young adults and teenagers. Following reports of hospitalizations due to dehydration and alcohol poisoning, several states banned the sale of such beverages outright. In response to these concerns, FDA requested that the industry provide information to support the contention that caffeine added to alcoholic malt beverages was generally recognized as safe ("GRAS"). In response, one company provided FDA with a lengthy GRAS Notification that included published studies and an expert panel opinion supporting its view that caffeine was safe in alcoholic beverages at levels up to 200 parts per million.

After a year-long review, FDA sent Warning Letters to four manufacturers of caffeinated alcoholic malt beverages in November 2010. FDA concluded that the marketers' "safety" claim was unfounded and that the combination of caffeine and alcohol was an "unsafe food additive" that posed a public health concern. FDA stated that caffeine can mask some of the sensory cues individuals might normally rely on to determine their level of intoxication and lead to risky behaviors and hazardous or life-threatening situations.

Critics of FDA's position note that individuals have been mixing alcohol with caffeinated drinks for years, and that the decision to stop the sale of the premixed beverages defies common sense. FDA has held firm to its position, grounding the decision in the food additive provisions of the Federal Food, Drug, and Cosmetic Act ("FDCA"). This action follows two years of FDA's increased scrutiny of food products and labeling that is arguably unprecedented. We expect the agency to continue its focus on food products, particularly with regard to the rapidly growing "functional food" markets.

E-Cigarettes

In September 2010, FDA sent a letter to the Electronic Cigarette Association asserting that it would regulate e-cigarettes as drug products. FDA then issued Warning Letters to five e-cigarette companies for violations of the FDCA, including unsubstantiated claims and manufacturing control issues. Notably, the agency took this action despite a January 2010 injunction granted by the D.C. District Court barring FDA's regulation of e-cigarettes as drug products absent the marketer's claim of a therapeutic use. FDA chose to fight the injunction and appealed the District Court's decision in order to pursue its proposed regulation of e-cigarettes as drugs.

On December 7th, the D.C. Circuit Court of Appeals dealt a blow to FDA and upheld the lower court's injunction. The Appeals Court found, under both the precedent set 10 years ago in the *Brown & Williamson* case and the newly enacted Family Smoking Prevention and Tobacco Control Act ("Tobacco Act"), that FDA: 1) cannot regulate customarily marketed tobacco products under the FDCA's drug/device provisions; 2) can regulate tobacco products marketed for therapeutic purposes under those provisions; and 3) can regulate customarily marketed tobacco products under the Tobacco Act. The court found that the language of the Tobacco Act applies to any product "made or derived from tobacco" including the liquid nicotine used in e-cigarettes.

FDA's loss at the Circuit Court of Appeals has not dampened the agency's aggressive enforcement stance. On December 21, FDA filed a petition for a rehearing *en banc,* requesting a review of the case by the full bench of the D.C. Circuit Court of Appeals. In addition to pursuing this case, we expect that FDA will continue its efforts to exert control beyond "traditional" tobacco products and regulate – perhaps even ban – novel products that are marketed as alternatives to cigarettes and cigars.

Prosecution of In-House Counsel and Executives

A former in-house attorney for a large pharmaceutical firm pleaded not guilty to criminal charges for obstruction of justice in November 2010. The indictment

charged the attorney with lying to federal investigators during what started as a routine inquiry by FDA in 2002 of the firm's promotional materials. The government alleged that the in-house attorney intentionally failed to hand over certain documents, including slideshow presentations that discussed off-label (unapproved) uses. The indictment also alleged that the attorney denied to FDA that doctors had promoted the off-label uses, despite her knowledge to the contrary.

This indictment was a bold and unusual move, rarely seen in FDA-regulated circles. Pursuing an individual in-house lawyer is far from commonplace in off-label investigations. While it is too soon in the case to state with any certainty, there is a possibility that the government is pursuing these charges in an attempt to obtain potentially incriminating information against her former employer. This case should be watched closely by industry as it may point to an increased use of such tactics by the federal government.

Separately, in a December 2010 decision, a federal judge barred three former pharmaceutical firm executives from participating in federally funded health care programs for 12 years, upholding a decision of the U.S. Department of Health and Human Services, FDA's "parent" agency. The executives had earlier pleaded guilty to misbranding one of the firm's best-selling drugs by down-playing the addictive properties of the drug in a marketing campaign. The executives argued that the debarment was too harsh since they were convicted under the "responsible corporate officer" doctrine based on their executive leadership roles, rather than any direct or active participation in fraudulent marketing. The court disagreed, further reinforcing FDA's promise to increase its use of the "Park Doctrine," which holds that company officials can be guilty of misdemeanor crimes for violations of the FDCA where the official was in a position of authority over the violative activity, even if he or she was unaware of such prohibited activities.

Conclusion

The past year has shown time and again FDA's willingness to regulate novel products and entire industries that were previously outside of its control (such as chain restaurants and their menus, which the U.S. Congress asked FDA to regulate in March 2010). Consequently, domestic and foreign manufacturers, distributors and marketers should be watchful for statements by FDA or agency prognosticators implying that the agency wishes to put a novel item under its regulatory umbrella. If you were not FDA-regulated this year, you might be next year!

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Aviation and International Emissions Trading

In 2008, the European Commission took the major step of including aviation in the European Union Emissions Trading Scheme (EU ETS) from 2012. This unprecedented action created controversy between the EU regulator, the aviation industry and states as to the legality of the extension of the EU ETS to aviation and the best approach to regulate aviation emissions. The International Civil Aviation Organization (ICAO), the United Nations agency responsible for international civil aviation, has led key aviation industry efforts to advocate coordinated actions against climate change.

At the Sixteenth Conference of the Parties of the United Nations Framework Convention on Climate Change (COP-16) held in Cancun from November 29, 2010 to December 10, 2010, the aviation industry put forward, through ICAO, the consolidated statement of continuing ICAO policies and practices related to environmental protection – climate change. The main thrusts of the ICAO submission at Cancun were (i) to reiterate the determination of ICAO member states to continue to play a leading role in global efforts to address climate change by working through ICAO to limit or reduce greenhouse gas (GHG) emissions from international aviation and (ii) to outline ICAO Assembly Resolution A37-19 of October 2010 (A37-19). Highlights of A37-19 include:

- the setting of aspirational global goals of annual average fuel efficiency improvement of 2 percent until 2020 and a fuel efficiency improvement rate of 2 percent per annum from 2021 to 2050;
- not to attribute specific obligations to individual states, allowing the different circumstances, respective capabilities and contribution of developing and developed states to the concentration of aviation GHG emissions in the atmosphere to determine how each state may voluntarily contribute to achieving the goals;
- encouraging states to submit their action plans outlining policies, actions and annual reporting on aviation CO_2 emissions to ICAO, preferably by the end of June 2012;
- establishing a *de minimis* threshold below which states are not expected to submit action plans towards achieving the global goals, in order to accommodate states which have low aviation activity or difficulty complying with standards or recommended practices;
- developing a framework for market-based measures in international aviation in accordance with specific guiding principles;
- encouraging operators wishing to take early action to use carbon offsetting, particularly through the use of credits generated from the Clean Development Mechanism (CDM) of the Kyoto Protocol;
- accelerating the development and implementation of fuel efficient routings and procedures to reduce aviation emissions;
- developing policy actions to accelerate the appropriate development, deployment and use of sustainable alternative fuels for aviation;
- developing a global CO_2 standard for aircraft emissions by 2013; and
- undertaking a study on the possible application of the CDM to international aviation.

A Global Sectoral Approach to Aviation CO_2 Emissions

ICAO advocates a global sectoral approach to tackle aviation CO_2 emissions and considers A37-19 to have established the first globally harmonized agreement for a sector to limit CO_2 emissions. While A37-19 does establish a common basis for action to reduce aviation emissions and the development of market-based measures, it falls short of expressly supporting the EU ETS as a possible building block for a global aviation emissions trading scheme. During the ICAO Assembly which adopted A37-19, the EU stated that EU ETS legislation made it clear that if there is agreement at ICAO on global measures, the EU will consider adapting the EU ETS. The EU stressed that it was important for ICAO to develop a global framework for market-based measures that facilitated effective action. A future global framework could well develop through linking or mutual recognition of measures developed at a state or regional level.

Challenge to the EU ETS

Notwithstanding broad support in the aviation industry for a global emissions trading scheme and action to reduce GHG emissions, there has been considerable resistance from the U.S. aviation industry to the extension of the EU ETS to aviation. Indeed, in December 2009, the Air Transport Association of America and several U.S. airlines filed an application for judicial review in the English High Court against the United Kingdom Secretary of State for Energy and Climate Change in relation to the inclusion of international aviation in the EU ETS. The plaintiffs argue that the EU has no jurisdiction to regulate flights flying into and out of the EU and the unilateral application of the EU ETS to non-EU carriers is in breach of international law. In May 2010, the English High Court referred the matter to the European Court of Justice for a preliminary ruling. The key challenges are that inclusion of international aviation in the EU ETS:

- breaches Articles 1, 11, 12, 15 and 24 of the Chicago Convention (on the principal basis that ICAO, not the European Commission, is the proper authority to regulate international aviation);
- breaches Articles 3(4), 7, 11 and 15 of the Open Skies Agreement between the EU and the United States (including the granting of rights, application of laws, charges and environmental measures);
- contravenes Article 2(2) of the Kyoto Protocol (the reduction of aviation GHG emissions should be pursued through ICAO); and
- breaches customary international law (including the right of states to complete and exclusive sovereignty over their air space).

Some of the arguments against the challenges are:

- the Chicago Convention was not drafted to deal with climate change issues (it came into force in 1947);
- both the United States and the EU have long-standing histories and case law exercising extra-territorial jurisdiction (such as in antitrust matters);
- the extension of the EU ETS to aviation is not discriminatory as it applies to both EU and non-EU carriers;
- the EU ETS is not a tax, customs duty or charge;
- the EU ETS does not regulate flights originating and terminating outside the EU; and
- reducing GHG emissions is not the province of any single state but in the common interests of the international community.

A ruling by the European Court of Justice is not expected until 2012.

What This Means for the Aviation Industry

Pressure will inevitably continue to be exerted on the aviation industry to reduce GHG emissions. As a highly competitive, investment-intensive and tight-margin sector, the aviation industry will need carefully designed and implemented policies and regulations from governments at international, regional and domestic levels. The industry has strong arguments to apply principles of common but differentiated responsibility and non-discrimination to measures that reduce GHG emissions (as opposed to more risky and complicated arguments based on the breach of international law and extra-territoriality outlined above). Policy makers and regulators will need to evaluate the nature and needs of the aviation industry so as to apply realistic measures while enabling sustainable growth. It may in reality be difficult to prevent a rise in absolute emissions in the short to medium term without posing a risk to growth in the aviation industry driven by increasing global economic activity and social mobility. All actors should be reminded of the fact that sustainable development principles require a balancing of economic, social and environmental priorities, where no one priority may outweigh the other to produce a sustainable outcome.

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Looking Ahead: What the Consumer Product Safety Commission's Budget Tells us about its Direction in 2011

Government budget documents are dry—Atacama Desert dry, martini without vermouth dry. However, the Consumer Product Safety Commission's ("CPSC") 2001 Performance Budget, while perhaps not destined for any best-seller lists, contains good GPS-like guidance to the direction CPSC intends to take in 2011. While it may be diverted by unforeseen emerging hazards or a newly Republican Congress, the CPSC has at least told us where it intends to go and how it intends to get there, particularly in light of steps taken by the agency in the past year.

Regulatory Developments

In 2010, CPSC continued to implement Consumer Product Safety Improvement Act of 2008 ("CPSIA") requirements and provided crucial guidance. For example, CPSC implemented a new "recall" rule to implement the new notice provisions incorporated into the CPSIA. It also defined the critical term "children's product" that would be subject to special requirements including lead testing, tracking labels, and third-party testing by accredited laboratories. CPSC began the process of accrediting labs to test children's products. It also completed safety standards for infant bath seats and infant walkers and a revised standard for baby cribs.

CPSC also initiated rulemakings to revise safety requirements for bassinets and cradles, among others. CPSC proposed a testing and sampling rule to establish procedures and recordkeeping requirements to support product certification. CPSC also initiated the process to create rules declaring hair dryers without immersion protection devices and upper infant garments with drawstrings a "substantial product hazard." Many of these rulemaking efforts are likely to produce final rules in fiscal year 2011.

With an eye toward 2011, CPSC also requested comments on whether it is technologically feasible to lower the lead requirement for children's toys to 100 ppm on August 14, 2011. CPSC reacted to newspaper articles and consumer group concerns by conducting several recalls and requesting voluntary standards for cadmium in children's jewelry and toys. (The latter will effectively become a mandatory standard if the voluntary standard process is completed in 2011 and CPSC wishes to adopt the standard that emerges.)

Emphasis on Enforcement in 2011

While some of these rulemaking requirements will be completed in 2011, and lab accreditation efforts will likely continue, the CPSC Performance Budget for 2011 suggests that CPSC will shift some of its emphasis from implementing rules and requirements of the CPSIA to enforcing those requirements already implemented. Although the agency is not scheduled to receive additional funding for 2011, it planned to add 46 full-time equivalent employees ("FTEs"). Forty-one of these new FTEs would be devoted to the compliance and enforcement efforts of the commission including 16 FTEs for the import surveillance effort, 10 FTEs for defect identification, and 15 FTEs for regulatory enforcement. These increases put more people at the ports and at Customs and Border Protection ("CBP"), targeting and sampling imported products. These changes also reflect an increase in the number of compliance staff and technical support staff that conduct investigations and negotiate corrective measures, and an increase in the number of attorneys to support those efforts and seek penalties for violations.

In the context of a small agency such as CPSC, these are significant increases in resources. Many of these personnel have already been hired and were "on board"

With the addition of several new compliance attorneys, CPSC can be expected to pursue more, and likely harsher, civil penalties for failures to comply, to properly certify, to report and other violations.

and working in their new positions as this article was being written.

In 2011, CPSC's import operation will target and collect more samples for testing. CPSC enhanced its targeting efforts with CBP in 2010 and has already added staff at additional ports as well as some of the infrastructure to support these efforts. CPSC also plans to undertake more investigations, and CPSC will likely use inspections and investigative letters to "look behind" manufacturer's Certificates of Compliance. While CPSC's focus will be on the compliance of a firm's products, CPSC will likely be interested in what testing and record-keeping systems support certificates of compliance and will examine the credibility of those systems.

The increase in compliance staff also suggests that the agency will be conducting more investigations of possible defects and non-compliance with rules that will lead to product recalls and other corrective action. With the addition of several new compliance attorneys, CPSC can be expected to pursue more, and likely harsher, civil penalties for failures to comply, to properly certify, to report and other violations.

Congressional Oversight

While CPSC has certainly "telegraphed its punches" with respect to increasing its enforcement efforts in 2011, not everything CPSC will do in 2011 can be anticipated. Each year, some new hazard emerges, or some new concern will be advanced regarding heavy metals or chemicals, or other hazards, particularly in children's products. Predictably, CPSC will feel pressure to react quickly to such concerns. However, a Republican House of Representatives likely will seek to moderate anything it perceives as an overreaction.

The shifts in Congress present opportunities on a number of fronts. In 2011, there likely will be an attempt to revise the CPSIA to eliminate some of its more burdensome and least supportable requirements. Sentiment for eliminating some of the unintended consequences and regulatory burdens of the CPSIA has been expressed by key senators and representatives of both parties. Congress may shift the balance toward regulation based on risk and give the CPSC more room to make "common sense" decisions. It may also limit the products subject to certain requirements or find other ways to reduce the lead and phthalate requirements to make them align better with the actual risk of injury.

The Republican ascension in the House of Representatives likely means increases in oversight hearings. Merely by asking the right questions, Congress can influence CPSC activities. Ultimately, Congress can wield its budget powers as well as its ability to write legislation as a means to influencing CPSC's direction in 2011. Such activities may be policy-driven, or merely reflect efforts at deficit reduction across the government.

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The Year of Privacy Protection

Significant commercial, technological and policy developments in 2010 have all set the stage for new privacy laws and regulations to emerge in Europe and the United States in 2011. We expect the United States and the European Commission to actively consider imposing new requirements on companies to address the collection, use, protection, retention and disposal of personally identifiable information ("PII").

Commercial and Technological Developments

There is an increasing recognition by governments, businesses and individuals that existing laws protecting privacy have been outrun by the pace of technological development. Consider:

- Publicly reported data breach incidents in the United States in recent years show no meaningful reduction in the number of such incidents or the number of personal records exposed each year. In the EU, there is a growing concern that data breaches are under-reported and that this issue must be addressed for both consumer protection and public policy reasons.
- During 2010, *The Wall Street Journal* published a landmark series of investigative articles that detail the powerful new technologies and their extensive and hard-to-detect use that enable Internet business to build up extremely accurate "profiles" of individual users.
- Some Internet companies have begun deeming "public" certain previously private information requiring users to take greater affirmative actions to protect their information.
- The European Union and the United States have been involved for several years in negotiations to establish a comprehensive framework for privacy protection to address information (such as financial and airline passenger data) exchanged for law enforcement purposes.

Policy Developments in the United States

2010 brought a number of significant policy developments in the United States, including:

- Federal Trade Commission Report: In the United States, the FTC has significant federal jurisdiction over privacy protection. During 2009-2010, the FTC held a series of privacy roundtables dealing with technological developments and privacy concerns. In December 2010, these resulted in the release of a preliminary FTC report entitled "Protecting Consumer Privacy in an Era of Rapid Change" ("FTC Proposal"). The FTC Proposal sets forth a broad new framework that seeks to significantly expand the current legal regime for privacy protection in the United States.
- Department of Commerce Report: A major Internet privacy report was issued by the U.S. Department of Commerce's Internet Policy Task Force on December 16, 2010. The report is a "Green Paper" entitled "Commercial Data Privacy and Innovation in the Internet Economy: A Dynamic Policy Framework."
- White House Group: The White House recently created a Privacy and Internet Policy Subcommittee of the National Science and Technology Council. More than a dozen federal departments, agencies and offices are represented. The purpose of the subcommittee is to develop principles and strategic directions with the goal of fostering consensus in legislative, regulatory and international Internet policy realms.
- Congressional Interest: The new Chairman (and ranking Democrats) of the House Commerce and Judiciary Committee and key subcommittees all have demonstrated interest in privacy legislation. Indeed, the new Republican chairman and ranking Democratic member of the key House Subcommittee are known for being aggressive on privacy matters. They join their Senate counterparts who held hearings and began developing legislation this year.
- Massachusetts Law: In the absence of national legislation, the states continue to adopt new laws dealing with privacy protection and information security. Perhaps the most notable development is the comprehensive data protection regulations adopted by Massachusetts that took effect in March 2010. These regulations purport to apply to the personal data of residents of Massachusetts wherever they may be located and wherever it may be gathered. While several states have security obligations, Massachusetts' regulations are the most comprehensive and include broad and detailed personal information protection and computer system security obligations for all businesses.

Developments in Europe

Europe also had a number of significant developments regarding privacy protection in 2010, including:

- Data Protection Directive Update: On November 4, 2010, the European Commission issued a Communication concerning "A comprehensive approach to personal data protection in the European Union" ("Communication"). The

Communication, which like both the FTC Proposal and the Green Paper was preceded by careful public consultation, is intended to set the strategy for revision of the EU's Data Protection Directive, which would raise the collective bar for privacy protection in Europe.

- European Parliament Resolution on New Advertising Practices: On December 15, 2010, the European Parliament approved a strong and comprehensive resolution asking the EU Commission to carry out an in-depth study of "new advertising practices," including behavioral advertising.
- Council of Europe Recommendation on Profiling: Regarding individual profiling, the Committee of Ministers of the Council of Europe added a powerful European voice in the direction of opt-in controls on profiling. It adopted a recommendation to all member states that profiling be permitted, subject to certain exception, only if "the data subject or her or his legal representative has given her or his free, specific and informed consent."
- Data Breaches: The annual report of the UK Information Commissioner's Office ("ICO") for the 2009-2010 reporting year states that during that period 464 security breaches were reported, and that the ICO entered into 57 remedial "undertakings" with entities that had breached their privacy protection obligations.
- EU Enforcement Actions: On November 22, 2010, UK ICO imposed a fine of £100,000 on a local council for sending sensitive personal information by fax to the wrong recipients, twice in two weeks. On the same day, it imposed a fine of £60,000 on a private employment services company that kept an unencrypted database of sensitive personal information on a lap-top that was stolen. On November 23, 2010, the Data Protection Authority of the German federal state of Hamburg imposed a fine of €200,000 against a financial institution for profiling its customers and for permitting its customer service representatives to have improper access to the sensitive data of the institution's customers.

Common Themes

Though there are significant differences, the developments in Europe and the United States have common themes, which are illustrated by comparing the FTC Proposal and the EU Communication. Both of these proposals deal with nearly all the same essential topics and both do so in the same general policy direction. Examples include:

- Promoting greater transparency in the sense of shorter and standardized privacy information and providing them in more accessible ways;
- Introducing stricter prior consent mechanisms;
- Considering the use of "privacy by design" concepts;
- Addressing profiling by various technological and legal means;
- Imposing clearer and shorter data retention requirements (including a "right to be forgotten");
- Providing stronger remedies and sanctions for violations of privacy; and
- Requiring privacy impact assessments.

Need for Involvement

As the U.S. federal government and the EU develop legislative and regulatory proposals, companies should engage to shape these proposals so that they do not impinge upon domestic or international business operations or impose unnecessary burdens, while still enabling individuals to trust in their businesses. The significant integration of the U.S. and EU economies, the presence of multiple corporate offices in each others' jurisdictions, and significant personal data flows between the two economies also underscore the need to seek convergence in the legal regimes for privacy protection.

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A Smaller SEC Enforcement Program?

The most important factor impacting the SEC's Enforcement Division over the next year will be what Congress ultimately chooses to do about the SEC's budget and when. The SEC is presently burdened with extensive new Dodd-Frank duties while government-wide budget differences in Congress are holding the SEC to pre-Dodd-Frank funding levels. As a result, new programs and offices created by Dodd-Frank are not moving forward, and core SEC programs are being trimmed back. The impact will be particularly acute on the Enforcement Division, the SEC's largest unit, which reportedly is already cutting its travel, testimony-taking and expert witness expenditures.

In the debate over Dodd-Frank, Congress acknowledged that the SEC's funding has failed to keep pace as the industry it regulated grew in size and complexity, and that particularly with new responsibilities imposed on it by Dodd-Frank, the SEC would need a significant budget increase. The original proposal was to put the SEC on the same budget footing as the federal banking agencies, which are allowed – subject to congressional oversight – to set their own budgets but then must raise their own funding through user fees. For over a decade, the SEC has similarly funded itself but, even though it thus spends no taxpayer dollars, it has had to go through the annual congressional appropriations process each year to have its budget formally set. The compromise ultimately reached in Dodd-Frank was to leave the SEC in the appropriations process for now, but to promise annual budget increases that would roughly double the SEC's budget in increments over five years.

Only months later, Congress has failed to appropriate the first of the promised SEC budget increases. It may be that the SEC will not get any increase at all in the present fiscal year and have to remain at pre-Dodd-Frank funding levels. If this happens, we expect the promised increase in the SEC's size and activity level to be postponed for a year or more, and the Enforcement Division's presence will necessarily shrink at least in the near term.

More Ponzi, Fewer Financial Reporting Cases

The SEC has been spending much more time on Ponzi cases and much less time on labor-intensive financial reporting cases. With the strained SEC budgets in recent years, and with the SEC currently frozen at pre-Dodd-Frank levels, this is perhaps understandable. This shift in case mix also reflects the abundance of Ponzi cases floating to the surface in these tough times, as well as agency attention to such cases following the Madoff matter.

In the SEC's annual case statistics, the "Securities Offering Cases" category, which includes Ponzi cases, grew in fiscal 2010 to 21percent of the enforcement program from only 10 percent three years earlier. Over the same period, its "Issuer Reporting and Disclosure Cases" category fell in fiscal 2010 to 18 percent from a high of 33 percent three years earlier. Significantly, the Reporting and Disclosure category also includes FCPA cases, which have been trending upward, which means that the percentage of traditional reporting and disclosure cases, which are not separately broken out, is probably a good deal lower than 18 percent. The only other notable change over this three-year period was that the SEC's "Investment Advisers" case category rose in fiscal 2010 to 15 percent from 11 percent three years earlier.

Ascendancy of the New Specialized Units

Much of the energy and direction in the SEC enforcement program over the coming year will likely come from the five "specialized units" the Enforcement Division has created to focus on what it has defined as key enforcement priorities: (i) the Asset Management Unit, which will focus on investigations involving investment advisers, investment companies, hedge funds and private equity funds; (ii) the Market Abuse Unit, which will focus on large-scale market abuses and complex manipulation schemes; (iii) the Structured and New Products Unit, which will focus on complex financial instruments; (iv) the Foreign Corrupt Practices Unit, which will focus on FCPA enforcement; and (v) the Municipal Securities and Public Pensions Unit, which will focus on various aspects of the municipal securities market.

By last August, each of these five new units was fully staffed, and by year-end the units were actively producing cases. Modelled along Justice Department lines, the units represent a new way of doing business for the SEC. Each unit will operate nationwide as a network of specialists based both at SEC headquarters and at regional offices around the country, with the goal of breaking down geographic silos and encouraging free exchange of information and ideas across programs. Particular cases will be staffed with unit personnel from different offices in what the SEC terms "horizontal" staffing. The units have promised to stress rigorous and continuous training – both general and case specific – from in-house and outside experts as a means to develop sophisticated teams of technical specialists with a law enforcement focus.

Expanded '40 Act Enforcement

After years of leaving '40 Act concerns to regulatory lawyers, the Enforcement Division's new Asset Management Unit is already starting to bring a substantial number of cases against advisers and other fund-related persons. For mutual funds, the unit has said it will focus on: (i) adequate disclosures relating to strategies, performance, valuation and risk; (ii) boards' discharge of their responsibilities, particularly as to valuation and fees; (iii) director independence issues; and (iv) personal trading, including redemptions before material disclosures. For hedge funds, the unit will focus on: (i) investigation of aberrational performance indicators; (ii) valuation processes and use of side pockets; (iii) registration of advisers; (iv) conflicts, including relationships among funds under common management and among affiliated entities; (v) compliance programs and internal controls; and (vi) attention to private offering requirements.

Millionaire Whistleblowers

Dodd-Frank requires the SEC to set up an aggressive whistleblower program that will promise a 10 percent to 30 percent bounty from recovered funds to those giving the SEC the information it needs to prosecute. The SEC has published proposed rules to implement this program and is presently evaluating a large volume of comments from a wide range of sources. The principal choice that the SEC will have to make in adopting final rules will likely be how far to go in requiring prospective whistleblowers to first report to internal corporate programs before going to the SEC with their information. Over the long term, the SEC's whistleblower program may be one of the most significant changes to its enforcement program flowing from Dodd-Frank.

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Supreme Court

The current Supreme Court term promises a number of decisions of interest to the business community. The court has yet to issue most of this term's opinions, and so we preview here the cases that raise the most significant issues.

In perhaps the most notable addition to its docket, the Supreme Court will review a decision certifying the largest plaintiff class in history: 1.5 million women alleging gender bias by Wal-Mart in pay and promotions. *(Wal-Mart v. Dukes,* No. 10-244). The decision is noteworthy not only because both the class and the potential monetary liability are large, but because the appeals court allowed the class action to proceed under the federal rule governing class actions seeking injunctive relief, even though the plaintiffs are also seeking billions of dollars in monetary relief. The Ninth Circuit rejected the "incidental damages" test that other courts have adopted to prevent such a result. Under that test, an injunctive class action that also seeks damages can be certified only if the monetary relief would be automatic, or computable by objective standards without additional hearings, if liability for injunctive relief were found.

If the Supreme Court agrees with the Ninth Circuit, the decision could dramatically increase the exposure of businesses in the United States to large class actions based on a broad variety of legal claims, under a legal rule with fewer procedural protections than are provided by the rule that generally applies to large class actions seeking money damages. Argument is scheduled for March 29, 2011, with a decision likely in June 2011.

As we noted in our last report, the interplay between arbitration and class-action litigation has been an important recent issue on the court's docket. In November, the court heard argument as to whether the Federal Arbitration Act ("FAA") preempts a state law rule that conditions the enforceability of arbitration provisions on the availability of certain procedural mechanisms such as class-wide arbitration. *(AT&T Mobility, LLC v. Concepcion,* No. 09-893). The Ninth Circuit held that California law as to "unconscionability" prohibited a wireless provider from relying on a provision in its service agreement that disputes must be resolved in individual arbitrations. At oral argument, the justices struggled with weighing the right of states to determine which contracts are "unconscionable" against the strong federal endorsement of arbitration manifested in the FAA. Thus, while the court last year protected companies from class-wide arbitrations imposed on them without their consent, the ability of companies to protect themselves contractually from judicial class actions is in doubt.

The court also agreed in December to decide whether states and private parties can bring litigation seeking judicially created caps on greenhouse gas emissions. *(American Electric Power Co. v. Connecticut,* No. 10-174). The court will consider whether such parties have legal standing to seek emissions caps on utilities in an effort to address global warming, and whether such an action can be implied under federal common

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law and is the proper province of the courts. The court will review a ruling by the Second Circuit that allowed eight states, a city and three nonprofit land trusts to seek to hold utilities liable for creating a "public nuisance" in the form of climate change. Similar suits are pending against automobile manufacturers, chemical producers and oil-and-gas producers. A decision in favor of the plaintiffs could be of particular significance in encouraging plaintiffs to seek judicial regulation in areas that the more conservative new Congress, or an EPA cautious about regulating absent express statutory authority, may choose not to regulate. The argument will likely be set for the April session, and the decision would then issue towards the end of June.

The court heard two cases in January determining whether U.S. state courts have jurisdiction over non-U.S. companies that simply place products in the "stream of commerce" if it is reasonably foreseeable that they will wind up in the state, for example, by selling them to an appointed exclusive distributor that resells them in the state. (*J. McIntyre Machinery v. Nicastro,* No. 09-1343; *Goodyear Luxembourg Tires, S.A. v. Brown,* No. 10-76). The Supreme Court has never squarely decided whether the "stream of commerce" theory can support personal jurisdiction, though a prior decision suggests that the plaintiff must identify additional conduct showing that the defendant purposefully directed its activities at the forum state. Non-U.S. companies have a significant interest in this question because product-liability suits can be much more expensive in the United States than overseas.

Finally, while it is widely expected that constitutional challenges to the 2010 federal health care legislation will ultimately make their way to the Supreme Court, that will likely be in the October 2011 – June 2012 term. The court will likely want the challenges to percolate through the courts of appeals rather than to step in to hear them sooner, and appellate decisions on the issue will not begin to issue until late spring or summer.

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2011: The Year Ahead—Anticorruption Law

Law enforcement efforts against corruption in international business transactions gained enormous momentum in 2010. U.S. authorities continued to bring unprecedented numbers of cases and collect ever-higher fines and penalties for violations of the Foreign Corrupt Practices Act ("FCPA"), while the United Kingdom undertook a wholesale revision of its antibribery laws to make them even more rigorous than the FCPA. For 2011, the risks of running afoul of these laws, and the consequences of doing so, have never been greater.

United States

U.S. authorities have designated FCPA violations as a top law enforcement priority – one that they often mention in the same breath with the fight against international terrorism.

More cases, bigger penalties. Viewed strictly by the numbers, FCPA enforcement continued to increase exponentially, as it has over at least the past five years. Both the Department of Justice ("DOJ") and the Securities and Exchange Commission ("SEC") have increased the resources devoted to pursuing FCPA violations, and public reports indicate that there are at least 140 open investigations against companies and individuals. These agencies brought a total of 74 actions in 2010 – up from an average of 37 per year in 2007 – 2009, and approximately 11 per year in 2004 – 2006. By way of comparison, U.S. authorities had brought only 19 enforcement actions from the enactment of the statute in 1977 to 2004.

The cases brought in 2010 increasingly stressed the criminal prosecution of individuals, with the prospect of individual fines and significant prison time, and the imposition of ever-greater fines on companies. By way of example, in 2010 U.S. authorities levied eight of the 10 largest FCPA penalties ever paid, ranging from $56 million to $400 million; one company was dissolved by court order as a "criminal purpose organization," and one individual received an 87-month prison sentence – the longest prison sentence ever imposed in an FCPA case.

If anything, however, these numbers understate the lengths to which U.S. authorities will go to pursue these matters.

Aggressive enforcement tactics. U.S. authorities are now employing the kinds of investigative methods previously reserved primarily for narcotics and organized crime cases. Nearly one-third of the FCPA actions brought in 2010 resulted from a single sting operation, in which FBI agents posed as representatives of a foreign defense minister. It should be expected that the authorities will also use video and audio surveillance, wiretaps, paid undercover informants, undercover agents, and grants of immunity, to build FCPA cases.

Expansive jurisdiction and creative legal theories. U.S. authorities have not shied away from pursuing cases at the very edges of their jurisdictional reach. The FCPA provides for the prosecution of corrupt payments to foreign officials on the basis of U.S. citizenship or a relatively minimal connection to the United States. In a number of recent cases, however, the U.S. nexus appears to have been particularly slim (if not non-existent).

U.S. authorities have been keen to make an example of those it believes to have made improper payments, even where there appears to be little or no basis for FCPA jurisdiction (or insufficient evidence to satisfy all of the FCPA's elements), by stretching the limits of statutory jurisdiction or asserting charges of other violations of law. For example, after British authorities initially declined to bring bribery charges against British aerospace manufacturer BAE plc, U.S. authorities reached a $400 million criminal settlement with the company. In light of what appeared to be a lack of basis for FCPA jurisdiction (or perhaps an inability to prove an FCPA case), the U.S. charged the company with making false statements to various U.S. agencies about its anticorruption compliance program and with failing to disclose to those agencies certain commissions paid on foreign arms sales, and in conspiracy to defraud the U.S. government. Indeed, though the apparent motivation for the charges was a belief that bribe payments had been made (and the plea agreement reads like a bribery scheme), authorities did not charge any FCPA violation.

Bounty payments for whistleblowers. U.S. authorities also anticipate receiving a significant increase in information about potential FCPA violations as a result of the Dodd-Frank whistleblower provisions, which create substantial monetary incentives for individuals to report potential wrongdoing under a variety of laws, including the FCPA. Those who provide independent information leading to a successful enforcement action in which the government obtains monetary penalties of $1 million or more will be paid a "bounty" ranging from 10 to 30 percent of the total amount.

There is widespread concern that this program will undercut the effectiveness of anticorruption compliance efforts, as potential violations may be reported to the authorities in the first instance, rather than to company officials seeking to identify and address such activity. Whether or not this is the case, it seems certain that the SEC and the DOJ will have an abundance of tips, and that companies will have even more at stake in seeking to prevent FCPA violations in the first place.

United Kingdom

The UK's new Bribery Act (the "Act"), which is scheduled to take effect in April 2011, provides for civil and criminal penalties even greater than those that may be imposed by U.S. authorities under the FCPA. Several components of the Act are particularly significant.

- **Broad jurisdiction.** The Act provides for new and very expansive jurisdiction over companies doing business in the UK, which can be prosecuted for bribery undertaken on their behalf without regard to where it occurs. It is not precisely clear what will constitute "doing business" for this purpose, but the threshold is sure to be low.
- **Strict corporate liability.** Companies subject to the Act will be strictly liable for bribes given or offered on their behalf, by any person, acting anywhere in the world, and without regard to whether anyone in the company had knowledge of the bribe. This means that it will be easier for UK authorities to prove a violation of the Act than for U.S. authorities to establish an FCPA violation.
- **Adequate procedures defense.** Unlike the FCPA, the Act provides a complete defense to strict corporate liability where a company can establish that it had "adequate procedures" to prevent corrupt payments from occurring. This creates a compelling reason for companies to ensure that they have effective compliance mechanisms to prevent improper payments.
- **Commercial bribery.** The Act covers not only improper payments to foreign government officials, but private commercial bribery as well.

UK authorities can be expected to make use of their new powers under the Act, as they brought significantly more anticorruption cases in 2009 and 2010 than in prior years. That said, there are major uncertainties, such as the following, about what this will mean in 2011 and coming years:

- **Jurisdiction over non-UK companies.** How aggressively will the UK authorities interpret their authority to pursue allegations of corrupt payments by companies with a minimal business presence in the UK, where the payments have no other connection to the UK?
- **Facilitating payments.** Will UK authorities bring charges against companies making facilitating payments? Unlike the FCPA, the Bribery Act makes no exception for such payments.
- **Gifts and entertainment.** Will UK authorities provide clarity on permissible business gifts and entertainment, given that the Act appears to prohibit them entirely? Thus far, the authorities have advised companies to trust in proper prosecutorial discretion.
- **Enforcement resources.** Given its massive budgetary crisis, which has already led to social unrest, will the UK government devote significant resources to the pursuit of foreign bribery cases, particularly those at outer reaches of the Act's authority?

Other OECD Countries

International efforts against corruption date from the 1997 Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, which was entered into by the member states of the Organization for Economic Cooperation and Development ("OECD"). While all 38 member states had, by 2002, adopted laws similar to the U.S. FCPA, the enforcement of those laws varies greatly from country to country.

The United States was the driving force behind the OECD Anti-Bribery Convention, with a primary objective being to "level the playing field" abroad for U.S. companies subject to the FCPA. That goal remains a distant one, notwithstanding the efforts of the United States and the UK. A 2010 report by Transparency International indicated that only five other OECD members were actively enforcing those laws – Denmark, Germany, Italy, Norway, and Switzerland. The report noted that there was little or no enforcement activity by 20 of the 38 OECD member states, and only moderate levels in the remaining ones.

Whether in fact the playing field will ever be leveled will depend on whether these and other nations have the political will to prosecute matters involving international corruption. That seems, at best, unlikely at a time when the solvency of many national governments appears to be at risk.

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Government Litigation in 2011: Notable Developments Concerning the State Secrets Doctrine and the Alien Tort Statute

2011 is likely to usher in litigation developments in two areas of particular interest to multinational corporations.

- With respect to government contracts, a case pending before the U.S. Supreme Court focuses on whether the government may seek default terminations of government contracts while at the same time limiting the defense of such claims by invoking the state secrets doctrine.
- With respect to commercial operations outside the United States, a recent decision from the United States Court of Appeals for the Second Circuit has clarified the extent to which U.S. district courts have jurisdiction over tort claims by foreign individuals directed towards the actions of corporations outside the United States.

The "State Secrets Doctrine" as Both Sword and Shield

In the 1980s, the U.S. Navy sought proposals for the development of a stealth aircraft called the A-12 Avenger. Successful bidders General Dynamics and McDonnell Douglas ("Contractors") had assumed that they would have access to stealth technology information already developed in other programs for the U.S. Air Force, but this information was not forthcoming, and the Contractors subsequently determined that they could not meet the proposed specifications and time line for development of the A-12. Ultimately, the U.S. Navy sought a default termination, claiming that the Contractors had failed to prosecute the contract and make adequate progress. As part of the default termination, the government demanded payment of over a billion dollars, plus interest.

The Contractors filed suit in the Court of Federal Claims to vacate the initial default determination. A key defense of the Contractors was that the government had caused the delays that ultimately resulted in the termination by breaching its duty to share "superior knowledge" regarding stealth technology that was unknown to the Contractors. The superior knowledge doctrine is a rule of contract fairness that prevents the government from knowingly allowing contractors to pursue a harmful course of action where the government has special knowledge, not shared with the Contractors, which is vital to contract performance. Indeed, prior cases have established that, where the government has this special knowledge, it has an affirmative duty to disclose that knowledge to the contractors.

The Contractors attempted to proceed with discovery on this issue, but the government invoked the state secrets doctrine to prohibit such discovery, arguing that inquiry into the alleged superior knowledge would necessarily implicate state secrets. Following a series of appeals to the Federal Circuit and related remands, the trial court ultimately upheld the Navy's default termination,

while at the same time rejecting the Contractors' defense of superior knowledge, concluding that disclosure of such information would have implicated the state secrets doctrine. By this point, the government default termination had grown into a multi-billion dollar claim against the Contractors.

The Supreme Court granted certiorari as to whether the government may prosecute a claim against a party while at the same time invoking the state secrets doctrine to preclude that party from raising affirmative defenses to that claim. *See General Dynamics Corp. v. United States (No. 09-1298),* consolidated with *The Boeing Company v. United States (No. 09-1302).* Although the context of the dispute involves contracts with the military, the case has broad due process implications for any party contracting with the government. Should the government prevail, there will be more uncertainty and risk in government contracts, especially for research and development contracts. Should the Contractors in the case succeed, the Supreme Court would likely articulate a broad due process standard under which the government, which traditionally contracts from a position of strength, will be limited in exploiting that position in the contracting process. The outcome of this case should be closely monitored by anyone who contracts with the United States.

Corporate Liability under the Alien Tort Statute

Corporations engaged in international business should also be aware of a recent decision by the United States Court of Appeals for the Second Circuit with respect to the Alien Tort Statute ("ATS"). Enacted in 1789, and apparently unlike any other jurisdictional statute in the world, the ATS provides in relevant part that U.S. district courts shall have original jurisdiction "over any civil action by an alien for a tort only, committed in violation of the law of nations or a treaty of the United States." 28 U.S.C. § 1350. The statute was dormant until the 1980s, when the courts began to recognize that the ATS provides jurisdiction over tort actions brought by aliens for violations of the law of nations, such as tort actions for "war crimes." However, through the mid-1990s, plaintiffs brought suit under the ATS only against foreign individuals, and the question of whether the ATS could be extended to corporations was unclear. In a recent decision, the Second Circuit addressed the unresolved question of whether the jurisdiction granted by the ATS extends to civil actions brought against corporations under the law of nations. *Kiobel, et al. v. Royal Dutch Petroleum Co., et al., 621 F.3d 111 (2d Cir. 2010).*

The *Kiobel* case involves claims by Nigerian nationals against Dutch, British, and Nigerian corporations engaged in oil exploration. Plaintiffs claimed that the defendant corporations aided and abetted the Nigerian government in committing violations of the laws of nations. The Second Circuit determined that corporate liability for violations of international law is not the "norm of customary international law." As a result, corporations may not be held liable under the ATS. Although the decision did not preclude ATS suits against individuals, including officers or directors, or otherwise limit corporate liability under other laws, the clear holding in Kiobel is that the ATS does not establish subject matter jurisdiction over ATS claims against corporations.

The Second Circuit reached this outcome by examining the "customary" international law, which consists of only those norms that are specific, universal and obligatory in the relations of states. In particular, the court noted that while customary international law imposes individual liability for a limited number of international crimes (including war crimes, crimes against humanity such as genocide, and torture), customary international law has "steadfastly rejected" the notion of corporate liability for international crimes, and no international tribunal has ever held a corporation liable for a violation of the law of nations. While the decision currently precludes jurisdiction over corporations due to the state of customary international law, this area of the law will require continued vigilance. In addition to potential developments in other circuit courts in the United States, should customary international law begin to develop theories regarding corporate liability for torts, the underlying premise of the decision may come under attack.

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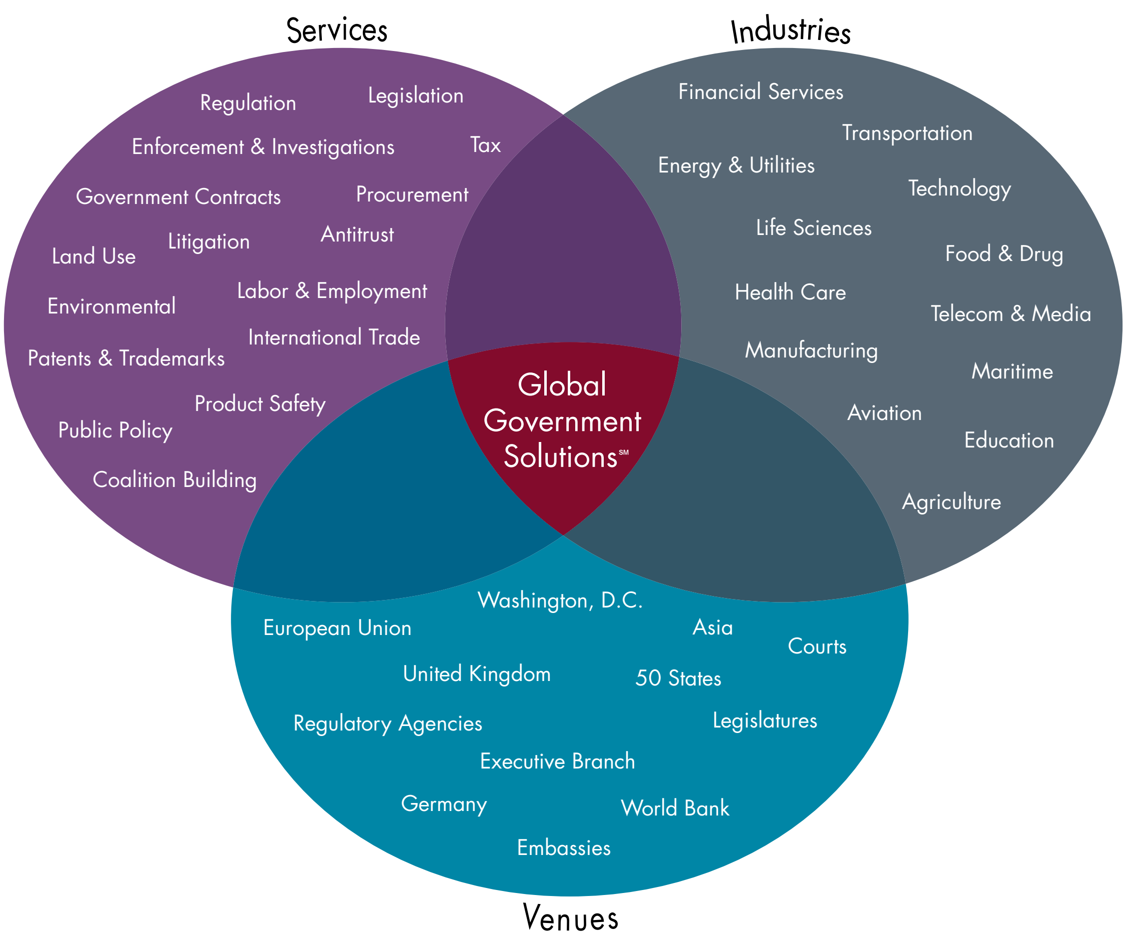

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