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Why the EU needs a common consolidated corporate tax base

Recalibrating EU-China relations

MENA Supplement

Driving global expansion

Nelson Raposo Bernardo, Global Managing Partner, Raposo Bernardo, on services delivery globalization

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Big bang needed

Another quarter, another crisis. Muddling through isn't working. Europe's leaders have announced that there may be sovereign defaults in the eurozone after 2013. Buyer's are wary of peripheral eurozone debt, thus raising the cost of the further rescue operations which are on the horizon. The cost of muddling through is increasing by the day.

It is not enough for the eurozone nations to bail out each economy as it falls into a crisis — they must address the root causes of the continent's problems. The only way out seems to be a big bang; to deal with all the problem cases in one go. The argument against a restructuring has always been that this would lead to contagion. But contagion is already a fact, and it focuses on countries with real problems. Greece has suffered. Ireland has suffered. Portugal looks next, then possibly Spain and Belgium. Under normal circumstances a bail out would not be needed. But these are not normal circumstances, and it is not possible to deal with each country in sequence as the markets then target the next one. Only a big bang can resolve the impasse.

The question is whether the eurozone will survive. This is a political more than an economic issue. It is possible for a currency union to survive sovereign defaults. The question is whether members believe the arrangement remains beneficial. Is the cost of a debt crisis worth leaving the eurozone? If a debt crisis has occurred the cost would be less. If competitiveness and growth is not restored, is the union a bad deal?

The eurozone is manoeuvring itself into a position where it confronts the choice between two alternatives considered "unimaginable": fiscal union or break-up. If Europe doesn't move quickly, within two or three years it will probably be very difficult, if not impossible, to engineer fiscal union. By then domestic politics are likely to be too unstable for the European political elite simply to arrange union over the heads of the population.

The full diplomatic might of the European Union, the ECB et al will be deployed quickly to hold the whole thing together, and we will be told that Europe was put to the ultimate test and proved itself.

Was this really the ultimate test? If history is a guide, this crisis will re-emerge in different places every few months until it is truly resolved, and increasingly the crisis will manifest itself in the political realm.

It is possible to draw a map of outcomes: growth will slow sharply and there will be several short-term liquidity panics, during which time the political consensus will be become increasingly fractured, and increasingly fractious. In some countries the political system might radicalize, and anger will increase. This will go on until finally we have the grand resolutions of the crises.

A simple way out would be for the euro area to underpin its members' guarantees with a measure of fiscal support conditional on domestic reform and retrenchment. This would be the deepening of the union which was anticipated by its proposers. There is not sufficient political support for that at the moment, particularly in Germany.

Any solution aimed at preserving the euro, or an orderly debt restructuring that protects the European banking system, must take place while the current political elite, left or right, is still in control. The longer we wait the less likely a coordinated solution.

Finally, it is with sadness that we inform you of the death of Stanley Crossick, a regular and popular contributor to World Commerce Review. On behalf of all our staff and readers we offer his family our deepest condolences. ■

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Please see the article: "Agile, Adaptable Global Supply Chains Need to Incorporate International Trade Compliance" by Aaron Gothelf, International Trade Counsel, Tyco International Ltd., and Kathleen Murphy, Partner, Drinker Biddle, in this issue of World Commerce Review.

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Why the EU needs a common consolidated corporate tax base

Algirdas Šemeta is the EU Commissioner for Taxation, Customs Union, Audit and Anti-Fraud

It is not often that an initiative in the field of EU taxation policy receives the resounding support of almost 80% of the business community[1], before a proposal is even tabled. Yet this is what we find with the idea of a Common Consolidated Corporate Tax Base (CCCTB), and with good reason. The CCCTB is a great opportunity which we need to grasp. Common EU rules for establishing the tax base of companies wishing to operate cross-border would eliminate large costs and complexities for European enterprises and make the EU a more attractive market for foreign investors. In doing so, it would contribute to economic growth and sustainable development within the EU, which is needed today more than ever.

The single market is the cornerstone of EU integration and the basis for a strong economy. Over the years, we have seen barrier after barrier broken down to build up a single market which brings great benefits to businesses and citizens throughout Europe. However, when it comes to corporate taxation, the barriers are still very strong. Fragmentation remains the rule and companies still face 27 different systems for calculating their tax base when they operate cross-border within the EU.

> **"The establishment of a CCCTB in the EU is undoubtedly an ambitious project, and certainly not without its challenges. But it is a project that I take on with great pride and enthusiasm"**

This means high compliance costs, heavy administration and complex re-adjustments for enterprises operating in more than one member state. It also means a high level of uncertainty. National rules on company taxation evolve and change over time, in a way that companies in that country manage to adapt to. However, when faced with twenty seven systems evolving at different paces and in different directions, companies are being forced to adapt and re-align themselves to new rules on an almost constant basis. This continual change in national tax rules can also lead to overlap in their application, resulting in double taxation. High costs, high complexity and high levels of uncertainty are not the ingredients for a healthy business environment. As the EU works towards economic recovery and growth, we need to do everything possible to facilitate business and encourage economic activity. The CCCTB is clearly going to be a crucial step in this process.

So what exactly would a Common Consolidated Corporate Tax Base offer? The CCCTB would allow companies or groups of companies active in more than one EU member state to file a consolidated tax return with the tax authorities of their 'principal' member state for the whole of their activity in the EU. It would include the consolidation of profits and losses at EU level in order to fully take into account the cross-border activities of the business.

This single consolidated tax return would establish the tax base which will then be allocated to all the concerned member states according to an apportionment formula. The formula will take into account three factors of equal importance: assets, payroll and turnover. After apportionment, member states will be allowed to tax the tax base allocated to them at their own corporate tax rate. This "one stop shop" approach would make things far simpler for businesses.

It would put an end to discussions on transfer pricing within the internal market, as well as to questions on cross-border imputation of losses. It would also bring about major simplifications as regards cross-border commercial activities and company or group restructurings. The automatic offset of losses within a group would mean no more double taxation. In short, we would have a system that is easier, cheaper and more convenient for businesses wishing to operate in more than one member state. Not only would this benefit companies already in the EU, but it would also make the EU a much more appealing market for foreign investment.

A key priority for me in this exercise is to ensure that the CCCTB is accessible to every size of company, not only to multi-nationals. Currently, small and medium size enterprises (SMEs) are deterred from expanding their activity to a neighbouring member state because of the burdens they would face in terms of tax compliance. These companies do not usually have large legal services and tax advisors to assist them in understanding and adapting to the different member states' systems, and often the challenge is just too overwhelming for them to take on. Small and medium size enterprises make up 99% of European business and are the key to a dynamic economy. We neglect them at our peril.

Under the CCCTB, SMEs could choose to work within one single EU framework if they wish to expand beyond their own member state, with far less cost and administrative burden than they face at present. This would give them greater potential and incentive to tap into whole new customer bases within the EU and to finally enjoy the full benefits of the internal market. Since the CCCTB would be an optional scheme, purely domestic businesses with no intention of expanding cross-border would remain free to ignore it if they choose.

The establishment of a CCCTB in the EU is undoubtedly an ambitious project, and certainly not without its challenges. But it is a project that I take on with great pride and enthusiasm. It is much awaited by the business community and much needed in order to strengthen the Internal Market. In fact, I believe that it has the potential to be a real milestone in EU fiscal policy and that, in years to come, businesses will look back and wonder how we ever managed without it. I look forward to putting my proposals for a CCCTB forward in the spring of 2011. ■

[1] *Harmonized corporate tax base – are European businesses for or against it? Pan-EU survey results investigating reactions to proposed Common Consolidated Corporate Tax Base – Jeff Wagland - KPMG 09/2007*

NINE COUNTRIES. TWO CONTINENTS.

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Health IT shows the way forward

Nicole Denjoy is Secretary General of COCIR[1]

That the health of citizens in OECD countries is improving is not in question. How sustainable the health care systems are however is more of an issue. The OECD works on 'health system priorities when money is tight' strikes a chord with COCIR, the trade association representing the electromedical, radiological and healthcare IT industry in Europe, as it highlights some of the challenges our health care systems face. Because European prosperity is dependent on the health of its citizens, there is a strong case for policymakers to stimulate investment in healthcare as a means of achieving long-term public health, social and economic objectives.

Evidence is growing that Europe's current healthcare systems will become unsustainable if unchanged over the next 15 years. The pressures we see today are set to rise as a result of ageing populations, evolving people lifestyles and the changing patterns of disease. Chronic diseases, such as cancer, are the biggest obstacle to the sustainability of many public healthcare systems. Not only are our health care systems ill-equipped to deal with this shift in demographics and diseases, they are also faced with increased public scrutiny and demand for more and better quality services.

If we continue with today's treatment-based healthcare model, the predictions of an unprecedented escalation in costs and demand are formidable. All healthcare stakeholders must act now together to develop new health strategies which can drive health care efficiencies, improve the quality of care and address the patient safety issues. We believe that innovation will be a fundamental requirement to address the many challenges our health care systems are facing. Encouraging innovation will also be key for making real progress towards more efficient health care systems. The BIAC Task Force on Health Care Policy, which I chair, actively supported the OECD Innovation Strategy, which was submitted to the OECD Ministerial Council Meeting in May and encourages further cross-cutting OECD work on fostering an innovation-friendly environment to address global challenges, including in the area of health.

> **"... citizens and patients will demand more and more IT and policymakers must be in a position to respond to this need"**

Innovation is needed in a wide range of areas, including in the provision of health services, funding schemes, solutions and devices, as well as in the organisation and management of medical facilities. Information technology can play an important role in improving patient safety through the reduction of medical errors and in empowering the patient by giving them the ability to receive medical care remotely and stay in their homes for longer. It can make patient records more easily accessible to professionals with the right credentials as well as resulting in improved efficiency, for example by avoiding the duplication of examinations and in better use of healthcare professionals considering the shortage in some speciality disciplines.

On the basis that clinical care needs to be disease and patient specific, we need to build an IT infrastructure in every European country for patient records, clinical decision support and disease management programmes. Such systems, when in place, must have the capability of exchanging data with each other, at the very least at country level. eHealth applications and infrastructures have been developed and tested throughout Europe for at least a decade, although this has been done in isolation leading to creating today's interoperability challenges. In some countries, notably the Nordic countries and the UK, applications such as Picture Archiving and Communication systems (PACS), e-prescribing, electronic patient record systems and IT-supported screening and disease management programmes are already up and running and achieving good results. OECD in its report *"Improving health sector efficiency: the role of information and communication technologies (ICT)"*, recognized the incontestable benefits derived from Picture Archiving and Communication Systems (PACS) leading to increased capacity, more effective healthcare, and more satisfied consumers. However while the potential benefits of eHealth are enormous, a number of barriers continue to hinder the introduction of Health IT and eHealth solutions, or prevent them from achieving optimal benefits. These barriers amongst which lack of political vision, too fragmented governance and un-sustained investment, must be addressed to encourage a more rapid translation of innovation into patient benefits and health care efficiency.

In some quarters, there may be concern about the cost of IT in the health sector as IT is seen as a rather intangible investment which can make it difficult to understand in the corridors of power. It is true that proper investment is required from the start and that in these tight economic times it can be hard to make the case. But we are convinced that investment in health IT saves money. Good governance and internationally-recognised standards such as DICOM are key to the success of projects. Users must accept IT as a tool rather than an obstacle. It takes time to promote change and build trust.

The Ten COCIR Recommendations for successful implementation of healthcare IT[2] highlight the need to:

1. Define a vision
2. Overcome governance fragmentation
3. Develop innovative economic model
4. Build trust
5. Support citizen-patient empowerment
6. Foster standards and interoperability
7. Achieve legal certainty
8. Enable market development
9. Strengthen international position
10. Stimulate innovation

At the end of the day, citizens and patients will demand more and more IT and policymakers must be in a position to respond to this need. ■

[1] COCIR is the European Coordination Committee of the Radiological, Electromedical and Healthcare IT Industry. See http://cocir.org
Nicole Denjoy also chairs the BIAC Task Force on Health Care Policy. BIAC is the Business and Industry Advisory Committee to the OECD. Visit www.biac.org
[2] http://cocir.org/uploads/documents/-24-cocir_pp_ehealth_rel_short.pdf

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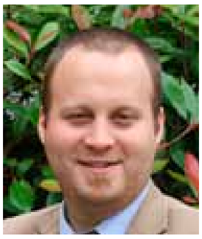
Recalibrating EU-China relations



Carsten Dannöhl is a Senior Advisor, International Relations, at BUSINESSEUROPE

In its very recent communication *"Trade, Growth and World Affairs"*, the European Commission pointed to the strategic dimension of the EU-China relationship and called to make it a priority. A few weeks ahead of this major document, the European Council on 16 September 2010 also rightly debated the EU's strategic partnerships with its main economic partners. We applaud these efforts to develop a more strategic approach to the EU's foreign relations. The EU needs to create a European economic diplomacy that is responsive to the needs of EU companies. Given its economic strength and growing global responsibilities, China is a strategic partner of paramount importance.

A part of the current strong ties are linked to China's strong export performance which stands out as one of the principal features of today's international trade landscape. As a result, from 2000 to 2006, China's share in total world exports more than doubled, from 5.2 to 11.1%. With the aftermath of the global economic crisis, enhancing business between China and the EU will be one important path to accelerate global recovery. China is already the EU's 2nd largest trading partner after the US, and Europe's fastest growing export market. However, there is still a lot of room for improvement. For example, with € 97.6 billion compared with €78.4 billion, the EU in 2008 still exported more goods to Switzerland than to China.

> **"The EU and China should join forces and move the Doha Round towards a successful conclusion"**

With €5.3 billion of EU inward investment 2009, the engagement of European companies in China is high. However, European companies are still confronted with a large number of investment barriers, such as mandatory joint venture rules. Moreover, in 2009 China inward investment to EU was low with only €0.3 billion. In order to enhance bilateral investment, the EU should open negotiations on a bilateral investment agreement. An ambitious agreement would provide legal certainty from both sides seeking to promote cooperation on trade and investment.

These facts and figures on trade and investment show that the scope for increases is great. EU-China trade and investment clearly is below of its potential!

A recalibration of the strong existing links is overly more important as in recent times business leaders have been increasingly concerned about the deteriorating business climate for foreign companies in China. Policy initiatives like the national indigenous innovation policy, compulsory certification and licenses, state directed technology transfer, and discriminatory procurement policies restrict the ability of European companies to conduct their business on fair terms. Even where the national provisions are changed to become less discriminatory, regional implementation is unclear at best and sometimes even more discriminatory than the original national provisions.

Open up domestic procurement markets

A number of recent concerns relate to public procurement where foreign companies have the impression that there business opportunities are shrinking. On a global scale, European companies are highly competitive in procurement markets, for example in sectors like public transport, medical devices or green technologies. The Chinese procurement market is among the largest in the world, and European companies are eager to market their products in this constantly growing area. But in order to achieve this, European companies need the right framework conditions in China.

One important step would be China's rapid accession to the multilateral WTO Government Procurement Agreement (GPA). This has been expected to happen since 2001 when China committed in its WTO accession agreement to become a member of the GPA. The recent revised Chinese offer, published last July, is an improvement over the first one. However, it falls short in comparison to the commitments made by other GPA members. European companies cannot accept the threshold for open tenders which would remain about 50% higher than other GPA members, and the very restricted coverage. Sub-central government entities, state-owned enterprises and crucial parts of the construction sector would not be covered. In addition to this are the very long transition periods.

A very serious concern remains the announced Chinese *"National Indigenous Innovation Policy"* (NIIP) as it does not give European companies the possibility to operate on equal terms with their Chinese competitors. This policy could effectively exclude European companies from Chinese government procurement markets. It is positive that the issues raised by foreign companies related to the NIIP have been recognized by the Chinese Ministry of Science and Technology, and that they are attempting to find an acceptable solution. This being said, China has yet to provide clear guarantees that European and other non-Chinese companies will not be excluded from the market, whether centrally or at provincial level. The new draft regulation, released by the Chinese government on 10 April 2010, is showing clear improvement compared to the previous version and could give foreign invested companies in China a real chance to take part in the process. However, the core issue, namely how to build up a sustainable innovation capacity via open and fair competition and without restricting market access, remains untouched.

Ensure effective IPR protection and apply international standards

Counterfeiting and piracy is a global problem and it is therefore important that China and the EU cooperate bilaterally and multilaterally. We are encouraged that China is reviewing some key legislation in this field but the real issue here is the enforcement of the rules. As the Chinese economy moves up the value chain towards an innovation-oriented economy, China's own interest in protecting IPR becomes clearer. This is evident in the growing number of IP disputes between Chinese companies themselves. Therefore both the EU and China should join forces in support of strict enforcement of intellectual property rights in line with international standards.

Linked to this question are Chinese mandatory certification schemes such as the China Compulsory Certification (CCC). These are a very challenging and harmful practice, which affect a broad range of industries. Apart from its very complex application, Chinese Compulsory Certification forces companies to provide highly confidential business information to non-commercially independent certification bodies when they seek certification. Insufficient protection of these business secrets would be highly damaging and could even end up in the withdrawal of business activities from the market.

In the field of information security products and wind power equipment, existing regulations and their implementation are explicitly discriminatory against foreign invested companies. European companies therefore call for the application of international common standards and norms in order to facilitate business and to reduce costs. Unjustified country-only standards and related mandatory certification schemes seriously hamper business development, to the detriment of both China and the EU.

Respect global commitments and responsibilities

In today's globalised world, leading economies like the EU and China have to set the example by respecting the rules and pushing forward multilateral trade negotiations. Moreover, they should join forces in order to move the Doha Round towards a successful conclusion. We are encouraged that China also subscribes to the fact that an ambitious outcome must provide real new market access for all WTO members, but expect more concrete and deeper Chinese commitments towards achieving this goal. An ambitious result would also have to include specific sectoral agreements.

Joint WTO leadership obviously also includes removing rules when they are not WTO compatible. On raw materials, BUSINESSEUROPE is alarmed by China's decision in July 2010 to reduce export quotas for rare earths while seemingly maintaining availability for locally owned consumers of rare earths in China. This unexpected situation has created a number of negative impacts for the EU industry, such as strong price increases and delivery shortages. Rare earths are essential for a multitude of industries and very often cannot be substituted. They are key to the emergence of green technology, such as the new generation of wind-powered turbines or compact fluorescent light bulbs. European business therefore counts on leadership from both the EU and China to strive towards a market-driven policy on access to raw materials, guaranteeing a level playing field.

The International Energy Agency predicts that 97% of the Greenhouse Gas emissions increase between now and 2030 will come from non-OECD countries. Consequently, emerging economies have to be committed partners in establishing binding policies with equally strong emissions reduction targets. Cooperation with China on climate change will be central to achieving an ambitious global agreement to cut emissions. China is the world's 3rd biggest economy and leading exporter, and the world's second largest greenhouse gas emitter. It should take account of its major contribution to global emissions at present and in future, and commit to significant emissions reductions targets at global level.

In addition, the EU and China should intensify efforts to cooperate on clean and energy efficient technologies. Transparent and non-discriminatory rules for trade, the protection of intellectual property, investments and procurement in this field would go a long way toward fostering more private sector cooperation on technology. In addition, China and the EU have a common interest in having transparent and non-discriminatory rules to promote the use of clean development and other offset mechanisms to reduce emissions in the most cost-effective manner.

Finally, European, Chinese and US authorities should engage into a more intense dialogue on macro-economic imbalances in order to avoid a repeat of the financial crisis that has thrown the world economy into disarray. It is our strong belief that a precondition for a return to global growth and financial stability is to ensure that macroeconomic and exchange rate policies are sustainable and conducive to maintaining open markets.

Strengthen EU-China links

BUSINESSEUROPE is very interested in working towards a further deepening of the existing economic and trade partnership with China. We count hereby on the EU-China High-Level Economic Dialogue (HED) which is the right tool to advance the bilateral relationship as well as to tackle the numerous barriers to trade and investment. A strong economic dialogue that removes trade and investment impediments is central to EU and China. European business should be closely involved in this exercise in order to focus on the most pressing business concerns. We look forward to the next meeting, scheduled to take place end of December, to deliver concrete results on a number of important trade impediments. Without the stability that an open and reliable investment and market access framework brings, it will else be difficult to significantly enhance business between the EU and China. ■

Agile, adaptable global supply chains need to incorporate international trade compliance

Aaron Gothelf, International Trade Counsel at Tyco International Ltd, and Kathleen Murphy, Partner, Drinker Biddle & Reath LLP

Introduction

Well-intended articles on supply chain management routinely discuss ways in which companies with global procurement strategies can build agile, adaptable and resilient supply chains that can withstand disruptions with minimal economic impact. It should come as no surprise to anyone, then, that when two international trade attorneys are asked for their opinion on the subject, they would write an article discussing how regulatory compliance is a key factor in an efficient supply chain and why a compliance program for managing risk and ensuring compliant customs and export controls transactions should be at the top of every supply chain manager's "to-do" list. While we do believe that most companies genuinely want to comply and do the right thing, we are not naïve enough to believe that the necessary resources are always available to place trade compliance at the top of all global traders' priority lists.

We offer the following to entice you to read further: the American Association of Port Authorities reported that in 2008 there were approximately 435.7 million TEUs that moved through the top 125 ports around the world[1]; the Bureau of Economic Analysis reported imports of $456.9 billion and exports of $305.7 billion in the first quarter of 2010.[2] As lawyers, we know that any time there is a slow down or a delay in the supply chain, our clients lose time and money. From our perspective, most compliance-related delays are triggered by an information exchange of some sort between a link in the supply chain and a government agency. This article provides a summary of what upper management can do to help build compliance into the supply chain and to plan for effective management when government agencies make inquiry or show up unexpectedly with a subpoena or search warrant.

We hope after considering this article readers will be aware of how compliance gaps or deficiencies can cause supply chain disruption and will feel compelled to move the action item "establish a trade compliance program" from the "nice to have" list to the "must have" list.

Overview of regulatory compliance regimes

A. Where are information exchanges taking place?

The regulatory underpinning of international trade compliance typically is imposed by a variety of agencies or other governing bodies that issue the rules and requirements by which we conduct cross-border trade. While these agencies may or may not directly interface with international supply chains, their rules and requirements will be loosely organized under two over-arching and diverse regulatory structures.

1. Customs regimes

While not obvious to most importers, a nation's customs service is generally the agency most often involved in the import process. For those new to the world of importing, customs regimes typically are responsible for determining whether goods are admissible in the first instance, assessing and collecting duties on imported goods, examining containers and goods for contraband (narcotics or other prohibited imports) and enforcing a myriad of diverse laws and requirements that fall under the purview of numerous other regulatory bodies.[3] In many countries, the customs regime is housed in the government department responsible for taxation or for homeland security.

In terms of information exchanges, the import process in most countries requires that accurate information be transmitted to the customs regime by the importer or the importer's agent. Often, customs uses computer systems (sometimes sophisticated; sometimes not) to analyze the data it receives at the time of importation to make various determinations, including whether more information is required or whether physical inspection of the goods is warranted. Sending accurate and complete information to the relevant customs authorities, therefore, leads to fewer physical examinations and general inquiries. The computer systems used by customs sometimes disagree or make random decisions to conduct further scrutiny, however. It's like a customs slot machine - every customs declaration is like a coin inserted, and sooner or later the right combination will come up, and the goods will require physical inspection and/or the importer will be questioned or audited. In addition to transmitting accurate data, global traders need a strong compliance program so that they are well prepared to respond when, through the luck of the draw, their goods must be physically inspected or they must submit more information to the responsible regulator.

"Companies need an adaptable, agile supply chain that can manage interruptions by government agencies checking for compliance"

As noted, customs authorities often are housed in the same department or agency as the tax and revenue authorities. In some cases, the export controls authorities are also housed in the same place. While not universally the case, these different authorities often will share their findings on a particular company. As a result, a tax audit can lead to a customs audit or to an export controls investigation, and vice-versa.

Companies with international supply chains consisting of related or affiliated parties also may find their global approach to transfer pricing in the countries in which they transact business at odds under the separate and disparate laws of the tax and customs authorities. To optimize taxable income within national boundaries, tax authorities favour a low entered value for goods entering their country; however, to generate high import tariffs and fees, customs agencies favour a high entered value on the same goods. The so-called "whipsaw" effect of the competing national or regional tax and customs interests can cause internal strife within an organization, pitting tax and trade compliance personnel against one another.

To avoid being caught off guard and subject to harsh penalties and enforcement actions, global traders not only need a strong network of internal controls for all areas subject to government scrutiny, but also they need to establish across their international operations open channels of communication among the different functional areas of the company that impact cross-border movements so as to remain vigilant of the possibility of one government inquiry spawning others. In other words, companies need an adaptable, agile supply chain that can manage interruptions by government agencies checking for compliance.

2. Export control regimes

Every import was someone else's export. And in several countries, there are strong export control regimes in place to monitor and control export activity. By control, we mean that the regime implements regulations designed to prevent military-type items and items that may have both a military and civilian use (ie, so-called "dual-use" items) from being delivered to individuals, companies or countries that are considered to be bad actors by the exporter's home country. Often, a country's export controls regime will have multiple agencies involved in different aspects. For example, in the United Kingdom, both HM Revenue and Customs and the Department for Business, Innovation and Skills have shared responsibilities for implementing export controls. In the United States, the Department of Commerce, Department of State and US Customs and Border Protection play various roles in regulating exports.

In terms of information exchanges, before they can ship their goods, exporters will often be required to submit license applications to the various regulating agencies for pre-approval. One major area of difference between customs rules and export controls, however, is in the treatment of intangibles. By international agreement, namely the General Agreement on Tariffs and Trade (GATT) and the World Trade Organization (WTO), many countries do not consider intangible electronic transmissions to be transactions (or imports) that need to be declared to the customs regime. By contrast, however, as a matter of national sovereignty, many countries have stringent controls in place for outbound transfers of technology and technical data that can be used to create the specific items sought to be controlled. The information itself often is controlled for export.

That point bears repeating. ***Information itself can be controlled for export***, whether it is sent via an electronic mail message as an attachment, downloaded from a web site, shown during an inspection or tour, or communicated orally by an engineer talking to a person in another country. Without a rigorous export compliance program in place that includes appropriate human and systems safeguards, global traders often find themselves subject to harsh penalties and fines, to public censure, and to loss of export privileges, or even criminal penalties and jail time.

B. What happens when a government authority is less than satisfied with information exchanges?

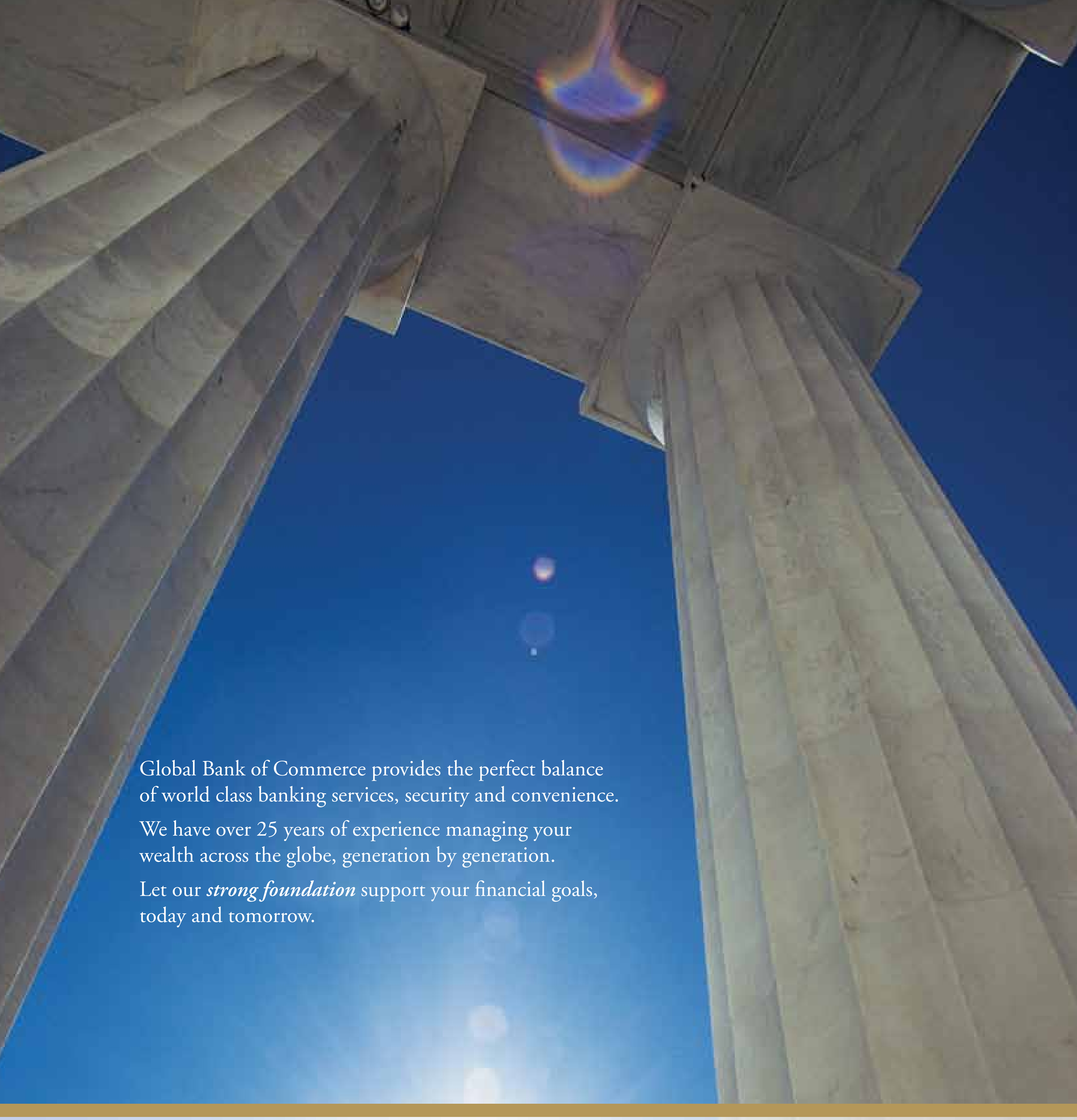
At the risk of stating the obvious, interaction between a company and government authorities often can be a slow and arduous process. Government agencies that regulate cross-border trade interact with so many different entities in the supply chain and are responsible for a multitude of diverse product lines. Further, these agencies must frequently apply vague or contradictory legal requirements, thereby impeding their ability to facilitate border crossings. At the same time, global traders often weigh down this process by not knowing or bothering to understand the myriad rules and requirements that govern the movement of goods across national boundaries.

Companies may need to make several attempts to communicate to customs and other authorities the exact information needed for these agencies to reach a decision or render a determination on whether goods can enter or leave a country without the need for further dialog. To minimize the frequency and scope of such needless or protracted delays, full and accurate information must be submitted to the relevant government regulators at the earliest opportunity. Government agencies often are dealing with so many different variables, however, that additional scrutiny or inquiry surrounding an actual or attempted cross-border movement ultimately may be inevitable. And while most customs authorities will fervently deny that they are motivated by economic considerations, many of their decisions can and do contribute to the financial well-being of their sovereignty (eg, tariff collections and anti-dumping assessments). For the global trader, the unfortunate counter-balance effect is decreasing or disappearing margins or profit levels.

On the export side, incorrect or inaccurate information often can lead to export license delays or outright denials, either of which can lead to very unhappy customers, as well as other entities comprising the supply chain.

International trade compliance programs

The informed and risk-averse global trader has a formal code of conduct policy that clearly states that the company and its various affiliates will obey the laws of the jurisdictions in which they do



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business. We believe that even their smaller counterparts engaged in global procurement would not disagree with the importance of staying on the right side of the law. An initial benefit of having an adequate trade compliance program is the ability to operate in those countries or regions that are strategic to an organization's business plan.

A. Why have one?

1. License to operate

Companies that are heavily dependent on their ability to continue importing or exporting to sell their goods or services must have as part of their overall compliance initiative an international trade compliance program (an ITCP). This function within an organization having a global supply chain is similar in nature to those programs that manage tax information and reporting, environmental health and safety programs, and anti-bribery (Foreign Corrupt Practices Act) programs.

While not nearly as well known or perhaps as engaging as other company initiatives, an ITCP can help keep a company's supply chain running smoothly when importing and exporting is involved. An ITCP also has other benefits that can help return money to the company, including the ability to take advantage of duty-savings programs such as free trade agreements, free or foreign trade zones and duty-drawback (refund) programs.

Numerous countries also have established supply chain security programs, which are typically administered by their respective customs authorities. These programs offer special benefits to their members, such as reduced cargo inspections, expedited clearance and fewer compliance audits and related inquiries. Membership in these programs requires an ITCP. As numerous global traders will confirm, each of these programs can have a heavy compliance cost and significant penalties for making mistakes. Companies should not undertake any special program unless they can meet the rigors of the program.

2. Free trade does not mean easy trade.

Most countries that not only encourage but also promote cross-border trade offer global traders special duty elimination or reduction if they can satisfy the rigors of their programs. These programs are typically designed to promote trade (and the relationship) between two countries, to strengthen an economic or culturally diverse region or to fortify large trading blocs. To ensure that "outsiders" do not unintentionally benefit from these arrangements, state and national legislatures, as well as regulators, will impose qualifications that must be met to take advantage of program benefits. Looking across the extensive free-trade models that are most common today, these qualifications may consist of the need to satisfy a particular rule of origin, a tariff-shift requirement (non-originating materials must undergo a change in tariff classification), a local content (certain percentage of direct cost of processing must be attributed to qualifying country), or a combination of any one or more of these tests.

As these program requirements almost universally have legal underpinnings, they fall by default into an ITCP. While the compliance responsibility associated with free trade agreements can be heavy from a resource and operations standpoint (many of these programs have special documentary, certification and audit requirements), annual monetary savings can add substantially to a company's bottom line. The flip side is that failure to heed the compliance responsibility can cost a company millions in penalties and fines, bring about diminished standing in the eyes of local regulators, and tarnish the company brand through negative publicity.

B. What are the elements of an effective ITCP?

Taking its cues from the serious ethical and financial reporting lapses that occurred in the United States close to a decade ago, US trade regulators identified various characteristics that have become iconic of an effective ITCP. They are:

- Control environment — this element pertains largely to the organizational structure, policies and procedures, and assignment of responsibility for trade compliance. Organizations that have high focus on strategic collaboration across the company and on risk management generally locate responsibility for trade compliance under supply chain. Many organizations ensure executive awareness of the function by assigning ultimate responsibility for compliance at the Senior Vice President or Chief Compliance Officer level, with direct or in-direct oversight to the law department. Such programs also have a network of policies and procedures that are compliance driven and clearly espoused by upper management.

- Risk assessment — this covers tools and approaches used by the organization to identify, analyze and manage risk. The "rules of the road" for trade compliance often are subject to the whims of the national and global market place, and organizations must constantly assess how compliance considerations will impact the overall supply chain. The trade compliance function should, at minimum, have a solid understanding of the compliance regimes that may inhibit or impede the free movement of goods across national boundaries and, at the same time, add capabilities that will support the organization's strategic projects.

- Control procedures — formal policies and procedures are the centrepiece of a compliance program and are meant to ensure management's directives are carried out. These internal controls can take many forms and should spread across the organization. At minimum, however, they should be documented and made readily available to all company stakeholders who play a role in ensuring that import and export transactions are compliant (procurement, engineering, tax, finance, receiving, accounting, etc.). In addition, they may involve systems investments that allow an ITCP to "see around the corner" and to automate basic compliance activities and documentation.

- Information and communication — an ITCP should create a network of compliance stakeholders and ensure, either formally through organizational structures or informally through meetings or on the company intranet, that they are informed on customs requirements, cargo security, social compliance and responsibility, etc. By building proactive compliance requirements into each functional step in the supply chain, the organization will avoid or mitigate risk.

- Monitoring — an ITCP should have a process for assessing internal controls over a period of time. As noted above, trade compliance rests on an ever-shifting foundation. To ensure that the organization remains informed and proactive, an ITCP should align global compliance solutions with supply chain and financial IT systems. Further, an ITCP should periodically test import and export transactions and develop performance metrics that, in turn, flag when enhancements are needed.

Conclusion

A global trader's supply chain is only as strong as its weakest link. If sourcing strategies, as well as operational processes and procedures, are not backed up by a strong ITCP, the supply chain can become kinked (and possibly crippled) by compliance-related risks. For this reason, senior company personnel responsible for seeking and exploiting open trade lanes to further their company's business strategies would be well-advised to ensure that the risk management principles of an effective trade compliance program are not only in place, but also being followed. By doing so, they ensure (to the extent it is within their control) that the business enterprise has open and continuous access to its supply chain. ■

1. http://www.aapa-ports.org/Industry/content.cfm?ItemNumber=900

2. (FN1 See http://www.bea.gov/newsreleases/international/transactions/transnewsrelease.htm)

3. For example, in the United States, US Customs and Border Protection, which is within the US Department of Homeland Security, is responsible for enforcing the regulations and requirements of over 40 other agencies involved in international trade. These include, for example, the Departments of Agriculture, Commerce, Energy, and Transportation; the Consumer Product Safety Commission; the Environmental Protection Agency; the Federal Communications Commission; the Federal Trade Commission; the Food and Drug Administration; and the Nuclear Regulatory Commission.

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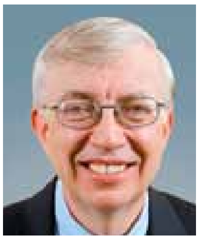
ICC Incoterms® 2010: how are companies learning the ropes?



Bill Armbruster is a freelance journalist specializing in international trade and shipping. He is the former editor of *Shipping Digest*

The rules of international trade have changed – and even some of the old rules no longer apply the way they used to. Tom Dirmyer, export-import manager for Emerald Performance Materials, found that out when he attended a recent seminar on Incoterms® 2010, the latest update to rules first introduced by the International Chamber of Commerce (ICC) in the 1930s.

The seminar was led by Frank Reynolds, the US representative on the ICC committee that revised the rules, and organized by ICC's American affiliate, the United States Council for International Business (USCIB), as part of a nationwide series aimed at getting users up to speed on the changes and how companies are using them.

"Frank threw a wet blanket over some of our practices," Dirmyer said, by casting doubt on the use of CFR (Cost and Freight) and CIF (Cost, Insurance and Freight) for container shipments.

Reynolds explained that those terms apply only to port-to-port transport and do not cover multimodal transport, such as vessel and truck or train. *"We have to take a long hard look at that because we use those two terms frequently,"* according to Dirmyer.

CFR and CIF are two Incoterms® rules held over from the previous version, Incoterms® 2000. ICC simplified the rules by dropping four arcane terms and replacing them with two new ones that are more appropriate for 21st-century commerce. That reduced the total number of Incoterms® rules from 13 to 11.

> **"Incoterms® 2010 will make things simpler for the trade community because there are fewer rules for companies to learn and to distinguish from each other"**

The Incoterms® rules are critical because they clarify the responsibilities, costs, and the risks of buyers and sellers in the delivery of goods. Under the Incoterms® rules, "delivery" is the point at which the seller hands over responsibility for the goods to the buyer. It does not necessarily refer to the arrival of the goods at a specific physical destination.

Failure to understand the Incoterms® rules can be costly. For example, if you are the buyer and incorrectly assume that the seller is responsible for insurance, you could be stuck with a big loss if the goods are damaged or lost at sea. If you had settled on a more favourable term in your negotiations with your trading partner, you could have averted a major loss. The same goes if there's a misunderstanding about transportation costs or the payment of import duties. You could be stuck with a big bill.

Now applicable to domestic commerce

Besides reducing the number of Incoterms® rules, the new version clearly distinguishes between those that are applicable only to maritime transport and those that can be used for all transport modes, including multimodal. The new rules also take into account changes in cargo security rules and the increased use of electronic commerce. But perhaps the biggest benefit for US companies is that the new rules are far more applicable to domestic commerce.

Despite the changes, the fundamental considerations remain the same.

"Companies still have to decide what works for their business," said Stanley Pfrang, export development manager for the Wisconsin Department of Commerce, who attended a seminar Reynolds conducted in Brookfield, Wisconsin. *"Do they need more control in the transaction? How much can they accept? Are particular terms needed to meet or beat the competition? How comfortable are they doing business with a particular customer?"*

Pfrang, who works one-on-one with Wisconsin exporters, said, *"We always discuss the Incoterms® rules as a way to help structure the deal and make sure that costs and risks are recognized."*

The new Incoterms® rules were announced on September 16 and take effect on January 1, 2011. Companies may continue to use the old rules afterwards, and Reynolds suggested companies should do that until both they and their partners fully understand their responsibilities under the new rules.

For many companies, the biggest decision is which of two new terms they should adopt in place of Delivered Duty Unpaid. DDU was very popular but could be confusing because it did not apply to goods that were resold domestically after the original buyer paid the import duties.

The new terms are DAT (Delivered at Terminal) and DAP (Delivered at Place). Both may be used for any mode or modes of transport, with the signal difference being that DAT provides for delivery of the goods unloaded by the seller, whereas DAP provides for delivery of the goods ready for unloading by the buyer.

According to Kathy Bushart, a compliance specialist with Eastman Kodak Co, the new terms are a lot clearer. *"DAP removes ambiguity,"* she said.

Kodak will most likely use DAP, she said, although some countries may require use of DAT or CPT (Carriage Paid to) for imported goods. For inbound and domestic trade, Kodak will most likely continue to use FCA (Free Carrier) for air, ground and ocean shipments that are less than a full container, and FOB (Free on Board) for full ocean containers, so it can control the transportation chain, Bushart said.

In cases where it used DDU, Emerald will probably replace it with CIP, but with additional conditions regarding transportation to destination and which party will be responsible for charges on the receiving end, according to Dirmyer. *"Every time we use a new term or a different interpretation of an existing term it will be a learning experience for the person at the other end,"* he noted.

Fewer rules for companies to learn

Beata Spuhler, a trade compliance attorney with the law firm Drinker Biddle & Reath LLP, said the Incoterms® 2010 rules will make things simpler for the trade community because there are fewer rules for companies to learn and to distinguish from each other.

Spuhler suggested that this is a good time for companies to revise all of their contracts and purchase orders. That will ensure that they use the terms that *"truly reflect what the parties expect from the transaction, including when the risk of loss will pass from the seller to the buyer, who handles carriage and exactly from what point to what point,"* said Spuhler, who attended a seminar Reynolds gave in Chicago.

USCIB and Reynolds spearheaded the drive for revising the Incoterms® 2000 rules for several reasons. The first was that the deletion of the old shipment and delivery terms from the Uniform Commercial Code in 2004 made the Incoterms® rules an attractive replacement. Secondly, the old Incoterms® rules did not include a duty-neutral term for domestic sales of pre-imported goods, added Reynolds, the author of several books on trade, including *Incoterms® for Americans*. A third reason for the revisions was a potentially vague area in CPT and CIP.

The new rules clarify that issue by including warnings that the parties should agree to both the delivery point and the place to which the seller pays transportation, according to Reynolds. He said people should become familiar with all 11 Incoterms® rules, but that most companies will probably use just four or five.

The new rules are spelled out in an ICC book entitled *Incoterms® 2010*. It may be ordered from ICC Books USA (http://store.iccbooksusa.net/). Attendees at Reynolds's seminars receive a copy of the book along with other materials, including *Incoterms® for Americans*, an updated edition of which will be available for purchase from ICC Books USA in early 2011.

The seminars will continue through mid-March. A partial schedule is available by clicking

http://www.uscib.org/calendar.asp?cat=Incoterms.

It will be updated as new seminars are added. ■

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Incoterms® 2010
by the International Chamber of Commerce (ICC)

Incoterms® 2010

The terms in the first group below are applicable to all transport modes, including multimodal transport and maritime. Those in the second group apply only to maritime transport. Within each group, the terms are listed in increasing order of the seller's responsibility for delivery of the goods. "Delivery" is the point at which the costs, risks and responsibilities are transferred from the seller to the buyer. It does not mean the physical delivery of the goods to a specific physical destination.

Applicable to all transport modes:

EXW – Ex Works. The seller's responsibility ends when it places the goods at its factory or warehouse for the buyer to pick up.
FCA – Free Carrier. The seller is required to deliver the goods to the carrier or another person nominated by the buyer at the seller's premises or another named place. The seller is required for export clearance, if it's an international transaction.
CPT – Carrier Paid To. It is similar to FCA, except that the seller must pay for transportation.
CIP – Carriage and Insurance Paid to. This is similar to CPT, except that it also requires the seller to pay for insurance covering loss or damage to the goods during the transport process.
DAT – Delivery at Terminal. This is one of the two new terms. The seller accomplishes the delivery when the goods once unloaded – whether by vessel, aircraft, truck, train or pipeline – are placed at the buyer's disposal at the specified terminal at the port or destination specified in the contract of sale.
DAP – Delivery at Place. This is the other new term. It is similar to DAT, except that delivery can be accomplished at any place mutually agreed upon.
DDP – Delivered Duty Paid. It is similar to DAP and DAT except that if it's an international sale, the seller is required to arrange import clearance and pay any customs duties.

Applicable only to sea or inland waterway transport:

FAS – Free Alongside Ship. The seller completes its responsibility to the buyer once the goods are placed alongside a vessel at a port named by the buyer.
FOB – Free on board. This is similar to FAS, except that the seller is responsible for the loading of the goods.
CFR – Cost and Freight. This gives the seller the additional responsibility of paying for the waterborne transportation. However, it does not necessarily designate the port from which the goods are to be shipped, so the buyer has to negotiate that with the seller if it wants to include the port.
CIF – Cost Insurance and Freight. This is similar to CFR, except that the seller is also responsible for buying insurance. It's also similar to CIP, except that CIF only applies to marine transportation.

The four terms dropped in the 2010 revision of the Incoterms® rules are:

DAF – Delivered at Frontier; **DES** – Delivered Ex Ship, **DEQ** – Delivered Ex Quay; and **DDU** – Delivered Duty Unpaid. DEQ was replaced by DAT; the others were replaced by DAP.

Important disclaimer: These descriptions should not be construed as authoritative. See the ICC publication Incoterms® 2010 for full explanations of each term.

Deepening collaboration between government and business

Even before the last session had finished, the verdict was in – Korea's innovative Business Summit had delivered an effective platform for injecting business views into the G20 process. This was confirmed in the final Declaration by G20 Leaders, which called for the Business Summit to be a feature of future G20 Summits.

The Summit brought 13 G20 heads of government together with some 120 corporate chairmen and CEOs for up-close discussions on the most pressing challenges to the global economy:

- Revitalizing trade and foreign direct investment
- Enhancing financial stability and supporting economic activity
- Harnessing green growth
- Delivering on the promise of corporate social responsibility

The Summit itself however, was the culmination of four months of preparatory work. Under the leadership of 12 'convening' CEOs, working groups deliberated on 12 critical issues facing the global economy. They produced a robust report addressing much of the G20 policy agenda and putting forward no fewer than 90 recommendations for actions G20 governments can take to stimulate economic recovery, drive sustainable economic growth and create jobs.

The International Chamber of Commerce (ICC) played a leading role at the international gathering voicing the views of global business on vital issues and demonstrating that increased cooperation between business and governments is crucial to the global economic recovery and to sustained economic growth.

"Although the majority of issues tackled by the G20 are directly related to global business, the G20 process has no formal means to solicit input from business leaders on its agenda and work," said Rajat Gupta, ICC Chairman and head of the delegation of ICC leaders to the G20 Business Summit, which included ICC Vice-Chairman and HSBC Group Chairman Stephen Green; ICC Honorary Chairman and Li & Fung Group Chairman Victor Fung; Past ICC Chairman and SEB Chairman Marcus Wallenberg; and ICC Secretary General Jean-Guy Carrier.

"The G20 Business Summit is a welcome innovation and we are grateful to Korean President Lee Myung-bak for opening this door and reaching out to business," Gupta said.

"Having long served as a trusted voice of business, providing business

A gathering of the G20 Business Summit participants, following a luncheon keynote speech by Angela Merkel, Chancellor of the Federal Republic of Germany

SEOUL G20 BUSINESS SUMMIT
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The Role of Business f
November 10

“We must ensure that trade volumes continue to grow by creating additional opportunities through trade liberalization, while nurturing a supportive environment for trade finance, and improving the governance of trade”

views to previous G8 and G20 meetings, ICC believes the Business Summit provides a unique opportunity for business to be more engaged on the ground during discussions,” said Fung. *“In response, we have accepted the challenge and we have been delighted to see the world business community respond so enthusiastically,”* he said.

In the lead up to the G20 gathering, ICC was heavily involved in shaping business messages, which included positions on trade finance, financial regulatory reform, green economies, sustainable development and facilitating the ability of small- and medium-sized enterprises to contribute to economic growth.

Prior to the gathering, Gupta met privately with the Korean President to deliver ICC’s recommendations to the G20 Summit on behalf of global business.

ICC Vice-Chairman Stephen Green, who chaired the B20 working group on nurturing small- and medium-sized enterprises, one of the Summit’s 12 roundtable discussions, stated: *“Discussions provided a direct opportunity for G20 heads of government to listen to our messages and to learn from companies who have the expertise and who understand the practical consequences of regulations and policy decisions on the economy and on jobs.”*

Green emphasized: *“The SME sector is vital to our world economy and the role of these businesses is increasingly viewed as that of a powerhouse of employment, innovation and entrepreneurial spirit. But this sector often does not get the support it needs from governments, financial institutions and capital markets. We call on G20 governments to remove regulatory and financial roadblocks that hold back their development. Moreover, we ask governments to establish national, regional and global funds to support the capitalization of SMEs and to spur innovation, research and development by strongly encouraging government-university-industry R&D collaborations to include SME partners,”* he said.

Marcus Wallenberg, who chaired the B20 working group on financing infrastructure and natural resources, noted: *“The G20 can make a lot of progress on its agenda by putting in place clear and rational legal frameworks, providing targeted incentives to move the economy in the right direction, and building public-private partnerships to tackle major development goals such as access to energy and water, training for employment and expanding healthcare systems.”*

Wallenberg said that G20 efforts to define a standard, global model for public-private partnerships will facilitate private investment to upgrade aging infrastructure in developed countries, meet the demands of urbanization and improve living standards in developing countries, build transportation infrastructure to facilitate growing international trade, and achieve sustainable development goals.

He added: *“Our working group found an estimated US$600 billion annual shortfall in project funding, which jeopardizes the potential for infrastructure and natural resources to contribute to economic growth and social progress. Private investment can fill the gap, if the G20 can deliver predictable policy frameworks and stable investment regimes.”*

20 BUSINESS SUM
or Sustainable and Balanced Growth
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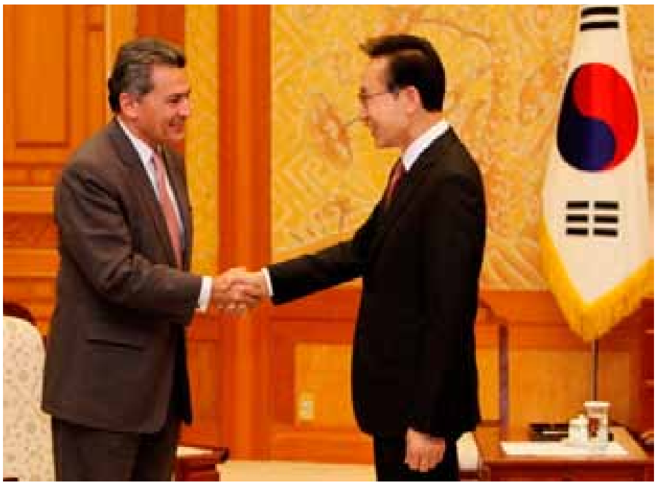

ICC Chairman Rajat Gupta met Korean President Lee Myung-bak

ICC Honorary Chairman Victor Fung, who chaired the B20 working group on revitalizing world trade, noted that trade volumes have started to recover since the outbreak of the global economic crisis and stated: *"We must ensure that trade volumes continue to grow by creating additional opportunities through trade liberalization, while nurturing a supportive environment for trade finance, and improving the governance of trade."*

"Trade is the lifeblood of the global economy and the world needs more of it at this critical moment, not less," Fung added. *"G20 leaders must personally engage in completing the Doha Round of multilateral trade negotiations and resist protectionism and trade-restrictive practices that impede the flow of goods and services."*

Ongoing business input to the G20 agenda

"Of paramount importance to world business is the issue of trade," said ICC Chairman Rajat Gupta. *"The essential mission of ICC is to promote cross-border trade, fight against protectionism and encourage the strengthening of a rules-based multilateral system."*

Gupta continued: *"In addition to listening to business views on policy, ICC hopes that the G20 will recognize the value of the G20 Business Summit and will create a permanent role for business at future G20 Summits and in the policymaking process between summits."*

"The Business Summit demonstrates that there are very good reasons for increased collaboration between business and government. The commitment and product of the CEOs compels a mechanism to continue the dialogue," Gupta said.

ICC Secretary General Jean-Guy Carrier stated: *"ICC calls upon the G20 leaders to establish a mechanism for business and G20 governments to follow up implementation of actions and proposals emerging from both the B20 and G20 Summits."* He added: *"As the representative voice of global business, ICC has long-played a role in bridging the gap and deepening collaboration between government and business. We welcome the opportunity to play such a role in order to maintain the dialogue and collaborations between summits."*

"ICC encourages G20 leaders to continue the Business Summit and hopes that France and Mexico will build on the initiative taken by Korea," said Carrier. ■

Building respect for intellectual property (IP): sustainable solutions to a global problem

Parvis Hanson is the Executive Director of the Global Congress Secretariat

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Paris, February 2-3, 2011

The global phenomena of counterfeiting and piracy remain a great concern to policymakers worldwide. While an exact quantification of the scope and economic effects at the aggregate level remains challenging, it is recognized that the trade in fake goods today affects virtually all economic sectors that are driven by creativity and innovation, and is prevalent in all economies. While luxury goods producers have been the traditional targets of counterfeiters, today, industries as diverse as entertainment, cosmetics, foodstuffs, electronics, auto parts, and most alarmingly, medicines, are concerned, counterfeiting and piracy represent direct losses to the individuals and companies who innovate and develop original products, but their impact reverberates throughout the global economy. Widespread availability and consumption of counterfeit and pirated goods undermine trust in a rules-based system, and, depending on the particular circumstances, may translate into lost opportunities for innovation, lost earnings, lost jobs, lost tax revenues and a weakening of state-funded services.

Formulating a policy framework to effectively address counterfeiting and piracy poses substantial challenges. Depending on the priority issues at stake, this may involve legislative, public health, law enforcement, intellectual property, technological and development-oriented considerations. In addition, educating consumers remains crucial, as is the need for working towards effective enforcement infrastructures and techniques. We continue to witness significant efforts by a number of countries to further develop existing frameworks, both at national and at international levels. This includes negotiations on multilateral agreements, for instance in the context of the draft MEDICRIME Convention, negotiated under the auspices of the Council of Europe, or the draft Anti-Counterfeiting Trade Agreement (ACTA). Other initiatives focus on the distribution of counterfeit products and protected content over the internet, and explore, for instance, voluntary cooperation models between the various stakeholders.

The World Intellectual Property Organization (WIPO), a specialized agency of the United Nations with 184 member states, is dedicated to developing a balanced and accessible intellectual property system that rewards creativity, stimulates innovation and contributes to economic development while safeguarding the public interest. WIPO's work in the field of IP enforcement is guided first by the need for an in-depth understanding of the elements that fuel the trade in illegitimate goods. The Organization takes a broad, cross-cutting approach that is more inclusive than the narrower concept of enforcement. It takes into account the interest of broader societal interests, development-oriented concerns and consumer protection and aims at enabling sustainable progress, by working towards an environment that is conducive to fostering respect for IP rights. The

2011

Paris, February 2 and 3, 2011
Cité des sciences et de l'industrie

GLOBAL CONGRESS
Combating Counterfeiting & Piracy

Building Respect for IP: Sustainable Solutions to a Global Problem

The Director General of the World Intellectual Property Organization, Mr. Francis Gurry, the Secretary General of INTERPOL, Mr. Ronald Noble and the Secretary General of the World Customs Organization, Mr. Kunio Mikuriya invite you to attend the Sixth Global Congress on Combating Counterfeiting and Piracy to be held in Paris on February 2 and 3, 2011.

Counterfeiting and piracy are global problems that affect us all. They threaten the health and safety of consumers; deprive national economies of vital tax revenues; embolden; criminal organizations and erode respect for intellectual property rights.

This Sixth Global Congress brings together key stakeholders

- government ministers and policy-makers
- business leaders
- senior law enforcement officials
- judges and lawyers
- stakeholders from intergovernmental organizations (IGOs) and nongovernmental organizations (NGOs)
- consumer groups
- members of academia

with the aim of building cooperation to enhance public awareness – and concerted action – to successfully confront these problems.

The Congress is structured to encourage maximum interaction and dialogue among the 800 expected participants. Discussion will cover a broad range of new issues, including:

- "knowing the enemy": methodologies for measuring the scope of the problem
- breaking down distrust: keeping the balance between the rights of IP holders and the needs of governments and consumers
- respect for IP rights as a key component of sustainable development
- innovative options for financing enforcement
- responsible destruction: eco-friendly and socially equitable disposal of infringing goods
- corporate social responsibility; its role in nurturing respect for IP
- enforcement of IP rights in the context of social and economic welfare
- committing to help least developed countries in enforcing IPRs
- know your customer – protecting the supply chain to combat counterfeiting
- dealing with the growing problems of trade over the internet
- awareness and education – new approaches

For more information and registration please see www.ccapcongress.net

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focus is on international public and private sector cooperation; on supporting a constructive and balanced international policy dialogue; and on legal and technical assistance to WIPO member states, upon request, to strengthen their capacities for the effective enforcement of IP rights.

Within this strategic direction, WIPO has since 2004 partnered with the World Customs Organization (WCO) and INTERPOL, the International Chamber of Commerce (ICC/BASCAP) and the International Trademarks Association (INTA) in the organization of the Global Congress on Counterfeiting and Piracy. The Global Congress has become a leading global forum for building cooperation to enhance public awareness – and concerted action – to successfully confront counterfeiting and piracy. It brings together government ministers and policy-makers, business leaders, senior law enforcement officials, judges and lawyers, stakeholders from intergovernmental organizations (IGOs) and nongovernmental organizations (NGOs), consumer groups and members of academia.

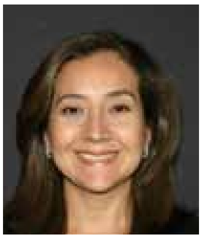
> **"Widespread availability and consumption of counterfeit and pirated goods undermine trust in a rules-based system"**

In 2011, WIPO is the lead organization and, as such, the Chair of the Global Congress Steering Group. Discussions at the 6th Global Congress will reflect a balanced approach to combating counterfeiting and piracy, including with a view to underscoring the link between building respect for IP and sustainable development. The theme of the Congress is "Building respect for IP: sustainable solutions to a global problem." Overall, it will seek to create a better understanding of the elements underlying the trade in illegitimate goods, and to discuss sustainable solutions to stop it. Discussions will cover a broad range of new issues, including:

- Methodologies for measuring scope and impact of counterfeiting and piracy;
- Refining enforcement techniques, including with a view to detection and new challenges posed by small consignments;
- Protecting consumer safety vis-à-vis the multiple risks associated with counterfeit goods;
- Ensuring fair use of IP rights, including with a view to small and medium-sized businesses (SMEs) and the protection against abusive enforcement practices;
- IP enforcement and sustainable development; including an analysis of elements that fuel IP infractions in a broader societal context, and addressing the need for balance in IP enforcement regimes;
- Fighting counterfeiting and piracy online: new trends and responses, including regulatory and voluntary partnership models;
- Innovative approaches for financing enforcement;
- Responsible destruction: eco-friendly and socially equitable disposal of infringing goods;
- Corporate social responsibility: its role in nurturing respect for IP;
- Trade agreements at multi- and bilateral levels and their effectiveness in confronting counterfeiting and piracy;
- Committing to help least developed countries in enforcing IP rights;
- Securing the supply chain: new technologies; role and responsibilities of intermediaries;
- Awareness and education – new approaches.

The 6th Global Congress will be co-hosted, under the high patronage of the President of the French Republic, by the French Institut national de la propriété industrielle (INPI). It will be held in Paris on February 2 and 3, 2011. The Congress is structured to encourage maximum interaction and dialogue among the 800 expected participants, featuring ministers and high-level speakers from around the world. Registration and more information at www.ccapcongress.net. Inquiries, including information on sponsorships and exhibit opportunities, to secretariatgc@gmail.com. ■

More challenges in the fight against piracy in El Salvador



Morena Zavaleta is a Partner at Arias & Muñoz El Salvador

Christian Poveda, a French-Spanish journalist, filmed a documentary called *"La Vida Loca"* (The Crazy Life) about the daily life of a Salvadoran gang. Only 3 days after its transmission in Spain by Canal + España, the documentary reached the streets of San Salvador and was being sold at 4 dollars – one for the vendor and three as "tax" for the Mara 18 gang. A couple of weeks later, Poveda was killed by Mara 18 members.

On similar news, it is reported that after an investigation, Microsoft found that gangs were marking the illegal software they made with the figure of a scorpion, which is used as a symbol that it was produced by these gangs. It is also reported that in Central America, El Salvador is the only country in which gangs have taken control over software piracy.

These are only a couple of stories about illegal organizations related to counterfeit. However, they are a brief sample of the seriousness and difficulty to obtain developments in the fight against piracy in El Salvador, due to the involvement of informal vendors and gangs.

The Central America Free Trade Agreement signed with the United States (CAFTA-DR), in force since March 1st 2006, required the ratification of various Intellectual Property Treaties and the inclusion of legal amendments to national laws as to enforce the compliance of intellectual property laws, including "ex-officio" actions of investigation and seizure of alleged counterfeit products and customize measures in order to preserve proofs and to prevent the continuation of the activity.

Due to these amendments, several raids were possible resulting in the seizure of thousands of illegal products; however, these procedures provoked public riots, vandalism and disorders, discouraging authorities to make them in a continued basis. After these incidents, the police changed their aim to focus on the producers and wholesale distributors, which is a positive measure but not sufficient to decrease the sale of counterfeit goods.

By the end of 2009, 16,000 informal vendors are estimated to operate in the capital city and an organization called the "National Movement of Vendors" has been created, whose president assures to have given conferences in universities and having been in a US "tour" promoting the rights of vendors. She affirms that the organization has a seat as the representative of the informal sector in the Economic and Social Counsel, formed by the current government, and their philosophy is that intellectual property should not be applied in poor countries such as El Salvador. She allegedly has proposed remedies to the government such as applying a tax over blank discs, destined to pay 25% for the state, 25% to multinationals, 25% to national artists and 25% to be destined for credits to informal vendors that wish to leave the counterfeit activity.

> **"6 out of 10 people believe that piracy should not be criminalized and that buying a pirated product means to save, not to steal."**

Mixed with the informal vendor problem is the gang intervention in piracy. According to police investigations, some of these informal stores are used by gangsters to hide arms and extortion or drug based money. Gangs currently have their own rudimentary laboratories were they keep all their raw material such as blank CD´s and printers, and even own their storage facilities.

This means that despite the existence of modern laws and the participation of governmental entities, the fight against piracy must comprise a strategy that includes the formalization of vendors and to create incentives to leave the piracy goods sale activity.

Up to this date, no official study has been made of this problem, making it very difficult to define an effective solution. A good start would be to make a research of the amount of informal vendors and "formal" vendors that sale pirated goods, the type of products they sell and the income obtained from these activities.

With this information, the Ministries of Economy and Treasury, jointly with the city mayors, should prepare a strategy – that could include amendments to the necessary laws – to formalize vendors and discourage the sale of pirated goods.

This formalization could also lead to the increase of the tax payer's base, the reordering of streets, and to define alternatives for the sale of other types of legitimate goods in combination with the access to credits.

Jointly to this study, Customs should make a verification of the amount of blank CD´s, DVD´s and packages imported to the country and identify who are the major importers as to investigate if their destination is piracy activity and also determine the creation of an additional tax over this type of goods. These funds should be used for the fight against piracy.

Finally, a crucial point is to educate consumers of the benefits to avoid the purchase of counterfeit goods. According to a 2008 study made by the American Chamber of Commerce - AMCHAM, 6 out of 10 people (all with university studies or a college degree) believed that piracy should not be criminalized and that buying a pirated product means to save, not to steal. What they should be informed is that the money they pay finance gangs and other illegal activities that generate public insecurity, which according to recent surveys, is the biggest concern of the Salvadoran citizens, even more than economic issues. ■

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arias & muñoz

Exploitation of photographs on the internet without the author's consent

Bogdan Fischer PhD is an Attorney at Law at Chałas & Partners Law Firm, Cracow Branch

While preparing articles for publication on the website, one has a temptation to enrich it by posting illustrative pictures, easy to obtain from search engines. Sometimes such actions may be justified for information purposes, but not commercial use.

While posting an article on the website, for example about a known photographer, is it allowed to add some photographs taken by the artist which demonstrate his style? Is it sufficient to sign the photographs by the photographer's name and surname as a lawful indication of the source of the photographs? And what about the remuneration for the photographer?

No universal common copyright in the European Union

In accordance with article 345 of the Treaty on the Functioning of the European Union (TFEU) "The Treaties shall in no way prejudice the rules in member states governing the system of property ownership". TFEU treats copyright as a form of ownership. It is possible to regulate this issue under EU law, arising from article 114 TFEU, which empowers the European Parliament and the Council to adopt measures for the approximation of the provision laid down by law, regulation or administrative action in member states.

According to the principle of non-discrimination expressed in article 18 TFEU the national legislation cannot deprive the authors from the other member states of the rights granted to nationals. Unequal treatment on the grounds of nationality would therefore constitute a violation of this rule. A citizen of another member state, appearing before a national court may refer directly on article 18 TFEU and demand to ensure the protection stipulated for nationals.

The situation in Poland

How is the situation in Poland, despite the concurrent policy in member countries? In order to determine the grounds upon which the author may claim compensation for the use of photography of his authorship in given article, it is necessary to determine whether a violation of his copyrights occurred. Under the copyright laws, when there are no other specific regulations, the author shall have the exclusive right to use the work and to determine the use (so-called field of exploitation) and the right to remuneration for the use of his work. Therefore in general the publication of photographs without permission of their author is a violation of his rights and justifies the submission of the compensation claims. One should always consider whether there exists any of the circumstances which, under the provisions of the Law on Copyright and Related Rights, allows the use of others' works without their permission.

It should be underlined that already disseminated, current opinions and reporter's photographs can be disseminated in newspapers, radio and television for the informational purposes. But can we classify the internet among above mentioned media categories? Whether the photographs used in the article are the actual reporter's photographs defined in the Act?

"Press" can also constitute the periodical publications on the internet, if they meet the requirements set in the Act on press law, ie. do not form a complete entirety, appear at least once a year, bear the permanent title or name, current number and date. In this situation it is allowed to take advantage of a permitted public use on the internet on par with its traditional counterparts (newspaper print). More liberal views consider the press function as the decisive point, without the specific requirements of the press law. Reporter's photography ie. documenting the events, "retained in the frame" must be current as to the speed of information flow. Topicality of the photography extends to the duration of the event and the short period after its ending. Lack of obligation to obtain the consent of the author to use his photographs in informational purposes does not preclude his right to remuneration as well as the obligation to fulfil other conditions ie. mentioning the source and the name and surname of the photographer.

Although it is often used, it is not enough just to mention the name and surname of the photographer without identifying the source (according to the customs established in the environment). In case of using of the photographs appearing on other websites it is necessary to provide an internet address from which they were derived.

The amount of remuneration of authors

Infringement of copyrights entails the possibility of the relevant claims: cessation of violating one's rights, removal the effects of a breach, compensate for the damage, repayment of received benefits. Implementation of the first two claims means to remove the referred material from the website. From the viewpoint of the author's interests, it is important that he has the possibility of pursing compensation.

Apart from setting the claims on the general principals of Polish Civil Code and proving the amount of damages the holder may alternatively claim to charge the violator with the sum of money corresponding to twice and in case of culpable violation – three times the remuneration which would be payable for granting permission for use of the work.

There are no rules forcing the author to use any of the given methods to assert his rights. Therefore it is considered that he can choose the method which in his opinion suits his needs the best. The simplest way to indicate the amount of the remuneration is to base it on the remuneration schedules of the given collective management organization or to base in on the provisions of the contract concluded by the parties.

Collective organization managing the copyrights and related rights regarding the petro(photo)graphical works in Poland is the Association of Polish Art Photographers (ZPAF). The authority of the collective management organization to manage and protect the copyrights arise from the contracts with the artists and performers. Moreover the organization is allowed to represent the foreign artists – but only on the grounds of separate agreements on managing and protection of copyrights. In case there is no collective management organization or in case there are no provisions between parties regarding the remuneration, its amount will have to be determined by the court. In this situation, determining the values will depend on the facts of the given case.

Reaching an agreement with the author or his representative (an agency for example) is always the best solution. Reason to lower the remuneration may be eg. informational or even the promotional (for the author and the agency) character of the publication. While negotiating, it is wise to refer to set by the collective management organization (in Poland: ZPAF) fees for the use of photographs on the internet, due to their height and the differentiation between the promotional or informative character of the photographs. ■

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Driving global expansion

Nelson Raposo Bernardo, Global Managing Partner, Raposo Bernardo, in a Q&A with World Commerce Review, discusses services globalisation and the management of growth

Nelson Raposo Bernardo reference practice areas are Banking and Finance, Capital Markets, Corporate Law, Mergers & Acquisitions, Project Finance and Private Equity. He advises national and multinational leading players, in operations concerning debt, equity, structured finance and securitisation, M&A, project finance, private equity, restructuring and regulation.

He is also strongly experienced and reputed in legislating, being co-author of the present Portuguese Securities Code and led several legislative reform committees, in several countries, in banking, financial, real estate and construction areas. He has published books and articles on corporate law, banking and contract law, and participated as a speaker seminars and conferences in Portugal and abroad. He was a member of the Higher Commission for the approval of ad-hoc judges (2000) and consultant for Capital Markets of the Portuguese Auditors Association (1998-2006).

He holds a degree in Law from the Law School of the University of Lisbon, a Masters in Juridical Sciences (Corporate Law) from the same School (1998), where is he is also presently working on his doctorate in Corporate Law. Assistant Professor of Corporate and Commercial Law at Law School of the University of Lisbon (1991-2006) and in Entrepreneurship and Family Enterprise Start-Up and Management courses at INDEG/ISCTE (Audax) (2005-present), one of the most reputed business school in Portugal. Chairman of boards of general meetings of several companies and associations. He is fluent in Portuguese, English, French and Spanish.

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Do you believe that models like business internationalization and services globalization still make sense in the current global crises context?

Yes, I have no doubt that it still makes sense. Those are two independent realities. The crises to which you refer only require some prudence in terms of the means and resources involved in the international expansion operations. But that doesn't mean any abandonment or denial concerning a model that brings together levels of demand that benefits of geographical interdependencies and that even elevates the services culture to a higher level when compared with what is usual and can be transposed with success and advantages to those who deliver the service and to whom benefits from them.

Does that mean that in services delivery the way won't be the specialization in specific markets?

I don't believe that specialization is incompatible with my vision on globalization. One of the greatest benefits of globalization phenomenon in history has always been to allow the global community to seize the advantages that can be brought to each local culture, to each specific country. In our law firm's case, globalization doesn't mean that we adopt in Poland, Spain, Angola or Brazil always the same procedures. Obviously there has to be some adaptation to local characteristics. But there are some attitudes that globalize themselves and that can be used in each one of those locations.

From my experience, I can assure that one of the biggest benefits of globalization in services delivery is the awareness that globalization exists. It is also a matter of attitude. For example, today I present investments in Africa to Canadian or North American investors or projects in Brazil to Arab or Asian business men more easily and these are evaluated with broader views when comparing with the ones of twenty years ago when we presented projects to business men form neighbour countries. Nowadays distances aren't relevant, they don't restrain. Before this wave of globalization distances weren't only geographical but also cultural, political, social and others.

Which are the client's expectations, in the current context, concerning an international law firm of legal advisory and services such as Raposo Bernardo?

There are timeless expectations such as quality, efficiency, focus on problems resolution and being able to provide solutions. Our clients have always expected these and will always demand them. We take great pride from knowing that they expect this from us because that is the level of service to which we usually deliver. However, today there are some expectations that result from the current context in which we do business, such as value for money, quickness in the response and an open mind to understand and accompany the client's activities around the world. Furthermore, in the case of a firm with activities in three continents and business relations all around the world, such as ours, clients expect that we are a very active partner in the assembling of operations and businesses from anywhere. Not long ago I was returning to Portugal from our office in Poland, where we were putting together an operation that involves investors form five eastern European countries, with British financing and corporate structures based in Luxemburg and Spain, for projects to be developed in all Latin America and Africa. Two or three generations ago these kind of operations were of exceptional character and today are common and very frequent. Our clients expect this capability from us.

Portugal has been through a hard period in economic and financial terms and has been heavily affected by international juncture. In this context how do you manage a law firm that, although international, is originally Portuguese?

Raposo Bernardo is currently a law firm established in nine countries and with interests and operations in many others. Even though it is true that Raposo Bernardo originated from Portugal in 1995, today its activity is much more focused in a global Iberian perspective but also in Eastern Europe, North of Africa, Portuguese-speaking African countries, Brazil, all of Latin America and even the Middle East. Although we advise in projects beyond this geography, our current interests are focused mostly at this level. We are also very close to Canada, a country in which we are very interested in terms of investment gathering and cooperation with local law firms with clients with investments in Europe, Africa, Brazil and Latin America and also with business associations.

Concerning Portugal, the country is currently going through a difficult period in result of some unadjusted policies, but also because of its small dimension and an incomprehensive structural incapacity in terms of production. Another of Portugal's problems is still the lack of definition of a national strategy. But it is a country with great strength and courage and Portuguese people are conquerors by tradition and they can suffer but will always be able to come around and surpass all difficulties.

In times of crisis which is the best bet: to go forward with pre-established internationalization project or to restrain until the markets stabilize?
It depends on the company's profile, the sector in which it develops its activity, the capability of investment with its own resources and especially on the ambition, attitude and soul of its teams.

Part of your work consists in advising companies that, like Raposo Bernardo, are internationalizing their businesses. Do you feel that those operations have been dropping or, by contrary, there has been an increase in the number of companies that have internationalized their business in a time of crises?
From our experience I would say it is clearly increasing the number of companies expanding from their countries of origin. In most cases, the crisis that affects certain countries stimulates this action. We see today many companies that want to invest in Africa, Latin America and Asia, regions that the crisis hasn't affected with the same severity. And this is normal; it is all about searching for opportunities where they exist. It is a company's managers and administrators duty.

Having Raposo Bernardo an important track record in legal advisory in markets and financial contexts (Banking, M&A, Private Equity, Project Finance, etc.) do you think companies are resorting more to financing mechanisms or acquisition of investment capability in order to proceed with their businesses or, giving the markets inconsistency and banking contraction there has been a cutback? Which are your feelings about this? Which do you believe will be the tendency?
This has been one of the most relevant issues in 2010 concerning financial markets, mergers & acquisitions activities and project development. One of 2010 historic marks in the corporate world will be the distinction between those who have and those who don't have money. And this will happen because the financial system, mostly the European, stopped feeding the markets. It needs the money for itself, to comply with its ratios.

Despite all this, the M&A market shows a growth tendency and it is natural that in 2011 the acquisitions and merging of companies returns in full force. But those operations will only be possible for companies that are capitalized, because it is no longer possible to buy assets with loans guaranteed by the asset itself, as it is also no longer possible to develop complex "financial engineering". At this stage we are seeing a back to basics, insofar that a company that has all the capacities will grow and move forward and the one that hasn't will experience some cutback or even disappear. It is the market's relentless rule, nothing less than the survival of the strongest before the weakest, nowadays also with the survival of the fastest before the slowest.

> **"It is obvious that markets will stabilize, confidence levels will be re-established and investments will return to a security level necessary for them to take place in a consistent manner"**

But do you believe it is a temporary situation or is it here to stay?
It is obvious that markets will stabilize, confidence levels will be re-established and investments will return to a security level necessary for them to take place in a consistent manner.

But nothing will be has it was, not only in companies life's, but also in all of our life's, from our personal area to life in society. The human being has the enormous capacity to withstand thru the harshest situations. So much that sometimes, when the adversity is gone, he seems to instantly recover and carry on as if nothing ever happened. But the truth is that this crisis is deep, it has been slow, it affected all sectors, shook down real estate, broke out financial markets, states collapsed, governments trembled and tumbled and social repercussions, all over the world, are growing. We still don't know the outcome of this situation. We only know that it is going to be difficult and it will leave a scar for several generations to come.

Markets are still changing, but people's lives will also suffer with decisive changes. More and more there will be less space for market's irrational exuberances, for financial products inventions and fictional businesses. But also, people and companies consumption has to be conscientious. Actions of the few that can influence many have to be wise. Life has to be lead with realism and with a bit more of simplicity. In a way, in this first half of the 21st century we have watched the Human being destroy an important part of he's principles and values patrimony. What in the financial markets and also in world consumption came with an aura of evolution and sophistication was nothing more than an illusion, an excess and an irrationality that would have its price. We will have to take a few steps back so we can move forward more consistently. I hope that by that time we won't forget all that has happened.

When we think about people, their habits and their lives at companies and in society, a law firm such has yours, with offices in several countries, has human resources from very distinct nationalities. How do you manage the several nationalities your company has?
The number can vary at a given moment, but there will about 15 different nationalities in our offices. Obviously there are relevant differences concerning the law practice culture and life habits, for example, from a Polish to an Angolan, from a Spanish to a Brazilian or from a Romanian to a Portuguese. From our experience, the best way to deal with this reality is using a very simple method: to acknowledge the differences, embrace them as inherent characteristics that cannot be bypassed but that are positive, try to collect from that diversity the best in terms of creativity, complementarities and experiences. Of course that there is a common core of principles and values that we all share and that are reflected in the firms culture.

Which compensation systems, besides wage, do you believe are more important for the cohesion and commitment of such a diverse team?
Without any question the assurance of participation in the development of an international law firm that is a bit of all those who work in it. A stimulating environment of continuous learning, internal and externally, as well as access to major international businesses and operations, are clearly also factors that stimulate our teams.

On the other hand, it is also important that those same teams see their performances recognized by the most prestigious international entities that evaluate lawyers work in each country. And for Raposo Bernardo's lawyers it is a great pride to have achieved in 2010 more than 100 awards for all our offices, from which we outline ACQ Law Awards, Corporate INTL, ACQ Country Awards, ACQ Global Awards, Finance Monthly Awards, to receive important acknowledgments from Chambers & Partners and Legal 500 directories, and to be on the first places in M&A deal count from Mergermarket, Thomson Reuters and Bloomberg. These awards and recognitions comprise more than a dozen areas, from financial, to banking, capital markets, private equity, project finance, tax, employment, competition, energy, and several others, and all countries were we have offices have been contemplated with several awards. These important acknowledgments are extremely gratifying to all of our teams and give them the motivation to carry on with the excellent work that they have been doing.

Doing businesses in several countries with economies in different stages of development – in Europe, namely in Portugal and Spain, we are living a very difficult economical moment, whereas, for example, in Africa countries like Angola, Mozambique or Cape Verde are in a clear growth – how do you manage the motivational component within teams?
Motivations results from a wide set of factors. Apart from those I have mentioned before, and that have a decisive importance, our lawyers are confident and self-motivated. On the other hand, even in countries where the crisis has been more severe, we have had some growth. It is possible that work on real estate and projects has decreased, but it has increased exponentially in restructuring, tax, financial, regulation, labour and dispute resolution. We are at a stage where you work more for less, but it is still true that in overall we are growing.

This year Raposo Bernardo completes 15 years. And now, after these 15 years, which are your medium term projects, where do you want to go?
We have been very happy in this 15 year journey. Our main goal is to continue to be happy and to provide that happiness to a growing number of people, which means necessarily more clients, more lawyers, new geographies…

In terms of geographies, which is your most immediate goal?
More than new geographies, our daily challenge consists in maintaining an above average quality of work that is recognized by our clients. In each detail we have to show all we are, to have a very positive attitude, to develop very serious work. A Raposo Bernardo's lawyer always has to contribute to solve problems and find solutions to our clients, be prepared to learn every day, with humbleness, dedication and a great deal of ambition.

As for new geographies, we have been working mostly in countries that are receiving foreign investment, such as Poland, Romania, Portugal, Spain, Angola, Mozambique, Cape Verde, Brazil, São Tomé and Principe, etc. We will soon commence operating in North Africa, where we already have intervened in specific projects, but we will also expand to Turkey, in other Eastern European countries and in the Middle East.

We plan, in 2012, to broaden our intervention and approach to foreign investment emitter countries, which may lead us to United Kingdom, Canada, USA, and other European countries, although in these cases always in a perspective of cooperation with existing leading law firms and companies with investments in geographical areas where we are present. ■

Enabling the next generation of e-business in Bermuda

One of the hallmarks of Bermuda's economic environment since World War II has been the "partnership" between the private and public sectors. In many ways, the private sector proposes and the public sector disposes, but the two proceed from a shared understanding of the advantages that a well-managed jurisdiction providing a business-friendly environment can offer its people as well as its entrepreneurs.

A good example of this shared participation has been the way that, rather than merely supporting its information communications technology (ICT) sector, the Bermuda Government has always taken a leading role in its development.

The Government was itself one of the earliest adopters of ICT. Realising that the island's traditional remoteness would be changed by the advent of the internet, the Bermuda Government decided that it must lead, rather than follow, the private sector in this area. Merely keeping up with commercial developments would leave the Government at a huge disadvantage, it was felt.

As early as 1999, ICT had its own Ministry in Bermuda and thus a representative in meetings of the Bermuda Government's Cabinet. The Electronic Transactions Act (ETA) was published that year and presently a public consultation is underway to ensure that Act remains relevant, given the rapid technological changes of the last decade. Government itself continues to advance towards the goal of increasing its online services offering to both business and the public. Although the project is not yet complete, the way in which the population interfaces with its Government in Bermuda has become increasingly electronic, in the payment of taxes, vehicle licensing and registration and in many other ways.

The Hon Patrice K Minors JP MP, Minister of Business Development and Tourism

With the appointment of a new Premier and Government leader in Bermuda in October — The Hon Paula Cox, JP, MP remains Finance Minister, as well as taking on her new leadership role — the Cabinet's responsibilities were reconstructed. A new Ministry, Business Development and Tourism, was established to concentrate on supporting and encouraging business efforts on the island. As electronic commerce is a key component of Bermuda's and the world's business development, the Department of E-Commerce comes under the aegis of the new Ministry.

The newly-appointed Minister, The Hon Patrice K Minors, JP, MP, was quick to confirm her interest in furthering the island's attractiveness as a base for E-Commerce. *"Geographically remote though Bermuda may be, we have retained our relevance to the global business community by staying in the lead pack of those countries who have adopted e-business as a cornerstone of their economic base,"* the Minister said, adding *"It is very much our intention to remain a market leader."*

Internet governance

Internet governance has been defined as the development and application by Governments, the private sector and civil society, in their respective roles, of shared principles, norms, rules, decision-making procedures, and programmes that shape the evolution and use of the internet.

Within that area, a recent initiative by the Department of E-Commerce, was the creation of an internet Policy Advisory Board (PAB). A number of jurisdictions incorporate PABs into their governance structure to help in developing and implementing internet governance policies.

Bermuda has for a number of years retained a high e-readiness ranking in the comprehensive annual report prepared by The Economist Intelligence Unit in conjunction with The IBM Institute for Business Value. Bermuda routinely places among the top 25 jurisdictions around the world, no mean achievement, given the island's small size and consequent inability to match the larger countries in certain aspects that e-readiness measures and digital economy measures.

It is important that Bermuda retain its high ranking by ensuring that its domain name registry remains robust and resilient (Bermuda internet addresses are currently identified as .bm) and provides best of class service in line with other equivalents. A number of evolutionary changes are taking place within the domain name system and the broader internet, and the Minister will be charging the new PAB with ensuring that the island's best interests and professional expertise in this area are monitored and protected.

In Bermuda, the Information Technology Office (ITO) is responsible for managing the .bm Country Code Top-Level Domain (ccTLD) technical infrastructure and the Registry General is responsible for the day-to-

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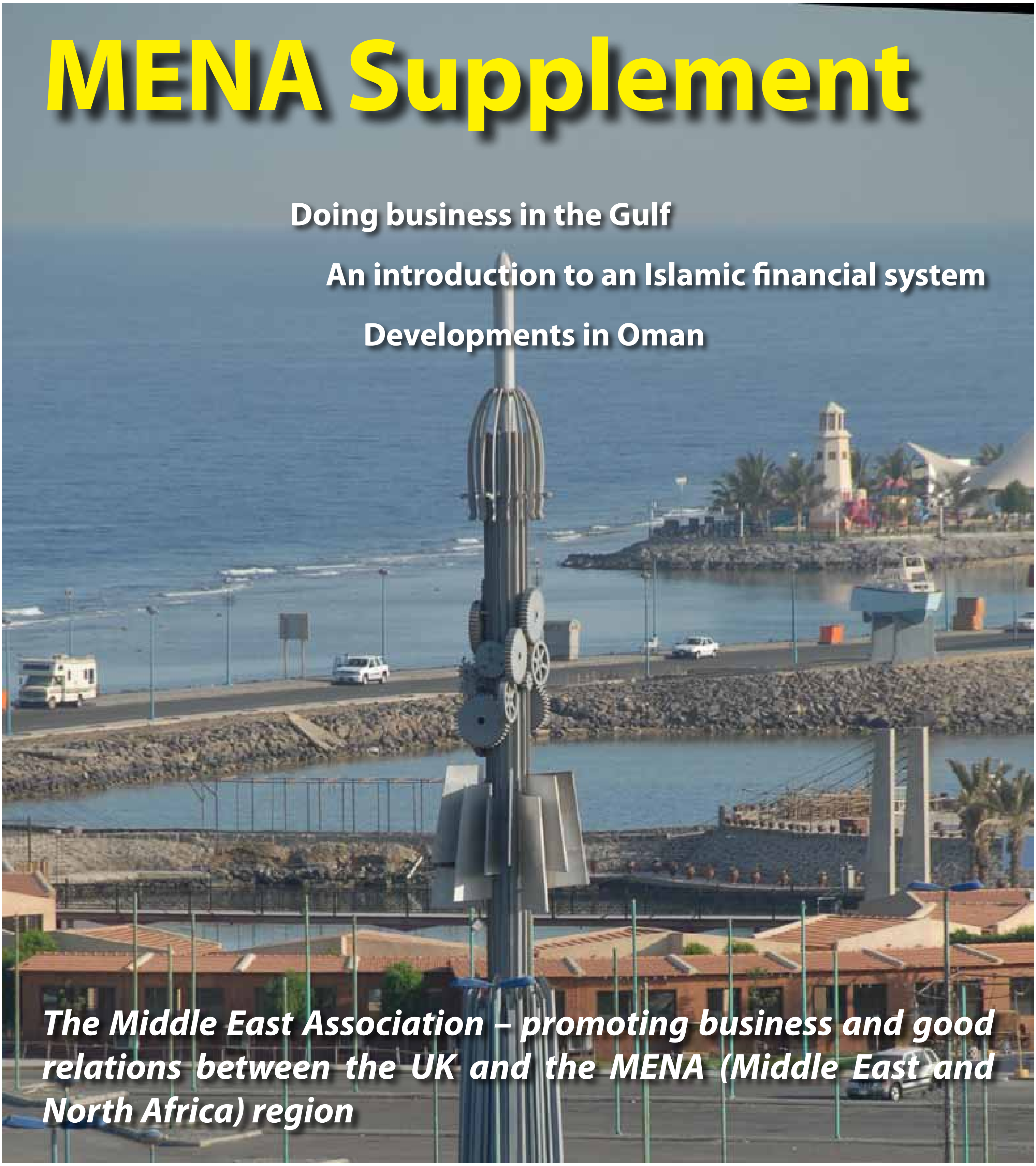

MENA Supplement

Doing business in the Gulf

An introduction to an Islamic financial system

Developments in Oman

The Middle East Association – promoting business and good relations between the UK and the MENA (Middle East and North Africa) region

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Oman Trade & Investment Forum promotes Oman/British business relations

The Middle East Association's Oman Trade & Investment Forum, which took place on 21 October and marked the 40th anniversary of the accession of HM Sultan Qaboos bin Said, was a resounding success. London's prestigious Mansion House was full to bursting for the landmark event, which was attended by over 270 delegates, including around 60 senior Omani government representatives and business leaders accompanying HE Maqbool Ali Sultan, Oman's Minister of Commerce & Industry.

Organised with the full backing of the Oman Centre for Investment Promotion and Export Development (OCIPED), the Embassy of the Sultanate of Oman in London, the Omani British Friendship Association Business Council and UK Trade & Investment, the Forum opened the eyes of British business to the latest developments and opportunities in Oman, highlighting Oman's achievements over the past 40 years and the country's attractions for foreign investors. While the strength of the UK's relationship with Oman was underlined, speakers warned against complacency, with Baroness Symons, Conference Chairman commenting that the relationship *"needs to be refreshed to grow stronger"* and Alan Duncan MP, UK Minister for International Development characterising Oman as a *"loyal and generous ally, but who we must never take for granted".*

> **"Oman is a high growth, low risk, stable, competitive and resource rich country"**

Opening the conference Michael Thomas, former Director General at the Middle East Association, underlined the need for British companies to be *"up to speed with the latest developments in Oman"*, noting the $14.5 billion industrial investments in the Port of Sohar and plans for the development of secondary industries. He spoke of the significance of Salalah, now the port of choice in the region for the four largest container lines in the world and the potential for the establishment of joint ventures in the free zones as a secondary industries centre serving the region. *"Oman's doors are wide open to British business people and it is up to us in the UK to take advantage of this,"* he said.

Steady development

Baroness Symons highlighted Oman's steady development in areas ranging from international relations to infrastructure, national institutions and education as well as the impressive growth in its economy and trade. It is an increasingly attractive investment destination as a result of its tax and other reforms, its diversifying economy and development of tourism, ICT, financial services, water and energy industries. She acknowledged Oman's commitment to its young people and the development of human capital, and the potential for the UK to forge *"important lasting partnerships"* in education and skills development.

Former Lord Mayor of the City of London, Alderman Nick Anstee, commented that in the 40 years since the Sultan came to the throne Oman has been "transformed", noting the Sultanate's progress towards a diversified knowledge based economy with an expansion of education, development of scientific research and IT. *"You are investing in the oil and gas industry, but also in infrastructure development for tourism, in protecting Oman's coasts, and in preparing Omani citizens for a greener future with the development of renewable energy,"* he said. Record budget surpluses are adding impetus to Oman's ongoing infrastructure and industrial development programme. *"It goes without saying that within this new Oman there is a wealth of opportunities for UK firms to work in partnership with Oman."* He highlighted in particular the scope for cooperation in education, training and qualifications, SME development and investment in both directions.

Alan Duncan MP, UK Minister for International Development, highlighted the strong relations between the UK and Oman, The 40th anniversary would soon be celebrated by a State Visit of HM the Queen. *"I am certain that this will help to pull us even closer together and to open up new possibilities for greater partnership,"* he said. He pointed out that the UK was the largest overseas investor in Oman in 2009 and trade with Oman had increased by 60% over the past five years. He noted however that the UK is losing market share, both to established competition and to emerging markets such as India, China and Korea. While British companies continue to win significant levels of new business *"we could and should be doing more"*. He noted the multi-stranded infrastructure development programme underway focused primarily on free-trade zones, industrial hubs, ports, road and core utilities and noted that more than $10 billion of civil, industrial, transport, petrochemicals, oil and gas and tourism projects are planned, as well as $7 billion in power generation and water desalination projects. He also mentioned opportunities in enhanced oil recovery, the development of a new generation of solar and wind projects and the "critical" importance of education, where the UK has an "outstanding reputation". "*Realising those opportunities together would be the best way to celebrate the 40 years of His Majesty's rule and the great association between the Sultanate and the UK,"* he said.

HE Maqbool Ali Sultan, Oman's Minister of Commerce & Industry, addressing the conference

HE Maqbool Ali Sultan, Oman's Minister of Commerce & Industry, highlighted Oman's "remarkable achievements" over the past 40 years in both social and economic development, noting in particular the progress achieved in the empowerment of women. Oman faces two

> **“We want the UK to be Oman’s - and the wider Gulf’s - commercial ‘partner of choice’. British business and expertise have much to offer the region”**

main challenges, he said – further diversification of the economy, and human resources development. Discussing Oman’s economic diversification strategy, he noted that Oman has been successful in attracting multinational investors in many industries such as methanol, fertilisers, aluminium and steel and is now diversifying into non-oil and non-gas sectors such as tourism, knowledge economy, fisheries, food, trade, minerals and manufacturing. He called for further British private sector investment in Oman to sustain the strategic relationship between Oman and UK, and to support SME development and employment creation. *“British companies should look at Oman as a strategic location using it as a hub for trade with countries like Yemen, Iran, East Africa, GCC and others, benefiting from Oman’s political and economic stability, its excellent relations with all its neighbouring countries and its friendly and flexible laws which welcome foreign investments.”*

Business environment

A panel session moderated by Martin Amison, Co-Chairman, OBFA Business Council and Partner and Head of International, Trowers & Hamlins, painted a picture of the excellent business environment in Oman and the Government’s focus on encouraging business and investment. Attractions include clear laws, strong regulation, an independent judicial system, low taxes (flat rate of 12% corporate tax, no personal income tax), free trade agreements with various trading partners including India, the USA and Arab countries, the availability of OCIPED as a one stop shop for dealing with Ministries, and investor friendly laws relating to ownership of businesses, land and labour. As Eng Awadh Salim Al-Shanfari, CEO, Salalah Free Zone Company pointed out, *“Oman is a high growth, low risk, stable, competitive and resource rich country.”*

In particular discussion focused on the advantages of Oman’s Indian Ocean ports and associated free zones, which are successful manufacturing bases for many businesses with the availability of strong local infrastructure, excellent communications, support and incentives from the Government and advantageous geographical location outside the Arabian Gulf. Salalah, with its competitive freight costs, has developed as a major transhipment port, and its free zone has attracted more than $4 billion of international investment over the past two years. Sohar is a major industrial port with hydrocarbons, metals and minerals clusters, and its adjacent free zone is focusing on logistics, downstream industries, manufacturing, services and niche industries. Duqm will develop as a huge port over the next ten years, with the world’s largest dry dock.

A panel session on financial services, moderated by Ewan Stirling, CEO of HSBC Oman, discussed Oman’s diversified, robust and well regulated financial services sector and the role of this sector in underpinning economic development. It was noted that Oman’s banks had survived the financial crisis in good health. Encouraging statistics were provided as to growth, with real GDP growth per capita forecast at 4.5% for 2010. $2.4 billion has been allocated to new infrastructure projects in 2010, including airport projects, petrochemicals, aluminium smelting and the expansion of LNG facilities. The panel felt that considerable advances had been made and would continue to be made in the sophistication of the financial services industry in Oman. It was suggested that corporate bonds, asset management, and insurance would be areas for future development and offer scope for co-operation, while education, training and qualifications, would continue to offer opportunities - there have been significant British successes here, such as the Chartered Institute for Securities & Investment (CISI) agreement with the CMA to develop management programmes for intermediaries in the capital market.

A panel session moderated by Dr Phil Goddard, Director, The Energy Industries Council, discussed power, water and renewable energy. Oman was the first country in the region to implement a privately financed independent power project, and private sector involvement in the power and water sector has grown strongly. There will be huge expansion in the power and water sector over the next five years, focusing on expansion of networks and transmission. Further IPPs will be rolled out on a well established model. There is also currently a focus on the development of renewable energy projects. At the present time, Oman is looking to set up small scale pilot solar and wind projects and policies are being developed to support large scale projects and further research. A feasibility study for a large solar project was initiated in 2009. Oman has good solar and wind resources and it is believed there is great potential for CSP projects in particular. A mix of technologies is being rolled out and there is a supportive regulatory environment.

Strong ties

In a keynote speech Dr Noel Guckian OBE, HM Ambassador to Oman, stressed the strong ties between the UK and Oman, particularly in education, with 37% of Oman’s overseas students studying in the UK and all Oman’s English teachers having been taught by Leeds University. He referred to the 40/40 scheme that was supported by the British Government through British Scholarships for Oman. Dr Guckian encouraged British educational establishments to establish branches in the Sultanate.

The strong potential for cooperation in education and skills development was further discussed in a panel session moderated by Stephen Thomas OBE, CEO Renaissance Services. Oman’s Omanisation programme has been very successful but there is a continuing need to equip Omanis with skills to contribute to Oman’s growing and diversifying economy, to develop initiatives to create new jobs, and

Alan Duncan MP, UK Minister for International Development, addressing the conference

to promote SME development. There is tremendous scope for British companies to assist with capacity building to develop a skills base aligned to industry needs, for example in enhanced oil recovery, where new skills and competencies are required, tourism and hospitality, enterprise skills, English language skills and other areas relevant to the Omani economy.

The private sector is playing an increasing role in higher education, and there are opportunities both for the development of affiliations with private higher education institutions, and for the establishment of branches of UK universities, as well as in assessment and accreditation.

A panel session moderated by Alison Cryer, UK Director of Oman Ministry of Tourism Representative Office, discussed tourism and hospitality. Delegates were treated to a slide show illustrating Oman's amazing natural beauty. Tourism currently accounts for 2.9% of GDP and plays a valuable role in employment creation. Current levels are expected to rise, with arrivals growing at an average annual rate of 13%. Oman's commitment to sustainable development through tourism was underlined. A number of new hotels are due to open from 2012 onwards and forts are being renovated into boutique hotels. Oman Air's routes, with a growing fleet of long range planes, will bring tourist trade to Oman from all around the world, and Oman is working to develop markets such as Russia, India and China. The conventions and events side is developing as are cultural and niche tourism, with the Royal Opera House due to open next year and other international attractions being developed.

Making the closing speech, UK Foreign Office Minister for the Middle East, Alistair Burt MP, underlined the priority which the UK Coalition Government attaches to elevating commercial relations with the Gulf, mentioning that the conference fell during a week of Gulf-related activities. He noted that UK trade with Oman continues to rise – up by 46% over the first quarter of this year and by 61% since 2006. *"We want the UK to be Oman's - and the wider Gulf's - commercial 'partner of choice'"* he said. *"British business and expertise have much to offer the region."*

The conference was very well received, serving as an inspiring introduction to British companies new to Oman, while those already involved in the market appreciated the opportunity to meet up with Omani contacts. It was followed on Friday 22 October by business to business meetings at the Middle East Association offices, when members of the Omani delegation met with representatives of Middle East Association companies to explore partnership opportunities. ■

The Middle East Association is taking a trade mission to Oman from 4-8 February 2011. Contact Feride Alp (feride@the-mea.co.uk, tel: 020 7839 2137) for further information.

Middle East Association

Doing business in the Gulf

Alan Wood[1] is a Partner and Head of the Pinsent Masons' Corporate Group

This week I had the pleasure of speaking at the Britain in the Region event in Dubai[2]. The event attracted over 300 British companies and, although hosted in Dubai, allowed delegates access to UK Trade and Investment advisors and private sector experts from across the whole of the Middle East and North Africa region from Egypt in the west to Oman in the east. The event has been mirrored by events organised by other European governments and the US government to promote and assist their companies trading in and with the Gulf region.

The size of the event this year and the number of UK companies attending was a further sign of the growing importance of the Gulf region for many international companies. Indeed, at a time when the economic and business conditions for European businesses in their traditional markets remained extremely challenging, the opportunities for doing business in the Gulf region represent a significant opportunity for many to grow their business internationally and diversify their customer service.

> "As well as the opportunities in the Gulf region itself, the regions geographic location means that it is increasingly being seen and used as a hub for, and gateway into, the surrounding markets on the Indian sub continent and Africa"

Even a cursory look at the figures in terms of year on year growth in GDP for countries across the region and their respective plans for growth over the next fifteen years reveals the almost mind boggling aspirations they have for their economies. Those aspirations are typically set out in 2020 or 2030 growth plans and include a multitude of projects on the hard and soft infrastructure side, all aimed to enable countries in the region to attract an array of businesses across various sectors and so to reduce their dependence on oil and gas. For some in the region like Abu Dhabi, Qatar and Saudi Arabia this long term aim is being funded by current production, but for others, most notably Dubai, who have only very limited oil and gas reserves, the programme is having to be funded by the trade it intends to generate.

As well as the opportunities in the Gulf region itself, the regions geographic location means that it is increasingly being seen and used as a hub for, and gateway into, the surrounding markets on the Indian sub continent and Africa. Once again the opportunities those markets provide are staggering and so it is no surprise that the Gulf generally, and the lower Gulf in particular, has come to be known as the new silk road. So what do companies need to think about when considering whether to enter the Gulf region or, for those who are already operating in the region, taking those operations to the next level?

Like any international expansion, the process and pitfalls can appear daunting when encountered for the first time and clearly new entrants need to take their time and seek advice from those in the region to demystify some of the regional peculiarities and explain the process. They also need to recognise that whilst the legal systems adopted across the Gulf States are broadly similar (they are all based on a civil law system of Codes), there are differences between jurisdictions and nuances which need to be taken into account. One area where this is true is in terms of the degree to which Sharia law is applicable to businesses in different Gulf States.

For those completely new to the market there are various options for entering the market.

Agents and distributors

For many foreign companies the preferred way to start trading in the Gulf is to appoint a local agent or distributor to market their products. This approach has the added attraction of allowing foreign companies to draw on their local agent/distributor's connections and relationships in the region, and avoids the need to devote large amounts of their own manpower or capital to support the operation and develop their regional brand. Sectors where agents and distributors are particularly popular include automotive and retailing. For those looking at this option there are nonetheless some pitfalls to watch out for. Those issues include the agent/distributor's ability to deliver what they promise in terms of market penetration and the ability for the foreign company to end the arrangement if things do not work out as planned.

Deliverability

Invariably when talking to local agents/distributors they will promise much in terms of their ability to market and sell products and penetrate the local market. At this level this is no different to appointing agents/distributors anywhere else in the world and, as with all such appointments, that confidence needs to be tested to establish industry sectors and jurisdictions where the agent is particularly strong or weak.

The Gulf generally and indeed even the GCC remains a fragmented series of markets in terms of jurisdictions and so the right choice of agent/distributor for the UAE may not be the best person to market the same product in KSA or Qatar where their relationships and business connections may be less. Indeed, even within the UAE, foreign companies may find that an agent/distributor with strong connections in Dubai is far less well connected in Abu Dhabi.

Termination

What perhaps makes the issue of deliverability more important in the Gulf than in other regions is the fact that anyone looking to appoint an agent/distributor in the Gulf needs to understand their ability to and the cost of ending the arrangement, either after a period agreed at the outset or sooner if the agent/distributor is not delivering what they promised. The issue here is that in many Gulf States the agent/distributor will be a "local" and the laws have been drafted in their favour, either preventing termination or non-renewal or entitling the agent/distributor to compensation and an ability to block imports of a principal's product whilst any dispute is being resolved.

Foreign companies need to be particularly wary of commercial arrangements designed to avoid the protective aspects of agency laws in the region. Often, for example, a franchise arrangement designed to fall outside the ambit of agency laws will be treated as an agency agreement and so it is always advisable to have professional advice before committing to such arrangements.

Establishment

For those looking to go a step further and establish their own presence in the Gulf there are a bewildering number of choices which vary (at least in terms of terminology) between the different Gulf states. Business will be bombarded with references to mainland versus freezone entities, LLCs, WLLs, branches, representative offices and many others.

Again, the key is to take advice to establish what structure will work best for a particular company and to ensure that the proposed vehicle will enable the business to do what they want in the relevant jurisdiction.

A particular mental hurdle for many foreign companies looking to establish a regional company is the restriction on foreign ownership which still exists to differing degrees in different countries and industry sectors in the region. Whilst those restrictions have started to ease and look set to be relaxed further, they still apply in some of the key jurisdictions in the Gulf such as the UAE and are often a deterrent to foreign companies. Like many of the regional issues faced by foreign companies the issue need not, in reality, be as daunting as it first appears. A custom and practice has developed to allow compliance with the legal requirements whilst also accommodating the underlying intention of the foreign investors in terms of entitlement to profit and the management of the local entity.

For many the process of establishing their own entity in the Gulf proves to be somewhat of an endurance test. Certainly, foreign companies need to understand that, relative to the time and process involved with establishing a company in many western countries, the time and process involved in doing so in the Gulf is considerably greater. One particular example of this is the need for documents in relation to foreign companies to go through a process of being notarised and then legalised (both in the home jurisdiction and within the Gulf State where an application is being made), often by three separate government offices, and then having to be translated into Arabic.

"...laws have had to adjust to reflect the dramatic change in the size and nature of business in the region over the past three decades"

A final point to note is in relation to licensing. Typically in the Gulf, not only must a company be properly incorporated as a legal entity but it must also be properly licensed by the relevant government ministries. Licensing will take a considerable amount of effort on the part of a company in dealing with the generally numerous demands from government ministries to file and submit various applications and documents.

Joint ventures

It is certainly true to say that the Gulf retains a very strong relationship culture when it comes to business. This fact and the continued growth of regional companies who have developed a strong position in a number of sectors (for example, construction and telecoms) mean that many foreign companies see the best road to market their products or services to be to joint venture with a local company. Drive around any of the Gulf States and the signage on buildings, shops and showrooms illustrates this. An example is Carillion's joint venture with Al Futtaim in the UAE.

For those looking to joint venture or partner with local companies in the Gulf many of the issues which need to be considered will be the same as those discussed above in relation to the appointment of an agent or distributor in the region. Whilst the phrase is somewhat clichéd, overseas investors need to remember the old adage of "marry in haste, repent at leisure" since like the appointment of an agent or distributor, they are likely to discover that once they have chosen their joint venture partner they will face a number of legal and commercial obstacles if they want to make a change. One particular question to ask is what are the local JV partner's drivers for entering the relationship and what other joint ventures or agency/distributorships are they a party to.

Whilst other interests may demonstrate the strength of their knowledge of and relationship in the sector, foreign companies need to take care to ensure that those other interests will be complementary to and not competitive with the partners or agent/distributor's promotion of their business in the region.

For companies already operating in the Gulf there are other things to be aware of and these will include:

Bribery and corruption

As well as the regional challenges in doing business in the Gulf, companies operating in the region will also need to be aware of and comply with the laws of their home jurisdiction which have extra territorial reach and so which also catch their overseas operations.

In recent years the best example of this has been the impact of "domestic" legislation in relation to the prevention of money laundering and bribery and corruption on international companies operating in the Gulf. Whilst the provisions of the US Foreign Corrupt Practices Act and the UK Bribery Act applicable to those operating in the Gulf are the same as those applicable elsewhere, the application of those provisions raises particular questions in the Gulf where the gift and hospitality culture have long been a feature of the way in which long term relationships are developed and maintained and business undertaken.

Transparency and corporate governance

Perhaps because of the size of their markets and the astonishing growth they have achieved over recent years it is easy to forget that most of the Gulf States are relatively young countries. Whilst all have adopted a codified legal system and all of them also apply, to differing extents, Sharia law, their laws have had to adjust to reflect the dramatic change in the size and nature of business in the region over the past three decades.

In the area of transparency and corporate governance that adjustment is still very much a work in progress and foreign companies looking to enter or do business in the Gulf are often surprised by the paucity of publicly available information accessible to them. This lack of information often makes it harder for foreign companies to gauge the size of the market for their products or services or to undertake due diligence on their prospective local business partners.

In addition, one impact on the region of the global recession has been to highlight the need for countries across the region to impose greater corporate governance obligations. Despite the cultural preference of many regional companies to maintain privacy in relation to their businesses, the need for change is recognised in the region and there are increasing rules for banks. There is also an increased move by many large regional companies to adopt a best practice approach to corporate governance and so to voluntarily adopt UK or US policies and procedures.

Decision makers

Many foreign companies doing business in the Gulf encounter the regional peculiarity of dealing with an undisclosed decision maker to whom the person they have been dealing with, often over the period of a prolonged negotiation, ultimately has to defer to seek final approval before concluding a transaction.

Real estate

Across the Gulf States there is a requirement for foreign companies looking to establish a subsidiary or branch to lease or (where permitted) acquire premises. This is another area where the laws of the different Gulf States have had to adapt to reflect changes in business practices, and where further changes are planned by many states to ensure that they are creating as business friendly an environment for foreign investors as possible.

Getting paid

The issue of getting paid for products sold and services supplied in the Gulf region has been a concern for many foreign companies for a number of years. Whilst the risks of payment default have often been exaggerated and generalised, the global recession has impacted on the liquidity of many regional businesses and so the issue has become a very real one for many companies in a variety of industries. Particularly in the real estate and construction sectors, the lack of attention to this area encouraged by the boom years has left foreign companies unpaid and unprotected over the past two years.

Whilst here again the issue is not specific to the Gulf, there are aspects of it which are particular to the region due in part to the historic approach on name lending and in part to the relatively limited options in terms of security which are available to support loans or trade credit. In the construction sector, for example, it is typical for a sub-contractor to accept a "paid when paid" clause to the recovery of its fees from a main developer. In the good times this was reasonable as the payment was underpinned ultimately by a government-owned sponsor. In today's climate however companies need to be circumspect as the credit worthiness of such sponsors is not to be relied upon and as UK companies embroiled in the Nakheel/Dubai World saga will testify, a government owned company will not always be good for its money.

Those looking to operate in the Gulf need to ensure that they take proper advice on their contractual documents to ensure that it affords them as much protection as possible and to ensure that, if relationships do break down and litigation ensues, that they have a neutral and effective forum for resolving disputes. For many this will mean electing for international arbitration but care needs to be taken to ensure that any award received can then be effectively enforced in the region.

Conclusion

Despite the challenges and regional peculiarities the opportunities for foreign companies who enter the Gulf market are remarkable and, in truth, those challenges are no different to the challenges of establishing international operations in many other parts of the world. Whilst there will be many keys to creating a successful business in the Gulf from a commercial perspective, from a legal one the key is to take advice. That advice will be available from a variety of sources, be it through the foreign companies' own government agencies in the region, national or sector business groups and professional advisers. ■

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[2] Britain in the Region 2010, Wednesday 24 November 2010, Dubai

An introduction to an Islamic financial system

M Fahad Mehboob is Relationship Director - Islamic Finance at Europe Arab Bank plc

Introduction

Much has been written about Islamic finance in recent years, and there are detailed books on what is and isn't allowed to qualify as Islamic finance, but what has been missing is a more basic understanding of the objectives of having an Islamic financial system.

Most Islamic finance practitioners, and even people who are merely interested in Islamic finance know that the main concepts in Islamic finance are the prohibition of interest (usury), gharar (uncertainty), maisir (gambling) and investments in a range of prohibited activities such as casinos, gambling, pornography, alcohol related businesses, and interest-based financial services. The current state of the Islamic finance industry revolves around "inventing" (also known as structuring) ways and legal structures that comply with sharia in form, but not entirely in substance. At this point, it is fair to differentiate Islamic finance (the broader industry) from Islamic banks. Unfortunately, most Islamic banks have adopted a debt-based model, which in its form, is completely sharia compliant, but the essence of sharia compliancy is missing. This, among others, remains the primary reason that Islamic banking is labelled as "smoke-and-mirrors" by some experts and purists alike.

> **"The concept of leveraging is something that is inherently contrary to the risk and reward sharing virtues of Islamic finance"**

Money – a sharia perspective

Reading through numerous books on Islamic finance, it is evident that sharia treats money itself as a "means of exchange" and not a product that can be traded. The very essence of conventional banking is that money itself is a product, which you can buy and sell at different rates, and in simple terms, make money from money. Under Islam, money is considered an 'amanah' (trust) from Allah, which implies that it does not belong to the individual who has possession of it. He is merely holding it in trust for future generations and for the betterment of society. Furthermore, the individual is answerable to each and every penny given to him by Allah, and does not have the right to demand a return on the money that does not belong to him in the first place, unless he is willing to take the underlying risk along with it.

Conventional banks operate on the basis of borrowing from their customers and the financial markets at a cheaper rate, and along with their own equity, lending the funds at a higher rate to their borrowers, hence leveraging. The concept of leveraging is something that is inherently contrary to the risk and reward sharing virtues of Islamic finance. However, we see that Islamic banks are no different in terms of their overall leveraging strategy, whereby the Islamic banks will use their cheaper clients' deposits and lend to their customers at a higher rate, albeit all based on sharia compliant underlying structures.

Islamic finance industry – going forward

With all the advancement in Islamic finance, especially in the last 30 odd years, and with all due respect and gratitude to the Islamic banking pioneers, perhaps it is time to move Islamic finance in a direction where it is not about replicating conventional products, but a meaningful effort is made to adhere to the principles of sharia in both form and substance. The changes required will be drastic and substantial.

As a start, the three main products Islamic banks should be offering on the deposit side are:

i) Physical cash deposit facilities

ii) Mudaraba/wakala based deposits

iii) Musharaka based deposits

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i) Physical cash deposit facilities

As the name suggests, this would be a simple cash-deposit safe keeping facility, very much keeping in view the prohibition of riba, but also the practical requirement of keeping one's wealth safe. There will be no "profit" paid on these amounts, and the bank will not be able to utilise the funds for its own business. It will, however, be able to charge the client a fee for safe-keeping the cash deposited with the bank.

This particular facility would go against everything fractional reserve banking teaches us, and without going into too much detail, one of the objectives of an Islamic financial system would be the avoidance of a fractional reserve banking system, ultimately. It would also encourage the banks' customers to utilise more of the musharaka or mudaraba based structures.

ii) Mudaraba/wakala based deposits

These are almost like asset management type structures, where the depositor acknowledges the banks' expertise in investments in certain assets, and would like to appoint the bank to manage his funds by investing in certain sharia compliant assets. Again, given the nature of the current lending practices where most of the assets in Islamic Finance are debt-based, initially these deposits will be utilised to fund debt-based sharia compliant structures (such as current sukuk, ijara and murabaha etc) and later developed into managing equity-type investments.

As in asset management, the depositor will take the underlying risk on the project/investment and will have limited recourse to the mudarib/wakil (asset manager). The client will benefit from all the returns from the underlying investment, subject to a management fee charged by the bank as wakeel, or a profit share as a mudarib. This requires a significant change in the mindset of the current Islamic banks' depositors, but is achievable provided the right asset managers with a proven track record.

iii) Musharaka based deposits

Many will argue that musharaka is the ideal Islamic Finance product, but given the current financial system and the risk mitigating mind-set of investors means that musharaka is only utilised by a very small minority. musharaka, or partnership, in essence, is a direct risk sharing structure where two or more than two musharaka partners share the risk based on their respective investment, but the rewards can be shared in any predetermined manner. A musharaka deposit would allow the banks' clients to enter into a risk-reward sharing agreement individual projects/investments, or more generally, allow the depositor a return based on the profits of the bank, hence making a musharaka deposit akin to an equity investment.

Again, as briefly stated, this would require a very significant change in the mindset of the current Islamic investors, but can be achieved if a musharaka based deposit is compared to equity investments.

Significant work will need to be carried out if any of the above products ever become a reality, but in addition to the current debt-based sharia compliant products, these will be a much needed alternative to the Islamic finance purists, who are not comfortable with the debt-based nature of the current Islamic banks.

On the lending side, again, the Islamic banks currently rely on debt-based structures such as murabaha, ijara and asset-based sukuk. This will also need to change with Islamic banks taking on underlying asset/project risk, and not just relying on the credit worthiness of the borrower. It will also mean that the banks employ people with a completely different skill-set, one which is more suited to a venture-capital or equity-type investments profile.

Conclusion

The Islamic finance industry is fast approaching a $1 trillion in assets, and yet, for all the innovations and sharia compliant structures, the practices of some Islamic banks still get referred to as a "sham" by not only conventional financiers, but by a majority of Muslims. It is high time that we move the Islamic finance industry towards a direction where equal emphasis is given to both form and substance of a transaction. This will require much needed efforts on educating the general public, who currently rely solely on the fatwas issued by the sharia boards of the Islamic banks or Islamic windows of conventional funds. Until the general public de-couples itself from the current conventional financial system and is willing to put "faith" in a riba-free financial system, we will continue to see Islamic banks replicating the conventional riba-based products and we will continue to accept them as "innovation". ■

The views expressed in the article above are the authors own, and may or may not reflect the views, opinions, policies, objectives or practices of Europe Arab Bank plc.

Largest ever UK trade delegation to Iraqi Kurdistan

David Lloyd, Senior Consultant at the Middle East Association (MEA), led a trade mission to Iraqi Kurdistan from 17-21 October, the focus being the Erbil International Trade Fair. Sir Andrew Cahn, Chief Executive of UK Trade and Investment, led a VIP delegation to the event. UK Trade & Investment, British Expertise, exhibitors and the MEA made up the mission which, at full strength, comprised 53 delegates representing 35 British companies, making it the largest British delegation ever to visit Iraqi Kurdistan. Nine companies, including several MEA member companies, exhibited at the Trade Fair, where a UK Pavilion represented the first official British presence at an exhibition event in Iraqi Kurdistan.

The mission was a resounding success, and the Trade Fair was very well attended. JCB had a loader on display and Landrover, which set up an agency in Erbil last April, had models on display and sold half a million dollars worth of vehicles during the Fair. Prime Minister Barham Salih and President Barzani toured the British Pavilion, and Sir Andrew Cahn received the President.

New benchmark

"I would like to think that this mission, which unquestionably had an impact on the Kurdish business community, has set a new benchmark for the presence of British companies in the Kurdistan region," said David Lloyd, who has led several MEA missions to the region over the past two years. *"The majority of mission members were new to the market and all were impressed by the market potential and the ease of doing business in this peaceful and prosperous region of Iraq."* All mission members are planning to return, and some are planning to open offices in Erbil.

The MEA has been at the forefront of British industry's engagement with Iraqi Kurdistan, being the only organisation in the UK to have led twice yearly missions there over the past three years. The presence at the Trade Fair of Sir Andrew Cahn, who undertook a punishing schedule of top level government meetings and site visits, was therefore very gratifying. *"There could not have been a stronger endorsement of British intent to take the Kurdistan market seriously and to send a forceful message to would-be British exporters to get out there fast,"* said David Lloyd.

A number of British companies have made their mark in Iraqi Kurdistan, including TRW; HSBC; Scott Wilson, which designed the new Erbil International Airport; Costain; Parsons Brinckerhoff, which is working on an electricity masterplan; Consultancy for Conservation and Development, which is working on the masterplan for the renovation of the Citadel; and the UK National School of Government, which has been advising the three governorates. UK Filter, which is involved in water management, and MCI International, which had stands at the Fair and have taken part in earlier MEA trade missions to Kurdistan, are now doing serious business there.

Iraqi Kurdistan offers tremendous opportunities to British companies across all sectors of the economy, from oil and gas to education, IT and telecommunications, power, environment and water, agriculture and financial services. Expertise and consultancy are required in all areas. There is a tremendous amount of construction and infrastructure development taking place, with a high level of investment from neighbouring countries. Relatively safe and secure, the Kurdistan region is a gateway for western companies to do business in Iraq. Its investment law, one of the most business-friendly in the region, offers foreign investors a number of incentives, and there is much goodwill towards the UK and a desire to see further British involvement. However our competitors are there in force – Turkey was by far the largest exhibitor at the Trade Fair and most of our leading EU competitors had impressive stands. British companies need to make up for lost time and take advantage of the opportunities offered by this stable, resource rich, emerging market. ■

In partnership with the Kurdistan Regional Government, the Middle East Association is taking its ninth trade mission to Iraqi Kurdistan from February 27th to March 4th 2011, with an opportunity to extend the mission until March 6th to coincide with the Erbil Building Trade Solo Exhibition. For more advice on the Iraqi Kurdistan market and the trade mission, please contact David Lloyd at the MEA (david@the-mea.co.uk or +44 (0)20 7839 2137). For a Mission Prospectus, email mea@ctgrouptravel.co.uk.

Fact and figures

Iraqi Kurdistan is an autonomous region of Iraq.

Population: 4.9 million (2007)
Area: 40,643 sq. km
Capital: Erbil (also known as Hewler)
Languages: Mainly Kurdish, Turkmani, Arabic, Armenian and Assyrian in some areas
Natural resources: Oil and other minerals; agriculture

Website of Kurdistan Regional Government: www.krg.org

David Lloyd (front row, fourth from right, light blue blazer) with mission members

MEA business briefing highlights Turkey's huge business potential

The Middle East Association held a very well attended business briefing on Turkey on Monday 11 October. It began with a video message from Prime Minister David Cameron, who has dubbed Turkey 'Europe's BRIC' and wants to double the level of the UK's bilateral trade with Turkey over the next five years.

Sarah Mooney, Head of UKTI Istanbul, highlighted Turkey's large and young population of over 76 million, its tremendous growth potential, diversifying economy, economic stability and openness to trade and foreign investment (the OECD estimates that it will be third fastest growing country after China and India by 2017). She also highlighted the importance attached to education and the growing skills base, the keenness to embrace the latest technology and the international outlook of its population, and discussed opportunities in a wide range of sectors, from software and construction, to defence, railways and marine and third country projects. She advised companies to be aware of the hierarchical business structure, the importance of identifying key decision makers and the importance of relationship building.

Yuksel Akca, Chief Commercial Counsellor, Turkish Embassy, highlighted Turkey's strategic position with access to a 1.2 billion market and its role as an energy hub, with a number of natural gas projects being developed. He highlighted Turkey's healthy economic position and its industrial strength, its various attractions for investors and its unique business environment as a result of its customs union with the EU and free trade agreements with various European and Middle Eastern trading partners. He gave an analysis of Turkey's trade with the UK.

Fadi Hakura, Turkey specialist at Chatham House, commented on the move from low productivity industries to high productivity industries and predicted that Turkey should enjoy high growth levels at its current rate of economic development, although structural reforms and improvements in the business regulatory environment are still needed.

Mina Toksoz, Head of Country Risk, Standard Chartered, argued that Turkey has weathered the global economic crisis well and is experiencing a strong domestic led recovery in 2010. The outlook for 2011 is broadly positive, although fiscal transparency needs improving and political risk remains an issue. The 2011 election will be critical.

Fact and figures

- Turkey is the 17th largest economy in the world and the sixth largest in Europe, with a GDP of $580 billion
- The OECD estimates that Turkey will be the third fastest growing country in the world after China and India by 2017
- GDP is forecast to rise by 7.5% in 2010
- Turkey is the EU's 5th largest export and 7th largest import partner
- UK-Turkey bilateral trade amounted to £6.6 billion in 2009
- UK exports to Turkey amounted to £2.3 billion in 2009 and increased by 26% in January-May 2010
- Turkey is the third largest exporter and producer of home textiles and the fourth biggest manufacturer of clothing
- Turkey is second ranked country in the top 225 international construction companies list, with 17 companies represented
- 65% of industrial exports from the MENA region originate in Turkey
- Over 2,000 British companies operate in Turkey

Brian Dent, International Trade Adviser, London International Trade Team, outlined the ways in which UKTI can help exporters to Turkey. Alan Stevens, Managing Director, Vector Consultants, which has an operation in Turkey, highlighted some of the diverse opportunities, from competency assessment programmes and HR services, to manufacturing, purchasing and supply chain and using Turkey as a regional hub. He discussed some of the challenges, and some of the factors behind the company's success, which include having a good local partner, a presence on the ground and an awareness of local culture and history, and making a contribution to local society. ■

For further information on Turkey and the Middle East Association's Turkey-related activities, contact Feride Alp, tel: 002 44 (0)207 839 2137, email: feride@the-mea.co.uk.

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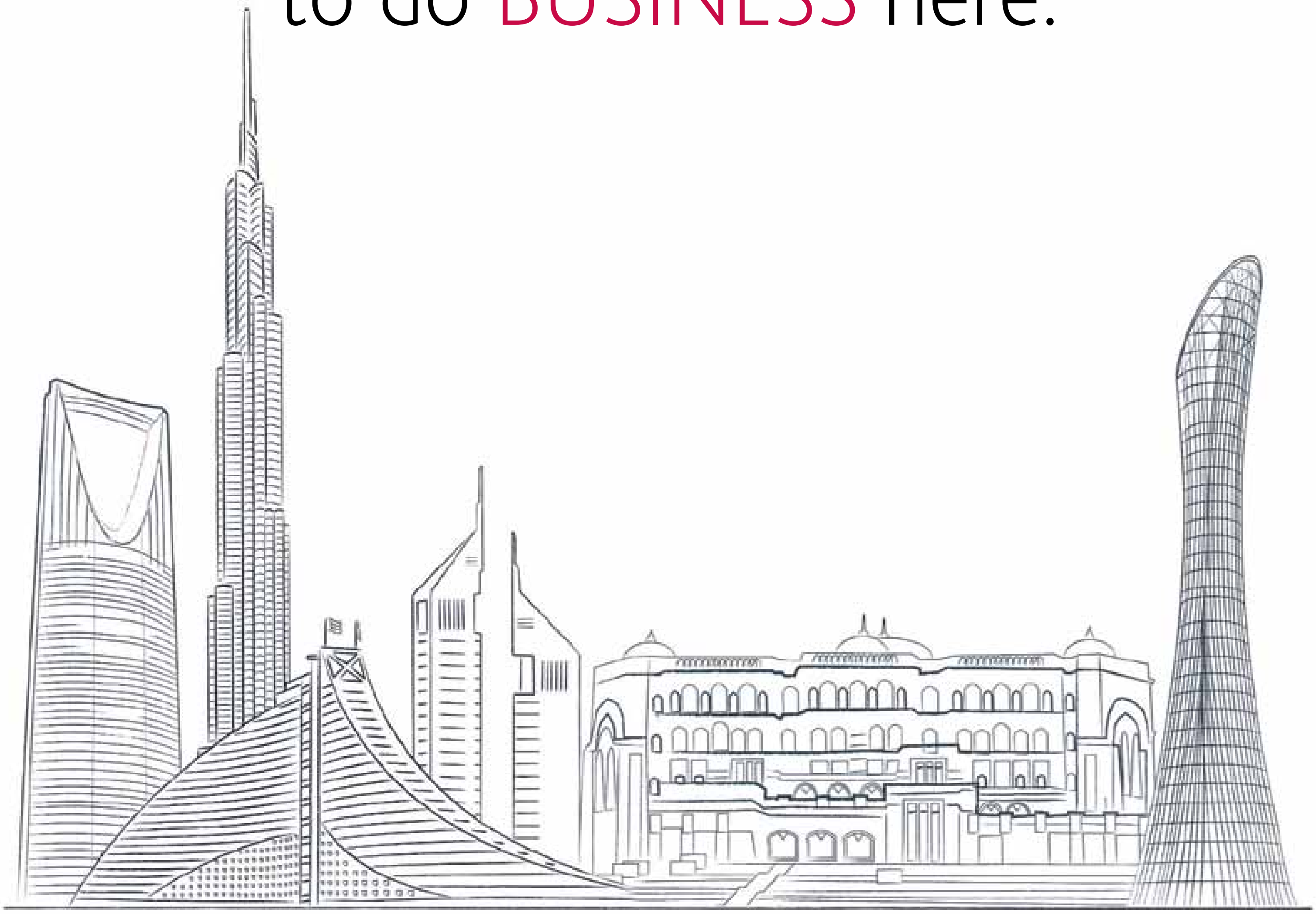

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to-day administrative functions. The Department of E-Commerce is responsible for developing and maintaining strategies and policies related to the .bm ccTLD.

The creation of the new Board stemmed from a number of important changes occurring internationally to key components of the internet's infrastructure, intended to increase the security, stability and resilience of this shared global resource.

These changes include: the introduction of version 6 of the Internet Protocol (IPv6); extensions to the security specifications for the Domain Naming System (DNSSEC), which addresses internet security and stability concerns caused by a proliferation of malicious activities; and the introduction of new TLDs, including internationalised TLDs that will empower the entire world's population to use the internet's domain name system in their native language.

The .bm Board in Bermuda is being structured as a public-private partnership chaired by the Department of E-Commerce, with representation from: the Registry General, ITO, the Departments of E-Government and Telecommunications, the Internet Service Providers and the ICT industry. The business community and the interests of consumers are also to be represented.

The core governance features of Bermuda's PAB include a charter that would require regularly scheduled meetings and suitable safeguards to ensure that the PAB operates in an open and transparent manner.

The PAB will help to provide recommendations and advice in connection with other policy matters related to the .bm domain and will also be tasked with producing an annual report of its activities, thus ensuring the openness, transparency and inclusiveness of its operations to the Bermuda internet community, in accordance with best in class practices employed by other ccTLD managers.

Internet addresses

Two types of IP addresses are in use today on the internet: IPv4 and IPv6. IPv stands for Internet Protocol version and is the Internet Layer Protocol for packet-switched internetworks and the internet. It is a fundamental principle of the internet's architecture that each host computer has a unique IP address. This system guarantees that the data packets sent or requested by a user in the course of browsing or using email will arrive at their intended designation — regardless of where on the planet the user and host computer happen to be.

IPv4 was the fourth generation of the Internet Layer Protocol, but the first to be widely deployed. IPv4 addresses are usually written in a dot-decimal notation (eg. 192.168.100). The addressing scheme permits a maximum of slightly more than 4.2 billion address spaces. Large though this number sounds, the amount of unallocated IPv4 space is quickly being used up and some experts estimate that it will be exhausted during 2011.

IPv6 is the next generation Internet Layer Protocol and was designated in December 1998 by the Internet Engineering Task Force (IETF) as the successor to IPv4. IPv6 uses 128-bit numbers will permit more than 340 quintillion addresses.

Assigning names and numbers

The internet has evolved from a computer network with its foundations in the US into a global communication medium. Bermuda, having one of the highest internet and broadband penetrations in the world and with so much of its economy dependent upon all types of electronic communications, is particularly sensitive to any material changes that may occur.

The Internet Corporation for Assigned Names and Numbers (ICANN) is responsible for the technical coordination of the Internet's unique identifiers: top-level domain names, such as .bm, and Internet Protocol (IP) addresses.

International organisations such as the EU, the International Telecommunication Union (ITU) and others are paying close attention to these changes to the internet's infrastructure and related issues. It is critical that Bermuda is engaged with these changes, because they will likely have a direct and material impact on the future of the internet within Bermuda.

In anticipation of the proposed changes, the Department of E-Commerce has been actively monitoring these developments within ICANN's Government Advisory Committee (GAC) — as the only Overseas Territory participating, as part of the UK delegation.

Naming the domains

Prior to the implementation of the Domain Name System (DNS) in the mid-1980s, internet users either had to type in an IP address for every website (and service) they wanted to access, or rely upon a HOSTS file — a list of host computer names and their corresponding IP addresses — that the user had to download regularly. As the number of internet users and hosts grew, this solution did not scale up.

The DNS is a set of protocols and services that allows user-friendly names when looking for other host computers, instead of having to remember and use the IP addresses for those hosts.

There are almost 300 top-level domains within the internet's domain name system. The majority, more than 250, are ccTLDs. Others include generic top-level domains and internationalised ccTLDs. The number of TLDs is likely to expand exponentially in connection with a number of initiatives that ICANN has undertaken.

As the internet evolved into the ubiquitous global communication medium that it is today, the inability of a large portion of the global community to use non-Latin and extend Latin scripts (ie. languages that cannot be directly represented with the US-ASCII character set) in the domain name system represented a fundamental problem.

Over the past decade, efforts have begun within the technical community to provide an Internationalised Domain Name (IDN) solution that scales on a global platform, while preserving the uniqueness of the naming and numbering system upon which the Internet is founded.

ICANN is also involved in coordinating the deployment of the IPv6 address space as the existing IPv4 web address space is exhausted. In May 2008, the importance of this issue was documented in a 2007 OECD Ministerial Background Report entitled *"Internet Address Space: Economic Considerations in the Management of IPv4 and in the Deployment of IPv6"*. The OECD reiterated the need for governments and business to tackle the internet address shortage together.

"Given the importance of the internet to business and the continued need for Bermuda to be seen as a jurisdiction which takes the security and stability of the Internet seriously and is business friendly, there needs to be a mechanism which allows for business input into the policy development process of the .bm ccTLD," Minister Minors said. *"Our international financial services sector in Bermuda relies heavily on the Internet to manage its global operations. It is therefore of utmost interest to the business community that the .bm domain is robust and secure and that the telecommunications infrastructure is evolving to keep up with the changing technical standards."*

Other initiatives

Bermuda has also taken a continuing leadership role in other international technology fora, including the hosting of the World Information Technologies Services Alliance (WITSA) 2009 Global Public Policy in Bermuda in November 2009, which was attended by many delegates from the global ICT community. In 2010, the Bermuda Government was recognised by WITSA with a special" ICT Industry Award", for efforts to encourage the development of the global ICT sector.

"The modern world moves at a very fast pace," Minister Minors noted. *"Bermuda is established as a market leader in several areas of international commerce, and will only retain that role if we stay on top of developments in the electronic world, and contribute to the debate. The Internet Policy Advisory Board is but one initiative we are undertaking to ensure that business is engaged as developments occur. No one should doubt Bermuda's seriousness in providing a platform for international business."* ■

Bavaria: the perfect location for Chinese R&D

The world today is rapidly changing. New technologies and innovations are discovered and implemented at a faster and faster pace. That means that enterprises as well as governments need to constantly be aware of future trends and breakthroughs. Not keeping pace with advances now can lead to serious economic problems in the future.

China has understood this need. Today it is quickly developing from the world's "workbench" into a high-technology nation intent on establishing long-term economic foundations. Its people have proven that they well understand the Chinese proverb: "When the wind rises, some people build walls. Others build windmills." To that end China has seen the need to be present on the international market where it can also benefit from research and technology transfer.

At the heart of technological innovation is research and development, and in this Bavaria – often referred to as the Silicon Valley of Europe – offers China invaluable synergies. It not only provides high innovation potential and is one of the most important research areas in the world, but it is also geographically right in the heart of Europe. Thus it is a convenient gateway to central as well as eastern European markets and allows Chinese companies to be in close proximity to their customers. In the state alone, companies have access to over 500 million consumers.

In addition, Bavaria's industries are highly productive and stable, a necessary prerequisite for building long-term cooperation. The reason for that is manifold. First of all there are a large number of academic institutions in Bavaria, ensuring a highly qualified workforce and potential for in-depth research and development. Secondly, an abundance of cluster initiatives and business networks support partnership and knowledge transfer. The Bavarian government also vigorously supports Chinese researchers with setting up business operations and identifying optimal locations. And Bavaria enjoys an extremely powerful economy with state-of-the-art energy, transportation and telecommunications infrastructures.

Chinese investors and businesses have already begun to discover Bavaria as a valuable partner. Chinese-German bilateral trade has increased tremendously over the last five years and the trend does not seem likely to end anytime in the near future. In 2009 that figure amounted to about 18.4 billion euros, or 7.8% of the entire trade volume of Bavaria. In 2008, China overtook Japan as the region's most important Asian trade partner. Today, imports from China have taken the number 2 position, after Austria – and before Italy and the USA.

Bavaria has a close and fruitful relationship to China, not only economically but also politically and culturally. It all started 23 years ago with the efforts of the Bavarian Minister President Franz Josef Strauss. He was instrumental in establishing the partnership between Bavaria and the province of Shandong in 1987. Early on, both sides declared their intention to cooperate on economic and technological matters. In 2004 another partnership was initiated with the province of Guangdong, and later 17 additional community partnerships were established. Especially important to future research cooperation are the partnerships with 103 universities.

Bavaria takes care to nurture the partner programs by travelling every year to China with business representatives, especially to Shandong. It also invites a number of delegations from China to Bavaria. Those visits include stopovers at both Bavarian and Chinese companies.

Today there are almost 2,000 Bavarian companies with business relationships in China. Those include some of the world's largest enterprises such as BMW AG, BayWa AG, MAN Nutzfahrzeuge AG, Siemens AG, Bosch Rexroth AG, Krones AG, Osram GmbH, Rehau AG & Co, Schaeffler Holding GmbH & Co. KG, and ZF Sachs AG.

Strong appeal for Chinese investors

Conversely, Bavaria is attractive to Chinese companies in part due to its economic power. The state has the highest purchasing power in Germany and the 8th largest economy in Europe with a €430 billion GDP. In October 2010 the unemployment rate in Bavaria was a mere 3.8%, the lowest in the entire country. Economic experts predict that growth in Bavaria in the next years will be higher than in any other state, with an average GDP increase of 1.2%.

In addition, Germany has the largest national economy in Europe and the fourth largest (by nominal GDP) in the world. The service sector contributes around 70% of the total GDP, industry 29.1%, and agriculture 0.9%. All of that translates into a fertile region for the growth of research and innovation endeavours.

Manuel Rimkus, head of State of Bavaria China Office in Qingdao, is convinced that Bavaria and China will see even more cooperation in the areas of research and development in the coming years. He especially sites China's newly initiated 5-year plan to drastically reduce carbon emission as a positive indicator that *"Chinese businesses will even more actively discover Bavaria as a research site."*

For those businesses concerned about protecting their intellectual properties, Rimkus counters with a logical argument. He states that

Bavaria: In the heart of Europe

when businesses cooperate on research and development, both will have a keen interest to safeguard their innovations and know-how. He believes that by working together *"solutions for know-how transfer can be found, that are advantageous for both sides."*

A major step into opening the research landscape even further is the joint project "Trans-European Train", which contains plans to start a direct freight train connection between Bavaria and China. The 10-thousand kilometre route would make travel from Shanghai and Peking to Nuremberg possible in only 17 days. Since a container ship needs 30 to 35 days, this train would impressively cut the travel time in half. Five test runs have already been successfully undertaken.

Garching Forschungszentrum: subway station to one of Bavaria´s leading R&D centres

Many Chinese companies – as well as Bavaria itself – have benefitted from the location of their business or subsidiary in the region. Some examples are Huawei Technologies, ZTE, Pearl River, China Eastern, Air China and Yingli Solar. Huawei Technologies is a world leader in the network and telecommunications fields and has been particularly successful in recent years. It was able to create a brand new centre for research and development, thus expanding its business and generating new jobs.

Bavaria's Minister of Economic Affairs Martin Zeil said Huawei's achievements even in the economically difficult times of the last year *"highlight the attractiveness of Bavaria."* Managing Director Peng Wei explained the expansion in Munich as a way to *"even quicker and more efficiently respond to the wishes and needs of our clients."*

Germany
Bavaria

One of the most positive acquisitions from a Chinese company can be seen in the example of Waldrich Coburg. This traditional company produces large, precision machine tools and is in fact a world leader. After being taken over in 2005 by the Beijing No. 1 Machine Tool Plant, it has seen earnings triple and 50% more employees hired. Contrary to the worries of some in those early days, there have been no mass layoffs and no production relocations. In fact, a new production hall has been built right in Coburg itself.

High-tech, high potential

With more and more Chinese companies moving from subcontractors to solution providers, Bavaria provides chances for the mutual benefits of intellectual cooperation. Especially in the high-tech and research sectors, Bavaria already has a strong reputation in China as a region of innovation and quality. Many Bavarian enterprises are global players and known the world over. These include Siemens, Osram, MAN, Wacker, BMW, Audi, The Linde Group, EADS, Adidas, Puma and many more.

More than one third of German DAX companies are located in Bavaria. However, 95% of all business in Bavaria is made up of mid-sized and small companies, thus providing a rich and diverse industrial population. Bavaria is home to some 650,000 SMEs in 19 different fields of competence such as ITC and bio-, medical-, energy and environmental technologies. Thus Bavaria has proven itself to be attractive to companies of all sizes.

The success of Bavarian enterprises is due in part to a highly skilled workforce and synergies provided from the many universities and research centres in Bavaria. Those include 9 Fraunhofer Institutes, 11 universities, 17 universities of applied sciences, 12 Max Planck Institutes, 3 Helmholtz research centres 10 research and transfer centres and 9 research associations. The benefits of this concentration of research institutes are apparent for any company considering locating in Bavaria.

Many significant inventions have come out of Bavaria. As far back as 1892, the diesel engine was conceived in Augsburg. In 1953 the first soccer shoes with studs. 1969 saw the development of the chip card in Munich. And the mp3 format? That came to the world from Bavaria in 1994, as well as Wi-Fi TV in 2007. In fact, each year more patents are registered within Germany than in any other country in the European Union. And more patents are registered in Bavaria than any other German state. In 2009 alone 12,641 patent applications were received by the German Patent Office – also appropriately located in Munich.

Adding to the attraction of Bavaria as a research centre is also its premier location in Europe. The Munich Airport is no more than a 3-hour flight away from over 30 major European cities. The airport provides a multitude of direct flights to China including 11 weekly connections to Beijing, seven to Shanghai and seven to Hong Kong.

Bavaria also boasts an extensive transportation network. That includes over 137 thousand kilometres of modern road networks and a railway system with over 6,600 kilometres. Easy access to both the North and Black Seas can also be found over the Rhine-Maine-Danube waterway.

Completing the network are the four cargo transport centres in Augsburg, Ingolstadt, Nuremberg and Regensburg.

Bavaria has a lot to offer Chinese businesses, in the area of R&D and business opportunities as well as in standard of living. Bavaria is one of the statistically safest regions in Germany. That is no doubt in part due to the high per capita GDP of €34,397, which is much higher than the German or even the European average. Within more than 70 thousand square kilometres Bavaria also offers many leisure and recreation activities. The legendary Neuschwanstein castle can also be found there, as well as the Bavarian Alps and the Bavarian Forest.

That Bavaria has been able to attract Chinese business is no accident. Bavaria's state government provides businesses with extensive support measures including a strong cluster offensive and innovation initiatives. The cluster management teams work to strengthen and enlarge networks between businesses, research institutions, investors and service providers.

The state of Bavaria specifically provides support in the area of research through a large number of research consortia. Thus exchange is enabled among companies, research institutes, institutions of higher education and other players.

The Bavarian Ministry of Economic Affairs also runs a business promotion agency called Invest in Bavaria. It assists foreign investors with working permits, business expansion, integration, real estate search, connection to networks and contact with government agencies. In addition it provides market information, branch analysis, site visits, proposal of locations and helps finding business partners. All of its services are free of charge, and – as they point out – also fast and confidential.

In addition, Invest in Bavaria offers a comprehensive Chinese-language website for potential investors. It has a presence in Qingdao, China and a Chinese staff member in its Munich office. The agency also organizes seminars and initiates targeted promotion campaigns to promote Bavaria – something which all businesses in the region benefit from.

Laptop and lederhosen. That's how Bavaria has often been described. Full of tradition and culture on one side, with Sissy, Ludwig II and high-spired castles. On the other side one of the strongest business locations in Europe with many high-tech companies and important research and development centres. Businesses have been attracted to the region and enjoyed subsequent success due to its high innovation prospectives, strategic location, potential for technology and know-how transfer, and network and cluster initiatives. It is clear that Bavaria is a high-tech location offering synergies in the areas of research and development that cannot be overlooked – thus making it the perfect location for forward-thinking international companies and research institutes. ■

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The use of hybrid legal entities in group structures of multinational enterprises, Part IV

Jos Peters is the Senior Tax Partner at Merlyn International Tax Solutions Group

In several previous issues of WCR we have described how hybrid legal entities could be used to reduce the worldwide corporate income tax burden of a multinational group, as a matter of legal principle. In this issue we will describe, at the request of several readers who have commented positively to my earlier articles, a detailed example of what is possible with hybrid entity tax planning in day to day tax practice.

The use of two hybrid Dutch entities for a chemicals production company that wants to enter Europe in various countries simultaneously

Phase one: avoiding exit tax upon IP transfers to the new jurisdictions

This case involved a company in a high tax jurisdiction that was considering start-of-production locations for their chemical products in various European countries. The company is profitable in its home country and seeks to avoid additional tax there on income related to the transfer of the intangibles it uses at home to the new European production locations; in addition it is interested in keeping foreign profits tax low. Can the Netherlands play a role in the tax planning required?

The first issue to address is clearly to avoid taxation on the transfer of product technology and production technology plus a marketing intangible (the "client list") from the parent company of the group to the new production locations. An immediate and taxable capital gain on such transfer can be avoided by transferring the intangibles mentioned to newly set up foreign subsidiaries against an "arm's length" royalty payment but this would still risk additional taxable income, as of day one, in the home country of the parent whilst the new subsidiaries will generate start-up losses so the tax deductibility of their royalty payments do not reduce foreign tax for a number of years.

An exit charge on the IP in the group's home country could perhaps be prevented by using a hybrid legal entity to transfer the IP to: this entity should form a so-called "permanent establishment" of the parent company abroad, which would avoid the exit charge because no transfer to a separate legal entity will take place under the home country's tax laws. If this could be coupled to a situation whereby the foreign operations are seen, under the tax rules of the country at the receiving end of the IP transfer, as a "tax entity" one might be able to get a so-called "step up in basis" for the IP which it receives from its foreign parent. Can such a hybrid entity ("permanent establishment" [non-resident tax payer] as seen from the parent in the group, local tax payer as if it was a separate entity [resident tax payer] as seen from the subsidiary itself) be structured in a country which will also allow other multi-country tax benefits? This question was asked by the foreign parent company to several tax advisers in European countries, including to me.

My answer for the Netherlands, but form a multi-country investment purpose, was as follows:

> A Dutch "Cooperative Association"' could well be the hybrid instrument to look for. It has all the hallmarks of a partnership under the tax laws of many foreign jurisdictions, which gives rise to a tax treatment in the home country as a foreign permanent establishment, but nonetheless, from a Dutch corporate income tax viewpoint it is an entity subject to tax itself: the "members" or "partners" will not become taxable in the Netherlands. The Coop will be treated like a Dutch limited liability company (see *WCR December 2009*[1]).

If a Dutch tax entity acquires IP for book value, this will have to be disregarded for Dutch corporate income tax purposes: assuming that the fair market value of the IP transferred (product technology and production technology plus one or more marketing intangibles) exceeds the book value for which the transfer will unavoidably take place, the Coop can take this difference into account in a tax favourable manner in Holland:

> The Coop may capitalize the entire fair market value (to be established on the basis of a transfer pricing report) in its tax balance sheet and depreciate it over the useful economic lifetimes (each IP element may have a different life cycle in this respect). Dutch case law holds that a transfer of a business asset between related parties for a "wrong" price can analytically be seen as 1) a transfer against the right price, in combination with 2) a gift by the parent to the subsidiary of the excess;
>
> An "advance tax ruling" is normally available in Holland to determine, at the outset of the new structure, what amounts the Coop can show as annual tax depreciation in its corporate income tax filings.

Once the above has been completed successfully, the group may, depending on its home country system to avoid double taxation:

> 1) Have avoided an immediate increase in its home country taxation because of the transfer of the intangibles;
> 2) Maybe also have avoided a future, annual, increase in its home country taxation because of the IP transfers;
> 3) Whilst at the same time safeguarding a meaningful tax deduction in the country to which the IP was transferred, if needed via tax loss carry forwards in case the Coop would run into start-up losses as is not unusual when starting up new business sin a new jurisdiction.

My advice, obviously, did not cover the home country tax system of the parent in the group. The obvious tax questions, to be answered by home country tax counsel or the in-house tax department, will have to focus on the ways in which a transfer of IP to a foreign partnership such as a Dutch Coop will affect taxable profit, not only upon the transfer but also in future years. How does the home country tax system deal with foreign "branch" profits? Will they be exempt? Or will there be a credit for the foreign tax incurred? This is beyond the scope of this article, however.

Phase two: expanding the tax effective IP usage to other European countries

The client clearly wanted to set up businesses in several European jurisdictions in a tax effective manner simultaneously, so the tax planning continued. Could we use the IP, transferred to a Dutch hybrid Coop, in other European countries as well and would some further creative tax structuring be possible with the Dutch Coop as the starting point?

In an earlier article (*WCR March 2010*[2].) we have discussed the possibility to make a Dutch BV disappear for tax purposes in Holland, whilst it did not disappear in other European countries where it did business. A simple but real hybrid entity therefore. The foreign European operations would then either need to take the form of genuine branch offices (permanent establishments) which is not a rocket science assignment, or one could work with foreign hybrid LLP's (the subject of another earlier WCR article I wrote, see *WCR June 2010*[3].). Such LLP's would be tax transparent in the countries of operations but Holland would treat them as foreign subsidiaries under the somewhat peculiar Dutch "foreign entity classification rules" in its Corporate Income Tax Act, which distinguishes between so-called Open Limited Partnership and Closed Limited Partnerships for Dutch purposes. But my country uses these same rules to classify foreign "joint venture" models, to distinguish them between foreign "quasi-subsidiaries" and foreign "quasi-branches", regardless of how the country of operations classifies these LLP's itself.

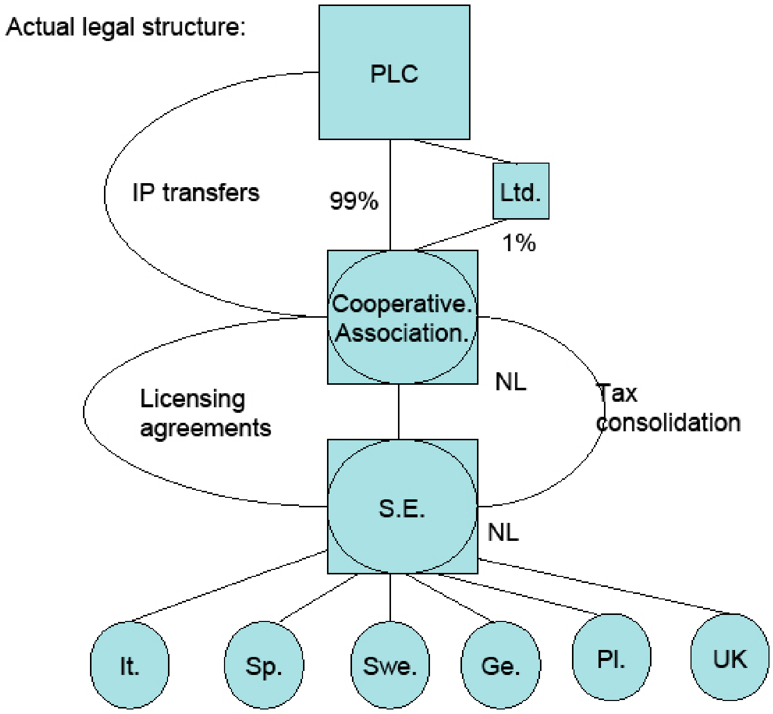
"...for Dutch corporate income tax purposes the SE does not exist!"

A third and even very intriguing possibility, to arrive at a Dutch tax payer with foreign branch operations, is to create a pan-European legal entity structure in the form of an SE (*Societas Europaea*), a legal entity proudly introduced by the European Commission in 2004 whereby one only needs one limited liability entity in the EU, which is then governed by the same civil law or common law rules in all EU countries. A big disadvantage of the SE concept has been that if an existing business, already consisting of different legal entities in various European countries (such as an SarL in France, a GmbH in Germany, an A/B in Sweden etc.) would be converted into an SE, this would imply the liquidation, for tax purposes, of all legal entities in all other countries than the country where the SE ends up, so exit taxes would become due so the SE has always been denominated as "the still-born EU child of 2004". But if one sets up new business, rather than converting an ongoing business, this disadvantage does not apply. In fact the disadvantage turns into an advantage: setting up an SE in one EU country, which subsequently does business in its own name in several other EU countries, will automatically and in very straight forward fashion lead to the desired tax result: a hybrid entity in one EU country with foreign branch operations in all other EU countries.

Note that setting up an SE entity is by no means an easy procedure for a group which does not already possess European legal entities, due to severe restrictions in the EU statute for SE's, but this aspect, however important, is outside the scope of today's article.

Turning back to the article I wrote on hybrid BV's in *WCR March 2010*[2], and emphasizing that "BV" can always be replaced by "SE" because the tax planning consequences will be the same, we will now structure the final piece of the tax planning exercise: the Coop on top of the Dutch structure possesses tax depreciable IP because of the step-up in basis discussed earlier. If it licenses this IP to its subsidiary-SE, which operates the branch offices elsewhere in Europe, the branches, under article 7 of the OECD Model Treaty, which has been incorporated – on this particular subject – in almost every real tax treaty, will become entitled to a tax deduction for their pro rata share of the royalty payments which the Dutch SE has to make to the Dutch Coop. Here the transfer pricing report needed to determine the step-up in Phase I will come in handy again, as it will show the "arm's length" value of the IP rights.

Exhibit 1



Let's say the Dutch SE also sets up business in Italy, Spain, Sweden, Germany, Poland and the UK. These operations will produce chemical products with the help of (perhaps even patented) product technology and production technology. In addition they will obtain the client list for their country and other marketing intangibles, previously in the hands of the parent company of the group before it decided to start operations in Europe.

Provided the royalty payments between SE and Coop are "at arm's length" and also provided that the division key which the SE uses to spread the royalty payments over its various branches is in order (again: a TP issue), the Italian, German, UK etc. operations will be able to get a tax deduction for these payments, even if the payments do not come from them but from the Dutch head–office (on their behalf).

How big a deal is this, then? We have royalty expense deduction in the foreign branches of the SE (pro rata), in the SE itself (for the Dutch production site) but this leads to royalty income in the Dutch Cooperative. This is a Dutch tax payer, subject to the standard 25% Dutch corporate income tax rate on all business income including the exploitation of intangibles, so why would anyone want to put income into it?

Here's where the hybrid character of the lower Dutch entity in the structure comes in: Dutch Coops qualify for Dutch tax consolidation, as parent companies. SE's qualify for Dutch tax consolidation either as parent companies or as subsidiaries (although this is not common knowledge at all in Holland, but we have written confirmation from the Dutch Ministry of Finance on this).

So if I now take you back to my earlier WCR article on hybrid Dutch BV's (*WCR March 2010*[2].), and now knowing that Dutch SE's are treated the same way, tax wise, as Dutch BV's and now also knowing that the SE can be part of what is known in Holland as "fiscal unity", you may draw the proper conclusions together with me:

1) For Dutch corporate income tax purposes the SE does not exist!
2) As a direct consequence of this fiction, the licensing contract between the Coop and the SE does not exist either! One cannot license intangibles to oneself (in the Dutch tax consolidation concept, the SE has been absorbed by the Coop, it has in fact become a Dutch permanent establishment of the Coop);
3) So from a Dutch corporate income tax viewpoint, there are no royalty payments from the SE to the Coop. And invisible income is non-taxable.

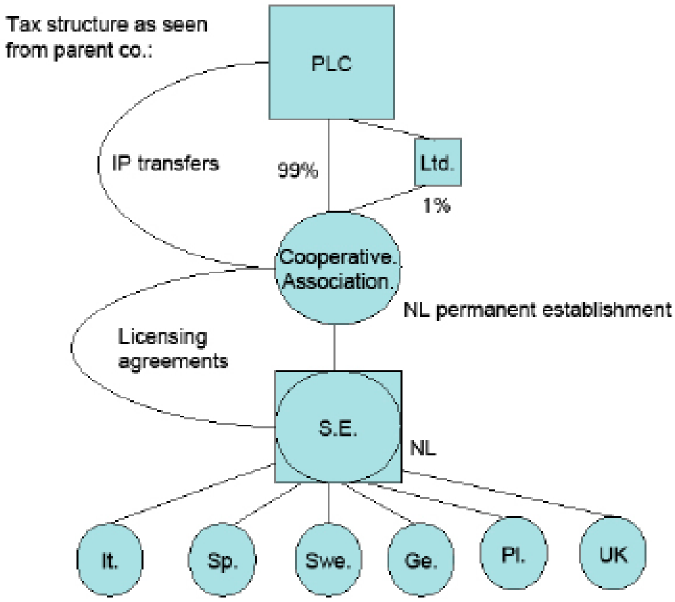
We therefore end up with a situation where, regardless of the fact that in Germany, Sweden, Poland, the UK etc. a tax deduction may be claimed and must be granted by the tax authorities on the basis of the tax treaty with Holland for a pro rata share of the royalty payments between the Dutch SE and the Dutch Coop, there is no income pick-up in Holland.

This "phase 2" set-up has been the subject of Supreme Tax Court litigation between 1987 and 2003 (that is how long it might take for a case to be finally dealt with in my country, but litigation time in Holland is no exception compared to other jurisdictions), with an ultimate total victory for the tax payer concerned. The Dutch Supreme Tax Court not only decided in 2003 that:

> (1) Set-ups like the one shown do indeed have the effect of disappearing income but also that:
> (2) This tax planning cannot be disregarded as abuse of law either, because in the Supreme Court's view there is no Dutch tax at stake: if the Coop would not set up an SE to license its IP to, and form "fiscal unity" with it, but would set up its own foreign branch offices, where its IP would be used, Dutch taxable income would equally not show royalty income: all income would be earned by the branches and all branches other than the Dutch one would be exempt from Dutch corporate income tax, under the standard Dutch foreign branch income exemption rules.

Below I have depicted the structure as seen under the tax rules of the countries involved, which clearly show two hybrid entities: the Dutch Coop and the Dutch SE. You will note that such structures are not necessarily restricted to the Dutch operations of multinational enterprise alone but can on the contrary be made to work, not only for many foreign parent company jurisdictions, but also for many operational jurisdictions. ■

Exhibit 2


Tax structure as seen
from parent co.:
PLC
IP transfers
99%
Ltd.
1%
Cooperative
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S.E.
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Exhibit 3

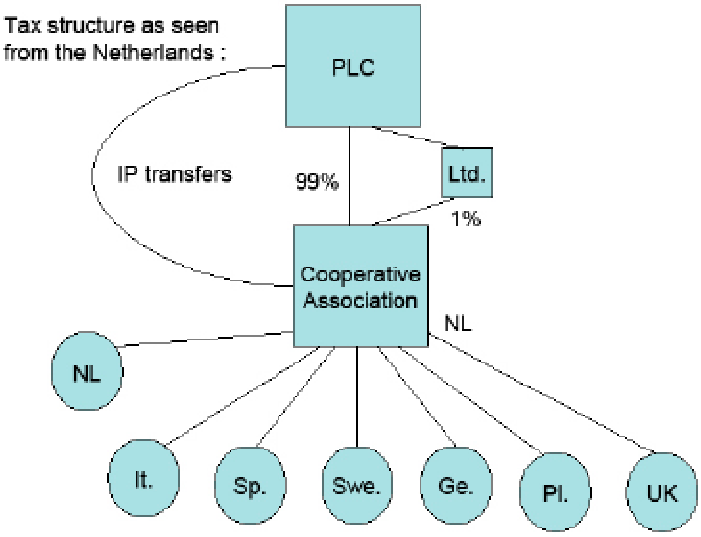
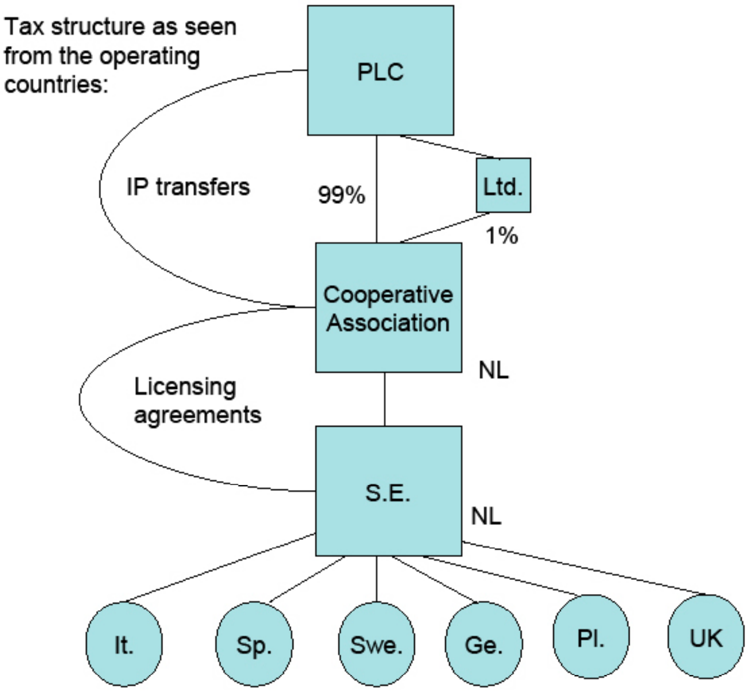

Tax structure as seen
from the Netherlands :
PLC
IP transfers
99%
Ltd.
1%
Cooperative
Association
NL
NL
It.
Sp.
Swe.
Ge.
Pl.
UK

Exhibit 4


Tax structure as seen
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agreements
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It.
Sp.
Swe.
Ge.
Pl.
UK

1. The use of hybrid legal entities in group structures of multinational enterprises, WCR Volume 3, Issue 4, December 2009 http://worldcommercereview.com/publications/article_pdf/202
2. The use of hybrid legal entities in group structures of multinational enterprises, Part II, WCR Volume 4, Issue 1, March 2010 http://worldcommercereview.com/publications/article_pdf/243
3. The use of hybrid legal entities in group structures of multinational enterprises, Part III, WCR Volume 4, Issue 2, June 2010 http://worldcommercereview.com/publications/article_pdf/273

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Competition policy in Ukraine: at the crossroads again

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Celebrating the 10th anniversary of the Competition Act, in 2011 Ukraine will again stand on the verge of major legislative breakthroughs. Having restated the Unfair Competition Act in 2009, the Ukrainian Parliament has accumulated quite a number of other legislative initiatives which include: setting of higher financial thresholds triggering merger clearance requirement, introduction of criminal liability for cartels, redesigning the framework for collection of evidence in antitrust investigations, reconfirming jurisdiction of commercial courts over competition cases, and granting broader investigation and fining powers to the regional subdivision of the competition authority.

The majority of the proposed legislative changes have been prepared by or with the involvement of the Antimonopoly Committee. The Committee developed such proposals mainly basing on the results of the peer review of Ukrainian competition law and policy made by the OECD in 2008. In its report the OECD identified a number of issues in Ukrainian competition law framework and made various remedial proposals. In particular, the report focused on the imperfections of the merger control regime, legislation on state aid, Committee's investigative tools as well as on the necessity to resolve conflicts between the Competition Act and the Commercial Code.

> **"Ukraine is again in anticipation of major changes in competition legislation"**

Recently, the Antimonopoly Committee has also extensively contributed at the sub-legislative level by, among others, adopting new and amending the existing block exemptions regulations.

Following almost two years of operating without the Chairman, in April 2010 the Committee at last got the "new old" Chairman Mr Kostusev, who also occupied this position from 2001 till 2008 and has effectively built up the competition authority to the standards it now operates at. Kostusev has made a number of stuff and policy changes and facilitated the enforcement efforts of the authority – the Committee has become increasingly active in investigating cartels and abuses of dominance focusing on retail and other "socially important" areas, capitalizing on consumer protection mottos. The Committee was also noted to operate in an unbiased and responsible manner, quickly responding to the issues arising on various markets such as aviation fuel, oil products, sugar, and pharmaceuticals. Competition offences by governmental and municipal authorities and unfair competition cases of varying magnitudes have also been among the authority' top priorities.

In late October 2010 Kostusev won Mayor elections in one of Ukraine's largest cities, thus 'beheading' the Committee again. On December 7, 2010 the President proposed the parliament to approve a new Chairman who currently serves as the Minister of Economy. It is almost certain that the Parliament dominated by the President's party will approve the nominee. So, Ukraine is again in anticipation of major changes in competition legislation and, possibly, the Committee's enforcement practices.

Some of the relevant draft laws have already progressed through the first reading in the Parliament. However, the prospects of their adoption are largely unclear; for example, the draft law increasing the notifiability thresholds has been awaiting final consideration by the Parliament since it passed first reading back in 2008. Certainly, this is the most anticipated change given that, apart from establishing very low thresholds triggering merger clearance requirement (assets value/turnover of €1 million for each party and €12 million combined), the existing law (as currently interpreted and enforced by the Committee) views local assets or turnover of either of the merging parties as a sufficient local nexus. Such ignorance of the ICN Recommended Practices, which state that jurisdiction over a merger should be asserted proceeding from the availability of the appropriate local nexus of the transaction, has been heavily criticized by the market and the legal community.

Fortunately, the Committee has brought this issue to the attention of the lawmakers. Though, at the sub-legislative level it still has not introduced a simplified (slim-form or fast-track) clearance procedure for mergers which lack reasonably sufficient local nexus test and apparently do not raise any competition concerns. Rather it keeps applying the standard review procedure to transactions where just one of the parties has Ukrainian asset or turnover.

It is also worth mentioning in this context that unlike in the EU, for the purposes of calculating the notification thresholds the assets and turnover of the entire group of undertakings the target belongs to prior to concentration are attributable to target's assets and turnover even where the seller loses any links with such target as a result of the concentration.

Further, the Committee has not yet developed a uniform approach to the joint/sole control issue. In the absence of clear 'joint control' and 'sole control' definition in the competition laws, the Committee believes that 'control' is vested, eg., with each of shareholders owning a company 50/50. For the purposes of assessment of notifiability of acquisition by one partner of other's equity, this implies that such transaction is purely intra-group. However, this seems to contradict the provisions of the Competition Act which, if fairly interpreted, view 'reaching' of 50% of votes and 'exceeding' of 50% of votes as two separate notifiable transactions.

Thus, it appears that being focused on the introduction of changes to the Competition Act and other related laws, the Antimonopoly Committee does not use to the full extent the instruments available to it at the sub-legislative level, ie., through adoption of regulations and guidelines which may either partially solve the relevant issues or at least mitigate their negative impact. Hopefully, under the new Chairmanship the Committee will take advantage of these instruments and start enforcing the competition policy and law more effectively. ■

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Austria: adapting to the changed environment

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At the end of October 2010 the Austrian Government announced the federal budget for 2011 and the supporting tax measures for its consolidation. The government intends to reach a budget that is within the Maastricht criteria by introducing new taxes and remodelling existing tax provisions.

We shall in the following briefly summarize these new laws as well as the changes to existing legislation and shall make an attempt to evaluate the consequences for Austria as a business location.

> **"Leaving aside the banking sector, the government has taken a balanced approach, taking relatively small measures to consolidate the budget. The challenge will be to adapt each business to these new, albeit relatively moderate changes"**

Taking effect 2011, Austria will levy the so called stability tax ("Stabilitätsabgabe"). Subject to the new stability tax are Austrian banking institutions, which also includes branches of foreign banks doing business in Austria. The stability tax will be levied in two forms: as a percentage of the balance sheet total and as a percentage of the total derivatives trade volume. The new Stability Tax Code contains detailed rules for calculating the total assets which will then form the basis for levying the tax. The stability tax for total assets up to €20 billion shall be 0.055% of this amount and if the total assets exceed €20 billion, 0.085%. The stability tax for derivatives will be 0.013% of all trades in derivatives by the institute in question. If in a derivatives trade there are two parts, purchase and sale involved, only one part will be taxed.

It remains to be seen whether this tax will generate as much revenue as the ministry of finance hopes, which many parties doubt.

Another new tax to be introduced will be the airline ticket tax ("Flugabgabe"). This will affect flights from Austrian airports. The amount will depend on the distance between the Austrian airport and the destination. The tax system differentiates between short/medium and long distance flights. Taxes will amount to €8.00, €20.00 and €35.00 per flight and are to be levied by the airline when selling the ticket. All European destinations will be short distance, as well as all states around the Mediterranean Sea and Russia.

Taxation of capital income will be changed to include taxation on realized capital gains as well as income from derivatives. These new taxes are called capital gains taxes and will amount to 25 percent. This will however only affect capital acquired from 2011 onward.

The tax system has also been changed with regard to private foundations. So far, a foundation's income derived from capital or through the sale of participations of the trust and received a privileged taxation treatment which meant a reduced corporate income tax of 12.5 percent. This will be changed to the general corporate income tax rate of 25 percent. Hence, private trusts lose their tax privileges. This in turn will create the necessity for owners of large fortunes to consider whether it would be beneficial to change from a private trust to a normal corporation, administering the assets. In future, the latter will have advantages over the administration of assets in the form of a private trust.

Apart from these new taxes, income tax incentives for families with children and tax deductions for people in need of care will be reduced.

In the area of consumption taxes, the legislator has decided to raise the petroleum tax ("Mineralölsteuer"). This will probably affect the end consumer the most, be it that he is the owner of a vehicle or be it that the raised petroleum tax is passed on to the consumer through a price increase on transported goods. The so called standard fuel consumption tax ("Normverbrauchssteuer"), an Austrian tax to be paid when buying a motor vehicle, will be raised. Tobacco tax will also be raised.

But taxes will also be lowered in some areas. The so called research bonus ("Forschungsprämie") will be raised from 8 percent to 10 percent. The taxation of credit or loan agreements, an oddity of the Austrian tax system, is henceforth abolished.

Apart from these new taxes, relatively little will change in the area of corporate taxation. Leaving aside the banking sector, other business sectors will not be subject to new taxes. Possibilities to structure businesses to the greatest tax advantages, which so far has been an advantage for Austria as a business location, will remain. This includes group taxation as well as the possibility to offset any balance sheet profits with losses generated by foreign entities owned by Austrian corporations. The tax accounting law has not been changed; amortization of the company value may still be claimed. A new wealth tax, requested by left leaning pressure groups, will not be introduced which is a relief to all tax payers.

Not so much a fiscal measure but more of a regulative measure, are the changes of the Austrian Gambling Code which have been decided together with the above mentioned tax changes. The Austrian gambling monopoly will be abolished as a consequence of European case law regarding gambling monopolies. It will not be requires for any private entity to have their seat in Austria in order to offer gambling opportunities in Austria. In accordance with the freedom to provide services, this may also be done from any other country in the European Union. A private entity offering gambling must however be subject to a supervisory agency at the place of business. The new code will regulate the conditions under which a private entity may acquire a gambling concession.

A concession may only be acquired by a corporation which has apart from a board of directors, a supervisory board and a minimum initial capital of €22 million. The conditions for acquiring a gambling concession closely resemble the conditions and prerequisites for opening a banking business in Austria. It remains to be seen how soon private parties will make use of this new statutory opportunity and how soon there will be real competition in the gambling market.

Leaving aside the banking sector, the government has taken a balanced approach, taking relatively small measures to consolidate the budget. The challenge will be to adapt each business to these new, albeit relatively moderate changes. ■

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Minority shareholders, emerging markets and initial public offerings

Leonard A Birmingham is a Partner and Head of Harneys Corporate Department

One of the most important issues in relation to a company being accepted for listing purposes on international stock exchanges is that of shareholder protection. Some stock exchanges take this far more seriously than others. For example while BVI companies have always been listed on stock exchanges in New York (both NYSE and NASDAQ), London, Oslo, Singapore and Toronto until recently, a listing on the Hong Kong Stock Exchange was not a possibility for a BVI company and one of the reasons given was that statutory protection for minority shareholders of BVI companies was less robust than it was felt necessary.

It is probably fair to say that in the past one of the shortcomings of BVI corporate statutes was that protection of the rights of minority shareholders required more emphasis. Apart from protective provisions that the shareholders would (and often did) put into the Memorandum and Articles of Association of the relevant company and protection afforded at common law, the statute gave relatively little comfort to minority shareholders. That lacuna in the law has however now been filled. The rest of this article examines how the law has been enhanced in this area.

Common law and general statutory protection

Until fairly recently the main protection for minority shareholders was the common law principle known as the Rule in *Foss v Harbottle*. This decision set out, among other things, the exceptions to the principle of majority rule.

> **"Until recently, a listing on the Hong Kong Stock Exchange was not a possibility for a BVI company and one of the reasons given was that statutory protection for minority shareholders of BVI companies was less robust than it was felt necessary"**

A basic protection available to minority shareholders provided by the BVI Business Companies Act, 2004 (as amended) (the "Act") is a requirement that, subject to the Memorandum or Articles of Association, any sale, transfer, lease, exchange or other disposition, other than a mortgage, charge or other encumbrance or the enforcement thereof, of more than 50 per cent in value of the assets of the company, other than a transfer pursuant to the power of the directors to transfer assets for the protection of such assets, if not made in the usual or regular course of the business carried on by the company, shall be approved not only by a Resolution of Directors but also by a Resolution of Shareholders.

In addition, the Act provides that any member of a company is entitled to payment of the fair value of his shares upon dissenting from several types of transactions (typically mergers, arrangements etc.) which can be collectively referred to as corporate reconstructions.

Owing to the way that the Act is drafted, there are real opportunities for writing bespoke protective provisions into the company's constitution. However the main protection for minorities lies in certain remedies that are set out in the Act.

Specific members' remedies

- Pursuant to the Act, the Court has the power, on the application of a member or a director of the company, to make an order directing the company or director to comply with, or restraining the company or director, from engaging in conduct that would contravene the Act or the company's memorandum or articles. This applies in a context where a company or a director engages in or proposes to engage in conduct that contravenes the Act or the memorandum or articles.

The wording of the Act suggests that the court may at any time (whether before or after the contravening action is taken) make an order either preventing the action or ordering that the action be stopped.

There is provision in the Act to the effect that no act of the company is invalid by reason only that the company did not have the capacity to perform the act. Whilst this could be read as a limitation on the ability to restrain the company from contravening the memorandum or articles, I think that the better interpretation is that notwithstanding the fact that an act done by the company is not invalid for lack of capacity only, such a lack of capacity on the part of the company may be pleaded for example, by a shareholder in connection with an application to restrain the company.

The court may make, at any time before the final determination of such an application, as an interim order, any order that it could make as a final order and has the power to order such consequential relief as it thinks fit. Such relief, presumably, might include compensation to parties deprived of benefits by the restraining orders. No doubt the BVI Courts will, in due course, give guidance on the principles underlying statutory injunctions under BVI law.

- Statutory derivative actions have not, so far as I am aware, been tested by the BVI courts, but there is quite a clear intent that derivative actions should be brought only under the Act and accordingly the common law right of the minority to sue derivatively under the exceptions to *Foss v. Harbottle* appears to be of historical interest only. This is the case in relation to so called "single" derivative actions. So far as "double" or "multiple" derivative actions are concerned, the common law continues to apply. A distinction should be drawn between the two types of derivative actions. The former applies to the "classic" derivative action in which a member of a company who feels that a wrong has been done to the company may sue the person allegedly responsible on the company's behalf. The latter however involves a member of a parent company taking legal action on behalf of a subsidiary company in respect of wrongs committed against the subsidiary. Specific provision is made in the Act for the former but it is absolutely silent as to the latter. As such whilst the common law right to sue derivatively under the exceptions to *Foss v. Harbottle* has, it appears, been abolished with respect to single derivative actions, the common law continues to apply in relation to "multiple" or "double" derivative actions. This was confirmed in the Hong Kong decision of *Waddington v Chan Chun Hoo Thomas FACV 15/2007*.

  In terms of the statutory procedure for commencing a derivative action, the starting point is that an application to the court must be by a member and is an application for leave to that member to bring proceedings in the name and on behalf of the company; or intervene in the proceedings to which the company is a party for the purpose of continuing, defending or discontinuing the proceedings on behalf of the company. Accordingly, I am of the view that the application for leave will probably be via interlocutory proceedings.

In determining whether to grant leave, the court must take into account several factors as follows:

- Whether the member is acting in good faith;

- Whether the derivative action is in the interest of the company taking account of the views of the company's directors on commercial matters;

- Whether the proceedings are likely to succeed;

- The cost of the proceedings in relation to the relief likely to be obtained; and

- Whether an alternative remedy to the derivative claim is available.

Once satisfied leave may be granted because the grant remains at the court's discretion. In order to grant leave the court will need to be satisfied that:

- The company does not intend to bring, diligently continue or defend, or discontinue the proceedings, as the case may be; or

- It is in the interests of the company that the conduct of the proceedings should not be left to the directors or to the determination of the shareholders or members as a whole.

This provision seems to be worded so as to be read as one or the other but not necessarily both.

> **"The main challenge for BVI or Cayman Islands holding companies now lies in the constraints (some justifiable) applied by so called emerging market jurisdictions"**

Furthermore, unless the court otherwise orders, 28 days notice of the application for leave must be served on the company which may appear and be heard. It means therefore that *ex parte* applications will not be available but the BVI Courts may accept in an appropriate and perhaps extreme case that less notice might be required. The absence of BVI decisions means that the position is not crystal clear.

- In terms of costs of the derivative action, where the court grants leave to a member to bring or intervene in derivative proceedings, it must, on the application of the member, order that the whole of the reasonable costs of bringing or intervening in the proceedings are to be met by the company unless the court considers that it would be unjust or inequitable for the company to bear those costs.

- Within certain procedural and legal confines, the manner in which litigation is conducted is normally up to the parties. The Act however provides that at any time after granting leave, the court may make an order it considers appropriate in relation to proceedings brought by the member or in which the member intervenes. The court therefore continues to have control over the matter, presumably to ensure that it is conducted in the interests of the company. The same control by the court applies in relation to settlement, discontinuing or compromise of proceedings.

- A shareholder may bring an action against a company for breach of a duty owed by the company to him as a member. Unfortunately the Act does not tell us what duties are owed and accordingly the common law subsists in this area.

- A member who considers that the affairs of the company have been, are being or are likely to be, conducted in a manner that is likely to be oppressive, unfairly discriminatory, or unfairly prejudicial to him in that capacity, may apply to the court for an order. If on an application the court considers it just and equitable it may make an order as it thinks fit.

- Where a member of a company brings proceedings against the company and other members have the same or substantially the same interest in relation to the proceedings, the Court may appoint that member to represent all or some of the members having the same interest, and may, for that purpose, make such order as it thinks fit, including an order:

  (a) As to the control and conduct of the proceedings:

  (b) As to the costs of the proceedings; and

  (c) Directing the distribution of any amount ordered to be paid by a defendant in the proceedings among the members represented.

This is the so called representative action.

Looking ahead

With these statutory provisions, BVI companies have come of age and the BVI has convincingly addressed the criticism that its laws left the minority out in the cold. This has been recognised by the Hong Kong Stock Exchange, which recently approved the listing of BVI companies on the exchange. (For more details on Hong Kong listings, see this recent news item http://www.harneys.com/news.php?npindex=556). Indeed for listing purposes, there is little distinction today between using an SPV domiciled in the BVI or the Cayman Islands; the differences are limited to, in the case of the BVI, faster incorporation and being generally more cost efficient.

However, the game continues to change. The main challenge for BVI or Cayman Islands holding companies now lies in the constraints (some justifiable) applied by so called emerging market jurisdictions. Across the world, several jurisdictions are, in different ways, tightening up on the use of offshore structures in international finance transactions. One of the latest and perhaps most prominent examples is the judgment of the Indian High Court in the Vodafone case. In its simplest terms, this involved a sale of shares in a non-Indian company (which very indirectly owned an Indian company) by a non-Indian company to a non-Indian company and the issues surrounded capital gains tax and withholding tax. The end result (so far) is that *Vodafone* must pay about US$2 billion in capital gains tax. It is said that the Indian authorities are also scrutinising the tax aspects of several other cross border deals.

Meanwhile, in China, the so called Circular 10, in no way related to the *Vodafone* case, purports to control "round tripping" by making it a requirement that certain approvals be obtained from various Chinese governmental bodies in the context of a Chinese company that is typically either (a) seeking a listing on a non-Chinese Stock Exchange by using an offshore company; or (b) merging into an offshore company.

Notwithstanding Circular 10, (and the likes of *Vodafone*) offshore vehicles continue to be used by Chinese operating companies for IPOs and several interesting structures have been devised to address the constraints of the Chinese rules. Whilst the structures used in this context have met with market approval, to my mind the more interesting point is that Chinese business owners and Chinese companies continue to use offshore vehicles notwithstanding restrictions imposed by their governments. At its simplest level it has to do with the restrictive nature of their capital markets on the one hand and the flexibility afforded by using BVI and Cayman holding companies on the other.

It may be that vehicles in tax treaty jurisdictions like Cyprus and Mauritius have a positive role to play given the tightening up by emerging market countries but SPVs, whether based in tax treaty countries or in "pure" offshore jurisdictions, are tools that can be usefully deployed as part of the mix within a financial system. Too much regulation will cause a system to eventually break down. Like all things organic it needs outlets. Therefore there is a role for such companies helping countries the world over to achieve that balance.■

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New possibilities in joint-venture financing in Polish law

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The role of the mortgage in Poland is on a constant increase. One can see that the difficult period in financing investments, especially in the real estate sector caused by the crisis, is slowly drawing to an end. The revival occurring after many months is manifested in the increasing number of commenced investments and entails, obviously, both investors as well as of financial institutions' interest in new forms of securing the financing of projects. Hence, the question on the role of the mortgage in commercial transactions returns.

Undoubtedly, the basic manner of securing a loan in Polish law is a mortgage although the possibility of securing a debt by the transfer of the title to secure a loan repayment, which can pertain both to a real estate as well as to movables or claims, is also admissible. The attractiveness of the latter manner of securing repayments has, however, decreased as of the moment of the entry into force of the amendment of the Act of 28 February 2003, the Law on Bankruptcy and Rehabilitation ("LBR")[1] by the Act of 6 March 2009 on the Amendment of the Law on Bankruptcy and Rehabilitation Act, the Bank Guarantee Fund Act, and the National Court Register Act[2].

The principle is that the asset components not belonging to the bankrupt's assets are excluded from the bankruptcy estate (Article 70 of the LBR) and the items the title to which had been transferred by a debtor onto a creditor were recognised to be precisely these types of components. The Amending Act introduced Article 70^1 of the LBR under which the provisions on the exclusion from the bankruptcy estate do not apply to objects, claims, and other property rights transferred by a bankrupt onto the creditor with the view to secure the debt. The provisions of the act pertaining to the pledge and pledge-secured debts apply respectively to these objects as well as to debts thus secured. However, in the literature, it is assumed that the said provision does not pertain to situations where a transferred object is held by the creditor while not by the bankrupt[3]. Hence, presently, in the event of the declaration of bankruptcy of a debtor, a creditor who concluded an agreement on the transfer of the title to secure the loan repayment with the debtor is unable to demand that the transferred object be excluded from the bankruptcy estate[4].

In the Polish law, the mortgage is regulated by the Act of 6 July 1982 on the Land and Mortgage Register and Mortgage (hereinafter: "LMRA")[5]. However, the said Act was written during the times when Poland was under a different political system, in the times of a planned economy, where the role of the mortgage was practically marginal. In the outcome of the social and economic transformations after 1989, the manner of regulating the mortgage has rendered it a manner for securing a loan increasingly less popular for investors and to an ever decreasing degree corresponding with the requirements of commercial transactions. The Polish legislator noticed this problem and with the Act of 26 June 2009 on the Amendment of the Act on the Land and Mortgage Register and Mortgage and several other acts[6], the LMRA was extensively amended.

The amendment shall enter into force in February 2011. Its objective is to introduce solutions which shall render the mortgage an effective, adjusted to practice, and flexible manner for securing cash claims[7]. Particular attention is due to the institution of the mortgage administrator, introduced by the amendment, which can find its application in the event of securing several claims used to finance the same venture and which different entities are entitled to, with the use of one mortgage[8]. This institution is rather complicated while to take advantage thereof the conclusion of a certain "complex" of agreements, to be presented below, is required.

Due to a rather inflexible regulation pertaining to the mortgage against the background of the LRMA, based on the "one claim – one mortgage" principle, until the amendment at issue has not been implemented, the possibility to secure consortium facilities, ie. loans where several entities are entitled to secured claims, with one mortgage has stirred multiple doubts. This issue has been of particular significance for banks in the event of big investments financing. However, a practice has been formed to secure these types of loans with a mortgage. This practice has been subject to diverse opinions of representatives of the doctrine. The issue of the admissibility of securing consortium facilities with a mortgage is undoubtedly of enormous significance since the recognition that hitherto Polish law has not allowed for such a solution may lead to the nullity of the agreement on the establishment of the mortgage which constitutes a danger to creditors. For this reason, the introduction of an unequivocal regulation of this issue in the LRMA was particularly desirable and it must be hailed with satisfaction.

The institution of a mortgage administrator shall apply, first and foremost, in the case of loans granted by bank consortium for financing a given venture. The assessment of the new regulation still remains an open issue – only practice can show whether it actually corresponds with the needs of the transactions and whether it duly secures creditors' interests.

As results from Article 68^2 item 1 of the LRMA, creditors shall appoint a mortgage administrator with the view of securing several claims which various entities are entitled to and which serve to finance the same venture with a mortgage. The administrator can be one of the creditors or a third party.

On the grounds of the said provision, it is not clear how the notion of "claims which serve to finance the same venture" is to be understood. As it seems, the joint "venture" is to credit the borrower's operations by the creditors. The notion of "a venture" used by the legislator, according to the definition to be found in the Dictionary of Contemporary Polish means[9] "that which has been planned, thought to be realised, that which has been decided to be carried out, a project, a realised intention". On the one hand, therefore, it is broad enough to facilitate the flexible application of the institution of a mortgage administrator, nevertheless, on the other hand, the legislator here introduces a certain restriction since, as follows from the dictionary definition of "a venture", it is an goal-oriented activity and, thus, accidental actions cannot be such, even if they form a set of interrelated activities. The administrator cannot be appointed in the event in which the premises of Article 68^2 item 1 of the LRMA are not fulfilled and, in particular, when there is no joint venture.

No doubts should arise that the institution of the administrator may apply already in the case of at least two claims and at least two creditors. A situation is also possible when the mortgage administrator is appointed in order to secure several claims which different (two at least) entities are entitled to in the situation in which each of these creditors is entitled to two or more claims[10]. It is inadmissible to appoint a mortgage administrator in order to establish a mortgage meant to secure one claim only.

To take advantage of the mortgage administrator institution, the entities intending to grant a loan are required to display huge precision of operation in getting involved in a number of activities. Since it is these entities that shall conclude the consortium facility agreement, the agreement on the appointment of the administrator, the loan agreement, and finally, the administrator shall conclude the agreement on the establishment of the mortgage. Without exaggerating too much, one can state that the mortgage administrator institution shall prove true in these cases where creditors (consortium participants) shall co-operate efficiently and act loyally towards one

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another. The lack of understanding between creditors shall signify, as a rule, the need to "quit" the consortium, which is possible by the division of the mortgage.

Agreement with consortium of lenders

Firstly, to ensure the effective operation of the consortium, the shaping of the relations between its participants, and especially of the rules for the settlement of accounts, the scope of the collateral, the potential mutual liability, is of particular importance. All these contractual regulations shall form the internal relations between creditors. They can be contained in one or in several agreements with consortium of lenders.

The agreement on the appointment of the mortgage administrator

Secondly, it is necessary to conclude an agreement on the appointment of the mortgage administrator which in order to be valid requires to be drawn up in writing (*ad solemnitatem*). It is a bilateral agreement where the administrator appears on one side with all the creditors on the other. Such an agreement constitutes a type of an authorisation for the administrator to conclude an agreement on the establishment of the mortgage; it is also indicated that this agreement sets out the limits of the administrator's competence[11].

> **"The administrator shall exercise all the rights and obligations of a mortgage creditor – on his own behalf, but on account of the creditors whose claims are covered by the collateral"**

Nonetheless, the administrator is not the creditors' proxy (therefore, no direct representation has been provided for here) but he acts on his own behalf to the benefit of the creditors (the indirect representation construction). The conclusion of an agreement on the appointment of the administrator is synonymous with awarding the person appointed the administrator the competence to shape the creditors' legal situation. Hence, the administrator takes over the role of the mortgage creditor while he is not entitled to the claim secured by the mortgage. Without the creditors' consent, the administrator may not renounce the mortgage and it is so due to the relation existing between the mortgage and the claims it secures. Simultaneously, since the administrator is an absolute direct representative, having established the administrator, the creditors cannot exercise any rights or obligations of a mortgage creditor other than those they are awarded in Article 68^2 of the LRMA and indirectly by granting their consent to certain activities of the administrator.

The agreement on the appointment of the mortgage administrator shall specify the obligations of the parties. First and foremost, it is going to be the administrator's obligation to conclude the agreement on the establishment of the mortgage and the creditors' obligation to disburse the remuneration for the administrator. The said agreement also ought to indicate the claims or legal relations from which the claims subject to being secured by the mortgage established by the administrator arise or shall arise from. In turn, it is not necessary to indicate "the joint venture" in the said agreement, however, it shall usually be done.

The creditors' relations with the mortgage administrator ought to be regulated in the agreement appointing the administrator to the post. In particular, it is possible to introduce a variety of restrictions as well as bar the administrator from engaging in certain actions without obtaining the creditors' consent expressed in a specified form first. All such restrictions of the scope of "authority" of the mortgage administrator shall be of solely internal importance, in the relations between the administrator and the creditors, and shall not bear on the validity and effectiveness of the activities performed by the administrator without such an internal consent or at transgressing the scope thereof. They may, however, substantiate damage claims of the consortium participants towards the mortgage administrator on the grounds of the improper performance of the agreement (Article 471 of the Civil Code)[12].

As it has been already indicated, the agreement on the appointment of the administrator shall be concluded in writing under the pain of invalidity, however, it is not clear whether this form is sufficient to disclose the administrator in the land and mortgage register since Article 31 item 1 of the LRMA provides that an entry in the land and mortgage register may be made on the grounds of a document with a signature certified by a notary if specific provisions do not provide for another form of the document. Therefore, a question arises whether Article 68^2 item 2 of the LRMA derogates the form requirement provided for in Article 31 item 1 of the LRMA.

It is a substantial issue since under Article 68^2 item 5 of the LRMA, it is the mortgage administrator that is entered in the land and mortgage register as the mortgage creditor. In consequence, also in the event of the change of the mortgage administrator, which is certainly possible, it is necessary for this change to be reflected by the disclosure of the new administrator in the land and mortgage register.

Admittedly, the literal interpretation of Article 31 item 1 of the LRMA could provide the basis to conclude that if the act provides for any form for a given action, then the form provided for in this regulation does not apply, however, a teleological interpretation advocates against adopting this latter stance. This is, first and foremost, advocated for by the function of the land and mortgage registers kept by courts with the view of establishment of the legal status of a real estate as well as the limited cognition of the land and mortgage register court in the course of the proceedings for the entry in the land and mortgage register.

The conclusion of an agreement for the appointment of the mortgage administrator in writing with signatures certified by the notary is, therefore, most purposeful, should one take into consideration the functions of land and mortgage registers and the fact that while examining the motion, the court examines exclusively the contents and the form of the motion, the documents attached thereto, and the contents of the land and mortgage register (Article 626^8.2 of the Code of Civil Procedure).

The agreement on the establishment of the mortgage

Another agreement in the process of the organisation of the consortium shall be the agreement on the establishment of the mortgage concluded between the mortgage administrator and the owner of the real estate to be encumbered with the mortgage. The agreement on the establishment of the mortgage ought to specify the scope of securing of individual claims and the venture the financing of which they are to be used for (Article 68^2 item 3 of the LRMA).

At the conclusion of the agreement on the establishment of the mortgage, the administrator shall have to be obligated to submit the agreement on his appointment as the mortgage administrator in order to demonstrate his authorisation to act, which shall enable a notary to verify the scope of the administrator's competence. The declaration of the owner of the real estate on the establishment of the mortgage shall have to have the form of a notary deed (Article 68^2 item 4 of the LRMA) even in the case when the mortgage administrator is a bank. It is so, for the legislator has unequivocally excluded the application of Article 95 of the Act of 29 August 1997 – The Banking Law[13] in this case (the said provision introduces an exception from the rule that a declaration of the owner of the real estate on the establishment of the mortgage must be submitted in the form of a notary deed).

The mortgage administrator is entered in the land and mortgage register as the mortgage creditor (Article 68^2 item 5 of the LRMA). To the motion of the creditors whose claims are covered by the collateral, the court changes the mortgage administrator entry.

The scope of mortgage administrator's operation

The administrator shall exercise all the rights and obligations of a mortgage creditor – on his own behalf, but on account of the creditors whose claims are covered by the collateral. The mortgage administrator cannot dispose of either the mortgage or the secured claims. Creditors cannot dispose of the mortgage, however, they can dispose of the claims they are entitled to. In such a case, a transferee accedes the legal relationship connecting a transferor with the administrator.

A person appointed a mortgage administrator ceases to be the administrator at the moment of the expiry of the agreement under which they had been appointed the administrator. In the event of the expiry of the agreement on the appointment of the mortgage administrator and in the case a new administrator is not appointed, each of the creditors whose claims are covered by the collateral may come forth with a demand for the division of the mortgage (Article 68^2 item 6 of the LRMA). As a result of such a division, mortgages securing individual claims, so far covered by the collateral of one mortgage established to the benefit of the administrator, will be created and the total of these mortgages must not exceed the total of the mortgage established to the administrator's benefit.

A question arises, however, whether creditors can engage in any actions, the competence to engage in which had been granted to the administrator, until the moment of appointment of a new administrator or until the mortgage has been divided. In the literature it is assumed that, exceptionally, in such a situation the rights and obligations of the mortgage creditor shall be discharged jointly by the creditors whose claims had been secured by the mortgage established by the administrator. The literature also proposes that the provisions on co-ownership shall apply *per analogiam*[14]. The adoption of the opposite view would have this result that until the moment of appointment of the new administrator or until the moment of division of the mortgage, there would be no person able to exercise the rights and obligations of the mortgage creditor.

The administrator enjoys the right to satisfy the secured claims from the mortgage object, it takes place by means of the enforcement proceedings. Of course, there is no need to conduct the enforcement proceedings in the event in which the owner of the real estate encumbered with the mortgage delivers the performance to the administrator's hands. The administrator is not authorised to accept a performance from a personal debtor. The literature indicates that creditors are entitled to accept the performance directly from the owner of the encumbered real estate. However, this view may stir doubts.

As it has been indicated, the mortgage administrator is an absolute indirect representative which means that by virtue of the act itself, all the actions performed thereby bear effects in the creditors' legal sphere. In view of the above, it is proper to state that there are no grounds to construct the transgression of the scope of "the authorisation" specified in the agreement on the appointment of the administrator. The transgression by the administrator of his obligations towards the creditors may, certainly, result in his compensatory liability.

Specific problems may appear in the event the mortgage administrator's bankruptcy is declared. As if predicting these complications and in particular taking the regulation of Article 62 of the LBR under which the bankruptcy estate covers the assets held by the bankrupt on the date of declaration of their bankruptcy as well as the assets acquired thereby in the course of the bankruptcy proceedings into consideration, the legislator had amended Article 63 of the LBR. Under the amended Article 63 item 1 point 3 of the LBR, the bankruptcy estate does not cover the amounts obtained on the grounds of the realisation of the registered pledge or a mortgage if the bankrupt served as the mortgage or collateral administrator, in the part which under the agreement on the appointment of the administrator, falls to the remaining creditors.

Doubts arise whether the function of the administrator is automatically taken over by the receiver in bankruptcy or whether the bankrupt remains the administrator upon the declaration of bankruptcy of the mortgage administrator. In this respect, the literature is far from being unanimous, however, it is proper to point out that it is in the creditors' best interest to discharge the person holding the function of the administrator, if only to avoid unnecessary confusion and complications.

The amendment of the act on bonds

The Act of 26 June 2009 on the amendment of the Act on the Land and Mortgage Register and Mortgage and several other acts amended also the Act of 29 June 1995 on Bonds[15]. Under the amended Article 7 item 1a, prior to the commencement of the issue of bonds, the issuer is obligated to conclude an agreement with the mortgage administrator who exercises the rights and obligations of the mortgage creditor on their own behalf but on the bondholders' account, in writing, under pain of invalidity. The bank acting as the representative's bank may also act as the mortgage administrator. The provisions of Article 31 item 2-5 apply respectively to the mortgage administrator. However, Article 7 item 1b provides that the provisions of Article 68^2 of the LRMA do not apply to the mortgage administrator.

Recapitulation

The institution of the mortgage administrator undoubtedly constitutes a step forward in rendering the mortgage functioning in Polish law more modern. It opens new possibilities for financing of joint ventures which constitutes a particularly relevant issue in the case of investments of a high value. It seems that due to this institution a mortgage collateral shall become not only more accessible but shall also be used more often. Financial institutions, but not only, have obtained a new instrument to be used to secure their claims.■

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[1] *Uniform text, Journal of Laws of 2009, No. 175, item 1361 as amended.*
[2] *Journal of Laws of 2009, No. 53, item 434.*
[3] *R Adamus, Upadłość a przewłaszczenie na zabezpieczenie. Komentarz. (Bankruptcy and the Transfer of Title to Secure the Loan Repayment), Warszawa 2010, Legalis.*
[4] *However, it is contentious whether said provision applies also to the transfer of the title to secure a real estate since it refers to the provisions on the pledge applied respectively while not to those on the mortgage, compare: S Gurgul, Prawo upadłościowe i naprawcze. Komentarz (The Bankruptcy and Rehabilitation Law. Commentary), Warszawa 2010, p. 243.*
[5] *Uniform text, Journal of Laws of 2001, No. 124, item 1361 as amended.*
[6] *Journal of Laws of 2009, No. 131, item 1075.*
[7] *The concept of harmonisation of the regulations on the substantive law, including the pledge laws within the frames of the European Union law has its advocates as well as adversaries, compare: S Kalus, Perspektywy stworzenia europejskiego prawa rzeczowego (The Perspectives for the Establishment of the European Substantive Law) , (in:) Rozprawy prawnicze. Księga pamiątkowa Profesora Maksymiliana Pazdana (Legal Dissertations. Professor Maksymilian Pazdan Memorial Booklet), Kraków 2005, p. 625 et seq. and the literature quoted therein.*
[8] *The collateral administrator institution is regulated by Article 16 of the Model Law on Secured Transactions constituting the model regulation of the European Bank for Reconstruction and Development.*
[9] *Słownik współczesnego języka polskiego (Dictionary of Contemporary Polish), B Dunaj (editor), Warszawa 1996, p. 875.*
[10] *M Kućka, (in:) Hipoteka po nowelizacji. Komentarz (The Mortgage after the Amendment. Commentary), Warszawa 2010, p. 211, p. 208.*
[11] *M Kućka, op. cit., p. 211.*
[12] *B Jelonek-Jarco, J Zawadzka, Praktyczne problemy nowelizacji ustawy o księgach wieczystych i hipotece cz. II (Practical Problems of the Amendment of the Act on the Land and Mortgage Register and Mortgage, part II), Rejent 2010, No. 10, p. 56.*
[13] *Journal of Laws of 2002, No. 72, item 665, as amended.*
[14] *M Kućka, op. cit., p. 220.*
[15] *Journal of Laws of 2001, No. 120, item 1300, as amended.*

Model region for electric mobility: North Rhine-Westphalia

Come on board, join the ride!

In an internationally networked and globalized world, mobility is the key to economic success. Regardless of whether we look at individual or business transportation, mobility today is based largely on conventional internal combustion engines. This has a considerable impact on our environment causing CO_2 and noise emissions, more traffic congestion and traffic jams.

These problems are set to worsen rapidly over the next 20 years. Experts expect that there will be 4.5 times more vehicles registered in 2030 than today, due in particular to the huge pent-up demand for individual mobility in the emerging and very heavily populated industrial nations such as China and India, as well as the countries of South America. The efficient use of resources and the development of new technologies must therefore be central to research. Making mobility affordable and ecologically compatible is a worldwide necessity and a vital opportunity in terms of industrial policy.

The German government has recognized the opportunities presented by this development, launching the *"National Platform for Electric Mobility"* in May 2010. It intends to subsidize the development of electric mobility to the tune of 1.2 billion euros from state funds. The German economy will use its own funds to contribute in equal measure. The goal is to have one million electric vehicles driving on Germany's roads by 2020.

North Rhine-Westphalia with the Rhine-Ruhr metropolitan region has been selected by the federal government as one of eight model regions, and with good reason. Alongside Paris and London, the state is one of the most densely populated metropolitan areas in Europe. Around 18 million people live in North Rhine-Westphalia on an area of just over 34,000 square kilometres. At present, there are 8.9 million passenger cars registered in North Rhine-Westphalia: 21.3 percent of all the cars in Germany or about 500 cars per 1,000 inhabitants. In parts of the Rhine-Ruhr region there are up to 1,300 vehicles per square kilometre.

Every day in North Rhine-Westphalia, 8.7 million people commute to work. Around 75 percent leave their home town and use their own car for this purpose. 90 percent of these car commuters cover a distance of less than 50 kilometres. This is already an ideal distance for the still limited range of today's battery technology.

North Rhine-Westphalia provides motorized passenger and product transportation with 139,000 kilometres of roads, of which nearly 2,200 kilometres are freeways. The state thus possesses one of the densest road networks on the European continent and an outstanding basis for the development of a user-oriented infrastructure for the operation of electric cars. Numerous inner city parking garages, parking lots and a network of around 3,300 filling stations can be used to establish charging stations.

North Rhine-Westphalia is a major metropolitan region with a strong industrial basis. The automotive sector is traditionally an important cluster. Every year, around 800,000 passenger cars and commercial vehicles come off the assembly lines of the production facilities in Cologne (Ford-Werke GmbH), Bochum (Adam Opel GmbH) and Düsseldorf (Daimler AG). Added to this are trailers, semi-trailers and containers as well as vehicle parts and accessories.

Over 200,000 people work in around 800 companies in the automotive and automotive supplier industry, generating annual sales of some 43 billion euros. It is therefore particularly important for the state to keep abreast of new technology. About 100 companies and institutes active in the fields of battery technology, automotive engineering, electricity generation, transmission and distribution and which possess great expertise, offer themselves as industrial and research partners.

No other product symbolizes the future of electric mobility technology better than the charging plug. Leading car manufacturers from Europe, Japan and the USA agreed at the beginning of 2009 on the basic parameters for a uniform European charging standard for the electric car of the future. The basis of the agreement is an innovative standard draft by the company MENNEKES Elektrotechnik from Kirchhundem in North Rhine-Westphalia.

The tasks of the charging plugs are more complex than one would assume at first glance as they need to cover a large variety of functions. The smart charging connection developed by MENNEKES meets all these requirements. The charging plug is no larger than a conventional 16A plug and suitable for both the single-phase 230V connection and the three-phase 400V connection up to a charging current of 63A. The charging technology provides not only an electricity supply, but also the required communication interfaces between charging station and vehicle. A "plug present" contact, for example, activates the immobilizer and a "pilot control" contact facilitates the exchange of data between vehicle and charging station.

STAWAG
LI-ION DRIVEN
PLUG-IN ELECTRIC VEHICLE
WITH RANGE EXTENDER
FEV
LIIONDRIVE

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Parties to the agreement include the automobile manufacturers Daimler, BMW, Volkswagen, Renault-Nissan, PSA Peugeot Citroën, Volvo, Ford, General Motors, Toyota, Mitsubishi and Fiat as well as the energy providers RWE, E.ON, EnBW (D), Electricité de France (F), Vattenfall (S), Electrabel (B), Enel (I), Endesa (E), EDP (P) and Essent (NL).

The charging plug is just the beginning: North Rhine-Westphalia wants to position itself as a model region for electric mobility in Germany and Europe. By 2020 the state aims to bring at least 250,000 electrically powered vehicles – from plug-in hybrids to purely battery-powered vehicles – into the market. It intends to significantly increase the market share of suppliers from North Rhine-Westphalia in the overall German market for electric mobility and to promote the settlement of new automobile manufacturers in order to utilize the market opportunities of this future technology for North Rhine-Westphalia and to move forward with the necessary structural changes in the automotive industry.

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To this end, the state has drawn up a *"Master Plan for Electric Mobility in North Rhine-Westphalia"*. The most important players are the companies and application-oriented research institutes which have the outstanding knowledge and project ideas to make the necessary research and development contributions. In the context of the current Target-2 Contest ElektroMobil.NRW, the state of North Rhine-Westphalia is also providing up to 60 million euros for research and development and industrial funding.

Within a very short time, sustainable, electric vehicles will be developed and prepared for market launch in North Rhine-Westphalia. The state intends to assume a leading role on the path from the internal combustion to the electric engine and invites competent partners from Germany and abroad to help shape a new mobility.

About NRW.INVEST

NRW.INVEST GmbH serves as the central contact point for investments in North Rhine-Westphalia. It provides potential investors from Germany and abroad with a one-stop service ranging from location information and business premises searches to arranging and guidance through negotiations and approval procedures. In addition to subsidiaries in Japan and the USA, NRW.INVEST operates foreign branch offices in China, India, Korea and Turkey. In China, NRW.INVEST is represented by three offices in Nanjing, Peking and Shanghai.

The expertise in the automotive industry and the excellent energy technology know-how present in North Rhine-Westphalia provide ideal conditions for innovative solutions in the field of electric mobility.

To effect a clear and resolute change of direction, however, many questions still have to be answered – particularly with regard to the battery as the new fuel cell in vehicles. Designers are faced with challenges due to its size and weight. Storage capacity, vital to the vehicle's range, still falls significantly short of requirements. And it is not only the high cost of battery production that gives manufacturers cause for concern. As they lack the necessary experience, it is difficult for them to guarantee sufficient warranty periods for the quality and service life of the batteries. North Rhine-Westphalia is well prepared for this new technology. Leading international researchers are working on lithium-ion technology and new kinds of energy storage at the Westfälische Wilhelms-University in Münster, where the range and durability of lithium-ion batteries are studied and tested in field trials. At RWTH Aachen University, a recognized centre of excellence for automotive engineering, a five-Volt lithium-ion cell with a long service life for hybrid and electric vehicles is currently under development.

At present, however, Asian producers from China, Korea and Japan dominate the battery market, of which they account for 90 percent. The future demand for electric cars will result in huge capacity increases. Ultimately, large quantities will have to be produced in the vicinity of the car makers as longer transportation routes are not compatible with weight and transport safety requirements. Consequently, Asian manufacturers will also establish production capacities in Europe in the medium term. NRW.INVEST, the economic development agency of the state of North Rhine-Westphalia, has set the goal of acquiring investors from Asia and North America for the Rhine/Ruhr region.

At present, nearly 100 companies and scientific institutes in North Rhine-Westphalia are involved in the subject of electric mobility. In order to become the leading region in electric vehicle production, it is necessary to identify as many companies as possible in the production process.

In North Rhine-Westphalia there are 13 companies and research facilities developing components for hybrid and electric vehicles alone. At RWTH Aachen University, for example, a team of researchers is developing the Street Scooter prototype, a low-cost electric vehicle for urban traffic, with the aim of producing 10,000 units per year from 2012. Also in Aachen, Ford operates the only research centre outside the USA. Together with the city of Cologne and the municipal electric company Rheinenergie, it is testing 10 electrically powered Ford Transits. The Essen-based energy agency Con Energy has launched its electro-mobile Mia. Priced at 20,000 euros and with a range of 70 kilometers at present, 10,000 units of the small city-mobile are planned to be produced next year. The Essen power company and the French car maker Renault are putting 150 electric cars on the road, to name just a few cases in point – all examples of pilot projects which have now been launched in the model region for electric mobility North Rhine-Westphalia.

The new players: energy suppliers in the no. 1 energy state

The question has long ceased to be whether we will one day be driving electrically powered cars – now it is only a question of when. With the development of infrastructures and networks for electric mobility, new players, such as energy supply companies that previously had little or nothing to do with the individual motorization of society, have become involved.

North Rhine-Westphalia is the number one energy state in Germany. Three of the five largest German supply companies are based here. One third of German electricity is produced in NRW and 40 percent consumed here. Furthermore, the energy industry recognizes the possibility of using electric cars as energy storage units on wheels for wind-powered electricity, which is only available irregularly. Using smart metering, these vehicles could collect electricity cheaply at night and, when parked during the day, feed their electric charge back into the grid at a higher price.

Energy supply companies have established a clear goal for themselves to bring electricity onto the roads. The establishment of customer-friendly charging stations in various German cities has already begun. Their declared goal is to combine a comprehensive network of public and private charging stations with an innovative accounting system that guarantees fast, safe and uncomplicated charging. On-the-spot charging should be available in parking spaces whether the driver is at work, shopping, eating in a restaurant or watching a movie.

As the energy suppliers will be the new players in electric mobility, NRW.INVEST expects good competitive opportunities. The energy suppliers contribute their expertise in terms of infrastructure and networks. Besides the large corporations RWE AG (Essen), E.ON AG (Düsseldorf) and Evonik Industries AG (Essen), local energy suppliers in Aachen, Bochum, Bonn, Dortmund, Duisburg, Düsseldorf and Krefeld have also entered into the planning of pilot projects in electric mobility. As the number one energy state, North Rhine-Westphalia possesses a dense research landscape in terms of the production and distribution of energy.

Electric mobility makes a wide variety of demands on the industrial environment. Different industries will have to cooperate with each other more than before: the automotive industry, energy supply, the chemical industry, information and communication technology and the recycling industry. The multi-faceted industrial landscape of North Rhine-Westphalia offers ideal conditions. Special demands on research and development, as well as on the development of new production capacities, are made in the areas battery and vehicle technology, as well as the development and establishment of infrastructures and networks. The model region North Rhine-Westphalia is well equipped in all three areas. Here investors will find a highly qualified research landscape, efficient R&D service providers and a wide variety of industrial cooperation partners.

Expertise in battery technology

What work is in progress?

At several locations, universities, R&D service providers and key players in the industry are involved in the research and development of new and improved energy storage units. At the universities in Aachen, Bochum, Dortmund and Duisburg-Essen, research is conducted in areas which include lithium-ion technology, battery safety and battery recycling. Top international research of lithium-ion technology and new kinds of energy storage is based at the Westfälische Wilhelms-University in Münster. The research of Prof. Dr M Winter, who holds an endowed professorship of German industry in applied materials science for electrochemical energy storage and energy conversion, is recognized throughout the world.

Expertise in automotive engineering

What work is in progress?

The “Ultra Low Emission Vehicle – Transport Using Advanced Propulsion” is a research project of the Laboratory for Automation Technology and Electric Drives at Cologne University of Applied Sciences. Research is being conducted on the “plastic-intensive electric vehicle” at RWTH Aachen University. Weight-saving through sheet steel lightweight construction and new vehicle architectures are also the subject of research and development here. As part of the “SmartWheels” project, research is conducted into the network integration of electric vehicles into the convergent IT structures of the energy system. Energy management, control and driver assistance systems are further topics of industrial research projects.

Expertise for infrastructure and networks

What work is in progress?

At RWTH Aachen University, research is conducted on mobility and vehicle use patterns as well as market launch scenarios and their consequences on infrastructure. In this context, the focus is also on the effects of different drive technologies on mobility in urban traffic. Other research topics are the effects of energy storage systems on energy supply and road traffic. RWE AG is working on the development of an electricity infrastructure for electric vehicles. In several cities in North Rhine-Westphalia, hybrid buses for public transport are being tested and scientifically monitored in field trials. The first hydrogen filling stations for vehicles with fuel cell drive have gone into operation. Fuel cell buses are already in use in Düsseldorf and in the Ruhr Metropolis region.

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The German automotive industry sets standards around the world. Its technological expertise is backed by a strong education infrastructure. In North Rhine-Westphalia twelve universities and universities of applied sciences alone offer automotive-related studies and conduct research on behalf of the automotive sector. Besides the excellent university landscape, the state can also boast numerous private-enterprise research institutes which, together with the strong automotive supply landscape, provide the perfect basis for intensive knowledge transfer. As a state-wide automotive cluster and in cooperation with regional networks, the “AutoCluster.NRW” strengthens knowledge transfer between research, development and production.

North Rhine-Westphalia still has far to go before it will become the lead market for electric mobility, but the route is clearly laid out. Come on board, join the ride! ■

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NRW.INVEST (NORTH AMERICA) LLC
NRW.INVEST (NORTH AMERICA) LLC, a wholly-owned subsidiary of NRW.INVEST GmbH, informs companies in North America (USA and Canada) about the business location of North Rhine-Westphalia, its environment and investment climate, as well as about legal and social conditions, towns, cities and locations, industries, and market opportunities. It identifies North American firms’ interest in locating and advises them as they make their move to North Rhine-Westphalia.

To this end, NRW.INVEST (NORTH AMERICA) LLC organizes visits to North American companies, as well as seminars and information events about North Rhine-Westphalia as a business location or about particular industrial or service sectors.

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North Rhine-Westphalia - Model region for electric mobility Come on board, join the ride!

Today North Rhine-Westphalia (NRW) is one of the most important automotive locations in Europe. With 18 million people it is both the most populous and the most densely populated federal state in Germany. With some 2,200 kilometers of expressways and 17,700 kilometers of highways and state roads NRW thus possesses one of the densest road networks on the European continent. The expertise in the automotive industry and the excellent energy technology knowhow present in NRW provide ideal conditions for innovative solutions in the field of electric mobility. Invest in electric mobility! NRW has a wide variety of possibilities to offer.

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