Skadden
Crisis Management

How to Manage Corporate Crises

An Interview with Peter A. Atkins, Esq., Senior Partner, Corporate and Securities Law Group, New York; Robert S. Bennett, Esq., Co-Head, International Government Enforcement Litigation Group and Criminal and Civil Litigation Practice, Washington, DC; and Sheila L. Birnbaum, Esq., Head, Complex Mass Tort and Insurance Group, New York, Skadden, Arps, Slate, Meagher & Flom LLP and Affiliates


Peter A. Atkins


Robert S. Bennett


Sheila L. Birnbaum

Do you have a set of rules at Skadden that defines how you prevent or handle a crisis?

Atkins: Crisis management is all about mitigation. On the prevention planning front, a critical step is to be able to identify the high-risk areas in the company, to foster risk mitigation and crisis avoidance. It's also essential to understand that the concept of crisis management is best served by early detection. If you sense something might be happening, to mitigate the crisis effect from the very beginning, you need to get there early and understand how to manage it.

Bennett: Companies must anticipate the possibility of a crisis and must take steps in the ordinary course of business to be prepared for one.

Atkins: And this can be very difficult to do since you can't define a crisis simply; it may stem from a financial or regulatory event, a mass torts exposure, a plant explosion, a senior executive death or departure, and so on. Managing crises requires advisors with a depth of experience, who have been there and done it and recognize all of the issues.

It sounds like these situations can quickly become unmanageable. How do you maintain control?

Birnbaum: Sometimes, executives think that the judicial system is out of control, but they don't anticipate that they could have so little control over a particular issue. In actuality, these situations can easily take on a life of their own and escalate.

Bennett: When a crisis-inducing event occurs, the company is often almost immediately put in a difficult situation. It must publicly respond to allegations before it knows all the facts. The art is to make statements that show concern and that the company is getting the facts and will do the right thing. At the same time, it can be a grave error to make a statement that you later retract, because the company will lose credibility, and its competence will be questioned.

Atkins: To attempt to control a crisis, management needs to work through it in a very short timeframe, before it explodes into an absolute disaster. There is virtually no margin for error in the key decisions, reactions, and communications at the front end.

How do you see crisis management evolving in the next 10 years?

Birnbaum: There's no end to the number of crises that companies or individuals are going to face in the next decade or so. We're going to find that this is a worldwide phenomenon, affecting not only U.S. corporations. Crises will have a more international flavor, as we've seen in a number of serious investigations in Europe. Firms that are well-situated globally are going to be advising and assisting their clients in handling these crises around the world.

Bennett: For example, multinationals in Europe are facing challenges that they haven't seen before. In many countries, they don't indict companies; they indict individuals only. Multinationals may have a false sense of security when their origins, principal executive offices, and key executives are from parts of the world where there is no such thing as corporate criminal liability. All of a sudden, companies with an international presence are facing inquiries that they have never heard of before, and they don't know how to react.

It sounds like these companies would be reluctant to call something a crisis, then.

Birnbaum: What often happens is that many corporations – even the higher echelons of corporations – don't know a crisis is brewing. They try to manage an issue so that it does not escalate, but they don't fully appreciate the crisis implications. Then it escalates, and we've seen many drug companies, for example, come under attack because they did not respond quickly enough.

Atkins: It's partly the denial mechanism; unconsciously and consciously, people running a business don't like to suggest it's in "crisis." This is the antithesis of what you normally would like to project – business as usual, things are under control. Another part is recognition of the media's and the public's intense search for crisis situations that will enable them to dissect a company and assign blame. This doesn't mean an incident has to explode into a disaster, though. The key is recognizing events and circumstances for what they are – including how they are likely to be perceived and dealt with by others – and designing a real-time action and communications program that fits.

Birnbaum: That's right. Most important is the judgment and the experience of the people who are responding. This is what people like Peter, Bob, and I bring to the table: experience and judgment. The experience we have from handling so many varied crises is invaluable. At Skadden, we're able to create a highly integrated team that can assist with the substantive parts of a unified response, whether it's white-collar crime, products liability, securities, Sarbanes-Oxley, or SEC regulations.

What legal resources are used to address crisis situations?

Bennett: The remarkable thing about Skadden is our team approach. We put the right team together, and do it very quickly. Each of us calls on the other very early on. From Peter's expertise with corporate governance issues, to Sheila's products liability and mass tort liability experience, to my group's civil litigation and criminal enforcement experience, we are well equipped to handle the highest stakes for global clients.

Birnbaum: Skadden is especially well-situated to handle crises of a global nature. We have very experienced lawyers in cities across the U.S. and in major countries and cities throughout Europe and Asia, and are used to dealing with matters that have multinational dimensions. I expect that we will be seeing more and more crises involving both domestic and foreign corporations, as well as multinationals. ●

Skadden
European Mergers and Acquisitions

Trends in European Mergers and Acquisitions

An Interview with Partners Michael E. Hatchard, Esq., Cross-Border M&A and Corporate Finance, London; Bernd R. Mayer, Esq., Cross-Border M&A and Corporate Finance, Munich; Paul W. Oosterhuis, Esq., International and Corporate Tax Law, Washington, DC; Tim Sanders, Esq., Tax, London; Pierre Servan-Schreiber, Esq., Cross-Border M&A and Corporate Finance, Paris; and Scott V. Simpson, Esq., Cross-Border M&A and Corporate Finance, London, Skadden, Arps, Slate, Meagher & Flom LLP and Affiliates


Michael E. Hatchard


Bernd R. Mayer


Paul W. Oosterhuis


Tim Sanders


Pierre Servan-Schreiber


Scott V. Simpson

The 2006 first-quarter volume of announced M&A deals in Europe was the highest for that period since 2000. What is fueling the activity and why?

Simpson: Europe has witnessed a boom in cross-border mergers and acquisitions since the beginning of 2006, particularly hostile takeovers. Purchases of European companies reached an unprecedented $418 billion within the first quarter of the year, compared with purchases of American companies totalling $211 billion in the same period. Europe has seen large pan-European hostile takeover battles, such as the fierce $25.6 billion merger of Netherlands-based Mittal Steel with Luxembourg-based Arcelor, the $26.9 billion takeover of Endesa of Spain contested between E.ON of Germany and Gas Natural of Spain, and the $14.5 billion takeover by Ferrovial of BAA, and large friendly combinations, such as the $14.3 billion merger of Autostrade of Italy and Abertis of Spain.

The upsurge in European M&A in the first six months of 2006 was founded primarily on favorable underlying economic conditions. Large European companies restructured their balance sheets substantially after the downturn that followed the March 2000 stock crash, implementing significant operational and financial cost-cuttings, and positioning themselves for growth opportunities as they arose.

Hatchard: The cost of capital has been relatively low, and capital has been fairly easy to raise, making it easier for strategic players and private equity funds alike to lever up and offer cash, as opposed to stock, as consideration. In fact, the proportion of cash that was offered in this merger wave to date marks one of the principal differences between the current takeover boom and the one at the end of the '90s.

Servan-Schreiber: Another clear driver has been the need for horizontal cross-border consolidation in Europe, to create a class of pan-European champions able to compete with their counterparts around the globe. The European market continues to be extremely fragmented in a number of industries that have been at the center of the recent increase in merger activity, such as utilities, energy, industrial, and financial services.

Mayer: Executives of European "national champions," as well as smaller players, are moving to grow by way of acquisition based on the realization that they need to increase the scale and geographic footprint of the companies they manage if they are to position them to seize growth opportunities in the principal developing economies, particularly the areas collectively known as BRICET [Brazil, Russia, India, China, Eastern Europe, Turkey]. Despite regulatory harmonization lagging behind its planned implementation, the EU single market and single currency have begun to create an environment that is conducive to this much-needed process of European consolidation.

Many major companies have a lot of cash to use for European acquisitions. From a tax perspective, does that mean structuring the transactions is relatively straightforward?

Oosterhuis: Yes, compared with transactions that must be tax-deferred for target company shareholders. However, in many circumstances, an otherwise straightforward cash acquisition can be complicated by the need to defer tax for key employees or a major shareholder. These circumstances can typically be accommodated by permitting the shareholder to retain some form of share interest in the target or security issued by the bidder, but have that interest exchangeable into acquiring company shares to provide liquidity. Beyond that, cash acquisitions are real tax planning opportunities. While most European jurisdictions have thin capitalization rules that must be followed, those rules typically permit substantial inter-company borrowing to fund acquisitions. That allows interest expenses to be deducted against the target's income after the acquisition, with interest income accruing in a jurisdiction with a relatively low tax rate. The result can be a lower worldwide tax rate on the target's income after the acquisition.

Hostile takeovers and unsolicited bids have increased recently in Europe. Why?

Simpson: Concurrent with the increased M&A activity, Europe has also seen an unprecedented rise in hostile takeovers, which was caused by an additional layer of factors. Timing is one of the principal dynamics at play here. Strategic industrial players have seized the window of opportunity opened by stable economic conditions to achieve growth by way of acquisition, which is faster than organic growth. But in order to snatch up opportunities as they arise, beat competition from private equity players, and force consolidation in the face of the reticence of target management, national governments and, at times, national regulators, strategic players have had to resort to aggressive takeover tactics. Changes in the structure of Continental European capital markets in past years have been crucial in laying the ground for this upsurge in hostile takeovers; in the last 10 to 15 years, Europe has seen an increasing number of companies coming to market, and over time, European stock has become more

widely held and increasingly liquid. All of these factors are causing a change in the way European executives and shareholders see hostile takeovers, which is reminiscent of the change in mentality that took place in the U.S. as a result of the wave of hostile M&A activity in the '80s.

Is government protectionism still an important issue in cross-border deals in Europe?

Servan-Schreiber: Notwithstanding the increase in hostile activity and the continued harmonization of European laws, national governments seem to find it difficult to abstain from intervening in cross-border takeovers. A few recent examples include the involvement of the French and Luxembourg governments in the early stages of the Mittal Steel-Arcelor merger, of France in the proposed takeover of Suez, of the Spanish government in the takeover of Endesa, and Italy's role in the merger of Autostrade and Abertis. National governments become substantially involved in virtually all high-profile mergers in continental Europe, and, if they are hostile takeovers, national governments are a formidable force to be reckoned with by bidders.

Simpson: That said, while in certain circumstances national governments have been able, and will continue, to influence the outcome of takeover battles, their power and appetites are diminishing substantially as European stocks become more widely held and stock market forces drive takeovers to completion. For example, Dutch ABN AMRO's takeover of Italian Banca Popolare Italiana, which was strongly opposed by Italy's government and Italy's central bank, was successfully completed in the first quarter of 2006. It is reasonable to assume that as stock markets continue to expand, market forces and industrial logic will prevail in Europe over national protectionism. But for the moment, certain industries may continue to be insulated by government forces from unsolicited mergers and acquisitions activity.

What is the status of takeover regulation in Europe? How do you see this process evolving?

Mayer: Another obstacle to European consolidation through unsolicited takeover offers is the lack of regulatory harmonization. While for the last 15 years, the EU Commission has been trying to create a regulatory infrastructure that would be conducive to consolidation, it has achieved mixed results at best. Certain milestones have been reached: the single currency, the EU prospectus directive, and one accounting standard for all listed companies – IFRS. However, in other areas, largely as a result of member states' lack of political willingness to put national champions up for sale, the EU Commission has not achieved its objectives to establish a uniform takeover code, or uniform set of corporate governance standards, and golden shares and other forms of veiled or blatant national protectionism continue to exist.

As hostile takeovers increase, what defensive measures are being taken by targets?

Simpson: The takeover directive, in particular, could have been an opportunity for the EU to establish a uniform takeover code. But the EU Commission's proposal to eliminate the ability to raise takeover defenses in connection with hostile bids – consistent with the approach in the U.K. – was, barring a few exceptions, widely rejected by continental EU member states as too radical a change in approach and would have opened the door to takeovers from outside the EU – especially, as most countries feared, the U.S. As a result, the rules against defensive measures were made optional, and, while the takeover directive has still not been implemented in many of the principal EU economies, most EU countries seem inclined to retain their existing framework with regard to a target company's ability to defend against hostile bids.

Hatchard: That said, a trend in continental Europe is emerging with respect to takeover defenses, which is a hybrid between the approach in the U.S. and the U.K. In the U.S., takeover defenses are allowed to a point, as they are subject to market scrutiny and a very sophisticated set of ever-developing rules established through more than 25 years of takeover-related court cases, primarily around the business judgment rule. In the U.K., in order to limit litigation, takeovers are regulated by a takeover code, supervised by a sophisticated regulator – the Takeover Panel – and takeover defenses are generally not allowed, beyond a merits-based response or steps that require stockholder approval.

Servan-Schreiber: The principal jurisdictions in Continental Europe generally contemplate that targets can erect structural defenses against hostile bids, provided that this ability is subject to the scrutiny of takeover supervisory authorities, whose degree of knowledge and sophistication varies widely, depending primarily on the historic level of mergers and acquisitions activity in that country. While the latitude afforded to target boards to defend against hostile bids differs greatly from country to country, and the regulatory approach is not always consistent, the acceptability of mechanisms implemented by target boards is increasingly subject to a more powerful scrutiny – that of the market, especially large institutional investors.

Mayer: Pan-European and global institutional investors, including hedge funds, are emerging as the most important driving force in the success or failure of defensive strategies. In the Mittal Steel-Arcelor takeover battle, for example, Arcelor's first set of defenses – an extraordinary dividend, a proposed buyback, and a lock-up of a strategic asset in an independent trust – was widely accepted, as the market expected it would trigger an improved offer by Mittal Steel. However, Arcelor's second defense – a proposed merger with SeverStal of Russia, subject to a much criticized EGM shareholder veto with a 50-percent quorum – was rejected by the market and, following a further substantial improvement in the offer terms proposed by Mittal Steel, the Arcelor board had no choice but to recommend Mittal Steel's superior offer.

Are transactions that are tax-free to target shareholders on the rise? If so, what tax planning concerns do they create?

Sanders: Under the EU Directives, as well as the domestic laws of most EU jurisdictions, transactions that are tax-free to target shareholders can be accomplished as long as those shareholders receive stock in, or other securities of, the acquiring company as their consideration. However, traditionally problems often resulted from a share exchange. In Continental Europe, most countries' corporate laws only permit cross-border combinations to be accomplished by exchange offer, unlike the U.K., which permits mandatory share exchanges under a scheme of arrangement, and the U.S., which permits subsidiary mergers using parent stock as consideration to target shareholders. Because acceptance-in-exchange offers inevitably fall short of 100 percent, dealing with minority shareholders can be difficult. As legislation implementing the new Societas Europaea (SE) and the Takeover Directive is adopted in more countries, we are hopeful that cross-border mergers will be more feasible as a technique to avoid this problem.

Hatchard: A second problem is what the investment banks call "flowback" – the tendency of target shareholders to sell down acquiring company shares that trade principally in another market. That is less of a problem for combinations between EU companies, but can be unmanageable for combinations between U.S. and EU companies.

In conclusion, how do you see the future of M&A in Europe?

Simpson: In summary, the future for M&A activity in Europe looks bright. In times of economic stability, European companies will be pushed by institutional investors to consolidate to achieve larger scale and improved efficiency. The markets will continue to expect and require ever-improving disclosure standards, which are quickly catching up with standards in the most demanding jurisdictions, such as the U.S., which, in turn, will attract more investment from institutional investors worldwide.

Servan-Schreiber: The EU, for its part, will inevitably continue to harmonize the regulatory framework, progressively reducing the ability of governments to protect their national champions where this is not supported by a sound industrial logic, hence fostering consolidation. ●

Skadden
Asia

Opportunities in Asia

An Interview with Partners Jon L. Christianson, Esq., Corporate, Beijing; Michael V. Gisser, Esq., Corporate, Los Angeles; Phyllis G. Korff, Esq., Corporate Finance, New York; Gregory G. H. Miao, Esq., Corporate, Hong Kong; Nicholas Norris, Esq., Hong Kong Law Practice, Hong Kong; Jonathan B. Stone, Esq., Corporate, Hong Kong; Dominic Tsun, Esq., Hong Kong Law Practice, Hong Kong, Skadden, Arps, Slate, Meagher & Flom LLP and Affiliates


Jon L. Christianson


Michael V. Gisser


Phyllis G. Korff


Gregory G.H. Miao


Nicholas Norris


Jonathan B. Stone


Dominic Tsun

What are the prospects for the internationalization of transactions from the emerging nations of Asia into the rest of the world?

Gisser: Merger and acquisition activity emanating from the leading economic powers in Asia, in particular China and India, has been catapulted into prominence with the recently announced $33 billion transaction between Mittal Steel and Arcelor of Luxembourg. In fact, events have been building in this direction steadily over the last five to 10 years, in those countries as well as in Korea, Taiwan, and elsewhere in the region.

Chinese companies have made a number of prominent acquisitions, notably policy-driven transactions in natural resources fields. Canadian and Canadian-listed companies have been the recipients of an outsized share of prominent deals coming from China. It is important not to misconstrue the political sensitivities that have interfered with major acquisitions from China into the United States. For every prominent transaction that might be blocked in Washington, DC, there are a number of transactions that might be intermediated by private equity firms or accomplished through offshore vehicles, achieving the same net effect – increasing Chinese exposure to U.S. assets. And whenever an asset in basic industries throughout the world becomes available, one can be certain that Chinese buyers are looking at it, whether it is in China's backyard in Asia, in the former Soviet Union, or in Africa, South America, Europe or North America. Chinese companies are continuing to build up a complement of sophisticated corporate managers with international backgrounds. Over time, through middle-market transactions in a wide range of industries as well as landmark deals, the leading Chinese companies will steadily become more effective competitors for assets in the international market.

Korff: Chinese companies have begun to invest abroad, but they face some challenges in doing so. First, Chinese companies need to overcome a number of hurdles in order to become successful acquirers of overseas assets. In addition, most would-be acquirers are not as experienced in negotiating and closing M&A deals as many other competing bidders. Chinese entrepreneurs come from a corporate culture of proceeding slowly and with caution to ensure the correct result, and they have not yet developed sufficient expertise in dealmaking or integrating acquired assets. These factors often hinder the Chinese acquirers' ability to become the preferred bidder, outside of offering a substantial price premium.

Second, Chinese purchasers are likely to experience a steep learning curve in developing the necessary management know-how to operate these assets in foreign countries with laws, cultures, and business customs that are very different than China's. Chinese business executives will need to spend time and money understanding the legal and cultural rules of their host countries and will need to adapt themselves to very different management styles and cultures in these countries.

Christianson: I think that Chinese CEOs and government leaders have come to view acquisitions in the U.S. or other Western countries as a significant risk. China's ability to influence public opinion in the West is quite limited, and, coupled with the fact that the politicians in many Western countries are willing – and even eager – to make these acquisitions political issues, an acquisition is going to have to be either very compelling or relatively certain not to attract attention before you see the SOEs [state-owned enterprises] making a bid. More activity by Chinese companies will take place in markets where the political system is less likely to make these acquisitions a political issue.

The other consequence of the politicization of these acquisitions is that the U.S. may lose the moral high ground in some aspects of trade negotiations. The phrases "national interest" and "strategic industry" will be heard more often by U.S negotiators as reasons for restricting access to China for U.S. companies. They will hear the same arguments that our own political leaders have made in recent months for restricting access to the U.S. markets by foreign companies. As a result, it will become harder for U.S. companies, including the private equity firms that are currently so interested in the China market, to complete acquisitions in China.

Are there more M&A opportunities in China for multinational corporations today, and are deals easier to make than before?

Miao: Yes. The Chinese government has decided to privatize the

300,000-plus state-owned enterprises – in industries that range from manufacturing to retail to software to consumer goods – to domestic and international investors through sales. Kodak, for example, has regained the market leader position from Fuji through its acquisition of the entire Chinese photographic industry. However, the government will continue to maintain tight control over its "strategic industries," such as oil and gas, telecom, power, transportation, media, mining, and banking, through its controlling stake in 198 – soon to be reduced to 100 – large state-owned companies.

New regulations have been promulgated to facilitate acquisitions of state- or privately owned Chinese companies by multinational corporations, through asset and/or share purchases. Starting in 2007, new accounting rules will take effect, giving parties more flexibility to evaluate the sellers' assets, which form part of the purchase prices. However, dealmaking remains more difficult for financial investors, as government policies have historically favored the industrial players.

Norris: Much of the recent increase in the level of M&A activity in China and Hong Kong has been a direct response to the desire of U.S.- and Europe-based multinationals to gain a strategic foothold in corporate China. A notable development, however, has been the continuing and growing interest of hedge funds and private equity funds.

While private equity funds have a long history of investing in China-based enterprises, the recent arrival of hedge funds has changed the landscape for M&A transactions in the region. Reflecting the experience in the U.S. and Europe, hedge funds have moved away from their more traditional business models and are now seen as increasingly aggressive acquirers of assets. Fueled by great liquidity and the search for good returns, hedge funds have been involved both as proprietary investors and lenders in leverage financed, "take private," and management buyout transactions. The hedge funds have shown a greater risk appetite than commercial bank lenders and have been quick to propose more structured "mezzanine" financings, which may include some form of "equity kicker." These funds have also been making "private investments in public equity," subscribing, for instance, in convertible, redeemable preference shares and convertible bonds in Hong Kong-listed companies, thereby securing a fixed return, but with the potential for an upside as the share price increases.

This trend reflects both an opportunity and a risk for business leaders. The funds provide an additional source of equity or financing for developing companies. Acquisitive companies, too, now have a broader pool of consortium partners and financing opportunities. At the same time, some of the more activist hedge funds can be unwelcome shareholders, leveraging their shareholding interest to push for changes in strategy or corporate governance.

How has the role of legal advisers in China changed?

Christianson: I should note that, unlike most firms, Skadden started its China practice in the '80s representing Chinese state-owned enterprises with their overseas problems. So, when the firm opened its office in Beijing in 1991, it was quite natural – though atypical – to work with large Chinese state-owned enterprises, such as China Construction Bank, Netcom, Sinopec, and Huaneng, as they began undertaking large financings. While each SOE has its own unique culture, there are a lot of common themes in those cultures. The extensive experience that Skadden has gained over the years in being counsel for these companies not only helps the firm to work more effectively with new Chinese clients, but many MNC clients find our insights into how SOEs generally make decisions to be very helpful.

Tsun: Traditionally, a significant part of the work done by lawyers is focused on a review and analysis of historical facts and confirming that the documentary trail actually matches up with prevailing reality. That is still a very important part of our work, but increasingly we need to give good advice on how things may change, or even how they are likely to change, in the foreseeable future. For example, an investor may want to know whether the "unique opportunity" that it has been presented with is going to stay that way when regulations open up. Likewise, they will want to know whether the rights they have under the governing agreements will in fact be enforceable in a meaningful way. For some investors, the availability of a qualifying IPO in Hong Kong as an exit is an important consideration and, in this regard, one needs to keep up-to-date on the thinking of the Hong Kong Stock Exchange on pre-IPO investments. No one has a crystal ball, but the ability to put these potential changes – which can be evolutionary or revolutionary, domestic or cross-border – into context for potential investors is increasingly important. Needless to say, any such explanation must be made in a way which is understandable, particularly for clients who do not regularly invest in this part of the world. It is a huge challenge, but always an interesting one.

How does India fit into the trend of internationalization, both for inbound and outbound investment?

Gisser: The Indian case is equally interesting. Major groups in India have been acquisitive over the years, in a wide range of sectors. Deal professionals will tell you that in competitive sale situations, when a buyer from a more conventional acquirer country triumphs, more often than not there was an Indian bidder playing the role of runner-up. The impressive network of persons of sub-continental origin in top management positions in major companies around the world facilitates an impressive flow of information about opportunities that Indian companies are poised to take advantage of, both as a management matter and, given their support by the investment banks, as a financial matter. Transactions out of China and India are set for explosive growth, and we will all see a stunning globalization of the international M&A business as a direct consequence.

Stone: India has come into its own. The relaxation of foreign investment restrictions in industries including banking and financial institutions, telecommunications, media and – most recently – real estate, has resulted in substantial growth in the number and size of foreign investments into India. Unlike China, where growth of the private sector followed the deregulation and privatization of large state-owned enterprises, India has long had a vibrant entrepreneurial private sector. Many businesses have grown through generations of families and, in the last four or five years, have attracted foreign financial and strategic investors and have listed on Indian, European, and U.S. stock exchanges.

Foreign investors looking to enter into strategic alliances or make acquisitions in India will often find themselves initially negotiating with a small number of large family shareholders or a single individual shareholder who, more often than not, will have a deep understanding of not only his business, but also of the substantive concerns for the foreign investor. For listed companies, general offer and other takeover rules administered by the Securities Exchange Board of India (SEBI) will also apply to most acquisitions above a 15-percent threshold.

India is still an emerging market and foreign investors need to be mindful of the significant regulation that still exists. Delays caused by requirements for regulatory approvals are not uncommon, and seeking redress to Indian courts to resolve commercial disputes is often not timely or practical. Nevertheless, with its large, well-educated, English-speaking workforce and growing consumer class, India is expected to continue to attract substantial foreign investment. ●

Skadden
International Arbitration

Experts in International Arbitration

An Interview with Partners John L. Gardiner, Esq., New York, Paul Mitchard, Esq., London, and Karyl Nairn, Esq., London, International Arbitration Group, Skadden, Arps, Slate, Meagher & Flom LLP and Affiliates


John L. Gardiner


Paul Mitchard


Karyl Nairn

What are the current trends in international arbitration?

Mitchard: Apart from an overall increase in the number of international disputes being referred to arbitration, we are seeing clear trends in the subject matter of cases being arbitrated, the regions from which arbitrations are arising, and the types of arbitration institutions and rules being adopted for the disputes. In addition to the traditional joint venture disputes, deriving in particular from infrastructure projects, there is an appreciable growth in the number of cases arising out of disputes in the energy sector. Given the recent volatility in this sector, the trend is not surprising. The cases are both upstream and downstream, and range from disputes over oil and gas concessions to the pricing of fuels.

Regional trends also are linked to energy and commodities disputes, with a clear growth in cases from Russia and the CIS [Commonwealth of Independent States, formerly the USSR]. We are handling disputes associated with aggressive action by certain countries in South America, and cases from Asia, including China and Indonesia, are becoming more commonplace.

Nairn: We're finding that leading arbitration institutions, such as the International Chamber of Commerce, are often nominated in the contracts under which numerous energy disputes arise. Also, many of the Russian investments in the late '90s adopted English law and arbitration provisions – in particular, references to arbitration under the London Court of International Arbitration [LCIA] Rules. Two of our billion-dollar-plus disputes are currently being determined in LCIA arbitrations based in London. In addition, the American Arbitration Association has seen an appreciable growth in the number of international disputes now being decided under the international rules of its ICDR division. There also is growth in bilateral investment treaty cases under the auspices of the International Centre for Settlement of Investment Disputes, as investors become more aware of the breadth of the potential relief available to them against foreign governments.

According to a study published recently by PricewaterhouseCoopers in conjunction with Queen Mary University, the confidence of corporations in international arbitration as a method of dispute resolution has increased. Is that your experience?

Gardiner: Yes, particularly because, unlike in a court, corporations generally have the ability to appoint one person on the arbitral panel. In addition, companies typically will have a say in the selection of the chairman. This is critical, as a number of our clients have had unfavorable experiences with courts in the counterparty's jurisdiction or in countries with less internationally experienced judges. Arbitration also has the advantage in that arbitrators who have experience in the subject matter of the dispute can be selected. Overall, the globalization of business is likely to continue the trend toward more, and ever larger, disputes being handled through arbitration.

With so much money at stake in large international cases, how are parties able to rely on the private arbitrators being neutral and free from corruption?

Nairn: While no one can guarantee freedom from corruption, the record for international arbitration is reassuring. Many clients turn to arbitration because of a distrust of appointed or elected judges in certain parts of the world. There is a large body of well-known and well-respected private arbitrators from whom to choose, whose reputation depends on their honesty and integrity. Skadden's experienced arbitration team has an in-depth knowledge of the candidates for arbitral appointments. We assess the language skills, legal knowledge, integrity, and subject-matter expertise, and we would only propose individuals with a proven record. Certain arbitral institutions have panels of arbitrators who are carefully vetted and this can be an important safety net for clients.

International arbitration is traditionally associated with the venues of England, France, and Switzerland. Has that changed?

Gardiner: Somewhat, although they remain the most popular seats. However, there are a growing number of arbitrations in the United States, principally New York, and it is likely that the Far East will see a growing number as well, as China emerges as an economic powerhouse. In addition, we continue to see changes to the composition of arbitral tribunals; it is not unusual now to find a mix of civil and common lawyers, with CIS arbitrators at a premium. There is also a greater number of U.S. arbitrators, reflecting a greater number of U.S-related arbitrations, particularly with the seat in London.

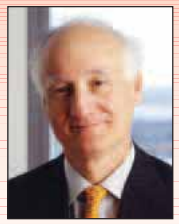
As an international law firm, what is the biggest challenge in dealing with clients on international arbitration cases in Europe?

Mitchard: Managing expectations and being alert to cultural issues. In some jurisdictions, expectations are dictated by civil law procedural norms. Steps such as anti-suit injunctions and aggressive discovery requests can come as a real shock and need to be anticipated and explained carefully. U.S. clients, for example, need to be made aware of differences in European arbitral practice. Some of these are quite subtle and are easily missed, but a failure to regard them can cost dearly, as we have seen in several cases where assumptions by the other party about local rules, laws, and practices have turned out to be wrong. In one case, our opponent did not appreciate that security for costs could be sought against an almost-insolvent company. In another, the failure to appoint someone with appropriate legal experience in practice shut out that party's nominated arbitrator from active input into most of the major decisions in the case. ●

Skadden
Russia

The Economic Ramifications of Russian Politics

An Interview with Partners Bruce M. Buck, Esq., European Practice Leader, London, and Pranav L. Trivedi, Esq., Corporate, London, Skadden, Arps, Slate, Meagher & Flom LLP and Affiliates



Bruce M. Buck

Pranav L. Trivedi

Given recent political and economic developments, what do you view as the greatest challenges in the next year or two for foreign companies doing business in Russia?

Trivedi: The greatest challenges facing foreign investors are political and legal uncertainty and instability. There is a great deal of uncertainty surrounding the 2008 presidential elections and the current government's consolidation of power at the federal level. Many attribute the frenzy in capital markets and M&A activity to an attempt by Russian companies to secure financing and an international shareholder base as a hedge against the uncertainty as to whether President Putin and his government will directly or indirectly retain power and whether the current policies to liberalize the economy will be maintained.

Buck: Against this backdrop is the dizzying pace at which laws and regulations are evolving. On a recent IPO, for example, over the course of a nine-month transaction, the Russian securities regulator fundamentally changed the manner in which Russian companies can issue securities in public offerings. In some instances, rules were being adopted weekly and bankers and lawyers were scrambling to find out what rules the regulator had adopted. This pace of reform is also true of other rules and other regulators in Russia. These factors inevitably make Russia a particularly challenging market in which to invest.

In which industrial sectors do you see the greatest opportunities in the next few years?

Trivedi: To date, of course, there has been tremendous interest in the Russian energy sector. Two sectors poised for significant growth in the ramp-up to the next presidential elections are banking and infrastructure, particularly electricity and power generation. The regulators overseeing these parts of the economy are undertaking significant changes to make these sectors more attractive to both foreign and domestic investment. The reforms undertaken to transform and ultimately to privatize RAO UES [United Energy Systems of Russia] will be particularly interesting for global investment by virtue of its size alone.

Lack of transparency in Russian companies continues to be a problem, not to mention the volatility in the country's stock market this year. What will be the effect on the IPO market?

Buck: Market observers have commented that many of the Russian "blue chip" companies have already come to market and, as the next generation of less well-established companies tries to access the capital markets, there may be greater concern regarding transparency and corporate governance issues. The domestic stock exchanges do not have rigorous requirements and those companies that elect to list overseas generally avoid the United States and the comprehensive periodic reporting requirements of the U.S. Securities and Exchange Commission. For high-profile listings, Russian companies have opted to list GDRs [global depository receipts] on the London Stock Exchange, which, under current rules, allows foreign issuers to avoid some of the mandatory transparency and corporate governance requirements that would apply to companies listing ordinary shares.

There has been a significant amount of cross-border M&A activity recently. Do you expect that to continue for the next several years?

Trivedi: I would certainly expect M&A activity to continue, if not accelerate. There are a finite number of companies positioned to take advantage of financing opportunities in the debt and equity capital markets. For those not positioned to do so, bringing in a strategic or portfolio investor is the only real option in order to have access to capital. I would also expect M&A activity to be driven by consolidation of various parts of the economy. For example, there are over 1,000 registered banking institutions in Russia. All of these institutions will simply not be able to survive in an increasingly competitive market; bigger banks will seek to establish national footprints through regional acquisitions, and smaller banks will attempt to merge with one another in order to compete.

Private equity is booming in other parts of the world. Do you see that same trend in Russia, and, if so, will the growth continue?

Buck: Private equity has already taken off in Russia. To date, the development of private equity has been driven primarily by domestic houses that have better knowledge of the market. I fully expect the global private equity players to jump into the market, as they have significantly greater financial resources and industry-specific expertise, and opportunities abound. There are also an increasing number of private equity funds being set up by oligarchs and financial-industrial groups. These funds have been created with the cash generated by liquidating existing privatized assets and are increasingly used to make selective investments across different sectors.

As more foreign investors enter the Russian market, do you anticipate Skadden's litigation and arbitration capabilities growing there?

Trivedi: We already handle substantial arbitration work generated through our Russian practice. Because of questions surrounding the enforceability of foreign court judgments in Russian courts, most foreign investors and investment banks elect to have disputes arbitrated in international forums and foreign arbitral awards are generally enforceable in Russia. As cross-border activity increases, the related arbitration work will increase as well. Currently, we do not have plans to develop a domestic litigation practice. Litigation in Russian courts is a highly specialized and localized field, and there are already well-established local litigation firms that we can turn to when we need assistance. ●

Skadden
Latin America

The Lay of the Land in Latin America

An Interview with Partners Paul T. Schnell, Esq., New York, Jonathan D. Bisgaier, Esq., New York, and Alejandro Radzyminski, Esq., New York, International M&A and Finance, Skadden, Arps, Slate, Meagher & Flom LLP and Affiliates


Paul T. Schnell


Jonathan D. Bisgaier


Alejandro Radzyminski

What business and economic trends do you see across Latin America?

Schnell: You can't really ask that question today about Latin America, as a region. In the past, Latin America has been plagued by the tendency of international investors to view the region as a single market, so if there were problems in one country, it negatively impacted investors' views of the entire region. These days, international investors and companies are increasingly differentiating among conditions in the various countries. It's remarkable that, under the same Latin American roof, you have an IPO boom going on in Brazil at the same time Bolivia is nationalizing oil assets. Investors have maintained their love affair with Brazil, despite extreme hostility towards a country right next door.

Radzyminski: More generally, some countries, like Brazil, Chile, Mexico, and Colombia, are taking some positive steps to embrace globalization, expanding exports, and enacting more market-oriented internal reforms in an effort to create the underpinnings for sustained economic growth. Other countries are adopting populist, anti-globalization, and anti-free-market policies.

How is this affecting your practice?

Bisgaier: Our business is booming in countries that have adopted a pro-investor approach. The number of IPOs and other equity deals in Brazil during the past two years – almost 60 in total – has been astounding, and Skadden has participated in many of these transactions. Most impressive is the range of businesses that have been able to access the capital markets.

What do all these IPOs say about the region?

Schnell: They reflect the increase in liquidity, transparency, and stability in some of the markets in the region. In just the last couple of years, there has been a dramatic change in how investment demand and liquidity for Latin American companies have shifted from international markets in the U.S. and Europe to domestic markets. Long-term, this can be a tremendous source of economic growth and development for these countries.

Bisgaier: It's also important to note that corporate governance in these new public companies has changed dramatically. In almost every case, the old, dual-class voting structures, which guaranteed control for the largest shareholder, have been abandoned, and all shareholders now have the same voting rights and the right to participate in the sale of the company at the same price as the controlling shareholder. This is likely to result in acquisitions in which stock, rather than cash, is used as consideration, as sellers, for the first time, become comfortable accepting a minority position in a liquid stock.

Radzyminski: We're also seeing, for the first time, public companies that don't have controlling shareholders; the number of these companies should continue to grow as the founding families sell down in the market.

Do you think the legal environment is ready for these new transaction and corporate structures?

Radzyminski: Lawmakers and regulators are working overtime to address the new model of companies having a widely dispersed shareholder base. It will be interesting to see if the region adopts some of the international practices used to maximize shareholder value, protect against abusive takeover tactics, and promote good corporate governance – an increase in independent directors, "conflict" avoidance mechanisms such as special committees and independent advisors, greater regulatory oversight and enforcement, "majority voting" and other shareholder democracy provisions, and anti-takeover provisions such as shareholder rights plans, classified boards, and advance notice bylaws.

Have you seen a slowdown in activity as a result of the turmoil in the markets in recent months?

Bisgaier: There were some concerns that the corporate finance market would slow down substantially this past spring, and some of our transactions were delayed. However, the markets already seem to be back on track; since the problems in May, our Latin American IPOs have continued to move forward, and we've gained many new mandates. We're hopeful that, unlike previous cycles, the slowdown will turn out to be a short-term event.

Have you seen changes in companies' strategic focuses?

Schnell: The leading companies in the region are no longer satisfied with operating just in their home country. Many have pursued acquisitions to become strong players throughout the region. América Móvil, for example, has had great success with this strategy. And others, like CEMEX, have transformed themselves into global powerhouses. Today, there are a number of world class companies in the region that are giving their global counterparts a run for their money.

How do developments in Brazil compare with the other BRIC countries?

Bisgaier: Compared to China and India, Latin America's technology sector has not received as much attention (although a few Brazilian technology IPOs have occurred). Leaders in the region are keenly aware of this distinction, and we think there will be a real push in the more forward-looking Latin countries to develop their technology industries. As in Russia, we also expect to see more transactions in the energy sector, particularly in alternate fuels. Brazil is already the global leader in ethanol.

What are the greatest challenges facing the region?

Schnell: Although there has been tremendous progress in some countries, the region still faces the same long-term issues that it has grappled with for many years: economic and social inequalities, "boom and bust" economic cycles, and threats to the rule of law. The last of these is something we, as lawyers, deal with all the time. We applaud the many efforts in the region to develop more professional and transparent regulatory and judicial systems. ●