ALLEN & OVERY

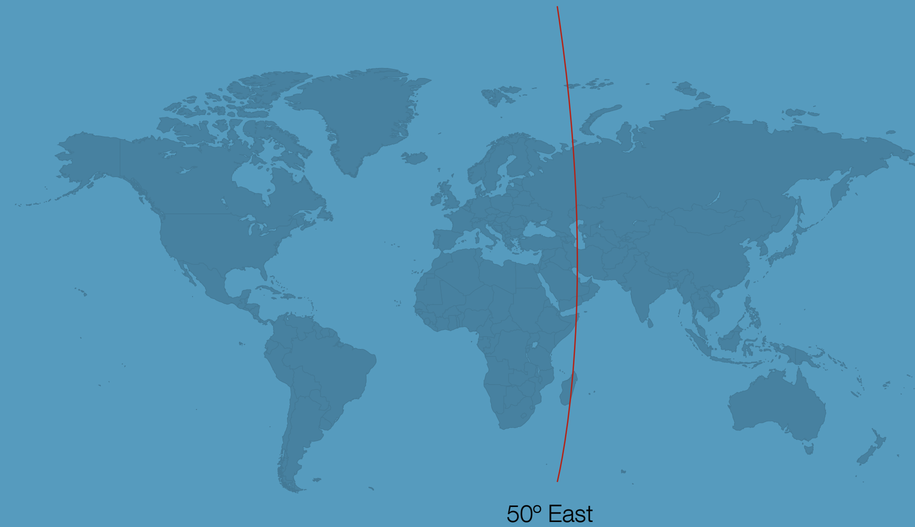
50° East

Risk and regulation: Harnessing or constraining business potential?

Part of a global study into changes in economic influence

www.allenovery.com | www.allenovery.com/50degreeseast

50° East



Contents

Foreword 04
Executive summary 07
Protecting intellectual property rights 08
Legal enforceability of contracts 10
Corporate governance 11
The A&O view: Perceptions and reality 12
The A&O view: Split imperatives 14
Bribery and corruption 16
Global regulation 17
The A&O view: Acts of bribery and corruption 18
The A&O view: Lost in translation 20
Project methodology 22

© Allen & Overy LLP 2011

Foreword

Tim House
Global Head of Dispute Resolution, Allen & Overy

Is the West accelerating the shift of economic power to the East by imposing ever heavier regulatory burdens on its banks and corporates? Is its regulatory response to globalisation and the financial crisis playing into the hands of more permissive regimes in high growth economies?

These are the questions underlying this third and final report in our 50 Degrees East series. And the answer emerging from our survey of over 1,000 senior executives across 19 countries seems to be a clear "yes".

The perception is that there is neither a level playing field between developing and developed economies, nor even a consistent rulebook in some home markets. For example, over half of those who expressed an opinion agreed that their business is at a competitive disadvantage in some of their markets because of the extra-territorial reach of anti-corruption legislation.

These issues have assumed a greater prominence for the executives interviewed than traditional concerns about the effective application of the rule of law, the competence and reliability of local courts, the sanctity of contract, the protection of IP and the quality of advice, all of which seem to be accepted as political and judicial risks of doing business in high growth and high return markets.

The challenge for the West seems to be to develop more consistent, less burdensome regulation, which promotes healthy competition domestically. It should also be wary of hampering innovation and entrepreneurial enterprise in developing markets through the extra-territorial reach of its regulations.

It is interesting that the largest proportion of our respondents believed that foreign investors should invest on the basis of best local practice, rather than import their own or international standards. Respondents in France, Germany and the Netherlands strongly held this view. One of the only countries where a majority believed that foreign investors should be expected to meet international best practice was the U.S.

Adopting best local standards would apply reciprocally, of course; there would be no relaxation of corporate governance or disclosure standards for companies from the developing economies seeking a listing in the U.S. or Europe.

The need for regulatory harmonisation is probably most acute in financial services. What is the prospect of the EU and the U.S. achieving this?

It is hard to be optimistic. Within Europe the regulators' general failure to agree a common regulatory response to the global financial crisis closely mirrors the failure of governments to agree a comprehensive solution to the Eurozone crisis. There has been neither strong leadership nor a market-wide approach.

The U.S. has gone in its own direction in the implementation of Dodd Frank and the Volker rule.

As one commentator, and a former senior UK regulator, put it: "There are clear signs that the early enthusiasm for global regulatory agreements has dissipated, with many countries going their own way, creating damaging uncertainty in financial markets. That is partly because, between summits, there is no sustained global leadership". (Howard Davies, *Financial Times*, 3 Nov).

This fragmented and nationalistic approach in the developed markets is a function of the differing political and economic realities of different countries, the struggle for compromise, the power of disparate lobbying groups, and the implicit threat of global institutions relocating to "friendlier" shores.

While these forces impede progress with market- or sector-wide harmonisation of regulation in developed markets, they do not constrain powerful economies like China to anything like the same extent. China has a greater ability to take collective action in the perceived interests of its national champions, investors and tax payers. It remains to be seen whether the ASEAN countries will fare better than the EU in this respect.

At the moment, in an effort to react appropriately to regulatory shortcomings in the past, politicians and regulators in developed economies worst affected by the global financial crisis are all, in their own ways, trying to create a new regulatory environment for financial institutions.

The new rules require such extensive de-leveraging and such complex consumer protection that they may conspire to drive business out of the regulated sector and accelerate the transfer of assets and business from the West to the East. While the motive may be to protect the interests of taxpayers and consumers, the longer lasting consequences may be exactly the opposite of what is intended.

If this trend continues across other sectors and is pursued with the current extra-territorial zeal, it may compound and entrench the wider economic woes of the EU and the U.S., further accelerating the shift of economic power already underway for more fundamental macro-economic reasons.

As our earlier reports in this series have demonstrated, the process of globalisation is not a simple one and shifts in economic power do not occur at the flick of a switch. Nevertheless, it is safe to say that, while flows of capital are globalising at a rapid rate, the laws that govern those flows are not yet global and investors remain constrained by conflicting national regimes. As their approach and application continues to fragment and intensify, investors and markets face ever greater challenges in making sense of it all.

© Allen & Overy LLP 2011

1,054

Quantitative interviews were carried out with 1,054 c-suite respondents in large international businesses across 19 countries.

© Allen & Overy LLP 2011

Executive summary

This is the third and final report in our 50 Degrees East series. It examines how the perceived shift in economic power from the west to the east may affect the risks that large multinational businesses face and the forces that may shape the regulations governing their operations around the world.

Key findings:

- On the face of it, the executives we interviewed are reasonably confident they can protect their intellectual property in some of the world's major markets. When asked to consider the BRICs (Brazil, Russia, India and China), United States (U.S.), Japan and European Union (EU) in turn, a majority were confident they could protect their IP in every market except Russia.
- When we asked executives if there were any markets in which they were not willing to do business because of the risk that legal contracts could not be enforced, 41% couldn't think of any markets they would avoid. That said, there are still a few markets that a small number of executives would rather steer clear of. Iran topped the list of countries with 8% naming it as a no-go area. China was picked by 7%, then South Africa on 5% and Iraq and Russia were both picked out by 4% each.
- Executives' views varied on what governance standards international investors should expect in return for their investment in local businesses. Some 44% say they should seek to invest on the basis of best local practice; 35% think they should expect changes to the local business such as board structure, composition, or accountability in order to meet best international practice; and 22% agree that they should just look for best possible return regardless of board and governance structures.
- Over half of survey respondents (59%) who expressed an opinion agree that their business finds itself at a competitive disadvantage in some of the markets in which they operate, due to the extraterritorial reach of laws such as the Foreign Corrupt Practices Act in the U.S.
- Nearly two thirds (62%) of respondents call for greater global harmonisation of regulations in their sector with levels consistent across industry sectors.

Protecting intellectual property rights

As globalisation has seen companies not only sell but design and produce their goods and services in an increasing number of markets around the world, the value of intellectual property (IP), and the desire to protect it, has grown significantly.

On the face of it, the global business leaders we interviewed are reasonably confident they can protect their IP in some of the world's major markets. When asked to consider the BRICs, U.S., Japan and EU in turn, a majority were confident they could protect their IP in every market except Russia.

In fact, Russia was the only market where more executives said they were not confident (47%) than were confident (42%), with the remaining 11% being unsure. This produces a net confidence score of -5%.

While the majority were confident they could protect their IP in all other markets, the net confidence score, calculated by subtracting the 'not confident' score from the 'confident' score, highlights the variance of opinion.

Perhaps surprisingly, there is not a clear split between the developed and developing economies. The United States leads the way with a net score of +60%, followed by the European Union on +53% and then India – leading the BRICs – on +44%, ahead of Japan on +40%, followed by China on +20% and Brazil on +12%.

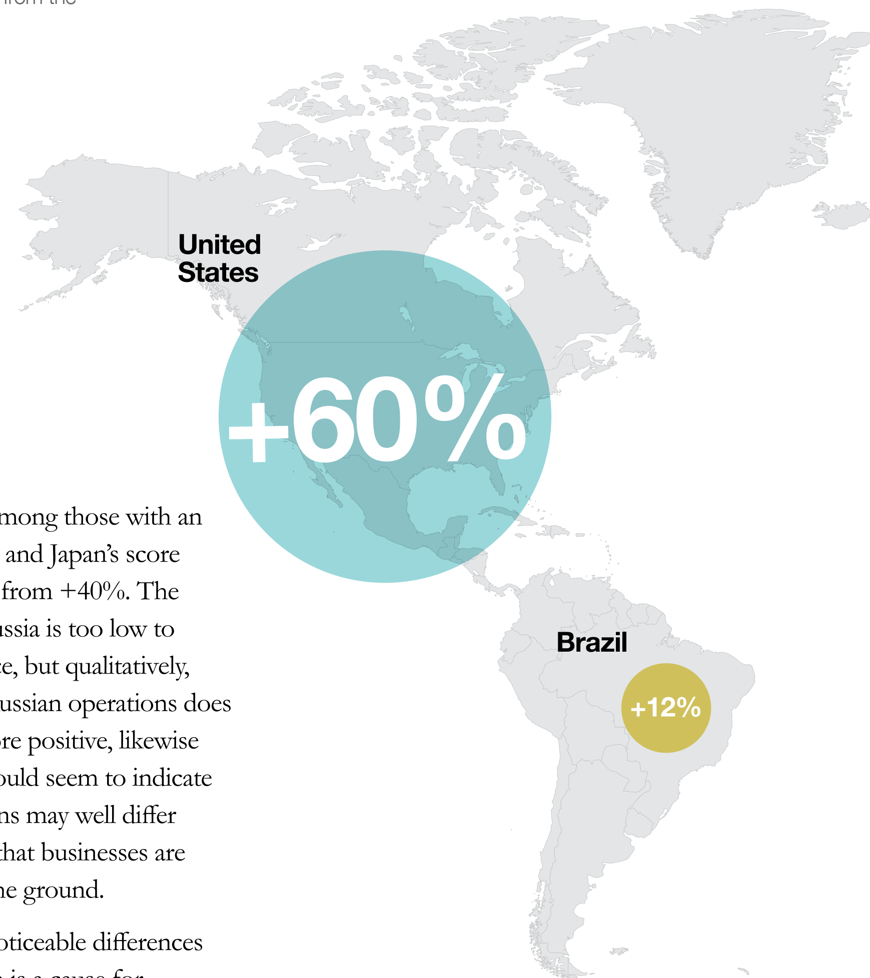
The net score for each country logically tends to rise among respondents whose businesses have an operation in that country. India's net score rises from +44% to +60% among those with an operation in India and Japan's score goes up to +69% from +40%. The sample size for Russia is too low to provide confidence, but qualitatively, the sample with Russian operations does seem to be far more positive, likewise for Brazil. This would seem to indicate that the perceptions may well differ from the realities that businesses are experiencing on the ground.

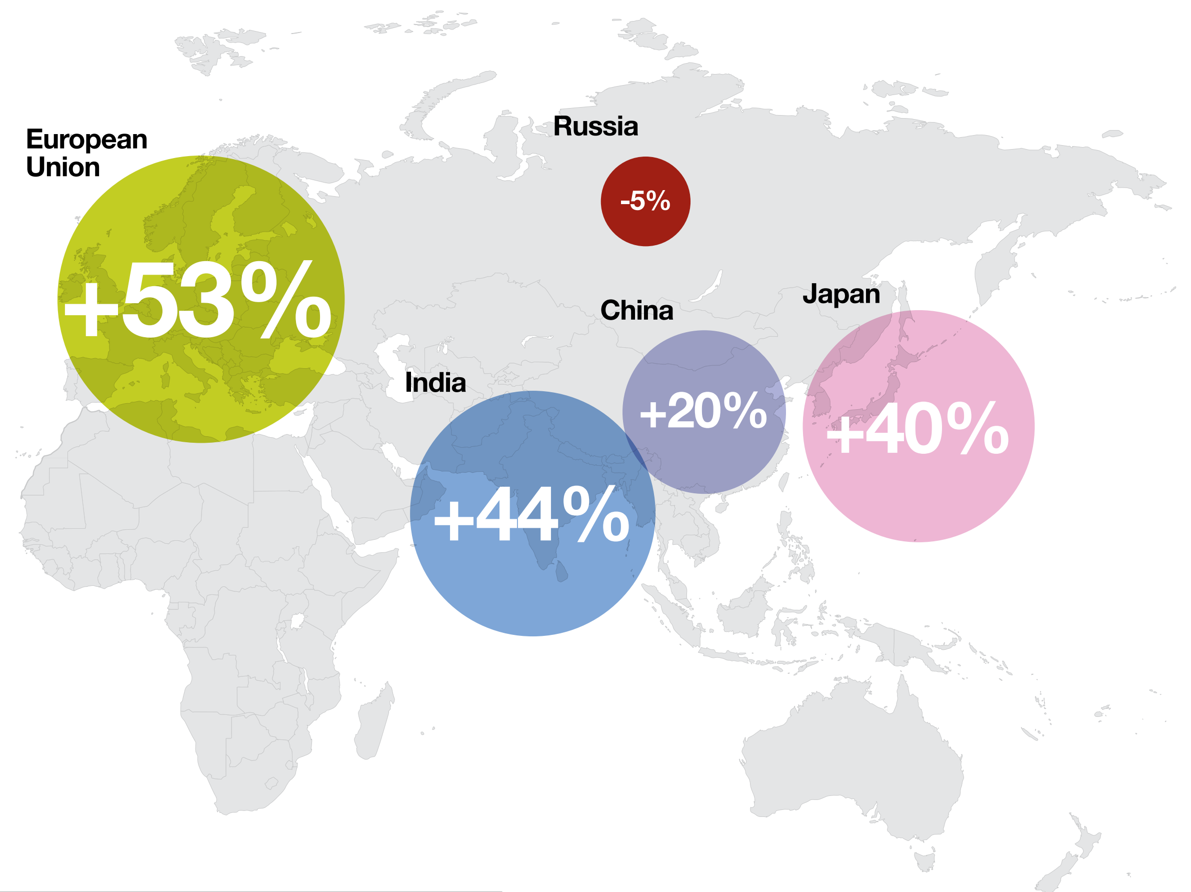
There are some noticeable differences by industry. Russia is a cause for concern from those in the property/real estate sector where the net confidence is -37%, finance and insurance is -24%, energy/natural resources/mining is -10%, and pharmaceuticals and life sciences is -8%. Manufacturing is the most positive sector on +23%.

Brazil also picks up a net negative score from property/real estate of -27%, while finance and insurance is also slightly negative (-3%). The telecoms/media/technology (TMT) sector is the most positive about Brazil with a net score of +29%. But property respondents are far more positive about India (+43%) and China (+23%). Executives in the energy/natural resources/mining sectors marked Japan down, giving it a score of only +13%.

AT A GLANCE: NET CONFIDENCE

The net confidence score is calculated by subtracting the 'Not confident' score from the 'Confident' score





THE FULL BREAKDOWN

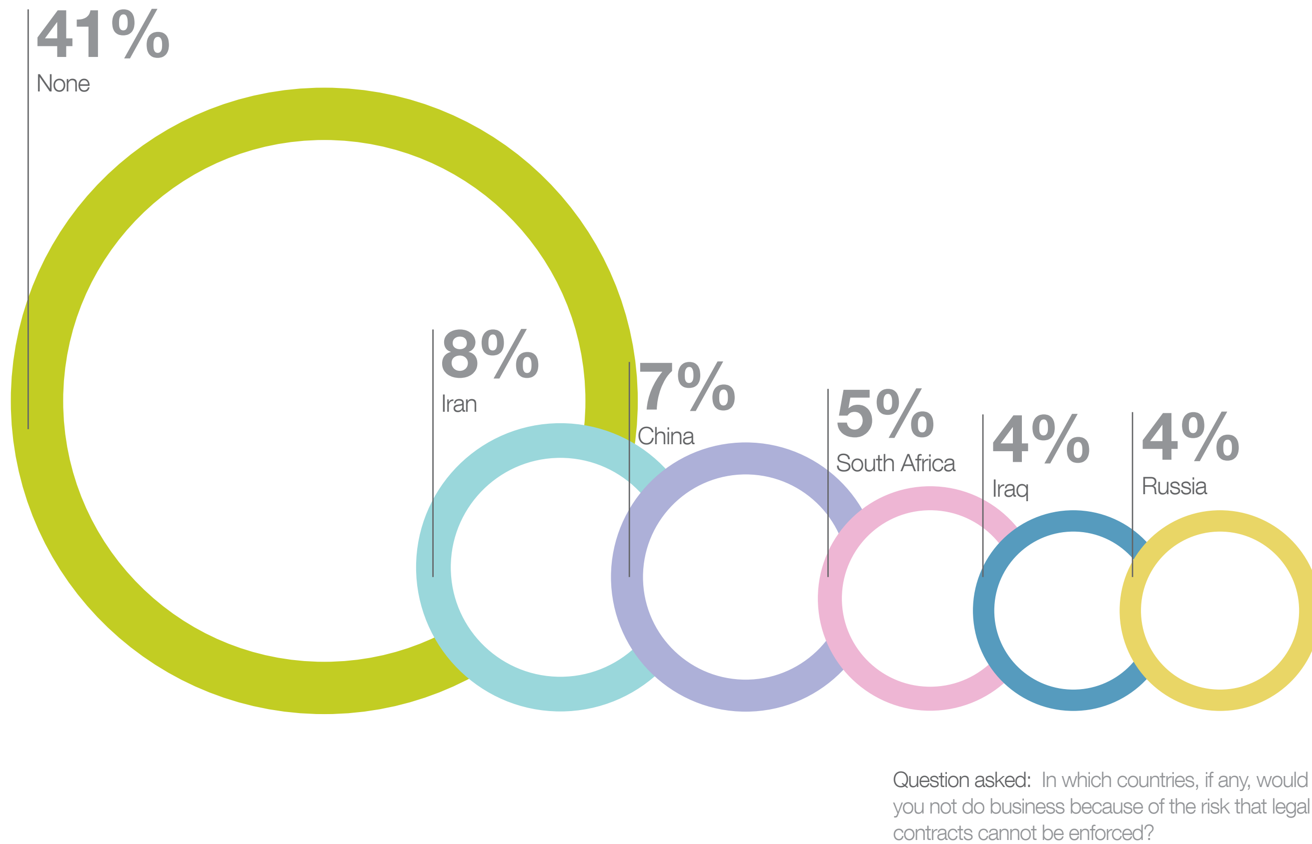
	CONFIDENT	NOT CONFIDENT	DON'T KNOW
UNITED STATES	78%	18%	4%
EUROPEAN UNION	73%	20%	7%
INDIA	69%	25%	6%
JAPAN	66%	26%	8%
CHINA	57%	37%	6%
BRAZIL	50%	38%	12%
RUSSIA	42%	47%	11%

Question asked: How confident are you that you can protect your company's intellectual property in the following markets?

© Allen & Overy LLP 2011

Legal enforceability of contracts

WHERE WOULD YOU NOT DO BUSINESS?



Question asked: In which countries, if any, would you not do business because of the risk that legal contracts cannot be enforced?

One of the major worries businesses have when entering new markets is whether or not they can enforce their contracts. Having contracts that aren't worth the paper they are written on would definitely put markets off limits. The risk simply becomes too high.

So when we asked executives if there were any markets in which they were not willing to do business because of the risk that legal contracts could not be enforced, 41% couldn't think of any markets they would avoid.

While this could be seen as a vote of confidence in the strength of the legal infrastructure around the world, another view might suggest that businesses are more likely to weigh up the risks and price them accordingly.

It also underlines an increasing comfort among executives, as highlighted in our first report in this series, to follow the growth opportunities they see around the world. Many multinational companies also take more care in ensuring that their contracts are enforceable and that their deals are structured appropriately in order to protect their interests in the markets in which they do business.

That said, there are still a few markets that a small number of executives would rather avoid. Iran topped the list of countries with 8% naming it as a no-go area. China was picked by 7%, South Africa by 5% and Iraq and Russia were both picked out by 4% each.

Corporate governance

As businesses seek investment opportunities and growth around the world, the markets they are seeking to enter often impose restrictions on foreign ownership. This forces international investors either to take minority stakes or enter into joint ventures in local businesses. But on what basis should they do so?

Is it right to expect local businesses to change their board structure, composition or accountability to meet international best practice? Or should they seek to understand and invest on the basis of local best practice? Or is corporate governance irrelevant? Should investors focus solely on obtaining the best possible returns regardless of board and governance structures?

The answer, it would appear, is very much a matter of perspective.

The largest proportion of respondents (44%) believe that foreign investors should seek to understand and invest on the basis of local best practice. This was particularly the case in Germany (77%), South Korea (65%) and France and The Netherlands (58%).

A smaller but still significant proportion (35%) believe that foreign investors should be able to expect changes to meet international best practice. The only countries where a majority agreed with this approach were the United States (56%) and Indonesia (52%), while 48% in Brazil also chose this approach.

The less interventionist approach of just looking for the best return regardless of structure gained the highest proportion of responses from Canadian and Russian executives, though both only reach 36%. Although this was chosen ahead of other options by the Russian respondents, it was second choice for Canadian respondents with more (43%) preferring local best practice.

With headlines about bankers' bonuses and the industry's perceived pursuit of profits at all costs, it is interesting to note that only 17% of those working in finance and insurance advocated investing on the basis of the best possible returns alone – the lowest proportion for any industry. This approach was also least popular among German (6%) and Dutch (8%) respondents.

WHAT INVESTORS SHOULD EXPECT

Question asked: Which one of the following best reflects your views about what international investors should expect in return for their investment in local businesses?

© Allen & Overy LLP 2011

The A&O view

Perceptions & Reality

China rises to the IP challenge – in its own way.

Misconceptions can be hard to shake off, and China continues – as our survey of multinational executives shows – to be seen as a place where the protection of intellectual property (IP) lags that in the West. Indeed, many of our respondents considered India to be a better jurisdiction to protect patents than China, or even Japan.

In our view, this is slightly at odds with ever-changing reality.

In recent years, both India and China have worked hard to build their economies and legal systems to support their phenomenal growth.

India's legal system, once notoriously slow-moving, has changed greatly in the last three years, not least with the introduction of expedited trials which ensure whole IP cases can be concluded within six months to a year in the first instance. Previously, the time scale was much longer, unless plaintiffs were lucky enough to obtain a preliminary injunction – the exception rather than the rule.

With the Chinese government now focused on an IP-led industrial strategy, the protection of patents and other IP rights has also become a matter of national priority. Huge changes are afoot and, as statistics gathered by Allen & Overy clearly show, China has come a long way already.

In 2010 (for the third time in a row), China saw more IP-related suits than any other country in the world, including the highly litigious U.S. Although many of the 42,000 court cases filed in 2010 were between local companies, the number of multinational companies involved in such IP suits – either as plaintiffs or defendants – grew sharply.

What is more, success rates for multinationals were unusually high – typically above 60%, and rising to 90% in some cities. This compares with typical plaintiff success rates in the U.S. and Europe of 60% or less.

Where IP litigation is concerned, China's legal system is still evolving, and it may not be immune from potential protectionism, political interference or corruption. But good litigators can devise strategies to minimise or neutralise their impact. After all, such problems exist, to some extent, in many parts of the world, including the U.S., where the respondents have the highest confidence in their ability to protect IP.

The favourable win rates for foreign companies in China thus far carry a few important messages for any multinational company planning to trade and invest in China. China has an increasingly effective system for protecting IP. Businesses operating there need to understand how it operates differently to other jurisdictions, and work with it.

This is a market with so much potential that few businesses, focused on growth, can afford to ignore it. There are many risks. But the biggest risk of all is the failure to understand and embrace the system.

As our figures show, companies making that mistake will either be unable to enforce their own IP – applications for intellectual property must be filed and granted locally to be recognised by Chinese courts – or will be sued if they infringe IP.

Another important lesson is to tailor your expectations. In developed Western markets we are seeing increasing and welcome harmonisation in IP law.

The U.S., for instance, is adopting a "first inventor to file" system and "post-grant opposition proceedings" for patents, which are similar to those in Europe. Europe is trying to emulate the U.S. in establishing a single court for patent enforcement cases, although some EU Member States continue to resist this move.

While the IP laws in China are largely TRIPS-compliant, nuanced differences are enough to snag the unwary. Investors should not expect China, or other emerging economies, to operate in exactly the same way as the West. China is thoughtfully building its own system in its own way, but harmonisation is not a priority right now – and it is hard to see it becoming one in the next few years.

But with Chinese businesses now investing aggressively around the globe, how does the picture look in the other direction?

While Chinese companies are developing IP at a fast pace, the reality is that most of them have a relatively under-developed approach to protecting and exploiting their IP globally. Their approach tends to be reactive, when the sort of strategic approach taken by many of their Western peers would guarantee greater value and security. Until they make that switch, IP disputes will continue to act as a constraint on their international growth. But that may change soon.

Progressively, therefore, China should begin to shake off misconceptions that it is the world's biggest IP danger zone. As we have shown, the reality is quite different: China and India are making real progress. It is time for some of the old stereotypes to go.

Russia, another emerging BRIC economy, appears to be increasingly adopting that mantel.

Some investors will ignore those risks, happy to chase the promise of high returns. More cautious and better-informed investors should always be ready to confront these risks with their eyes wide open. Many risks can be managed or minimised once appreciated. Unappreciated risks, coupled with misconceptions, present the greatest danger.

© Allen & Overy LLP 2011

The A&O view

Split imperatives

There's a clear divide in approaches to corporate governance.

Europe and the U.S. have seen their fair share of corporate governance scandals in the last two decades. But, in recent months, a number of emerging market businesses have stolen the headlines for governance failures, though none, yet, on the scale of Enron, WorldCom or Parmalat.

Separately, corporate governance has begun to climb the agenda in some Asian markets. The Hong Kong Stock Exchange, for instance, has recently implemented rule changes to improve standards of governance for listed companies and further changes are on the way.

On the surface it would appear that an issue that has dominated policy and boardroom agendas in Western markets for so long, is, equally, a growing concern in emerging markets too.

But dig below the headlines and it soon becomes clear that the agenda in developing markets is significantly different from that being pursued in developed economies.

And it's not a question of degrees of development. This is not about emerging markets playing catch up, although with many businesses in these markets only recently achieving a listing, it would not be surprising to find that standards lag behind those in the developed world.

It goes deeper. The principal focus in emerging markets is on finding ways to make companies more accountable to shareholders and on finding ways to stamp out fraud.

There has been considerable focus on fraud prevention and on enforcement against transgressors, but on accountability there is still a great deal of scope for improvement.

That's partly because cultural and structural issues are at play. One key issue is that emerging market companies, large and small, are predominantly majority-controlled by individuals, family or other large shareholder groupings.

While many companies listed on Asian exchanges observe high standards of accountability, a perception remains that they remain in the minority. Institutional and retail investors, with so small an interest in the enterprise, are relatively impotent when it comes to demanding a greater say in the running of the company.

So it's left to the regulators to find a point of external leverage. That's why, for example, the Hong Kong reforms place increased emphasis on the role of independent non-executive directors – not traditionally known for their activism.

For increased regulation to work, there needs to be enforcement of that regulation. It remains to be seen how stringently the new rules in Hong Kong will be enforced, and in particular how stringently they will be enforced against the independent non-executive directors. But increased regulation and the prospect of increased enforcement might persuade more independent non-executive directors – who, with no substantial stake in the business, have little to gain from lax governance – to take up the cudgel for investors and make bigger demands of business owners.

But in mooting reforms, the regulators have to play a very fine balancing game. More rigorous regulation might improve standards, but will impose an administrative burden and additional costs on all companies, including those that have an exemplary governance record.

At the same time, markets like Hong Kong – already in the top tier internationally and increasingly busy – are very keen to shore up their competitive position. Taking serious action on governance could be a good way to inspire confidence in and attract the money of international investors.

Regulators appear to believe there's enough to be gained from pursuing reforms, even if the scale and impact of those reforms is relatively modest.

All this is a far cry from regulatory activity in developed markets.

The pace of rulemaking on both sides of the Atlantic has accelerated since the financial crisis as policymakers, businesses and investors search, retrospectively, for ways to avert a repeat of the crisis. Just as hindsight initiatives like Sarbanes-Oxley were drawn up to tackle issues already uncovered by crises like Enron, a new barrage of rules is now being proposed.

In Europe, policymakers have focused on trying to develop common standards, which not only govern the way boards go about their business, but also tackle the role investors should play in ensuring businesses are managed better.

They range from new proposals on "stewardship", through to new financial reporting standards, and measures to curb executive pay and to bolster the representation of women on boards. It's an agenda of change few business leaders in emerging markets would recognise.

It's also an agenda that executives in mature markets are finding increasingly onerous. As an A&O survey of European executives this year found, the consensus view was that a "one-size-fits-all" approach to governance was unlikely to succeed. Instead it would increase the burden of red tape for boardrooms, and could act as a barrier to growth.

So there's a clear split in approaches to governance – and it's a divide we expect will last for some time.

What's more interesting, perhaps, is what happens when global corporate activity brings these two approaches into collision.

For example, analysis by Allen & Overy reveals that nearly 250 Chinese companies have successfully achieved listings in the U.S., without meeting the normally high standards of governance demanded of companies undergoing an initial public offering.

They've done this by making reverse takeovers of already listed U.S. companies, bypassing rigorous registration rules under the U.S. Securities Act. This presents regulators with a clear and difficult challenge, and on 9 November 2011, the SEC announced new rules that restrict the ability of companies to achieve listings in the U.S. following a reverse takeover.

Some exchanges, including London, keen to attract listing from faster-growing, emerging market businesses, have been prepared to accept more relaxed governance standards. But are we about to see a reverse of this trend in London?

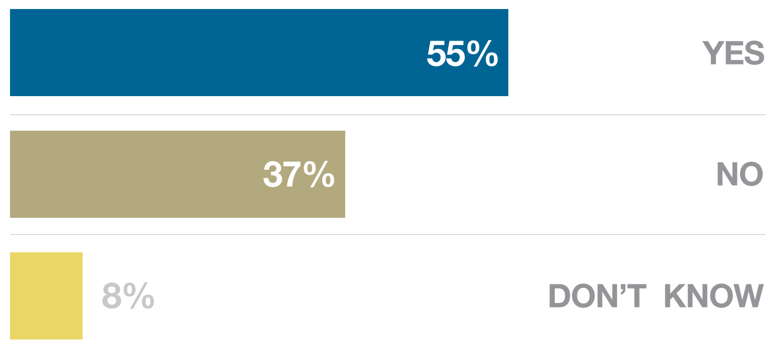
Institutional investors are concerned about the London market's reputational risk and are putting pressure on the regulators to ensure protection of minority shareholders. There are proposals to create a new set of UK indices, running alongside the current series, which would impose higher standards of governance, as well as a proposal to increase the free float eligibility requirement.

These debates and international discrepancies mean greater complexity – in an already complex world – for multinational companies and their investors.

© Allen & Overy LLP 2011

Bribery and corruption

AN UNEVEN PLAYING FIELD?



Question asked: Does the fact that some countries' regulations (such as the Foreign Corrupt Practices Act in the U.S.) affect business in other countries put you at a competitive disadvantage in some of the markets in which you operate?

Globalisation has led governments to take a greater interest in the global operations of the businesses active in their own markets. One noticeable trend has been the increasingly extraterritorial reach of one nation's laws into other jurisdictions around the world.

The most explicit and recent examples of this include the Foreign Corrupt Practices Act in the United States and the Bribery Act in the United Kingdom. But there have also been a number of examples of other laws, such as anti-terrorism legislation in the U.S., being used to extradite white-collar criminals to face charges.

But given these laws do not apply to all companies equally around the world, does it put some companies at a competitive disadvantage?

The answer would appear to be yes. Over half of the survey respondents (59%) who expressed an opinion (excluding those who said 'Don't know') agree that their business finds itself at a competitive disadvantage in some of the markets in which it operates.

But the responses don't give a uniform or predictable picture of the reasons why. One might have thought that U.S. or UK headquartered companies would be the most likely to say they are at a competitive disadvantage, as they are the most likely to be affected by their governments' focus on this issue.

It is surprising then, that South Korea topped the list of places feeling most under pressure by these rules, with 84% of respondents who expressed an opinion claiming to be disadvantaged by these laws. This is followed by China (80%), and over 70% in Singapore, Germany and Brazil.

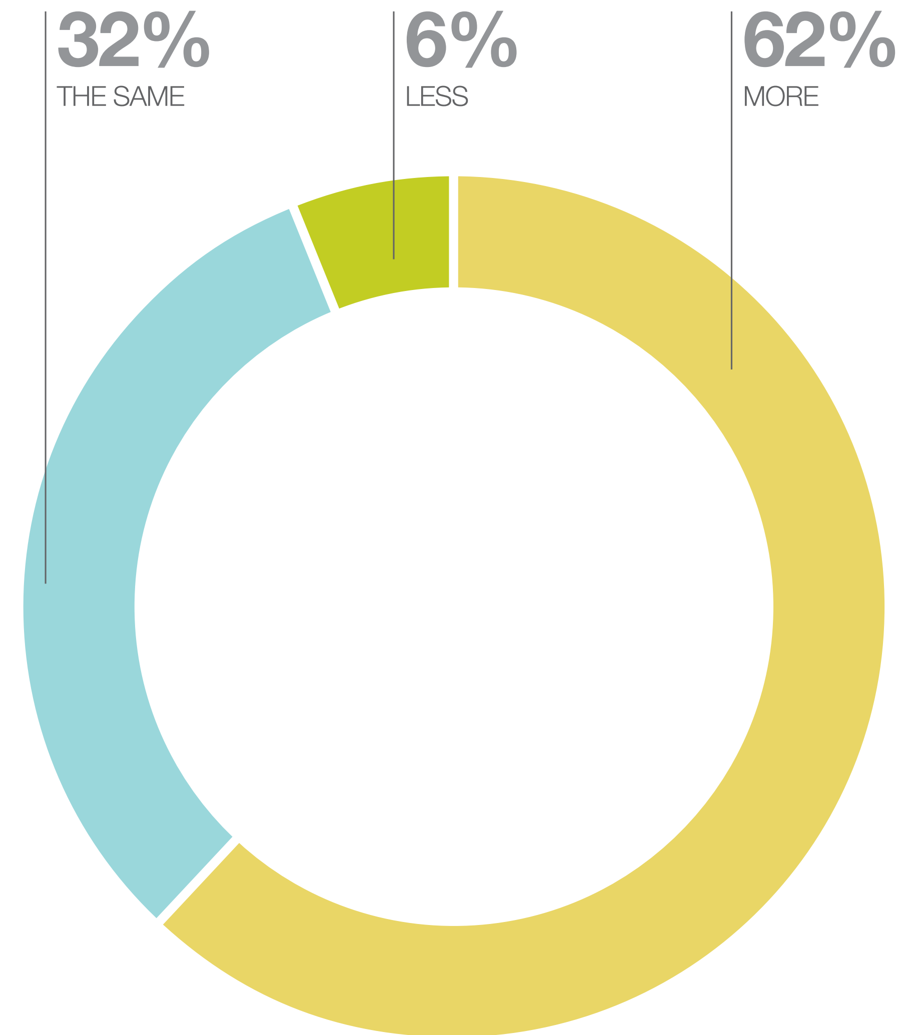
Canada (63%) and Australia (61%) were the only markets where a majority said they were not at a competitive disadvantage.

59%

of those who expressed an opinion, say the extra-territorial reach of some countries' anti-corruption laws put them at a competitive disadvantage.

Global regulation

MORE HARMONISATION?



Question asked: Do you think there should be more, less or about the same level of global harmonisation of regulations in your sector?

International businesses often struggle with the amount of local regulations they face and there is a clear message from respondents that there should be more global harmonisation across their sectors. Nearly two-thirds (62%) want more global harmonisation while 32% say they want it to remain as it is. Just 6% called for less harmonisation giving a net score of +56%.

The number of countries with differing views on this topic were limited. The greatest demand for more harmonisation comes from respondents in Singapore (81%), India (79%) and Thailand (71%) whilst only one country has a majority of respondents calling for less harmonisation: South Korea (65%).

Meanwhile, 50% of respondents in Russia thought there should be the same level of harmonisation, and executives in Japan were equally split 49% to 49% between those who thought there should be more and those who thought there should be the same.

© Allen & Overy LLP 2011

The A&O view

Acts of Bribery & Corruption

Lawmakers are zooming in on white-collar crime as never before. Executives need to act now to contain the risk.

Law enforcers across the world have noticeably stepped up their campaign to prosecute corporate crime.

The U.S. Foreign Corrupt Practices Act (FCPA), although in existence for over three decades, is being enforced more rigorously than ever before. Now, the UK's Bribery Act, introduced in 2010, has given the authorities another powerful, multi-jurisdictional weapon in the fight against bribery and corruption.

So it comes as no surprise that the executives we surveyed from multinational companies should feel, so overwhelmingly, that these tough laws are putting their multinational operations at a competitive disadvantage.

What is surprising, perhaps, is the strength of that feeling. In South Korea and China the figures are as high 84% and 80%, respectively. Executives in Singapore and, interestingly, Germany both came in at 75%. Only in India, Canada and Australia did a majority feel comfortable with the threat.

Globalisation is bringing huge opportunities for companies that step out of their home markets and become multinational. But with those opportunities come significant risks.

We're seeing this first hand. Regulators are mounting far more investigations and enquiries, particularly in the financial services sector of late. Demand from clients for help in understanding the provisions and scope of the FCPA and the UK Bribery Act has risen sharply, as has work to help them shore up their risk control mechanisms.

U.S. companies, for example, are now choosing acquisition targets in new markets with greater care in response to the FCPA. Scanning for potential corruption issues is playing an increasingly important role in the M&A due diligence process. Asian companies are often taken aback by how deep these due diligence probes go.

It is still early days for the new UK legislation, which – like the FCPA – gives law enforcers unlimited reach across the world. Regulators have yet to really show their hand in how rigorous they will be in enforcing the new regime. But we think it's safe to assume that the trend will be towards greater rigour rather than less.

And even though many developed economies are looking desperately to stimulate growth, there is no sign that regulators think this is a reason to relax their approach to corporate crime, competitive disadvantage or not.

Indeed we are seeing new anti-corruption initiatives emerging elsewhere in the world. Most countries, including emerging markets, have their own domestic legislation. Emerging markets, like China, have begun promulgating new rules – a sign that they too want to have an input into the debate about corporate cross-border corruption.

Since the global financial crisis we've also seen disgruntled investors making criminal complaints, rather than civil proceedings, sometimes for tactical reasons – to pressure banks for compensation for losses they have sustained.

Regulators will use a range of other measures, including anti-terrorism and extradition laws and new whistle-blowing provisions in the Dodd-Frank banking reform legislation, to bring alleged criminals to book.

Boards have little option but to take this risk very seriously. They need to look at it squarely, educate themselves about the law as well as the business reality and culture on the ground. Only then can they take action to enforce proper, proportionate and ethical standards across their global operations and swiftly remedy any risk that slips through the net.

That work will be easier in some sectors than in others. Financial services companies tend to be better prepared in terms of risk controls and appropriate risk management systems. They've had to be for some time in other sensitive spheres, not least in containing the risk of money laundering.

By contrast, some other players have a much bigger learning curve to negotiate. That's particularly true for small and medium-sized enterprises that may lack the people and financial resources to build proper defences against these risks, which go beyond just legal considerations into other costly areas such as systems and audit controls.

But the lesson is clear. Management concerned with business ethics and corporate governance will invest the time and money needed to create robust systems to ensure all their operations work to the same high ethical standards.

Those preferring to skirt the issue need to realise that their business models have become a great deal riskier, with much more severe consequences.

© Allen & Overy LLP 2011

The A&O view

Lost IN *Translation*

What happened to the idea of global financial regulation?

If you just listened to the pronouncements of G20 leaders, you could be forgiven for thinking the world is moving steadily towards a global system of financial regulation. "Global problems need global solutions," was their rallying cry at the height of the financial crisis and, publicly, this appears to remain an ambition for some.

It's a message that plays well with some audiences. As our survey for this report indicates, multinational companies – across sectors and across almost all countries – overwhelmingly say they want to see regulation applied in more consistent ways across borders, with 62% wanting greater harmonisation. In finance and insurance the figure is 64%.

At a time of increasing complexity – and continuing uncertainty – in financial regulation, you can see where they are coming from.

But all the evidence suggests that they could have a long wait on their hands. Their safest bet is to prepare for life in a world of far greater regulation - some of it overlapping, but most of it applied differently from jurisdiction to jurisdiction. At this level, divergence, rather than convergence, seems to be the order of the day.

With relatively few exceptions – namely capital requirements and aspects of derivatives trading regulation, where there is some consensus – the onslaught of new rules is heavily influenced by local market or national political imperatives.

Take the U.S., for example. The Dodd-Frank legislation is clearly seen as the preserve of the U.S. government. There is no underlying ambition to aim for harmonisation. The attitude is, pretty much: "This is how we will regulate financial services, take it or leave it."

In the EU, change is being introduced through a series of directives. But, while Europe may speak with one voice when framing legislation, it is safe to assume that each of its 27 Member States will interpret the new rules in subtly different ways, motivated, as elsewhere, by parochial interests.

Even in jurisdictions where changes are being introduced by treaty, no international enforcement mechanism exists to deal with infringements. The local rule of law holds sway.

Some markets are happy to play to the global regulatory agenda, but usually only so far as it serves a local one.

Hong Kong, for example, is embracing selected parts of the global effort to trade derivatives through clearing houses, demonstrating its willingness to stay in line with G20 agreements on the issue. Yet the authorities there are keenly aware of the dangers of embracing too much harmonisation. Anything that undermines its competitiveness with other jurisdictions, particularly Singapore, will come under intense scrutiny.

But, while those holding their hopes out for real standardisation of financial regulation are very likely to be disappointed, the trends are not all going one way.

We are seeing greater co-operation between authorities and, in some cases, markets, particularly in Asia. ASEAN stock markets will join together as a network in the coming months. Malaysia and Hong Kong have agreed to recognise each other's funds. China and South Korea, both committed to increasing their role in shaping future regulatory debate, are also keen to be seen as embracing increased co-operation.

We are also likely to see greater co-operation between regulators. Authorities belonging to the International Organisation of Securities Commissions have signed an agreement to do just that – although co-operation is limited to information sharing, rather than actual rule making.

Co-operation is a positive trend, but it is very different from full harmonisation.

Many financial services companies complain of facing regulatory overload at the moment. Multinational operators not only have to cope with increased regulation at home, but must also take account of new rules in other markets where they have operations.

On top of that they face a raft of rules that have extra-territorial reach across many jurisdictions, such as the Volker regime being drawn up in the U.S., and bribery and corruption laws in the U.S. and the UK.

Increasingly, our role in advising clients is to help them understand how this maelstrom of regulation will impinge on them and to provide them with the tools, such as GlobalView (http://www.aoglobalview.com), to monitor and manage conflicting regulatory demands in all the markets in which they operate.

The message is clear: complexity will be a fact of life for some time to come. For now, global harmonisation remains something of a myth.

© Allen & Overy LLP 2011

PROJECT METHODOLOGY

Allen & Overy developed the 50 Degrees East research to highlight the issues that major businesses are grappling with as the global economy sees a potentially strategic shift of power from developed economies to developing markets, particularly in Asia Pacific. Researchers carried out quantitative interviews with 1,054 C-suite respondents in large international businesses.

Over 50 interviews were conducted in each of the following countries, which include the G8, BRICs and other key Asia Pacific markets, with 100 in the U.S. to reflect its position as the world's largest economy: Australia, Brazil, Canada, China, France, Germany, Hong Kong, India, Indonesia, Italy, Japan, Netherlands, Russia, Singapore, South Korea, Thailand, UAE, UK, and the U.S.

All businesses had at least 500 employees and had international activities, with most having an operation in Asia Pacific and outside their home country. Companies were selected systematically using available databases and respondents were interviewed by telephone in their native language. The business sectors in which interviews were conducted reflect Allen & Overy's client base, with an emphasis on financial services, tech/media/telecoms, energy, real estate, pharmaceuticals and life sciences and infrastructure. Respondents from other sectors were not excluded and many were recruited from sectors such as manufacturing.

In-depth interviews were also conducted with individuals to provide further insights into some of the issues addressed by the survey, as well as to provide case studies on the experiences of businesses developing in Asia Pacific.

All interviews were completed between 4 July and 26 August 2011, with the research provided for Allen & Overy by YouGovStone.

Please note, not all scores in this report may add up to exactly 100% due to roundings.

50+

Over 50 interviews were conducted in each country, which includes the G8, BRICs and other key Asia Pacific markets, with 100 in the U.S. to reflect its position as the world's largest economy.

500+

All businesses had at least 500 employees and had international activities, with most having an operation in Asia Pacific and outside their home country.

© Allen & Overy LLP 2011

50º East

FOR MORE INFORMATION, PLEASE CONTACT:

50degreeseast@allenovery.com

GLOBAL PRESENCE

Allen & Overy is an international legal practice with approximately 4,750 staff, including some 480 partners, working in 39 offices worldwide. Allen & Overy LLP or an affiliated undertaking has an office in each of:

Abu Dhabi
Amsterdam
Antwerp
Athens (representative office)
Bangkok
Beijing
Belfast
Bratislava
Brussels
Bucharest (associated office)
Budapest
Casablanca
Doha
Dubai
Düsseldorf
Frankfurt
Hamburg
Hong Kong
Jakarta (associated office)
London
Luxembourg
Madrid
Mannheim
Milan
Moscow
Munich
New York
Paris
Perth
Prague
Riyadh (associated office)
Rome
São Paulo
Shanghai
Singapore
Sydney
Tokyo
Warsaw
Washington, D.C.

Allen & Overy means Allen & Overy LLP and/or its affiliated undertakings. The term **partner** is used to refer to a member of Allen & Overy LLP or an employee or consultant with equivalent standing and qualifications or an individual with equivalent status in one of Allen & Overy LLP's affiliated undertakings.

© Allen & Overy LLP 2011 I CS1110_CDD-486v7