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Articles

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Brussels Briefing

By Philip Bentley QC, Andrea Hamilton, Clive Stanbrook QC
and Wilko van Weert (McDermott Will & Emery/Stanbrook LLP)

European Commission Issues Strategy for "Modernized" Data Protection Rules - By Philip Bentley QC and Andrea Hamilton

The European Commission recently issued a detailed strategy underlining its revision – and modernization – of EU data protection rules.

The strategy document issued on November 4th is essentially a roadmap for EU policy changes in data protection, and follows a public consultation that initially began in 2009 to review the current legal framework in place since 1995. According to the strategy document, the next generation of EU data protection rules will be drafted with the aim of achieving five distinct policy goals.

The first of these goals, individuals' rights, envisages a fundamental right to the protection of personal data. The European Union seeks to create legislation that will minimize the collection of personal data, and at the same time increase transparency to individuals about how, why and by whom their data is collected, and for how long it is kept. In this respect, the Commission has proposed a "right to be forgotten" online. That is, individuals who wish to have their online data deleted, for instance from social networking sites, should be able to rely on the total removal of their personal data. Much attention is likely to be focused on the protection of individuals' data that is gathered and retained inadvertently.

The second over-arching goal is to improve uniformity among EU Member States' national laws to facilitate EU Single Market integration. The Commission is concerned that the divergent approaches taken by Member States implementing the existing EU Data Protection Directive has created significant administrative burdens for companies, and, in some cases, conflicting rules. The Commission aims to reduce these burdens and conflicts through legislative tools, set to be proposed in mid-2011.

Individuals who wish to have their online data deleted, for instance from social networking sites, should be able to rely on the total removal of their personal data.

The third policy goal deals with police and criminal justice. The Commission is notably non-specific as to how it seeks to reconcile law enforcement needs for data with its goal of promoting individual privacy. Instead, the Commission notes that the specific needs of this sector "will be" taken into account, and that the specific rules applicable to data retention – namely, the 2006 Data Retention Directive – are under review.

The fourth policy goal relates to data transfer outside of the European Union. The Commission's strategy again lacks specific proposals in this area, but rather states a broad goal to improve and streamline procedures for international data transfers. Issues related to data transfers outside of the European Union – particularly with the United States – have proven controversial in the past. Specific negotiations in October 2010 between the United States and the European Union likewise revealed that a future, over-arching data protection agreement between them is unlikely to cover data-heavy sectors, such as travel (i.e. passenger name records), IT and telecoms.

The fifth policy goal is to ensure more efficient enforcement. In particular, the Commission will seek rules that aim to strengthen and harmonize the role and powers of national data protection authorities. The importance of enforcement was underscored when, on November 5th, the Organization for Economic Cooperation and Development (OECD) revealed that its systems had been hacked by cyber-criminals seeking to steal its economic data.

Overall, the strategy document contains few surprises and is in line with the Commission's prior consultation and public statements. Broader questions remain as to specifically how the Commission intends to tackle complicated issues, for example those involving individual

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rights and the "right to be forgotten," cloud computing, inadvertent data collection, technology neutrality, issues particular to specific sectors and third country data transfers. The Commission will also undoubtedly face challenges when drafting rules flexible enough to keep pace with rapidly evolving technology.

Stakeholders have until January 15th, 2011 to comment on the Commission's proposals, after which the Commission will generate specific legislative proposals, likely in mid-2011. These proposals will then face a long road before being implemented, since the Commission will need to "negotiate" the rules with the European Parliament and Council.

Executives Fined Personally for Leading a Cartel in the Netherlands

By Clive Stanbrook QC and Wilko van Weert

On November 4th, 2010 the Dutch Competition Authority (known by its Dutch acronym "NMa") sent a strong signal to any high-ranking company officials who knowingly and actively engage in cartel activity, by imposing personal fines on three executives in the construction sector for the role they played in orchestrating a cartel.

The NMa held the executives personally liable for deliberately coordinating bids on construction contracts by means of "cover pricing". The fines imposed ranged from EUR 10,000 to 250,000, taking into account the personal financial situation of the executives concerned. This follows another recent case in which personal fines of up to EUR 350,000 were imposed on company management.

The Dutch Competition Act enables the NMa to impose personal fines of up to EUR 450,000 on directors of legal entities for breach of cartel rules, and the NMa seems to be employing this deterrence tool as an alternative to the ever-increasing fines at corporate level.

In addition to imposing personal fines for cartel activity, the NMa can also fine individuals who refuse to cooperate with the NMA during the course of an investigation. It has already imposed a fine of EUR 100,000 on an individual who held several management positions within a company investigated for refusing to cooperate with the case handlers, and it should be noted that the individual had long retired from the company in question. The NMa wanted to give a strong signal that no one is shielded from the obligation to cooperate in an investigation, regardless of their present connections with the company.

Interestingly, the NMa has also introduced the possibility for an individual to apply for leniency and be granted full immunity from personal fines by blowing the whistle on suspected cartel activity within their company. Even if the company applies for leniency, the whistleblower could still benefit from individual leniency if he can provide added value to the investigation. This, of course, implies an admission of personal and active involvement in the cartel, or an admission that he had given instructions to staff under his orders to participate.

Similar penalties already exist in a number of other EU Member States, where, for example in the United Kingdom, criminal sanctions may also be imposed. The case against the British Airways executives in the United Kingdom, however, which collapsed earlier this year due to lack of evidence, indicates an extensive burden of proof and respect for rights of defense that must be satisfied. This makes enforcement more onerous and puts a strain on resources.

The NMa has introduced the possibility for an individual to apply for leniency and be granted full immunity from personal fines by blowing the whistle on suspected cartel activity within their company.

Accordingly, the NMa's approach of using administrative fines against company directors might be perceived by competition authorities across the European Union as an increasingly important method to deter illegal cartels.

Personal fines could also provide a valuable addition to the European Commission's deterrence strategy, which until now has only led to massive fines at corporate level. As yet, however, this instrument is not available to the European Union.

Roundup

By Reuters

UK to Create New Visa, Intellectual Property Review to Boost High-Tech Sector

The British government will create a new "entrepreneur visa" and reform its intellectual property laws to try to attract high-tech businesses, Prime Minister David Cameron said.

Cameron set out plans to transform a stretch of East London into a high-tech hub to rival Silicon Valley, starting with new investments from the likes of Internet search leader Google, computer chipmaker Intel, and social networking site Facebook.

Cameron said he wants to create better conditions for the private sector to generate the jobs and growth that the public sector will no longer be able to provide.

He said a proposed new "entrepreneur visa" would allow people with great business ideas and the backing of serious investors to set up shop more easily in Britain. The proposal comes at a time when the government is working on plans to introduce a broad cap on immigration.

Cameron also said that a company like Google could never have started up in Britain because of a copyright system that is not as open to innovation as it is in the United States.

A review of the country's intellectual property laws will seek ways to "make them fit for the Internet age."

Companies Brace for UK Bribery Act Wake-up Call

British and overseas companies with businesses in the UK are in a race to tighten ethical procedures as the country poises to impose one of the most draconian anti-corruption laws in the world.

The Bribery Act, due to come into effect next April, has unsettled those eyeing a new offence of failure to prevent bribery, which makes businesses with any UK interest criminally liable if staff, subsidiaries, intermediaries or "associated persons" offer bribes on their behalf across the world.

The planned act is more draconian than the relatively fierce U.S. Foreign Corrupt Practices Act (FCPA), for it also bans the bribery of people other than public officials as well as "facilitation payments" -- to speed up services such as visa applications or approval for aircraft take-off slots.

Multinational firms with businesses in the UK have demanded clarification of the new rules, which are expected to hit those industries especially relying on myriad overseas partners, such as oil and gas, pharmaceuticals, insurance and private equity.

Watchdog Probes Dutch Banks' High Mortgage Margins

Dutch competition authority NMa is investigating banks including ING, SNS Bank and Aegon Bank because of high mortgage interest rate margins, the NMa said. The NMa said there was no suspicion of banks agreeing to fix prices, but it noted mortgage margins were high both historically and internationally.

NMa Chairman Pieter Kalbfleisch said high margins could indicate a lack of market efficiency, or there could be other explanations. Dutch homeowner lobby group VEH and consumer group Consumentenbond have complained the mortgage market might not be working optimally, citing lower financing costs but unchanged mortgage rates, NMa said.

UK Prime Minister David Cameron says a proposed new "entrepreneur visa" would allow people with great business ideas and the backing of serious investors to set up shop more easily in Britain.

UK Says EU's Tough Bank Pay Curbs Could Backfire

Europe's move to introduce the world's toughest curbs on bankers' pay could backfire, a UK government minister said.

Britain's financial services minister Mark Hoban told a financial forum that the EU has been prepared to move further and faster than the United States and the Far East in curbing banker pay, but this creates the risk of "an uneven playing field." He said global mechanisms were needed.

Bankers from top lenders in France last week also said, at a regulators' hearing on the EU draft rules, that the bloc's curbs on pay could cause Europe's banks to lose top staff to American or Asian rivals. The EU rules being now finalized by bloc banking supervisors are stricter than principles agreed to be G20 countries last year, which will be applied by the United States and leading Asian countries like Japan, China and India.

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Roundup *(from page 5)*

Germany Backs Tougher Bank Law on Securitization

Germany's lower house of parliament approved new guidelines that will force its banks to retain a bigger share of risks in securitized products.

The approval of the bill by the Bundestag lower house means banks will have to keep on their books at least five percent of risks from assets like loans and mortgages bundled together and re-sold as so-called asset-backed securities (ABS).

The new German bill was the result of a mediation committee between both houses of parliament, meaning that its passage through the Bundesrat upper house should be a formality.

To further cut risks, the bill also caps the size of claims one bank can make on another to 25 percent of the lender's equity capital and sets out to ensure that cooperation between national supervisory authorities in the EU is improved.

Court Upholds Ireland "Bad Bank" Structure

Ireland's High Court upheld Ireland's state-run "bad bank" structure and threw out a legal challenge that had threatened to complicate the country's recovery from financial crisis.

Paddy McKillen, who co-owns Dublin's Clarence Hotel with rock group U2 band members Bono and The Edge, had brought the first case against Ireland's National Asset Management Agency (NAMA) to try and stop it acquiring around 2.1 billion euros ($2.9 billion) in loans secured on his assets.

Lawyers for the Belfast man had argued that McKillen's loans are being repaid and have no place in NAMA, which was established to take over Irish banks' risky commercial property portfolios and draw a line under years of reckless lending that have brought the sector and the economy to its knees.

The court ruled that the NAMA act was a proportionate response to Ireland's "very grave financial situation."

EU Nears Carbon Offset Plan, Governments Express Doubts

The European Union's executive Commission wants to ban from 2013 the most common types of carbon offsets used by factories and power plants, to boost the credibility of its emissions trading scheme, two EU sources said. Some EU governments may oppose the plan, which requires majority approval by member states, environment ministries and industry sources told Reuters.

The EU Commission will propose the ban in the next two weeks, and not before Nov. 11, the source added.

Europe's emissions trading scheme caps planet-warming gases emitted by industry, but allows companies to offset emissions by paying for carbon cuts in developing countries, as a cheaper alternative to cutting their own.

The majority of the disputed carbon offsets are generated in newly industrialized countries such as China and India, and the European Commission aims to reform the scheme to include more projects from the least developed countries. The Commission also worries that the current system lures industrial investment away from the EU towards developing countries where they can earn the lucrative credits.

Shutting the main supply of offsets could push up carbon prices, if agreed by a majority of member states at a meeting of Commission officials and environment ministers later this month.

The UK Bribery Act, due to come into effect next April, has unsettled those eyeing a new offence of failure to prevent bribery, which makes businesses with any UK interest criminally liable if staff, subsidiaries, intermediaries or "associated persons" offer bribes on their behalf across the world.

Britain Rules Google Street View Breached Data Law

Google broke UK law by harvesting emails, Internet addresses and passwords while collecting data for its Street View maps service, Britain's Information Commissioner said. But the body charged with upholding information rights in the UK said it would not fine Google, as long as it complied with an audit of its data-protection practices and undertook to ensure such breaches did not occur again.

Google is also under investigation in Italy, France, Germany, Spain and Canada for collecting inappropriate data with the wi-fi equipped cars it dispatches around the world to collect photographs for Street View.

U.S. federal investigators closed a similar investigation last week, saying the company had taken steps to address privacy concerns it had raised.

The Luck of the Irish

By Walter Molano (BCP Securities, LLC)

Lucky is not a word that comes to mind when thinking about Ireland. Nevertheless, the inhabitants of the hardscrabble outpost on the periphery of Europe always seem to find mirth in the midst of adversity. Despite three centuries of oppressive British rule, countless plagues and diasporas, they always seem to see that theirs is a lucky lot. Now, it seems that their fate has played out again.

The collapse of the building boom laid low the country's financial system, and the government was forced to intervene. The three main culprits were Anglo Irish Bank, Bank of Ireland and Allied Irish Banks. Unlike Greece and some of the other peripheral European countries, Ireland's problems were not its fiscal or sovereign debt positions. Up to the onset of the financial crisis, the sovereign's credit metrics were in good shape. Dublin had prefinanced most of its borrowing obligations half way into 2011. Therefore, it was not under any liquidity constraints. However, the collapse of Anglo Irish Bank at the end of September forced the government to step in and recapitalize the institution with more than 30 billion euros. This pushed the fiscal deficit to 32% of GDP from 11.6% of GDP.

Given that the government would have to clamp down to rebalance the fiscal accounts, the market began to anticipate further problems in the Irish banking sector. It was at this time that the market began turning against the other European countries. The correlation between Ireland and the rest of Europe was not just by association, but by the size of the Irish banking sector. Although the Greek economy is much larger than Ireland's, the Irish banking sector is three times the size. Moreover, the exposure of European banks to the Irish financial sector is mammoth. For example, German banks' exposure to Irish banks is $139 billion (4.2% of GDP). The exposure of U.K. banks to Irish banks is $149 billion or 6.6% of GDP. Belgium's is 11.9% of GDP and France's is 2% of GDP. In other words, a collapse of the Irish banking sector would quickly translate into a major European financial crisis.

This was further aggravated by the Germans when they insisted that investors would have to bear part of the pain in the rescue of the Irish banks; in other words, they insisted that there would be forced writedowns of Irish bank bonds. The massive (80%) write-off recently imposed on the holders of Anglo Irish's subordinated debt made people shudder to think what would be the impact on the balance sheet of the continent's financial sector if a similar approach was applied by the other banks and to the holders of senior bonds. This immediately sent the euro into freefall late last week, and European policymakers went into weekend emergency mode as they cobbled together an 85 billion euro rescue package to help Dublin stabilize the rest of the financial system. Over the course of the last two years, policymakers dedicated many weekends to rescuing bankers out of their financial engineering follies. The Irish rescue package also assured that there would not be any automatic haircuts on bonds, but that the IMF would help Dublin decide on a case by case basis what sort of treatment would be applied to the holders of senior and junior debt instruments.

Spain's financial sector is more than twice the size of Ireland's and it is still teetering on the edge of collapse.

Now all eyes are on Madrid. Unlike Greece and Ireland, its numbers are not so bad. The latest fiscal numbers show that the fiscal deficit shrank by half. The country's debt to GDP ratio is only 53%, which is 20% below the Eurozone's average. However, Spain's financial sector is more than twice the size of Ireland's and it is still teetering on the edge of collapse. Moreover, the Spanish banks relied heavily on the private market to fund its expansion. Spanish banks and firms accumulated a debt load of 210% of GDP. Unfortunately, a slowdown in the global economy, the effects of the fiscal adjustment and the spill over from the financial problems in Ireland, Portugal and Greece will surely create new woes for Spanish banks and this will have a tumultuous impact on the rest of the continent.

It is now becoming clear that the European banks are heavily exposed to peripheral debt. As the rot comes to the surface, the EU will be forced to provide further assistance. The problem is that the European Emergency Fund will eventually need to be expanded. All of this monetary expansion will force investors to rethink their euro exposure, leading to a devaluation of the currency. Unfortunately, Europe's woes are coming at the same time that the Koreans are exchanging artillery fire, the Chinese economy is overheating and the Asian economies are slowing down. In other words, the goldilocks scenario that perpetuated in September and October is evaporating, and all we have is the luck of the Irish to get us through.

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Amendments to the Russia-Cyprus Double Tax Treaty

By Judith Harger and Anna Lessova (Dewey & LeBeouf LLP)

On October 7, 2010, the Russian Federation and the Republic of Cyprus signed a Protocol amending the Double Tax Treaty between the two countries. The new version of the Treaty will come into force once the Protocol is ratified by both states, and will generally be applicable to tax periods beginning on or after January 1 of the year following ratification. The Protocol will probably be ratified within the next few months.

The Protocol makes a number of significant amendments to the Treaty which has been in force since 1998. This article highlights the key changes which could affect Russia-Cyprus investment structures in the near future. It is important to note that there are various substantive differences between the signed version of the Protocol and the draft which was initialed by the two countries in April 2009.

New Taxes on Indirect Sale of Russian Real Property

The core changes in the Treaty remove a prior exemption from the taxation of capital gains arising from the indirect sale of Russian real property.

Currently, capital gains from the sale of shares in a Russian subsidiary by its Cypriot parent company are tax exempt in both jurisdictions, even if the subsidiary owns real estate in Russia. The amended Treaty will remove this benefit for sales of shares in Russian subsidiaries where more than 50 percent of their total assets consist of Russian real property.

Moreover, the wording of the amended Treaty will permit not only the sale of shares in a Russian real estate subsidiary by its Cypriot parent company, but also the sale of shares in any intermediate holding company (Cypriot or non-Cypriot), to be taxed in Russia. According to the Protocol approved by the Russian Government, the capital gain derived from the alienation of shares can be taxed in Russia if more than 50 percent of the value of such shares is represented by immovable property in the Russian Federation. Based on the literal wording of the Protocol, if there are two tiers of Cypriot holding companies owning a Russian real estate subsidiary and the first tier company in Cyprus is sold, the amended Treaty would allow such sale to be subject to Russian tax. However, the levying of tax in that situation would require amendments to Russian domestic law, as the relevant Russian tax law provision, imposing a tax liability on the sale of shares in real estate companies, currently applies only to shares in Russian companies.

According to the Protocol approved by the Russian Government, the capital gain derived from the alienation of shares can be taxed in Russia if more than 50 percent of the value of such shares is represented by immovable property in the Russian Federation.

Such significant changes will definitely have an impact on existing structures. The good news, however, is that the new treatment will not come into effect until 2015 at the earliest, so that during the transitional period investors will have an opportunity to develop new ownership and exit strategies and restructure accordingly.

The new regime will not apply to the following situations:

(i) the alienation of shares in the course of a reorganization;

(ii) the alienation of shares listed on a stock exchange;

(iii) the alienation of shares by a pension or provident fund, or by the Government of Cyprus.

Collective Investment Funds

Other important changes relate to collective investment funds, including those that invest in real property situated in Russia. Although the wording of the amended Treaty is not altogether clear, the intention seems to be:

(i) to reserve to Russia the right to tax, as real property income, income received through a collective investment fund (whether established in, or owned by, residents of Cyprus) that invest solely or primarily in real property situated in Russia (Article 6.5);

(ii) to reserve to Russia the right to tax, as dividends, the

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distributions by any other Russian collective investment vehicle out of its income and disposal gains, and to counter the argument that such distributions are exempt from tax in the hands of Cypriot fund members in reliance on the "Other Income" Article in the Treaty (Article 10.3). However, at the moment, Russian domestic law does not enable Russia to exercise the taxing right so allocated to it. Under Russian law, mutual investment funds are treated as transparent, both in terms of the ownership of the underlying property and the taxation of the income received by the fund. In other words, distributions by a Russian fund are not currently treated or taxed as a dividend. (This illustrates a common problem of applying double tax treaties to tax transparent entities.)

These changes will come into effect immediately, rather than in 2015.

Dividend and Interest Income

The Protocol does not diminish the important benefits provided by the Treaty with respect to dividend and interest income, such as the reduced rate of dividend withholding tax (5 percent or 10 percent, as opposed to the Russian domestic rate of 15 percent) and the tax exemption for interest payments. These benefits are still fully available to investors.

The changes extend the scope of the dividend tax regime, which will now also apply to:

(i) income from depositary receipts (this amendment seems to be a clarification of the existing regime); however, the sensitive issue of beneficial ownership of such receipts has not been addressed by the Protocol;

(ii) any distributions out of mutual equity funds (as mentioned above in section 2);

(iii) so called "excessive interest", i.e., interest payments that are treated as dividends, based on the Russian domestic thin capitalization rule.

The last point reflects the special attention which the Russian Ministry of Finance and tax authorities are now paying to the thin capitalization rule, i.e., to the limiting of tax deductions for interest payments in international intra-group financing structures.

Exchange of Information

The Protocol introduces an expanded Article on Exchange of Information between the competent authorities of the Contracting States. It complies with international standards set by the Organization for Economic Cooperation and Development (OECD).

Some commentators predict that the new provisions are likely to be used by the Russian authorities as a powerful tool to obtain information about the beneficial owners of companies incorporated in Cyprus and, thus, the beneficial owners of many Russian businesses.

The potential impact of the Protocol may turn out to have been somewhat exaggerated. The information exchange is restricted in various ways by the terms of the Protocol itself, and by the domestic laws of the Contracting States. For example, under Article 26.3 of the amended Treaty, Cyprus is not required to supply information which is not obtainable under its own laws or in the normal course of administration. Moreover, the new transparency requirements should not adversely affect legitimate tax-efficient structures.

The Protocol does not diminish the important benefits provided by the Treaty with respect to dividend and interest income, such as the reduced rate of dividend withholding tax and the tax exemption for interest payments. These benefits are still fully available to investors.

As an immediate, positive consequence of the revised Article, Cyprus will be removed from the so-called "blacklist" of non-compliant countries issued by the Russian Ministry of Finance two years ago.

The blacklist was part of the new Russian holding company regime, introduced in 2008, which provides a tax exemption for dividends from foreign subsidiaries of Russian companies under certain circumstances. The exemption did not apply to dividends paid from subsidiaries in countries on the blacklist.

As a result of removal from the blacklist, it is expected that Russia will treat dividends from Cyprus as tax-exempt (provided the other conditions are satisfied).

Tax Collection Assistance

Other important changes to the Treaty strengthen the obligation of Russia and Cyprus to assist each other in tax collection, consistent with current OECD recommendations.

The revised Treaty article on tax collection assistance is extended in scope to cover tax of any kind (whether or not the liability to such tax is affected by the Treaty), together with administrative penalties, interest and relevant costs, validly imposed by a contracting state (or any political sub-division thereof).

On request, the assisting state must collect the owed amounts in accordance with its own laws, as if the tax liability were a domestic tax liability. However, proceedings with regard to the existence, validity or amount of the tax claim are not allowed in the assisting state. In addition,

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any time limits or rules of priority over other creditor claims, relating to domestic tax liabilities in the assisting state, do not apply.

A contracting state is not obliged to assist in the collection of tax if:

- the measures are contrary to public policy, or the law or administrative practice of the assisting state;
- the requesting state has not yet pursued all reasonable measures of collection under its own laws; or
- the administrative burden for the assisting state is clearly disproportionate to the potential benefit to be derived by the requesting state.

Limitation of Benefits

The Treaty has also been amended by the insertion of a new Article on "Limitation of Benefits."

The operating principle of this new Article is that the benefits provided by the Treaty to Russian and Cypriot residents will not be available if the main purpose (or one of the main purposes) for establishing residence in one of the Contracting States is to obtain such tax benefits, which would not otherwise be available. This appears to be an aggressive new "anti-treaty shopping" provision, especially as it is not based purely on an objective test regarding ultimate beneficial ownership of any intermediate entities, but depends on a determination reached as a result of consultations between the two tax authorities.

On the other hand, the rule seems to have a relatively narrow application, as its scope is limited to companies that are not registered in either Contracting State but are nevertheless claiming Treaty benefits. So, it appears that this anti-avoidance rule would not apply to a Cypriot incorporated company or a Russian incorporated company.

UNITED KINGDOM

FSA Approves Taping Relevant Communications Conducted on Mobile Phones

By Prajakt Samant and Adam Topping (McDermott Will & Emery LLP)

The FSA recently set new rules obligating authorized firms to record the 'relevant communications' of their employees conducted on mobile and other handheld devices.

On November 11, 2010, the UK Financial Services Authority (FSA) published the results of its consultation paper 'Taping: Removing the mobile phone exemption'. The results set out new rules stating that firms, including banks, brokers, investment houses and financial and commodity derivatives firms, would be obligated to record the 'relevant communications' of their employees conducted on mobile and other handheld electronic devices issued for business purposes. The purpose of the heightened level of scrutiny is to provide the FSA with an additional source of evidence to draw on, to aid their investigation and enforcement work. The FSA hopes the increased monitoring of communications will deter individuals from engaging in illegal activity over the phone, namely market abuse and, more specifically, insider dealing.

The FSA hopes the increased monitoring of communications will deter individuals from engaging in illegal activity over the phone, namely market abuse and, more specifically, insider dealing.

'Relevant communications' are defined as those between an employee or contractor of a firm and the firm's client, during which there is an agreement for the firm to carry out activities on the part of the client, by acting either as principal or agent. The wide definition suggests the FSA intends to record as many communications as possible.

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The new guidelines on the taping of mobile phones follow the rules published by the FSA in March 2008, which have been in force since March 2009 and require firms to record conversations that take place on landlines, all e-mail and other electronic correspondence, including communications (other than voice conversations) on mobile devices. The new legislation indicates that traders will no longer be able to simply put down their desk phone and pick up their mobile phone, in the hope of avoiding having their conversation recorded. The delay in applying the taping rules to mobile devices was caused by the requisite technology not being in place in 2008, when the rules relating to the taping of landlines and e-mails were set out.

Exemption

For various reasons, including stringent domestic and European privacy laws, the FSA's new rules will only apply to mobile devices that have been issued by firms for business purposes, and hence do not cover communications that take place on employees' private mobile devices. Respondents to the FSA's consultation, which included leading financial institutions, argued that the stated benefits of the new rules would not materialize, given the ease with which individuals and firms could circumvent the new rules.

Firms will be under an obligation to take reasonable steps, however, to ensure relevant communications do not take place on private communication equipment. The FSA has stated that it will not prescribe exactly what constitute 'reasonable steps', as its strong view is that each firm must determine what are appropriate measures vis-à-vis their own business. However, the FSA has stated that, at a minimum, firms should be addressing this through their compliance training programmes. To the extent that it has not been done already, firms should be advised to update their compliance programmes to reflect these changes to the FSA rules. As was the case when the original rules came into force, the FSA has agreed to assist firms through the review of compliance aids prepared by trade associations. One obvious measure for complying with the rule would appear to be through prohibiting the use of private mobile phones for making / receiving relevant conversations. However, such a rule will only be effective if it is rigorously monitored and enforced.

There is some uncertainty regarding the position of employees using their business mobile device outside the European Union, and whether a firm would be required to record such conversations. Firms will have to self-assess to decide whether the rules would apply in such circumstances. Firms also would have to be wary of local privacy laws, if they prevent the recording of a conversation. In such circumstances, firms would not be obliged to breach local privacy laws to record a conversation.

Some of the respondents to the consultation questioned whether the cost of implementing the recording equipment would outweigh the benefits presented by the new systems, the benefits being hard to quantify. One respondent estimated the cost of implementation of recording equipment for the Blackberries of front office staff alone would be £2.6m per annum.

Relationship With Other European Legislation

The FSA guidelines will be subject to any new rules that arise following the European Commission's (the Commission) review of the Markets in Financial Instruments Directive (MiFID) and the Market Abuse Directive (MAD). Part of the Commission's ongoing review of MiFID will examine the rules each Member State has in place regarding taping of fixed lines and mobile phones. The rules in each Member State currently differ, thereby affording individual Member States discretion regarding issues such as how long recordings of telephone conversations can be held. The FSA's rules state that the recorded information can only be kept for six months, yet there is a suggestion that under the revised MiFID, there will be a retention period of five years. The Commission will report its findings on the revisions of MiFID to the European Parliament in the first quarter of 2011.

The new legislation indicates that traders will no longer be able to simply put down their desk phone and pick up their mobile phone, in the hope of avoiding having their conversation recorded.

The FSA also envisages that the E-Privacy Directive will be modified to ensure regulators are able to obtain the relevant date when investigating suspected cases of market abuse. The revised MAD will afford competent authorities, such as the FSA, all the requisite supervisory and investigatory powers needed to exercise their functions. It also requires strengthened and effective enforcement against market abuse.

Timeframe and Penalties

Firms will have until November 14, 2011 to put in place the requisite systems and regulations to ensure compliance with the FSA's new rules. It has been suggested that those firms failing to comply with the new rules would face a monetary fine of up to 10 per cent of their annual revenue.

NICE Powers May Be Clipped in UK Pharmaceutical Pricing Overhaul

By Grant Castle and Brian Kelly (Covington & Burling LLP)

The UK government will consult in the coming year on proposals to move the UK's National Health Service (NHS) towards a value-based system of pricing medicines from 2014. While official details are yet to be published, it is expected that doctors will be given powers to decide whether or not to make drugs available to patients. This would effectively remove the ability of the National Institute for Health and Clinical Excellence (NICE), the health technology appraisal body for England and Wales, to recommend which drugs can be reimbursed on the NHS. Rather, NICE is to take on an advisory role regarding the amount that the NHS would be prepared to pay.

Background

NICE currently takes a relatively inflexible and formalistic approach to health technology assessment that is based on the concept of the cost per quality-adjusted life year (QALY). In general, NICE will recommend a technology for reimbursement if the cost per QALY is less than £20,000, and may recommend reimbursement for a technology whose cost per QALY is up to £30,000. It is rare for NICE to give a positive recommendation for a technology whose cost per QALY exceeds the £30,000 threshold.

A simplistic view of NICE's QALY-based approach is that the Institute first produces a quality of life rating. This is typically between 0 and 1 (but can be negative), where 0 (or the negative value) indicates the worst possible health and 1 reflects the best possible health. Suppose NICE determines that a patient improves a health by 20% relative to the relevant baseline, which may be no or standard care, it would assess the quality of life rating as 0.2.

To convert this to a QALY, NICE must come to a view on the likely duration of the benefit. While it has significant discretion in this respect, it will often restrict itself to the duration of effect supported by the available clinical evidence. If the available data suggests that the improvement lasts for 3 years, NICE might conclude that new technology would result in 0.6 additional QALYs ((3 × 0.2 = 0.6 QALYs)), relative to baseline. Obviously, the longer the duration, the greater the number of QALYs.

If the cost of the new technology, including associated care, is £30,000 more than baseline over the relevant period, then the cost per QALY gained would be approximately £50,000 (i.e., £30,000 ÷ 0.6). NICE assesses technologies on a case-by-case basis, but maintains that, in general, a technology costing more than £20,000-£30,000 per QALY would not be considered cost effective.

Changes in the nature of products that NICE typically assesses means that its rigid focus on QALY thresholds appears more and more dated.

This somewhat rigid QALY-based system was devised and implemented in the 1990s, when the innovative industry was focused on drugs for large patient populations that were therefore more commoditized. Changes in the nature of products that NICE typically assesses means that its rigid focus on QALY thresholds appears more and more dated. In particular, many would argue that the Institute has struggled to perform a meaningful cost-effectiveness assessment for life-extending products, such as oncology drugs,[1] and many orphan and ultra-orphan products.[2] The Institute has acknowledged that rigid adherence to these thresholds means that it is unlikely to recommend reimbursement of many new technologies, although NICE has taken steps to increase its discretion with regards to life-extending products[3] and it has issued draft guidance on how it might appraise ultra-orphan drugs.[4] The UK government also announced in October 2010 that it will make £200 million a year in funding available for cancer drugs from April 2011 to the end of 2013.[5]

Value-based Pricing

NICE nevertheless still considers itself to be constrained by rigid QALY thresholds and the UK is falling behind many other member states in Europe with regards to the availability of new medicines.[6] The government's value-based pricing plans are intended to close this gap. Value-based pricing was proposed by the UK's Office of Fair Trading in 2007 as a means of making effective treatments affordable to the NHS.[7] Under a value-based pric-

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ing system, the maximum reimbursement price of a drug will be set according to the net health benefit it brings, taking into account the cost of the drug, its clinical benefit and the savings made from the drugs or health services that it displaces.

It is thought that a new value-based process will use NICE's appraisal of a drug to determine a fair price for the NHS to pay, with the appraisal made available to the NHS and the public to help inform local decisions on its clinical use. It remains to be seen, however, whether NICE will be involved in negotiating the NHS reimbursement prices for medicines or if that role will be carried out centrally by the Department of Health or some other body. However, the UK Health Secretary Andrew Lansley said that NICE's role with respect to pricing would "inevitably evolve." He also suggested that pharmaceutical companies should focus on developing medicines for a "significant unmet need." Mr. Lansley said:

> *"The NHS must use every penny wisely and reforming the way we pay for new medicines is a key part of this. We need a system that encourages the development of innovative drugs addressing areas of significant unmet need. And we need a much closer link between the price the NHS pays and the value that a new medicine delivers, sending a powerful signal about the areas that the pharmaceutical industry should target for development.*
>
> *"Over the next three years we will be working towards a new system of pricing for medicines, where the price of a drug will be linked to its assessed value. Value-based pricing will ensure licensed and effective drugs are available to NHS clinicians and patients at a price to the NHS that reflects the value they bring.*
>
> *"I am determined that not only will we have a reimbursement price for medicines which reflects their benefit to patients, but also one which incentivizes innovation, and supports those new medicines which respond to unmet healthcare need and those which provide wider benefits to society."*

Some commentators have expressed concern that shifting to doctors' responsibility for deciding who is treated with which drug, particularly in relation to the cancer fund, could lead to the "post code lotteries" that NICE was intended to end.

NICE Response

How exactly the system of value-based pricing and other initiatives, such as the cancer drug fund, will work remains unclear. However, NICE's chief executive, Sir Andrew Dillan, has stated: "We are confident that the government will want to take advantage of NICE's expertise

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and experience as it develops value-based pricing. The UK led the world in the appraisal of new health technologies, when it set up NICE in 1999. It can do the same in 2014 with a new approach to managing the entry of effective new treatments into the NHS, in a way which meets the needs and expectations of patients and which uses the health service's resources effectively."

NHS Reform

The proposals follow the publication of the UK government's ambitious plans to reform the NHS. In July, the government's White Paper, Equity and Excellence: Liberating the NHS, outlined plans to give GP practices full responsibility for commissioning care and services for local communities from 2013, with many GP practices beginning to take over commissioning from local health authorities as early as 2011. The report suggested NICE's remit would be expanded to developing quality standards to help inform commissioning decisions and "create a comprehensive library of standards for all the main pathways of care".

Comments

Some commentators have expressed concern that shifting to doctors' responsibility for deciding who is treated with which drug, particularly in relation to the cancer fund, could lead to the "post code lotteries" that NICE was intended to end. Others have suggested that companies will need to consider entering into local risk-share schemes or significantly discount their products to provide value-for-money at a local level.

What is clear is that the pricing and reimbursement landscape in the UK is changing rapidly and pharmaceutical companies need to keep abreast of these developments to ensure that their pricing strategies are aligned with the new UK pricing system.

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1 Exceptional Progress? Assessing the progress made in improving access to treatment for people with rarer cancers, Rarer Cancer Forum, March 2010. See

2 Strengthening National Commissioning Consultation, Summary of Responses to the Consultation on Proposals For Strengthening National Commissioning, Department of Health, 18 March 2010. See http://www.dh.gov.uk/prod_consum_dh/groups/dh_digitalassets/@dh/@en/documents/digitalasset/dh_114297.pdf, last accessed 10 November 2010.

3 Appraising life-extending, end-of-life treatments, NICE Supplementary Advice, July 2009. See http://www.nice.org.uk/media/E4A/79/SupplementaryAdviceTACEoL.pdf, last accessed 10 November 2010.

4 Appraising Orphan Drugs, Draft v3 (2006), National Institute for Health and Clinical Excellence, See http://www.nice.org.uk/niceMedia/pdf/smt/120705item4.pdf, last accessed 10 November 2010.

5 The government had already made available £50 million for cancer drugs between 1 October 2010 and 31 March 2011. The precise operation of the cancer fund is currently under consultation but it is expected that the few cancer drugs recommended as clinically and cost effective by NICE will continue to be funded by the NHS. For those cancer drugs rejected by NICE or yet to be approved by NICE, accessing the cancer fund is a possibility and funding decisions are expected to be based on clinical need rather than health economics.

6 The Influence of the Pharmaceutical Industry, Volume 1, Fourth Report of Session 2004–05, House of Commons Health Committee, March 2005. See http://www.publications.parliament.uk/pa/cm200405/cmselect/cmhealth/42/42.pdf, last accessed 10 November 2010.

7 The Pharmaceutical Price Regulation Scheme -An OFT market Study, February 2007. See http://www.oft.gov.uk/OFTwork/markets-work/completed/pprs, last accessed 10 November 2010.

UK Competition Appeal Tribunal Has No Discretion to Extend Limitations Period for Follow-on Actions Against Alleged Cartelists

By Frances Murphy and Tom Bainbridge (Jones Day)

On November 12, 2010, the Court of Appeal for England and Wales ruled that the UK Competition Appeal Tribunal (CAT) does not have discretion to extend the time period within which follow-on actions for damages may be commenced. The Court of Appeal's judgment provides important clarification of the scope of the CAT's discretion to extend the time limit for lodging a private claim for damages against a company found to have infringed EU or UK competition law.

In BCL Old Co Limited v BASF [2010], the Court dismissed an appeal by BCL for an extension of time in which to bring a follow-on action for damages against members of a cartel found by the European Commission to have infringed EU competition rules in the market for certain vitamins. The judgment is clear that the CAT does not have discretion under its Rules of procedure to extend the limitation period. Accordingly, the time limit for bringing follow-on claims for damages will be two years from the later of either the date of a decision finding an infringement or a final appeal upholding an infringement decision. This certainty is to be welcomed by both claimants and defendants.

Background

The Court of Appeal's judgment is the latest in a long-running litigation saga, arising from an effort by BCL to obtain compensation from BASF for damage BCL says it suffered as a result of BASF's involvement in a price-fixing and market-sharing cartel for certain vitamins. In January 2002, the European Commission adopted a formal decision fining BASF and others for involvement in the cartel. BASF appealed the level of fine it was required to pay, but did not appeal the infringement decision itself. Judgment in that appeal was delivered by the General Court on March 15, 2006.

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BCL lodged its claim against BASF on March 12, 2008. BASF argued that the action was out of time, since it should have been lodged within two years of the date of the liability decision of the European Commission, not within two years from the date of the judgment of the General Court, since BASF had not appealed liability, only the fine. The CAT rejected BASF's argument and decided that BCL was in time. According to the CAT, the two-year limitation period began on the date that BASF's time to appeal the General Court's decision had expired, without distinction between appeals on liability or the fine.

The Court of Appeal's judgment provides important clarification of the scope of the CAT's discretion to extend the time limit for lodging a private claim for damages against a company found to have infringed EU or UK competition law.

BASF appealed the CAT's ruling to the Court of Appeal and in May 2009, the Court held that BCL's appeal was out of time. The Court concluded that an appeal against an infringement decision would stop the clock for the commencement of a follow-on action, whereas an appeal against the level of a fine would not.

However, in its judgment the Court of Appeal also noted that it thought the CAT's Rules gave the CAT a discretionary power to extend the two-year time limit. In light of this, BCL applied to the CAT for a discretionary extension of the limitation period to allow it to bring a follow-on action for damages. The CAT ruled in November 2009 that, while BCL had made a reasonable mistake as to when the limitation period expired, it had not acted reasonably promptly once the window for bringing an action was open. Accordingly the CAT refused to extend the limitation period.

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Judgment

BCL asked the Court of Appeal to decide whether the CAT's Rules gave the CAT discretion to extend the limitation period for damages actions. If the CAT did not have such power under the Rules, BCL asked the Court to decide whether such a power should be treated as existing by reason of principles of EU law. If the Court found that EU law did confer discretionary power on the CAT, then the Court had to decide whether the CAT had exercised that discretion properly when it refused BCL an extension. The Court of Appeal decided:

- The CAT Rules did not contain a general discretionary power for the CAT to extend the limitation period.
- The discretion to extend time under the CAT Rules was plainly limited to case management directions and did not create a general power to extend time for initiating proceedings.
- A discretionary power should not be treated as existing in EU law. Accordingly, there was no need to consider whether the CAT's refusal to extend time was a proper exercise of a discretion conferred on it under EU law.

Conclusion

It remains to be seen whether BCL will seek leave to appeal to the highest court in England, the Supreme Court.

This issue is important to claimants and defendants alike. The Court of Appeal judgment provides certainty concerning the scope of the discretionary powers of the CAT and the limitation period for follow-on actions for damages. Claimants must initiate a damages action within two years from the later of either an infringement decision by an EU or UK competition authority or the outcome of an appeal against such an infringement decision. Defendants will not be subject to the prospect of open-ended private litigation. The certainty the Court of Appeal has delivered to the procedure for follow-on actions for damages is welcome.

Claimants must initiate a damages action within two years from the later of either an infringement decision by an EU or UK competition authority or the outcome of an appeal against such an infringement decision.