Looking ahead
Nine issues for UK Boards, GCs and Company Secretaries
April 2018

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Introduction

Increasing regulation, greater regulatory scrutiny and dramatic economic uncertainty make today’s environment a challenging one for companies. Boards, GCs and Company Secretaries are now expected to consider a much wider range of issues than ever before – not only as to whether something is legal, but also whether it is right. To do that means keeping on top of trends and always broadening one’s perspective.

This briefing highlights some of the key issues UK Boards, GCs and Company Secretaries other in-house professionals should keep in focus. To be forewarned is to be forearmed.
Proposed legislation and new regulations will step up pressure on companies and directors to show that they are making a positive contribution to society.

Just before she became Prime Minister, Theresa May said that she wanted to “get tough on irresponsible behaviour in big business”. One result of this promise is the revised UK Corporate Governance Code which the FRC published in draft late last year. Legislation is also expected to introduce new reporting and governance obligations for large UK companies including subsidiaries within groups.

In March 2018, the Government launched a further consultation regarding corporate governance in pre-insolvency situations.

The proposals set out in the draft code are not as stringent as Mrs May’s language might have suggested, but there are still some significant shifts of emphasis:

> contributing to society
> listening to the workforce
> board independence
> improving diversity (see “Don’t overlook the real meaning of the Parker review”)
> executive pay (see “Board pay: helping keep boards and Remcos out of the headlines”)

**Contributing to society**

There is increasing pressure on directors/their companies to make a positive contribution to society. This comes from institutional investors as well as from the UK Government – for example, in March 2018, the Prime Minister declared that housebuilding companies “should do their duty for Britain and build the houses our country needs”.

The idea that companies owe a duty to a country is, for the moment, only political rhetoric. But the draft revised UK Corporate Governance Code has taken up this theme. It begins with a new expanded principle:

> A successful company is led by an effective and entrepreneurial board, whose function is to promote the long-term sustainable success of the company, generate value for shareholders and contribute to wider society. The board should establish the company's purpose, strategy and values, and satisfy itself that these and its culture are aligned.” Principle A (emphasis added)

For the most part, there should be no conflict or tension between s.172 duties (see panel) and the sentiments set out in the proposed Principle A. Enlightened shareholder value theory says that doing the right things by community, customers and other shareholders will usually deliver the best shareholder returns, so there is no conflict. But this is not always the case. Take a takeover situation or other strategic turning point, for instance, where shareholders have the opportunity for immediate returns that would not be possible if the directors continued to pursue a longer-term strategy. In such a case, directors need to make finally balanced judgments but their duty is always to the company, not specific shareholders or stakeholders.

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Corporate governance: impact on boards

The Government is not proposing to amend s.172, but it would like to nudge companies towards being more receptive to the concerns of employees and wider stakeholders.

The reference to the "workforce", rather than employees, is deliberate and designed to encourage boards to consider their workers in broad terms. This means including direct employees, but also agency workers, self-employed contractors and other arrangements. Examples of engagement activities set out in accompanying guidance include listening groups, employee AGMs and focus or consultative groups. Staff surveys, on their own, are not considered a sufficient or reliable indicator of workforce views.

The new recommendations throw up a number of actions and questions for boards, including:

> who should be counted as part of the "workforce"?
> what kind of engagement activities will be best?
> if a director is appointed from the workforce, how would you go about selecting such a director? How would that director go about ascertaining and representing the views of the wider workforce?
> would an advisory panel be more helpful? In which case, what is the best way of drawing it up and who should be represented on the panel?
> what about using a designated NED? Is there a suitable director available to take on the role? How will the NED report back to the board and how will the board then take responsibility as a whole for taking forward issues raised?

"The board should establish a method for gathering the views of the workforce. This would normally be a director appointed from the workforce, a formal workforce advisory panel or a designated non-executive director." (Provision 3)

This being a provision (against which premium listed companies must "comply or explain"), it is open to companies to come up with their own solution (or do nothing at all) and explain why in the corporate governance report.

like to nudge companies towards being more receptive to the concerns of employees and wider stakeholders. Both the Code and new legislation (applicable to larger companies) will require disclosure on how stakeholder interests have been taken into account in decision-making.

So on the one hand nothing has changed in terms of the legal duties directors owe, but as we have seen with gender pay reporting, the very act of reporting can cause greater awareness and discussion of issues at board and management level. It will be interesting to see whether the obligation to describe engagement with stakeholders and its effect on decisions will make tangible differences to business outcomes or simply introduce further boilerplate text into annual reports.

Listening to the workforce

The Government has dropped the idea of mandatory employee directors but the FRC has taken up its demand that the voice of employees should be heard by the board. The draft code contains a new provision that:

"The board should establish a method for gathering the views of the workforce. This would normally be a director appointed from the workforce, a formal workforce advisory panel or a designated non-executive director." (Provision 3)

This being a provision (against which premium listed companies must "comply or explain"), it is open to companies to come up with their own solution (or do nothing at all) and explain why in the corporate governance report.
Corporate governance: impact on boards

Board independence

Possibly one of the most contentious proposals in the draft code is that the chair must be independent at all times, not just on appointment. That means any chairs in situ for nine years or more will fall foul of this requirement. If the proposal comes into effect, it may put longer-serving chairs into an awkward position. Pressure from proxy advisers and investors to comply with the code’s independence provisions is likely to lead to faster turnover of chairs, potentially depriving boards of valuable wisdom and experience. There could also be reduced retention of independent NEDs on the basis that an individual who has been a NED for a number of years would not be regarded as independent throughout a reasonable term of office as chair – instead potential chairs may choose to start afresh at a different company.

Other proposed changes will require that a majority of the board, including rather than excluding the chair, should be independent. (Under the current rules only half the board needs to be independent). In a company with eight directors, for example, where four NEDs plus the chair, are considered independent, the new provision would be met. If the chair is not, however, considered independent, the provision won’t be met.

Some may feel that the result of the changes as a whole is more work on succession planning but no better governance overall.

In summary, issues for boards to consider:

Assuming that the proposed changes to the UK Corporate Governance Code come into effect, companies which are affected should consider:

1. Whether the need to disclose the impact of stakeholder matters on their principal decisions will affect their decision-making processes and whether they need to document or record decisions differently.

2. How they can make disclosures that are not merely about standard processes and that demonstrate that their business judgments have genuinely balanced all relevant factors, avoiding the risk of unjustified criticism that they have not made decisions in a proper way.

3. Which of the draft code’s recommended models of engagement with the workforce they should employ, or how to justify a different model.

4. The new independence rules – will there be an impact? Will they accelerate succession planning?
Board pay: helping keep boards and Remcos out of the headlines

In the light of greater political, media and public scrutiny, companies, and in particular remuneration committees, must, more than ever, ensure that they are rewarding directors appropriately for performance.

Executive pay – always a hot topic – seems to have got even hotter in the last year.

The Linklaters Employment and Incentives team spend a great deal of time discussing pay and bonuses with Remco chairs concerned to get the balance right between rewarding performance and setting stretching targets. Their concern is not surprising. Take the recent examples of Carillion, Persimmon Homes and the University of Bath. Stories about either the size of pay/bonuses and/or the seeming failure of the Remco, to ensure that pay-outs were tied properly to stretching performance targets led to both the chair and Remco chair at Persimmon, and to the Vice-Chancellor at Bath University, resigning.

Perhaps not surprisingly, discontent about board pay levels has now made its way on to the Government’s agenda. The series of changes it has proposed will have significant implications on the way board pay is set and monitored. In some cases those proposals may result in Remcos having more powers to intervene in Persimmon type circumstances, but will also bring a whole host of new considerations and challenges, both when setting pay/bonuses and at pay-out time.

The changes will require companies to:

- give Remcos power to reduce Long-term Incentive Plan (LTIP) awards when pay-outs do not reflect wider performance;
- disclose the CEO: UK employee pay ratio, explain annual changes and how the ratio relates to pay and conditions across the wider workforce;
- establish a method for giving the workforce a greater voice in the boardroom, including on board pay (see “Corporate governance: impact on boards”); and
- report periodically on what they intend to do when any resolution results in more than 20% dissenting vote.

New responsibilities on Remcos will include having to set pay for senior management (one level below the board and the company secretary) as well as the board, and oversee the pay policy of the workforce when setting board pay policy.

The changes are likely to have effect at the start of 2019, for reporting in 2020 annual reports, but we would advise boards to start preparing now – not least to show that they are taking note of the prevailing public mood.

There is one change which has already happened and will ensure continued media focus on pay resolutions: FTSE companies which have received significant dissent (more than 20%), to any resolution will now appear on a public register and companies will need to update that register with details of any action they are taking. That register is, of course, a simple way for the media, and others, to find out very easily which companies have shareholders concerned over pay.

“Perhaps not surprisingly, discontent about board pay levels has now made its way on to the Government’s agenda. The series of changes it has proposed will have significant implications on the way board pay is set and monitored.”
So what can you do to help make sure your organisation stays out of the headlines?

1. Boards need to understand and agree with the philosophy behind the Remco’s remuneration principles and be satisfied that bonus and LTIP targets are truly linking potential outcomes to company strategy and performance.

2. Remcos need to consider worked examples of the different share-based outcomes so that they are fully aware of the figures. That is really the only way Remcos can say that the projected levels of pay would be justified by the required performance.

3. Remcos should consider setting an overall absolute limit on the pay-outs and/or have full discretion to reduce them due to the company’s performance, or prevailing conditions at payment. They should also have comprehensive clawback arrangements to recover payments made.

Remcos should also not shy away from considering whether long-term performance measures are really appropriate for the company’s business. In 2016, an Investment Association-led working group suggested that companies should choose the pay structures which suit their businesses best, including awarding restricted shares with no performance measures but with significantly reduced size of awards (by at least 50%, compared to the LTIP award). So far, few companies have adopted this approach. That is largely because shareholders have not thought that the particular company’s proposed discount was sufficient. But the time may now be right to reconsider restricted shares; they provide certainty of outcome, allow reducing quantum and would eliminate the criticism that LTIP awards do not link pay to performance properly and result in inappropriate pay-outs.

Although generally considered as an imperfect and possibly unfair tool, the disclosure of CEO: UK employee pay ratio is becoming a reality. Disclosure will be mandatory. Boards need to consider the narrative explanation accompanying the ratio to both contextualise it and reduce the risk of anyone misrepresenting the statistics. Boards may need to explain or change your overall approach on pay policies across the company. This could be done as part of strengthening the workforce voice.

So what can you expect in 2018?

The focus on board pay in the context of fairness and trust in businesses will certainly continue. Companies will be expected to show restraint on board pay and to reduce it where necessary. This is also in boards’ interests. If they do not, the public register and CEO ratio disclosure will bring unwelcome attention and send the wrong message within their own businesses. And, as the current various bonus rows show, they could well end up with unwanted, possibly unfair, criticisms and resignations.

In summary, issues for boards, Remco chairs and HR to consider:

1. Has your Remco considered worked examples of the different outcomes of LTIP pay-outs? Is there an overall limit on the size of pay-outs? Are there comprehensive clawback mechanisms?

2. Does your Remco have overall discretion to reduce LTIP pay-outs at the time of payment to take into account unforeseen circumstances?

3. What is the CEO: UK employee pay ratio? Is it likely to present particular issues to the business? How can it be put in context?

4. Should you change pay structures or practices in view of the ratio or workforce views?
Don’t overlook the real meaning of the Parker review

There is currently woeful underrepresentation of ethnic minorities on company boards. Companies should not just “tick the box” to redress this imbalance, because it is in their best interests to find, nurture and promote the best talent from across society.

In October last, the final version of the review led by Sir John Parker, “Beyond One by ’21: A Report into the Ethnic Diversity of UK Boards” was published. Even applying the broad definition of “ethnic minority” that the Parker review used, the statistics were stark – only 2% of all board directors were UK citizens with an ethnic minority background, more than 50% of the FTSE 100 company boards had no ethnic minority representation, and seven of the FTSE 100 accounted for over 40% of the identified ethnic minority board population. The report recommended that FTSE 100 Boards should have at least one director of colour by 2021, extended to 2024 for FTSE 250 Boards. Its recommendations heralded a mixture of sentiments, ranging from “not another checklist”, to ashamed confirmation of an overlooked truth, to the welcomed identification of a challenge to UK businesses enabling them to push forward even further.

Linklaters’ partner Tom Shropshire was a member of the Parker review and a key draftsman. Here we give a perspective that goes beyond the conclusions of the review.

While never expected to have the “game-changing” impact that the Davis review into gender diversity had, the Parker review has allowed the conversation to move beyond gender. Fundamentally Parker, as with other reviews, has an undeniable business logic: to reflect their customers and to be ready for future challenges, organisations need to embrace diversity, equality and inclusion. So the real question is what does that mean for boards and executives who are attempting to address the challenges put forward by the various reviews on gender and diversity, including Parker?

How to not “tick the box”

Your organisation’s approach to diversity must reflect its corporate priorities, strategy and ambitions, first and foremost. The proposition that success depends on talent is not controversial, so too it should be uncontentious for companies to remain open to all avenues and opportunities to find, train and promote the best talent, wherever that talent may be and whoever may have it (or the potential for it).

Parker makes it harder for companies to tick the box on diversity not because there aren’t any qualified candidates out there – that argument was dispelled by the review – but because it has moved the debate beyond a focus on gender and has opened the door to the broader questions about the need for a diverse workforce and management team.

With all of that in mind, here are our thoughts on how to seek, build, develop and promote ethnic diversity beyond Parker has moved the debate beyond a focus on gender and has opened the door to the broader questions about the need for a diverse workforce and management team.
Don’t overlook the real meaning of the Parker review

Parker’s recommendations:

1. **Revisit your diversity policies in light of your corporate strategy.** They need to be aligned and support the direction of the company. The diversity policy needs to ensure that inclusion is at its core, as a diverse population will then have a place to reside and grow. Ensure that your policies include ethnicity and emphasise the need for ethnic diversity and experience, culture and thought within your organisations. Also make sure that your policy is revisited regularly.

2. **Gain endorsement by the board, the Chair and the senior executives.** Leadership has to embrace diversity, including ethnicity, openly and transparently. Leaders must “walk the walk” and ensure that the culture within the organisation truly accepts diverse thought. That is harder than it seems as leading diverse teams is a huge challenge. You may want to suggest outside training on leading diverse teams – which is distinct from anti-bias training. Reverse mentoring may also be helpful.

3. **Revisit promotion and hiring criteria.** This should be done both internally and externally. Internally, each of the job positions and qualification criteria should be examined for any inadvertent or implicit bias. Companies may want to look back at the applicant pools for its positions as there can be indicators of implicit or explicit bias. Externally – with the use of executive search – be clear in your terms of reference that they are to help achieve your strategic ambitions, including helping you to build a diverse team from top to bottom.

4. **Challenge where a “long” or “short” list does not reflect diversity.** Not just based on gender, but also ethnicity. There is also a need to look beyond any specific appointment, and really assess the pipeline of talent. Beyond this person, for example, “Where are the next potential candidates?” Certainly, if diverse candidates aren’t in your pipeline and you aren’t developing them, progress will be slow or non-existent.

5. **Consider specific targets throughout all ranks of the organisation, and commit to them publicly.** Don’t boil the ocean, be pragmatic and realistic about first steps, but be clear and committed to the ambition. The pace of change is important and will be a measure of commitment. Targets and milestones can be helpful and powerful if thoughtfully applied, and focus on all stages of progression, not just in the senior ranks.

In summary, issues for boards to consider:

1. Does your diversity policy ensure that inclusion is at its core so that a diverse population will have a place to reside and grow?
2. Does the board “walk the walk” i.e. does it embrace diversity, including ethnicity, openly and transparently?
3. Promotion and hiring criteria need to be revisited regularly.
4. Parker is not just about board positions. Companies need to help create a pipeline of good diverse talent if progress is to be achieved. If diverse candidates are not in your pipeline, and you are not developing them, progress will be slow or non-existent.
5. Thought should be given to specifying targets and committing to them publicly. What gets measured tends to get done.
Activism not activists

A number of high-profile cases of shareholder activists putting company boards under pressure does not mean that boards should overreact. Nevertheless, boards, legal teams and IR should be prepared to respond to an activist.

Not all activists are the same, nor do they want the same things. The stereotypical corporate raiders of the 80s and 90s still exist, but they have been joined by the “sons of activists” who tend to take a longer-term view than the greenmailers of old. More traditional shareholders are now also employing activist methods to agitate for change or increased return. The bottom line is that these days every shareholder is a potential activist and therefore the issue is not one type of activist, but activism generally. This also means that a broader range of companies may now be approached. The professional activists were historically priced out of targeting large cap companies by the cost of taking a ‘significant enough’ stake to have influence. Now that activism may come from your current shareholder base, the financial amount a shareholder has to put at risk is becoming less relevant.

While not all activists are successful, (indeed research suggests that as many as 50% of all activist approaches do not result in any change of strategy by a company), it is clear that boards should be prepared to deal with activism arising more frequently and from a number of different quarters.

Preparation

If a company is already considering its strategy, operations and governance properly and is already communicating properly with its shareholders then arguably there is no need for it to do anything in anticipation of activist interest although, as is the case with all potential unwelcome corporate events, it is wise to have agreed governance and communications processes to be followed if an activist emerges.

The fear that an activist may emerge can, however, have a positive impact by encouraging a company to look at itself from a different perspective and spot issues that it might not otherwise spot. For example:

(i) by asking what issues an activist might raise, a company may identify issues that it ought to be considering or, at the very least, questions to which it needs to have a well-articulated answer. It is generally helpful to have outside assistance in relation to this because, as critical friends, outsiders can ask difficult questions that might otherwise remain unasked.

(ii) the company may consider whether it really is getting clear, open and honest feedback from its shareholders. Many companies have believed that they have highly supportive shareholders and then found, to their cost, that there are issues which concern the shareholders. Once again, obtaining external help in relation to shareholder communications is likely to be wise.

The bottom line is that these days every shareholder is a potential activist and therefore the issue is not one type of activist, but activism generally.
Legal rights and commercial tactics

Activists know their legal rights. Before taking a position in a company, an activist will have researched the relevant law and will be prepared to make use of every right available to it and even exaggerate its rights with a view to testing the knowledge and resolve of the target company. In our experience, companies are frequently much less well informed about the activist’s rights than the activist itself is. This may result in one of a variety of problems. For example:

- the company may become unduly fearful because it overestimates the powers of the activist;
- the company may be complacent because it ignores the rights of the activist; or
- the company may find itself caught out by not knowing how to respond to a demand of the activist in a pressure situation (e.g. a general meeting).

In fact, activists’ rights are real but limited – and will, of course, vary from jurisdiction to jurisdiction. Having regard to the fact that they will generally only hold a small proportion of the share capital, their main rights are likely to comprise the right to convene a general meeting (although frequently they will not hold the 5% of the voting rights needed in the UK to do this), the right in the UK to require that particular resolutions be considered at a general meeting (although this right is limited and may be completely nullified by the company’s articles), the right to exercise other rights of any shareholder at a general meeting, and the right to obtain a copy of the share register.

The consequence of this is that an activist cannot on its own achieve very much but it can make a nuisance of itself and seek to mobilise other shareholders and, in particular, make the life of the directors uncomfortable, particularly around the time of the Annual General Meeting and at the meeting itself. Preparation for things that may happen at an Annual General Meeting is particularly important if there is any possibility of an activist emerging. Put simply, the company needs to make sure that it is as up to speed in relation to the law of meetings as the activist is.

Companies frequently feel that they have very few rights in relation to an activist. This is largely based on the absence of legal constraints on the activist. In reality, the main right of the company is a negative one: it is under no obligation to do anything in response to the activist. Whether or not this is appropriate will very much depend upon the activist and the circumstances but, properly used, this is a powerful right.

In summary, issues for boards and GCs to consider:

1. Do you regularly think about the issues an activist might raise? If so, have actions been followed up?
2. Are you satisfied that you genuinely have a steady dialogue with key shareholders to keep them abreast of some of your decisions – and the reasons for them? A consistent, clear and open communications strategy will be much more effective than having to explain things if an activist appears.
3. Are you aware of an activist’s rights?
4. Do you have processes in place in case an activist emerges? A communications plan, for example, might help you engage with activists without being bumped into making statements you might later regret.
Planning for Brexit

The negotiations over what shape Brexit will finally take continue to show a marked divergence between political aspiration and legal certainty. Can businesses afford to put their contingency plans on hold following the EU and UK’s political agreement on a transition period?

The transition period is not certain

Although there is political agreement on the transition period, there will not be legal certainty on its terms until close to the end of this year – the legal text is agreed but will not be binding until it has been approved by the EU and UK Parliaments. There is still a risk that agreement on the withdrawal terms could fall over (for example because of unresolved issues over Ireland, Gibraltar or fishing rights), resulting in the UK leaving the EU in March 2019 with no deal agreed – the “chaotic Brexit” scenario.

If this happened the UK would become a third country trading with the EU on WTO terms, with relatively little preparation having been completed by businesses and governments. For example, without a transition period the UK Government may not be able to pass new domestic legislation or put in place systems (eg for customs controls) in time, and there is no clarity on planes being able to fly to and from the EU.

The scope of the transition standstill is not complete

The transition period is not the same as simply extending the status quo. Under the withdrawal agreement, the UK will no longer be a member state of the EU from 29 March 2019, but will be treated until the end of 2020 as if it were still part of the EU (but with the UK being excluded from EU decision-making procedures). This should work to ensure that there is no immediate change to the regulatory environment in the EU27/UK as from next March but there are
Planning for Brexit

question marks over whether the transition period will apply as far as third countries are concerned. The EU has a variety of free trade and economic partnership agreements and bilateral agreements on specific sectoral issues, covering around 100 countries in all. In some cases, third countries may argue that the transition does not apply to their agreements. This would mean that the UK would be bound by EU law to comply with the terms of those agreements but would not necessarily get the benefit of them.

Planning needed for the end of transition period

Even if most impacts of Brexit are deferred until the end of the transition period, the UK has accepted that it cannot continue to have the same benefits as it currently gets as a member of the single market. Changes to the likely future relationship between the UK and the EU, and the UK and third countries, look set to have significant impacts on businesses and the way they operate. In particular, businesses should expect new tariff and non-tariff barriers for trade in goods and services between the EU and the UK from January 2021. In practice this may mean that goods are more expensive or slower to move around, with more red tape and compliance systems needed, while some services may no longer be provided within existing organisational structures.

These changes may have direct impacts on your business, which can be planned and mitigated for. More difficult, perhaps, will be working out indirect effects, such as how your customers, service providers and suppliers will be impacted by, and react to, the changes that Brexit brings. For example, a UK exporter might decide to move manufacturing operations to the EU27 to be able to meet the needs of customers there and avoid exposing them to risks to just-in-time delivery and rules of origin compliance, but such a move may expose UK customers to those same risks.

When (and how) might the UK leave? Some potential scenarios:

1. “Crash out” in 2019 with no deal
   
   Why? EU27 and UK do not agree a withdrawal agreement, or EU or UK Parliament fail to approve the agreement.
   
   When? 29 March 2019, when the period set by Article 50 of the Treaty expires, or 31 May 2019 following a short extension to agree emergency measures (e.g. on aviation and security). An extension requires unanimity of member states, new EU Parliament elections are held at the end of May 2019 and this may be regarded as a hard deadline.

2. Limited Free Trade Agreement (broadly like Canada) from January 2021
   
   Why? Withdrawal agreement agreed and approved by EU and UK Parliaments. It includes a standstill transition under which UK technically leaves EU in March 2019 but continues to be treated as a member state for almost all purposes.
   
   During 2019 and 2020, negotiations on a FTA continue. Limited agreement possible in time available.
   
   When? The transition period expires 1 January 2021 and the FTA applies. This results in new tariff and non-tariff trade barriers for goods and services, requiring much of the same contingency planning as for the crash out scenario.

3. Bespoke Free Trade Agreement following longer transition
   
   Why? As in scenario 2, withdrawal agreement includes a standstill transition from March 2019, but the transition period is extended beyond 2021 (this is not provided for in the draft withdrawal agreement and extension would require all member states to agree, which may be difficult to achieve). A longer period would give more time to negotiate on a deeper and wider FTA covering goods and services with an extended transition period to allow for ratification and implementation.
   
   When? 2022, or later. Considerable organisational changes for business, governments etc may still be needed.
Planning for Brexit

There are many other issues to consider. Regulators have pointed out that systemic risks may arise unless long-term grandfathering arrangements are agreed, so as to allow continued performance of contracts such as derivatives and insurance contracts. Businesses that share data across the EU are anxious to see agreement to allow continuity of current arrangements, which may require specific agreement on the adequacy of the UK’s data protection regime.

The wider macro-economic impacts of changes in the market for recruitment of talent and foreign investment against a background of evolving and potentially diverging regulation will also need to be considered in assessing the likely impacts of Brexit.

To conclude, our recommendation to businesses is that they should not give up preparing for worst case scenarios, albeit they can take some comfort from the fact that they are now more likely to have two years and eight months rather than just one year to plan for the impacts of Brexit. For more information see our Brexit microsite.

In summary, issues for boards and GCs to note:

1. It is too early to say businesses can put contingency plans on hold – the withdrawal agreement and transition period could still fall over.
2. Businesses therefore need to continue Brexit risk planning to identify what arrangements might be affected by Brexit, directly or indirectly. If any are significant, what can be replicated/put in place to minimise the impact and what is the long-stop date for actioning them?
3. Businesses will need to be ready to make difficult judgment calls as to whether to press the “go” button on these plans or to hold off in anticipation of a transition period being legally agreed.
There is no doubt that the current economic environment, not helped by uncertainty over Brexit, has made this a challenging time for many companies in many sectors. And that poses a counterparty risk. If your counterparty/customer goes bust, are you clear as to your rights and protections? Many companies are surprised to find that those rights and protections are not quite what they thought they were.

For example:

> If looking to be paid for goods delivered or services already supplied, you are likely to be at the back of the queue on insolvency when distributions are made.

> Asking for “your” goods to be returned may not be straightforward, even though the customer may not have paid for them yet. Retention of title (ROT) claims are notoriously difficult to prove.

> While terminating the supply agreement may be an option, English insolvency law might require you to keep supplying the customer where the supplies are classed as essential. If the customer still doesn’t pay, then you can terminate, but you’ll need to wait 28 days first and, in any event, amounts due before the insolvency will not receive any additional protection.

> When a UK company goes into administration, that causes a stay on a broad range of actions that you might otherwise have considered – such as taking legal proceedings against the customer, enforcing security or even ROT rights. To do those, you will need the permission of the administrator or of the court, which can add to costs and delays.

> Sometimes a business may be sold on appointment of the administrator, the deal having been arranged in advance. There is no need for court or creditor approval. These pre-pack sales are a feature more or less unique to English insolvency law. The result could be that goods are no longer located where you thought they might be and, in any event, if they weren’t subject to a valid ROT claim, your claim would be that of a creditor, not an owner.

So, what can you do to protect yourself?

When dealing with troubled sectors you may want to think about what steps you can take to better ensure payment of amounts owed and to ensure that legal and commercial departments are on the case.

If you have concerns about a customer’s credit:

> do your due diligence including checking to see if a customer has published its Payment Practices and Performance Report;

> think about group guarantees, advance payments, deposit retention and Project Bank Accounts and try not to allow large sums to build up;
consider whether you are contracting with, or invoicing, the right entity; and

a properly incorporated retention of title clause will make a significant difference to your rights.

Whilst recent changes restrict certain essential suppliers of utilities and IT-related goods and services from withdrawing such supplies when a customer goes into administration (or puts forward a company voluntary arrangement), there is still scope for savvy suppliers to link price increases or changes in payment terms to non-insolvency events. Suppliers may also ask the administrator/CVA supervisor for a personal guarantee for payment of any continued supplies. While it is not something you can contract for beforehand, awareness of this right can ensure your payment for post-insolvency supplies is protected and you can also terminate the supply if they do not provide that guarantee within 14 days of receipt of the request.

Finally, remember insolvency law differs across countries (even within the UK to a degree) and there is no single European or global insolvency law. What works or does not work here will very often be different elsewhere. Non-English law contracts, goods located abroad, foreign customers – there are a range of factors which could be relevant, so whenever there is a significant cross-border element for your business, think about whether you need additional or different protection.

Some of these steps are simple but, taken together, should help contain the fallout when there is trouble in the supply chain.

In summary, issues for GCs to consider:

1. How much due diligence is being done to identify troubled counterparties? Have contracts with them got decent payment protection measures? Would you be able to identify your goods if required for a retention of title claim?

2. Do you know if you are an “essential” supplier whose termination rights may be restricted on counterparty insolvency? Do you know what to ask an administrator for if you are required to continue to supply an insolvent customer?

3. Do you understand variances in insolvency risk across your customer portfolio based on where they are incorporated and/or operate, where goods are supplied or the governing law of any supply agreement?
Increasing foreign investment control and implications for global deals

More countries are scrutinising inward investments and, in some cases, reforming their foreign investment plans. Businesses intending to invest cross-border can expect the process to last longer and be more difficult.

As a result of growing scepticism over globalisation and a perception that national security issues may arise in industries not traditionally thought to be sensitive, more countries are scrutinising inward investments by foreign investors and reforming, or considering reforming, their foreign investment laws. Anyone involved in strategic cross-border investment or M&A needs to be aware that they could find it more difficult to predict whether their deals are likely to be called in for review by governments or government bodies in the future. If they are, we expect longer timescales and greater execution risk to follow.

If we look at the UK first, the Department for Business, Energy & Industrial Strategy (BEIS) published a consultation paper in October 2017 considering broader powers for the Government to intervene in foreign investment deals which raise national security concerns. The proposals have some short-term and some longer-term implications.

In the short term, the Government is taking additional powers to block takeovers of companies in the defence and technology sectors which, so far, have not been caught because they are too small. These changes are actually narrower in scope than some had predicted and in reality amount to a fairly small and incremental change to the Government’s existing powers to intervene on national security grounds (as opposed to, say, wider political grounds). On 15 March 2018, the Government confirmed its decision (subject to Parliamentary approval) to reduce the jurisdictional thresholds for targets active in three sectors: the development or production of items for military or military and civilian use, quantum technology and computing hardware.

Longer term, the consultation looks more broadly at the way in which foreign investment in certain sectors is reviewed, with proposals for greater “call-in” powers under the current voluntary regime, or the introduction of a mandatory notification requirement. These proposals are more substantial and would involve a significant revision of the existing legislation. The Government says that it would retain an independent competition authority and a clear separation between competition assessments and national security-related ones. Thankfully, the proposals also make clear that the Government is not planning to amend the process for other public interest-related assessments – and by that we mean financial stability or media plurality. However, there is no clear definition of “national security” in the Green Paper and we shall have to wait to see how widely the test would be interpreted in the future. We expect BEIS to consult further on more detailed proposals later this year (possibly after the May elections), which may provide more clarity. The political row over the GKN/Melrose takeover might well embolden the Government to take more protectionist powers.

Turning to the EU, calls from Germany, France and Italy for rights under EU law to intervene in investments by state-controlled and state-funded entities (especially those which give access to key technologies) have resulted in the European Commission announcing similarly themed proposals to boost its foreign investment review powers and to give itself a co-ordinating role between its Member States. The proposals set out a new framework for scrutinising foreign investment in sectors of national importance. These include technology, cybersecurity, nuclear power and financial services. As
part of this, they list factors that may be taken into account when screening foreign investment, although this list is non-exhaustive. The so-called “co-operation mechanism” it includes requires each Member State screening a proposed investment to inform the Commission and the other relevant Member States and allow them to offer opinions and comments that must be given “due consideration” by the screening Member State. Also, where the Commission considers that a foreign investment is likely to affect the “security or public order” of the EU, it may offer an opinion to the screening Member State, which must take “utmost account” and provide an explanation if the opinion is not followed. While the proposals are intended to establish better screening of investments from third countries, they also reflect the Commission’s desires to avoid the risk of Member States adopting protectionist policies and to provide transparency to potential investors. Ultimately, the Commission wants to continue to encourage foreign investment in Europe.

It’s probably no great surprise that, given the Trump Administration’s openly aggressive protectionist stance, there are also attempts to extend the powers of the Committee on Foreign Investments in the United States (CFIUS), which conducts national security reviews of M&A activity involving a foreign investor. The proposals being put forward envisage stricter enforcement rules and the expansion of CFIUS’ jurisdiction and authority, with a focus on countries of special concern (in particular China). They also set out longer timeframes (so a single complete CFIUS review process potentially could take as long as 120 days, as opposed to 75 days under the current law) and new filing fees (the lesser of $300,000 or 1% of the transaction value).

Meanwhile, Germany has already enacted reforms to its regime. From July 2017, the existing rules were strengthened and the notification obligations were increased for acquisitions in specified industry sectors related to public security, i.e. sectors including information technology, telecoms and critical infrastructure. Whilst the amended legislation does not result in a material restriction on foreign investments in German companies, the extended application area, new notification requirements and extended review periods will require potential investors to engage with the regime proactively and early in the deal process.

Generally speaking, intervention under foreign investment rules is already much harder to predict than under the tried and tested merger control regimes. Our experience is that transaction timeframes are also subject to greater uncertainty, since many foreign investment regimes have very unclear and open-ended review timetables. Going forward, potential investors can expect their cross-border deals to take longer to complete, and they will need to consider foreign investment issues upfront to mitigate any potential delays. In addition, the various reforms and proposals will mean potentially increased scrutiny and execution risk for a broader range of deals in a number of jurisdictions. It is vital for deal teams to consider the practical considerations for managing this uncertainty and addressing individual transaction challenges upfront.

In summary, issues for GCs to note:

1. Potential investors can expect an increase in timeframes and complexity for a broader range of deals and will need to consider foreign investment issues upfront to mitigate potential delays.

2. Understanding governments’ policy priorities and the regulatory hurdles that may be involved will be an essential early part of planning any major transaction and is likely to be critical to the likelihood of successfully completing your deal.
U.S. tax reform: changing dynamics will influence deal-making in Europe and the United States

Radical changes to the U.S. tax regime, with possibly more to come, offer big advantages for European companies doing business in the United States, but watch out for unintended consequences.

In December 2017, U.S. President Donald Trump signed into law a sweeping tax overhaul bill, the Tax Cuts and Jobs Act (“TCJA”). The TCJA will have immediate wide-ranging effects on M&A, intercompany arrangements, financing, and investment for both U.S. and non-U.S. businesses. However, the TCJA is without precedent in many ways, including the speed with which it was passed and the lack of bi-partisan support for it. As a consequence, some aspects of it are unclear and will need to be further developed through regulations. In addition, certain provisions appear to have unintended consequences that will need to be remedied through further legislation. Finally, with mid-term elections approaching in November, changes in the political environment may result in some of the new rules being reversed in the future. Nonetheless, the effects of the TCJA are already being felt.

Below are some of the key provisions that boards and GCs of UK-based businesses with operations in the United States (or that are contemplating conducting operations in the United States) should pay particular attention to.

Reduction in U.S. corporate tax rates and new expensing rules

One of the most significant changes under the TCJA is the permanent reduction of the top corporate U.S. federal income tax rate from 35% to 21%, the lowest corporate tax rate in the United States in almost 80 years. In addition, the TCJA eliminated the corporate alternative minimum tax. These changes should result in immediate benefits to non-U.S. based multinational groups with significant U.S. operations in the form of increased after-tax returns and, depending on the particular operations of a group, these changes to the U.S. corporate tax regime may make the United States a much more attractive option for conducting business going forward. These changes may also influence the structuring of mergers and acquisitions by making inversion transactions (i.e., transactions to relocate a company to another tax jurisdiction) less compelling and increasing interest in structuring transactions as asset purchases instead of as stock purchases. U.S. corporations may also be incentivised to dispose of non-core assets in light of the reduction in tax cost on any gain on such dispositions.

Passthrough deduction

New rules introduce a beneficial deduction for individual owners of businesses organised as passthroughs (i.e., partnerships and LLCs) of 20% of business income. This rule doesn’t apply to passthroughs in certain service businesses, such as accounting, consulting, financial services, health and law. These changes are likely to influence the ways that U.S. businesses are set up and may create structuring challenges for incentivising management in acquisitions of smaller and middle market U.S. businesses, as managers may prefer to hold partnership or LLC interests eligible for this beneficial tax treatment, instead of stock in a corporation.

”...the TCJA will have immediate wide-ranging effects on M&A, intercompany arrangements, financing, and investment for both U.S. and non-U.S. businesses.”
U.S. tax reform: changing dynamics will influence deal-making in Europe and the United States

New interest deduction limitations

The TCJA introduced a new cap on interest deductions to the extent that a company’s net business interest expense exceeds 30% of its “adjusted taxable income” (i.e. EBITDA for taxable years beginning before 1 January 2022, and EBIT thereafter). This may reduce the benefits of using leverage to finance acquisitions, as debt becomes more expensive if interest is not deductible.

Full expensing

For the next five years, taxpayers will be able to immediately deduct 100% of the amount paid for certain depreciable property instead of capitalising the purchase price and depreciating the cost over time. This rule applies not only to new property, but also to used property acquired from third parties. Goodwill and other intangible property are not eligible for full expensing and continue to be amortisable over 15 years. Nonetheless, this change is likely to spur additional capital expenditure by U.S. businesses and further increase the appeal of asset acquisitions. Due to the significant benefits of the full expensing rule in the context of asset acquisitions, there is likely to be an increased interest in agreeing on purchase price allocations in advance of signing deals in order to avoid disputes after closing.

Territorial taxation

Prior to the TCJA, U.S. multinationals generally were subject to tax in the United States on all of their worldwide income. However, U.S. tax on operating income generated by foreign subsidiaries (i.e. controlled foreign corporations) generally was deferred until the income was repatriated. In addition, audit rules generally allowed U.S. multinationals to avoid recording a deferred tax liability to the extent that they intended to permanently reinvest foreign earnings outside the United States. As a consequence, many U.S. multinationals built up significant cash reserves outside the United States and were incentivised to invest those reserves in capital projects and acquisitions outside the United States.

The TCJA eliminates the U.S. system of worldwide taxation by introducing a quasi-territorial tax system. The primary feature of the change to a territorial system is a new participation exemption. Dividends paid by foreign subsidiaries to their U.S. corporate shareholders are now exempt from U.S. tax, provided the U.S. corporation owns at least 10% of the foreign corporation. Gains from the sale of stock may also be eligible for full or partial exemption under this rule (i.e. to the extent they are recharacterised as dividends). This change makes bringing cash back to the United States much more attractive. As a consequence, U.S. multinationals may be less interested in non-U.S. acquisitions and capital investments, and more inclined to pursue domestic mergers and acquisitions, repay debt, and return cash to shareholders in the form of stock buybacks and dividends. In addition, the elimination of tax on certain stock dispositions may make internal restructurings to move foreign corporations out from under U.S. shareholders more attractive.

Transition tax

In connection with the move to a territorial taxation regime, the TCJA imposed a one-time tax on the deferred foreign earnings of foreign subsidiaries of U.S. corporations. The tax is imposed at a rate of 15.5% for cash and cash-equivalents and 8% on other items. The tax is imposed on the U.S. shareholders of the foreign subsidiaries that own 10% or more of the stock of the foreign subsidiaries on the last day of the subsidiary’s year that began before 2018. As
U.S. tax reform: changing dynamics will influence deal-making in Europe and the United States

A consequence, for foreign subsidiaries with a fiscal year ending on 30 November, the U.S. shareholder that owns the stock on 30 November 2018 would be liable for the tax. Accordingly, acquirers will need to carefully consider the impacts of this rule in connection with their acquisition of foreign corporations, including U.S. groups that own foreign subsidiaries, in order to ensure that the cost of the tax is borne by the target’s selling shareholders.

Base Erosion and Anti-Abuse Tax and Global Intangible Low-Taxed Income

Although the reduction in tax rates and move to territorial taxation will generally reduce tax costs for groups doing business in the United States, the TCJA introduces guardrails designed to prevent U.S. corporations from reducing their U.S. tax base or shifting profits overseas.

Base Erosion and Anti-Abuse Tax (BEAT)

The base erosion and anti-abuse tax, commonly referred to as “BEAT”, is intended to protect the U.S. tax base by increasing taxes on corporations making significant deductible payments to non-U.S. related parties. Such deductible payments (also known as “base erosion payments”) include payments of interest and royalties and amounts paid or accrued to acquire depreciable or amortizable assets. However, payments treated as cost of goods sold are not considered as base erosion payments for purposes of BEAT.

The BEAT tax calculation is based on a complex formula that compares a U.S. group’s tax base with and without these base erosion payments. The BEAT tax applies if the difference between the two calculations exceeds a certain threshold. Multinational groups will need to determine whether they will be subject to the BEAT tax. If the BEAT tax is likely to apply, restructuring to reduce or eliminate the impact of BEAT may be warranted and further consideration should be given to determine whether certain payments could be recategorised in a manner that allows them to be excluded from the BEAT calculation. Among other things, replacing intra-group loans with third-party borrowing (possibly with a parent guarantee) may help to reduce the likelihood of the BEAT tax applying.

Global Intangible Low-Taxed Income (GILTI)

Although the TCJA generally moves the U.S. to a territorial system of taxation and eliminates the system of deferring tax on operating income generated by foreign subsidiaries, it also introduces a new tax on certain excess income generated by foreign subsidiaries (referred to as “global intangible low-taxed income”, or “GILTI”). This tax applies if the operating income of a foreign subsidiary exceeds a 10% return on the tax basis in the tangible business assets owned by the subsidiary. Foreign tax credits may be used to reduce or offset this tax liability.

Non-U.S. multinationals that have U.S. entities that own interests in foreign subsidiaries (i.e. sandwich structures), should consider restructuring in order to eliminate these structures in order to avoid the GILTI tax. In addition, U.S. acquirers are more likely to prefer asset acquisitions (or elections that allow transactions to be treated as asset acquisitions) to step-up the basis of assets for purposes of determining whether the GILTI tax will apply. U.S. sellers will likely prefer stock sales, since income from asset sales will increase income for purposes of calculating GILTI and stock sales may generate tax-free income to the extent gain is eligible for the participation exemption discussed above.

The reduction in U.S. tax rates, combined with the move to a territorial tax system, is likely to stimulate U.S. mergers and acquisitions activity.
In summary, issues for GCs to note:

1. The reduction in U.S. tax rates, combined with the move to a territorial tax system, is likely to stimulate U.S. mergers and acquisitions activity.
   > This is likely to include an increased interest by larger groups in disposing of non-core assets.
   > For acquisitions of U.S. targets, significant benefits may arise from structuring transactions as asset acquisitions.
   > In the non-U.S. context, U.S. sellers are likely to prefer stock sales and U.S. buyers are more likely to prefer asset acquisitions.
   > The changes are likely to increase the importance of the negotiation of tax provisions in acquisitions agreements, along with tax due diligence and tax structuring.

2. New interest deduction limitations may reduce the attractiveness of debt financing for U.S. operations and, where such financing is still beneficial, the new BEAT tax may make third-party financing of U.S. operations more attractive.

3. The impact of the BEAT tax on U.S. operations will need to be considered, along with restructuring steps to reduce or eliminate the potential impacts of the tax.

4. For groups with U.S. corporations that are shareholders of foreign subsidiaries, the impact of GILTI should be considered, along with steps that can be taken to move those foreign corporations out from under their U.S. shareholders.

These provisions are only a few of the myriad provisions contained in the TCJA, and depending on the operations of a particular multinational group, other provisions may also impact such group's business.
The changing face of SFO investigations – and the implications for GCs and compliance systems

The Serious Fraud Office is focusing more on compliance policies and on GCs when investigating alleged criminal behaviour.

With the introduction of Deferred Prosecution Agreements (“DPAs”) and of corporate “failure to prevent” offences, we are seeing the judgments and actions of GCs and those they manage under heavier scrutiny than ever before. This is down to the enforcement authorities’ increased focus on compliance systems, their increasing tendency to challenge privilege claims and their desire to control the scope and scale of internal investigations.

Scrutiny of compliance systems

The Bribery Act 2010 was the first piece of legislation to introduce the “failure to prevent” model (where a company can be liable for failing to prevent bribery committed on its behalf by its “associated persons”). The Criminal Finances Act (see panel) followed suit last year with its “failure to prevent” the facilitation of domestic and foreign tax evasion offence, again with a similar “reasonable procedures” defence. It is a model which the departing director of the Serious Fraud Office has repeatedly called to be extended to other forms of economic crime.

The inevitable result of this is an increasing tendency for a company’s compliance procedures to be central to any corporate defence, and therefore a key focus of the investigating and prosecuting authorities. Attesting to and evidencing those procedures will very often fall to senior members of a company’s legal and compliance functions.

The SFO is showing an increasing willingness to use its so-called “section 2 powers” (which include the power to compel any person to attend an interview and answer questions relevant to

The Criminal Finances Act

The new failure to prevent the facilitation of domestic and foreign tax evasion offence will only be committed where an organisation fails to prevent an associated person criminally (i.e. dishonestly) facilitating the evasion of tax, and where it cannot show that it had “reasonable procedures” in place to prevent that facilitation. As it is a strict liability offence, it does not matter if the organisation itself did not approve and had no knowledge of the underlying tax evasion or facilitation. The offence applies whether the tax evaded is owed in the UK or abroad.

Examples of prevention procedures that organisations may consider implementing include risk assessments and due diligence to identify internal and external risks, securing top-level commitment, communication and training, and the imposition of contractual obligations. In some cases it may be possible to align, to some degree, the reasonable prevention procedures designed to address this new offence with the anti-bribery and anti-money laundering measures that relevant bodies may already have in place. However, the Government has been clear that the new offence presents different considerations that need to be specifically addressed.

“If in a number of recent cases the SFO has taken the aggressive step of interviewing in-house legal personnel under caution i.e. as suspects, rather than witnesses, in their investigation.”
The changing face of SFO investigations – and the implications for GCs and compliance systems

its investigation), with the result that it is no longer uncommon for members of a company’s legal and compliance functions to find themselves answering questions under compulsion as potential witnesses in an investigation into their employer. Given the considerable challenges that this can present, not least in terms of protecting the company’s privilege, it is essential that specialist legal advice be sought before any interviews take place.

In the regulatory sphere, where the focus has shifted in recent years towards holding senior individuals accountable for corporate failures, the Financial Conduct Authority (“FCA”) controversially announced in 2016 that it was considering whether GCs and Heads of Legal should be designated as Senior Managers for the purposes of the new Senior Managers and Certification Regime. It appears to have parked the issues for now, but has said it will re-visit it in its 2019-2020 business plan. The merits of the proposal are beyond the scope of this briefing, but the FCA’s desire to explore it is perhaps a further indication of the increasing focus of regulators on companies’ legal functions.

Scrutiny of legal privilege

The second implication of the current enforcement environment for GCs and legal teams is the SFO’s aggressive stance towards legal privilege (broadly speaking, the right to resist disclosure of confidential communications relating to legal advice or documents produced for the purpose of litigation). We are seeing both more confidential communications relating to legal advice or documents produced for the purpose of litigation). We are seeing both more confidentiality challenges on whether material truly is privileged, and more pressure being brought before the courts, in a number of recent cases the SFO has taken the aggressive step of interviewing in-house legal personnel under caution (i.e. as suspects rather than witnesses in their investigation).

It is too early to predict whether or not these developments are the start of a continuing trend. Nevertheless, we would advise GCs to check their company’s directors and officers (“D&O”) insurance policy and take steps to ensure that they are covered by it. Many D&O policies are based on a narrow definition of “directors and officers”, and/or contain exclusions in respect of professional legal services. One way to extend coverage would be to ensure that the company has an appropriate employed lawyers’ liability (“ELL”) policy, in addition to standard D&O insurance.

Investigating the investigation

When a potential problem is discovered, a common response by a company’s senior management will be to launch an internal investigation to establish as quickly as possible what has happened. In many cases, responsibility for initiating and overseeing that investigation will fall to the company’s GC.

GCs should note, however, that the conduct of internal investigations is increasingly under scrutiny by interested regulators and other authorities. Both the SFO and the FCA have repeatedly made clear that they expect companies to engage in early communication regarding proposed investigations and not to take any steps that may prejudice or obstruct their own investigations. They are also increasingly seeking to impose limits on the internal investigation process by effectively prohibiting companies from interviewing relevant personnel. Given the incentives that may exist for a company to cooperate fully with the authorities, particularly where a DPA may be on offer, it is critical that those tasked with scoping and conducting internal investigations remain sensitive to these issues.

In summary, issues for GCs to note:

1. A company’s legal and compliance procedures are increasingly likely to be at the heart of the company’s defence to allegations that it failed to prevent the commission of certain offences by its employees and other associated persons. As a result, it is no longer uncommon for legal and compliance personnel to be the subject of compelled interviews.

2. The criminal and regulatory authorities appear increasingly willing to challenge a company’s claims to legal privilege, in some cases by invoking the crime-fraud exception.

3. Steps should be taken to ensure that any D&O policy extends to the company’s in-house lawyers.

4. It is increasingly likely that the conduct of a company’s internal investigation will come under scrutiny by the authorities. Care should therefore be taken to scope and conduct internal investigations in a way that is likely to be consistent with their expectations.
Round-up: where are we on the General Data Protection Regulation, cyber security and BEPS?

There are a number of issues that will remain high on the agenda of boards and GCs but where there have not been many legal developments since we last reported on them. Here we provide some useful links to previous briefings.

**The General Data Protection Regulation**

The General Data Protection Regulation will finally arrive in May 2018. It marks the biggest shake-up to EU data protection laws for 20 years.

While many of the core data protection obligations remain the same, the Regulation imposes a wide range of new requirements. Businesses will have to provide individuals with new privacy notices and upgrade contracts with suppliers who process personal information on their behalf. Added to this is the mandatory appointment of data officers (in some cases), mandatory privacy impact assessments, and new rights to data portability and to be “forgotten”.

The new regime will be backed up by a step change in sanctions with fines of up to €20m or 4% of annual worldwide turnover.

The GDPR is an EU regulation and therefore it will apply directly to the UK, and other Member States, from 25 May 2018. The UK could diverge from the Regulation and introduce its own data protection laws after Brexit. However, this seems unlikely and the Government has said the UK’s data protection laws will remain aligned to the Regulation.

This is, in part, to allow the free flow of personal information between the EU and the UK after Brexit. The optimum solution would be for the EU to find the UK “adequate” for data protection purposes – in other words, allow the continued free flow of personal data on the basis that the UK’s data protection laws will properly protect that data. In the absence of such an “adequacy” finding, other mechanisms will be needed to allow the transfer of personal data to the UK after Brexit, such as signing up to the so-called Standard Contractual Clauses (a standard form data transfer agreement approved by the EU Commission).

Click here to access our guide to the GDPR containing answers to frequently asked questions, checklists and everything else you need to get to grips with this new law.
Cyber security – breach notification obligations on the way

Last year saw an increase in the frequency and intensity of cyber-attacks, including the NotPetya attack, which brought several companies to a standstill.

This year will see significant changes to the legal framework as the General Data Protection Regulation, Network and Information Systems Directive and revised Payment Services Directive come into play. These laws impose new data security obligations and increased sanctions.

Importantly, they also impose strict breach notification rules. For example, under the GDPR, a personal data breach must be notified to the Information Commissioner within 72 hours if it presents a risk to individuals. If the breach is high risk, the affected individuals must also be notified. The deadline for notifying breaches under the revised Payment Services Directive is just four hours. Companies will need to make employees aware of these obligations and provide suitable reporting processes.

More information about cyber security is available here.

Concerns with tax avoidance and BEPS continue

GCs will be aware of the huge focus in recent times on tax avoidance, and in particular on so-called “base erosion and profit shifting” (i.e. moving profits from high to low tax jurisdictions, or exploiting differences between the tax regimes of different jurisdictions). This focus has led to what seems to be an unending stream of domestic, international and supra-national recommendations and proposals. For further details see “Operating within an Internationalised Tax World”.

As implementation of these recommendations and proposals is now underway and concrete measures are being introduced, some groups are finding it necessary to restructure operations, for example if their groups have high levels of debt or contain hybrid entities or instruments. In addition, groups are continuing to respond to “softer” reputational concerns, for example ensuring their operations are located in transparent and well-regarded locations, and that they can justify the tax treatment and tax strategy they apply. For further details see “Publishing a Board Approved Tax Strategy Online”.

Round-up: where are we on the General Data Protection Regulation, cyber security and BEPS?

“...groups are continuing to respond to “softer” reputational concerns, for example ensuring their operations are located in transparent and well-regarded locations, and that they can justify the tax treatment and tax strategy they apply.”
Key contacts

Corporate governance: impact on boards

Lucy Fergusson
Partner, London
(+44) 20 7456 3386
lucy.fergusson@linklaters.com

Bernice Dunsmuir
Consultant, London
(+44) 20 7456 4544
bernice.dunsmuir@linklaters.com

Alex Beidas
Partner, London
(+44) 20 7456 5903
alex.beidas@linklaters.com

Mirit Ehrenstein
Counsel PSL, London
(+44) 20 7456 3858
mirit.ehrenstein@linklaters.com

Board pay: helping keep boards and Remcos out of the headlines

Lucy Fergusson
Partner, London
(+44) 20 7456 3386
lucy.fergusson@linklaters.com

Richard Godden
Partner, London
(+44) 20 7456 3610
richard.godden@linklaters.com

Ian Hunter
Partner, London
(+44) 20 7456 3586
ian.hunter@linklaters.com

Nicole Kar
Partner, London
(+44) 20 7456 4382
nicole.kar@linklaters.com

Activism not activists

Richard Godden
Partner, London
(+44) 20 7456 3610
richard.godden@linklaters.com

Celebrating 10 years: a decade of market leadership

Paul Sidle
Senior PSL, London
(+44) 20 7456 4698
paul.sidle@linklaters.com

Don’t overlook the real meaning of the Parker review

Tom Shropshire
Partner, London
(+44) 20 7456 3223
tom.shropshire@linklaters.com

Richard Cumbley
Partner, London
(+44) 20 7456 4681
richard.cumbley@linklaters.com

Lynne Walkington
Partner, London
(+44) 20 7456 5718
lynee.walkington@linklaters.com

Upstream supplies: mitigating supply chain insolvency risk

Richard Hodgson
Partner, London
(+44) 20 7456 3797
richard.hodgson@linklaters.com

Richard Milam
Counsel, New York
(+1) 212 903 9050
shane.milam@linklaters.com

U.S. tax reforms: changing dynamics will influence deal-making in Europe and the United States

Richard Hodgson
Partner, London
(+44) 20 7456 3797
richard.hodgson@linklaters.com

Paul Sidle
Senior PSL, London
(+44) 20 7456 4698
paul.sidle@linklaters.com

Christian Ahlborn
Partner, London
(+44) 20 7456 3570
christian.ahlborn@linklaters.com

Bella Spring
Managing PSL, London
(+44) 20 7456 5864
bella.spring@linklaters.com

The changing face of SFO investigations – and the implications for GCs and compliance systems

Ely Proudlock
Counsel, London
(+44) 20 7456 2594
ely.proudlock@linklaters.com

Richard Cumbley
Partner, London
(+44) 20 7456 4681
richard.cumbley@linklaters.com

Peter Church
Counsel PSL, London
(+44) 20 7456 5495
peter.church@linklaters.com

General Data Protection Regulation and cyber security

Richard Godden
Partner, London
(+44) 20 7456 3610
richard.godden@linklaters.com

Ian Hunter
Partner, London
(+44) 20 7456 3586
ian.hunter@linklaters.com

Increasing foreign investment control and implications for global deals

Christian Ahlborn
Partner, London
(+44) 20 7456 3570
christian.ahlborn@linklaters.com

Bella Spring
Managing PSL, London
(+44) 20 7456 5864
bella.spring@linklaters.com

Elly Proudlock
Counsel, London
(+44) 20 7456 2594
ely.proudlock@linklaters.com

Richard Hodgson
Partner, London
(+44) 20 7456 3797
richard.hodgson@linklaters.com

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Ely Proudlock
Counsel, London
(+44) 20 7456 2594
ely.proudlock@linklaters.com

Richard Cumbley
Partner, London
(+44) 20 7456 4681
richard.cumbley@linklaters.com

Peter Church
Counsel PSL, London
(+44) 20 7456 5495
peter.church@linklaters.com

General Data Protection Regulation and cyber security

Richard Godden
Partner, London
(+44) 20 7456 3610
richard.godden@linklaters.com

Ian Hunter
Partner, London
(+44) 20 7456 3586
ian.hunter@linklaters.com

Increasing foreign investment control and implications for global deals

Christian Ahlborn
Partner, London
(+44) 20 7456 3570
christian.ahlborn@linklaters.com

Bella Spring
Managing PSL, London
(+44) 20 7456 5864
bella.spring@linklaters.com

Elly Proudlock
Counsel, London
(+44) 20 7456 2594
ely.proudlock@linklaters.com

Richard Cumbley
Partner, London
(+44) 20 7456 4681
richard.cumbley@linklaters.com

Peter Church
Counsel PSL, London
(+44) 20 7456 5495
peter.church@linklaters.com

General Data Protection Regulation and cyber security

Richard Godden
Partner, London
(+44) 20 7456 3610
richard.godden@linklaters.com

Ian Hunter
Partner, London
(+44) 20 7456 3586
ian.hunter@linklaters.com

Increasing foreign investment control and implications for global deals

Christian Ahlborn
Partner, London
(+44) 20 7456 3570
christian.ahlborn@linklaters.com

Bella Spring
Managing PSL, London
(+44) 20 7456 5864
bella.spring@linklaters.com

Elly Proudlock
Counsel, London
(+44) 20 7456 2594
ely.proudlock@linklaters.com

Richard Cumbley
Partner, London
(+44) 20 7456 4681
richard.cumbley@linklaters.com

Peter Church
Counsel PSL, London
(+44) 20 7456 5495
peter.church@linklaters.com

General Data Protection Regulation and cyber security

Richard Godden
Partner, London
(+44) 20 7456 3610
richard.godden@linklaters.com

Ian Hunter
Partner, London
(+44) 20 7456 3586
ian.hunter@linklaters.com

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Christian Ahlborn
Partner, London
(+44) 20 7456 3570
christian.ahlborn@linklaters.com

Bella Spring
Managing PSL, London
(+44) 20 7456 5864
bella.spring@linklaters.com

U.S. tax reforms: changing dynamics will influence deal-making in Europe and the United States

Shane Milam
Counsel, New York
(+1) 212 903 9050
shane.milam@linklaters.com

Clare Bouwer
Senior PSL, London
(+44) 20 7456 5727
clare.bouwer@linklaters.com