

Lawyers win where banks lose



The past year has provided some excellent growth opportunities for law firms in trade, commodity and export finance. There have been some landmark test cases and some interesting undercurrents, as Philip Carter reports.

“The one great principle of English law is to make business for itself”. So said Charles Dickens; but whether it be English or New York law, this bold statement has not quite been borne out over the past 12 months. Thanks to a strong global economy and commodities markets, the flow of transactions has yielded a fruitful year for lawyers specialising in international trade and export finance. “It was probably our busiest and most successful year ever in terms of the growth in our commodity and trade finance practice,” says Kyri Evagora, partner at Richards Butler in London. “The work has been quite varied, but there has certainly been more of an emphasis on transactional work rather than unpicking deals or workouts.”

When pressed to put a figure

on the increase in transactional work, he ventures an estimate of around 20%. An impressive rise, and one which reflects the buoyant performance shared by



Wynne at Denton Wilde Spate Time invested in helping to structure a transaction may not be rewarded at all

Who's the best law firm in trade finance?

GTR has received and counted votes by email and fax for its annual readers' poll of the best trade finance law firms. Rankings are based on which firm/s received the most votes. We asked voters which did they think is/are the best law firm/s undertaking trade finance business (both contentious and non-contentious law).

Position	Law firm	2005 Position
1	Denton Wilde Spate	1
2	Lovells	3
3	Clyde & Co	2
4	Stephenson Harwood	4=
5	Clifford Chance	10
6	Linklaters	4=
7	Sullivan & Worcester	7=
8	Allen & Overy	7=
9	Richards Butler	-
10	Greenberg Traurig	-

Also mentioned:

Ashurst; Bracewell & Giuliani; DLA Piper Rudnick Gray Cary; Freshfields Drew Napier; Gide Loyrette Nouel; Graf von Westphalen Bappert & Modest; Hughes Hubbard Reed; Law & Finance (Milano); Lofaro & Tanti Dougall; Milbank Tweed Hadley & McCloy; Norton Rose; Porter & Hedges; Simmons & Simmons; Sorainen Law Offices; Squire, Sanders & Dempsey; Studio Legale Chiomenti; Thomas Cooper & Stibbard; White & Case; Wikborg Rein & Co.

most of the main legal players in the market.

The background to the year has been the phenomenal performances of the global commodity markets. "The increased market activity has been directly mirrored in increased turnover for us," says Robert Parson, partner at Clyde & Co.

The implications of such vibrant markets are numerous for lawyers and the banks they serve: most are positive, but such conditions do bring their own pressures too. Higher prices mean that producers' credit quality is improving, diminishing the need for sophisticated structures, which in turn affects the demand for legal services. This is seen most vividly among the banks that make up trade finance lawyers key constituency.

"Increased liquidity in many markets, a faith in the ever-growing demand for natural resources and, perhaps, the greater comfort established by experience have led to longer tenors, reduced spreads, more open account trading and less emphasis on pre-agreed offtake and hedging arrangements," says Morris Blumenthal, associate at DLA Piper Rudnick Gray Cary in London.

This has made the past year a challenging one for most banks. High levels of liquidity in the market and plenty of lenders – not necessarily all banks – willing to provide funding have had to compete for mandates from borrowers that have increasing access to the capital markets.

Competition among sources of funding mean that banks have to do more to earn the business, leading to weaker overall transaction structures. "Structured trade finance often fills the time gap between initial equity funding and state support for national or local producers and access to corporate loans and capital markets," says Nigel Ward, partner at Norton Rose in Paris. "High commodity prices have led to significant cashflows in producers and this has attracted private equity, Toronto

Stock Exchange and Aim listings and in some of the bigger producers a switch to corporate lending, securitisation and bond issues. Structured trade finance lenders are compensating by being willing to take more risk, such as funding earlier in the exploration and production phase or relaxing their lending covenants."

This might be bad news for banks, but it is positive for lawyers. As banks give more away to win mandates on the one hand, they are taking a stronger grip on security with the other. With more risk comes a greater attention to legal issues and a more intense focus on the reality of the value of the traditional security that supports the debt.

"Higher commodity and, in particular, oil prices have led banks and financial institutions to instruct us more to improve their security arrangements to cover the increased exposure," says Charles Williams, partner at Thomas Cooper & Stibbard in London.

Competition intensifies

But, as with banks, competition among law firms is equally intense as the buy-side holds sway. More legal firms are looking to gain market share in the trade finance arena, creating greater pricing pressure.

This is not good news for those serving a sector which has a reputation for thriftiness. "Trade finance is a price-sensitive sector," says Michael Kenny, partner at Watson, Farley & Williams. "Unlike corporate M&A, for example, where legal fees represent just an insignificant fraction of total deal sizes and successful completion is the overriding consideration, in trade finance, emerging market borrowers view legal fees from centres such as London far more cautiously." So in an effort to gain market share, fees are being driven low, perhaps unsustainably low, says Jason Kerr, partner at White & Case in London: "There is serious low-balling by some

firms when it comes to winning business. It's very frustrating when a firm comes in and prices itself around 30% lower than what most would consider acceptable. Often these firms think they can fight it out at the back end. But how long that can really be sustainable is an open question. The issue with pricing at these levels is that it raises questions over service quality. Something has got to give; it's just not viable to keep staffing these deals with the experience that's required at the prices that are being quoted." Another source of pricing pressure is the generic and repeatable nature of certain types of structures.

"In some ways pre-export financings, which used to be the mainstay of financings, have become somewhat commoditised and consequently borrowers are reluctant to pay legal fees of any size notwithstanding the transaction might be more difficult," says Geoffrey Wynne, partner at Denton Wilde Sapte in London. This is especially pronounced on smaller transactions according to Ward. "Legal fees are clearly an issue in some of the smaller-sized structured deals – no less legal work is involved in a US\$10mn secured structured financing than in one for US\$100mn – but the willingness to pay is different," he says.

Coming into deals later

Such competitive pressure inevitably reduces itself to a hard-nosed approach from clients. "One of the main reasons for not being involved earlier in transactions relates to issues of legal fees that are payable and the desire of borrowers to see work put out to tender and to take the lowest quote," says Wynne. "This means that time invested in helping to structure a transaction may not be rewarded at all."

Perhaps unsurprisingly, lawyers see this as a false economy and push for early involvement in transactions. And in more



Parson at
Clyde & Co

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Blumenthal
at DLA
Piper
Rudnick
Gray Cary

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Evagora at Richards Butler

It is early days and there is uncertainty over how Chinese courts will view more complex structures

complex deals their wishes are often granted. "Clients increasingly involve their lawyers in transactions at an early stage and we are often called upon to provide advice and guidance in structuring transactions and in mechanisms for allocating risk between parties," says David Lacey, partner at Stephenson Harwood in London. "We are keen to be involved in transactions at an early stage as it provides a valuable insight into market trends and the types of transactions pursued by their clients. Equally, legal input at the structuring stage of the transaction can prevent parties pursuing a structure which, while it may have commercial benefits, suffers from some inherent legal defect." But, as Parson at Clyde & Co notes, early involvement does not necessarily mean bigger fees. "The tendency to use lawyers earlier does not however always translate into greater legal expenditure in all cases," he says. "And here is a lesson for risk managers – because money spent up front can often help shape what follows in terms of legal work more efficiently producing a cost saving. Also as lawyers we tend to be conscious of when the bank is spending speculative money looking at a project which does not yet have a client and a guaranteed income line at the end of it and there is generally a saving there too. So the message is 'use us early.' "

Standing out from the crowd

While fees are clearly a major motivator for clients, if work is pitched too low alarm bells will usually ring. A secondary aspect of the growing number of law firms competing for business is the less consistent range of competence on offer. "There appear to be more firms looking for a piece of the action," says Evagora at Richards Butler. "But there is a polarisation in the market between those firms that can do sophisticated trade finance deals and those that cannot.

Some firms don't have the degree of expertise you need for commodity and complex trade finance deals that banks really do want now."

So beyond being competitive on fees, being able to differentiate your firm from the field is crucial. Leading players draw on a variety of methods to help them stand out from the crowd, but all stress the importance of relationships and being able to deliver a high quality service. The use of panels of preferred law firms means that many deals are awarded on the basis of the lowest fee bid by a handful of firms that are all equally capable of doing the legal work.

"Relationships with the parties involved are obviously important, but not so that they overrule a genuine track record with the type of structure involved and the jurisdiction concerned," says Ward at Norton Rose. "Membership of the panels of preferred law firms is very important. While having teams that can combine to provide a range of skills, such as Islamic finance or securitisation, can be a big advantage. Similarly having experienced colleagues in offices in the jurisdictions in which the borrower is incorporated or the security is being taken is important." Increasingly globalised trade flows also suggest that lawyers need to have the geographic scope to tackle the multi-country nature of the business. This is a view embraced by many, with firms opening offices in traditional trading centres. However, whether a global firm has the local expertise to match its ambitions is, for some at least, still an open question. "As a result of the trend among Anglo-Saxon firms to merge and otherwise expand, it's now fair to divide law firms into two broad categories: those with a wide geographic footprint, ie, offices throughout the world, and those with a physical presence in fewer cities," says Michael Sullivan, partner at Sullivan & Worcester in New York. "It remains to be determined if one structure has

an advantage over the other. While the largest firms may have offices in, for example, Bangkok, it remains that the best attorney to advise on a Thai legal issue may not be the remote partner of your tried and true New York-based lawyer. And conversely, your tried and true London lawyer whose firm has fewer offices, might know precisely the best local lawyer to engage for Thai legal issues."

Awaiting Basel II

The move towards global one-stop shop legal firms is one which is likely to continue over the coming year. Beyond the world of legal services, the wider market that these law firms serve has also experienced a number of changes and developments over the past year. Some of these are long-running, of which the introduction of new capital adequacy limits for banks is one of the most significant. The spectre of Basel II looms ever larger, but quite how it will affect the sector is still something of an unknown. "It is more the talk of what Basel II is going to do to the market rather than its current influence," says Wynne at Dentons. "There is a fair amount of 'wait-and-see' until the fine print is finally released." Moreover, when the long-awaited regime is finally unveiled, its implementation will be staggered. For example, it is expected to come into force in Hong Kong next year, in the UK in 2008 and in the US in 2009. "This will lead to some tricky questions for banks operating in a range of jurisdictions – as to which approach is adopted in a particular jurisdiction," says Siân Fellows, consultant at Richards Butler. "There are also potential issues as regards consistency of the approaches adopted by the different supervisory authorities when granting IRB waivers. This is something the FSA is aware of and is dealing with by



Clifford Chance's Johnson

In Brazil there has been a considerable relaxation in terms of the tightness of structures as the lending market has become increasingly liquid





Ward at Norton Rose

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liaising with other regulators and supervisory authorities.” And while Basel II is undoubtedly a significant influence on the market, it is hardly a bolt from the blue and lawyers are already experiencing an increase in work based around it. “Banks have been tightening their belts for Basel II for some years and have now educated their lending officers and risk managers to approach transactions with the capital adequacy regime firmly in mind,” says Parson. “So we now see requirements for legal opinions and background enquiries about efficiency of enforceability of securities in certain countries as routine.”

PRI moves out of the shadows

Overlapping with the impact of Basel II is the growth of the private political risk insurance market. “Under Basel II credit insurance and derivatives are capable of recognition as credit risk mitigants provided certain requirements are met,” says Fellows. “There is therefore scope for greater use of credit insurance and credit risk mitigants under Basel II to mitigate potentially higher capital costs.” Offsetting this however, is the view among some banks of privately-sourced PRI as somehow less robust than equivalent cover extended through traditional multilateral agencies. A second and related issue is that if the paperwork is not impeccable private PRI can be less forgiving. “The disclosure and good faith requirements are seen as more serious and burdensome for private political risk cover than might be the case with a multilateral institution,” says Kerr at White & Case. “The trouble is that it is very difficult to ensure that you have

disclosed all aspects of a big transaction or project which might subsequently prove to be pertinent.” Despite this, privately-sourced PRI is being increasingly used by banks, often on a discreet basis after a deal has been signed. “The bank has been pressured by the client that the deal does not warrant PRI and the bank feels obliged to go along with the client to win the business,” says Kerr. “After this the bank quietly books its own cover in the private market.” However, a crucial distinction in the eyes of the Basel II

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While the increasing use of PRI post-Basel II is welcome, it's important not to overstate its role. “Insurance can only go so far in reducing the risk profile of a transaction,” says Lacey at Stephenson Harwood. “And it is important to bear in mind that insurance carries with it both the cost and all the difficulties inherent in a contract of insurance as opposed to a financial guarantee.” The fact remains that solid documentation and deep knowledge of the relevant jurisdictions are as essential as ever in ensuring a successful outcome for a law firm's client.

Fraud – ever present

At heart, trade finance is a business built on trust and expectation. And a corollary of this is the fact that fraud

remains a persistent threat – something lawyers are all too aware of. “There have always been a number of key stages in a transaction where a trader or banker is exposed to an increased fraud risk and some of the most celebrated cases are not the one-off scams where a corporate is set up as a vehicle for fraud, but where the long-standing *bone fide* trader lapses into fraudulent practices as the business goes off the rails,” says Parson. “That’s where you see the banks take the big hits, as Enron showed us.” By its very nature, gauging the extent of fraud is a tricky business. But there does not seem to be undue alarm about a significant rise in the past year or so. “At the moment it looks like it is at a low level particularly in the structured markets,” says Wynne. “I am sure there are a number of unreported frauds and we certainly see the odd

regulators means getting the right form of insurance is the key to generating capital pricing benefits. “It’s vital to ensure that a deal’s political risk insurance qualifies under Basel II,” says Kenny at Watson, Farley. One aspect under Basel II is that policies must provide for prompt payment. Yet insurers are naturally inclined to favour those policies which have a waiting period – allowing them to investigate a claim before a pay-out is due. The issue is whether this time lag will cut across Basel II requirements. Already some insurers are working on policies which will bridge this gap. “We see a great deal of work being done to build insurance products that meet Basel II criteria,” says Parson. “It’s an interesting market because some of the bigger name banks in trade finance will be able to operate on a more flexible basis than smaller ones and will not have exactly the same requirements in terms of the content of their operational and credit risk mitigants.”



White & Case's Kerr

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Sullivan at Sullivan & Worcester

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problem with letters of credit in particular.” Yet spotting a fraud is rarely straightforward and sometimes occurs where least expected. “When banks first approach us for assistance with recoveries, there may be no grounds to suspect a fraud,” says Lacey. “It is surprising how many of these claims do in fact turn into possible fraud enquiries. We continue to see a steady number of claims which, on investigation, reveal an element of fraud.”

The most common frauds stem from a borrower raising finance from several lenders secured on the same goods – often involving the collusion in the fraud by an employee of the warehouse keeper.

“In such cases documentation is of little, if any, value in preventing a fraud,” says Lacey. “But it may be of some benefit in helping parties divide recoveries and, depending on the type of the transaction, can have a significant impact on that especially where a party can demonstrate title to property rather than simply a security interest in it or an unsecured claim.”

The most efficient remedy to detect fraud is vigilance, notes Christian de Lima Ramos at Ramos e Zuanon Advogados in Sao Paolo, Brazil. “The importance of monitoring the collateral package cannot be overlooked by lenders,” he says. “And at the first sign of fraud, the lender must act fast so as to preserve its rights. Tolerance by the lender may jeopardise its position and severely reduce its chances of recovering the invested amount.”

Moreover, to reduce some types of fraud a change in technology rather than documentation *per se* is required, according to Parson. “Bill of lading falsification remains the main fraud practice in international trade,” he says. “Attempts to eradicate it will really only succeed once electronification of the trade system makes the creation and use of shipping documents much more immediate so that fraudsters

have no time to break security encryption codes. Despite lots of encouraging noises we do realistically remain a long way from that sort of electronic trading market however.” Experience shows, however, that ultimately fraud is part and parcel of international trade finance, and despite best efforts the scammers

obligations relating to deals that have soured for reasons wholly unrelated to the nature of the underlying commercial activity. The arguments are advanced nonetheless; and their reappearance corresponds with the emergence of the crisis *du jour*.”

In terms of the development of the law in the UK there has

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are usually at least one step ahead. “No guidelines and no documentation package will render any transaction bullet-proof, especially with respect to fraud,” says Sullivan. “And it remains true that lawyers and practitioners alike are more likely to ‘fight the last war,’ that is to draw documents that protect against the form of scam that has already been revealed, rather than anticipate the next iteration of fraud.”

Limited litigation

While deal volumes have been high, the past year has been relatively untroubled by contentious legal issues arising

been “little in terms of earth-shattering decisions in the courts,” says Parson. Although he is encouraged by the court’s underpinning of letters of credit and guarantees in the Tradigrain vs State Trading Corporation of India case on wrongful calls in demand guarantees and the PT Pan Indonesia Bank Limited TBK vs Marconi Communication International Limited (2005) case.

The latter dealt with the determination of governing law in an LC issued in Indonesia but providing for London negotiation. “The court upheld the principle that the law where the LC was to be negotiated according to the LC terms

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from international trade. If anything, the cases thrown up this year have been echoes of previous legal wranglings. “Some of the issues I’ve seen in the last year concern questions identical, or nearly identical, to questions I saw first in the 1980s, such as the difference between trade and trade-related financing,” says Sullivan. “Arguments relating to these issues are periodically trotted out by those who look to avoid commitments or

would apply in any dispute between the beneficiary and the issuing bank,” Parson says. “The same would therefore apply as between a confirming or negotiating bank and the issuing bank.

“Banks like certainty – and in the current phase of scrutiny of procedures and operational risk issues under Basel II – soundings like this from the courts. They are reassured, as there is a measure of certainty associated with the English court’s decisions on the



Stephenson Harwood’s Lacey

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application of UCP 500 and banking law in general, which banks rely on as the basis for many of their current policies in transactional export finance transactions.”

While the Pan Indonesia/Marconi case has addressed some questions from an English law perspective, others remain. “We have advised on a number of disputes over performance bonds and guarantees, particularly where banks find that supposed back-to-back indemnities are governed by different laws and may not be enforceable under those laws,” says Lacey. “Since March 2005 questions on governing law may be referred to the European

example, the timing of discovery of a fraud and the position of the holder of a bill.”

There have been a number of other decisions on the allocation of risk in the case of fraud and the coming year is likely to see some decisions on banks’ obligations to preserve and enforce their security and other rights.

Cases relating to Parmalat have been well publicised and have led to numerous legal actions, many of which are continuing. In the latest Parmalat-related decision, Standard Chartered Bank vs Banque Marocaine de Commerce Extérieur (February 2006), the Commercial Court rejected Banque Marocaine’s

names to move from secured borrowing to straight debt and capital markets-based solutions,” says Kerr. However, a new group of borrowers have come in to take up some of the slack – in the form of upstream reserve-based lending. This has grown significantly over the past year, driven by the high price of oil which has turned previously uneconomic reserves increasingly attractive to producers. Perhaps surprisingly given events such as the Yukos affair, commercial banks view Russia as an improving political risk.

“Banks tend to view Russian risk as more palatable,” says Kerr. “This is partly, of course, due to the high liquidity in the banking market, forcing banks to take on assets they may once have avoided.”

Historically, when doing business with Russian corporates, bankers and lawyers sought to move as much of the transaction’s risk outside of the country. All funding for the debt would be offshore with just the production risk remaining in Russia. But now, according to Kerr, deals are being structured in Russia with much of the risk remaining within the country. “Banks are going onshore in Russia and actually taking security over assets there,” says Kerr. “This presents a real challenge in terms of enforcing that security.”

Under Russian law, creditors cannot take control of an asset due to them in the case of a default but have to sell it through a public auction. “The concern is what happens to that asset during this time.”

While Russian courts do have some discretion to protect assets being claimed by creditors it is by no means clear that they would take this action. Nor has there been a large problem or workout with which to benchmark the performance of security of assets in Russia to date.

But the most significant development of the year in Russia has been the changes in legislation governing Russian



De Lima Ramos at Ramos e Zuanon

The likelihood of litigation will increase more and more

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Court of Justice, and it is quite possible that the ECJ would uphold a rule that the governing law of a particular obligation under a credit should be that of the place of business of the bank having the obligation under the credit. Although the Marconi case has made the English law position clear, further arguments on choice of law can be expected.”

The importance of choice of law and jurisdiction issues is always highlighted when the courts of another jurisdiction give a judgment that might have been decided differently elsewhere. “In Credit Lyonnais vs Canara Bank (October 11, 2005), the French Court of Cassation found that, under French law, a confirming bank discounting its own acceptance under an acceptance documentary credit was not protected from a fraud subsequently discovered,” says Lacey. “The English court might have formed a different view under English law. The case shows that different courts under different laws may allocate risk differently between the parties when considering, for

challenge to summary judgment for payment of promissory notes under a participation, which the bank argued on grounds of a common mistake – that the notes had specified that funds would be applied to foodstuff transactions, but had not been so used.

The court has allowed a counterclaim against Standard Chartered to proceed on other grounds.

Russian regime change

Beyond the confines of the courts, there have been more dramatic developments in terms of regulatory environments and market conditions in some of the biggest users of international trade finance globally.

Russia, notably, has experienced some significant changes which has seen its top-tier corporates de-emphasising their pre-export finance needs after several years of heavy use. “The traditional markets have become quieter largely as a result of Russia’s investment grade rating which has encouraged the stronger



Shaikenov at Salans

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**Nethercott
at White &
Case**

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currency control rules. "This has had a very positive effect on the Russian export finance market," says Grigory Marinchev at Gide Loyrette Nouel in Moscow. "Almost all of the banks involved in Russia are now looking to use this type of structure and we are working on four ourselves. The crucial point for any ECA transaction is that the insurance only becomes effective once an exporter receives payment. Until June of last year, Russian borrowers had to draw down borrowings into a Russian bank account which meant lenders were exposed to a set of Russian risks and effectively lost control of their money.

"Since the change in the law Russian borrowers are now allowed to draw down funds in overseas accounts. Typically this would be an account with the lending bank itself, where a disbursement is made to the importer's account and which is then transferred to the exporter, triggering the ECA coverage."

A similar move took place in Kazakhstan, Central Asia's largest economy. "The major change was the adoption of a new currency control law," says Abai Shaikenov, partner at Salans in Almaty. "The law significantly liberalises the currency control in Kazakhstan shifting from a licensing regime to a registration mode, and in some instances to notification mode. The law also provides even for further liberalisation starting from 2007 when the notification regime would be the most widely used regime in currency control. These moves should further increase activity in trade and export finance as exporters and importers will benefit from simplified requirements and procedures."

The dragon soars

Fuelling the year's commodity boom that has sustained much of the trade and export finance

markets over the past year has been China's continued unprecedented economic expansion. Indeed, the country's voracious appetite is redefining the global commodity landscape. "China's pursuit of access to natural resources, particularly oil, is continuing to change the global markets," says Blumenthal at DLA Piper. Despite the enormous scope for trade with China, serious difficulties remain in terms of legal and security issues from the perspective of many western firms. "China is still a challenge," says Evagora at Richards Butler. "Recent changes in the law relating to security make the type of structures commonly used in trade finance workable provided they comply with necessary requirements. But it is early days and there is

“ However, grey areas remain, which give rise to concern ”

uncertainty over how Chinese courts will view more complex structures."

Yet, China is simply too big an opportunity for most corporates and banks to be put off by the legal uncertainties and a readjustment of expectations is arguably the best way to approach the market. "The laws on title, security and insolvency are not as highly developed as in the west and it comes as a shock to some lenders when they have to cast aside much of their comfort zone and think in a different way," says Parson. But improvements to the Chinese legal trade environment are being made, albeit slowly and somewhat unsteadily. For example, in light of its WTO commitments, China revised its 1994 Foreign Trade Law in 2004. "The new law is generally regarded as a major increase in transparency and sensitivity to international trade law and WTO commitments," says Lacey.

"However, grey areas remain, which give rise to concern. For example, Article 16 states that

restrictions or prohibitions may be imposed in order to establish or accelerate the establishment of a particular domestic industry, whereas the WTO requires China not to take any such action without first submitting a special application to the other WTO members."

The biggest issues facing China in terms of international trade law cover anti-dumping and safeguard petitions lodged against it. The country is subject to more investigations for anti-dumping and safeguard protectionism than any other WTO member. And both domestic and foreign manufacturers in China may be subject to an increasing amount of anti-dumping litigation. According to Lacey, the main area of legal interest ahead is the WTO/China legislation

concerning rules of origin, which determines whether goods enter a WTO member country on

preferential or non preferential terms – a substantive issue bearing in mind that processed goods comprise 48% of China's total trade with the world. But with China's increasing prominence comes intensified scrutiny and wider currents are also at play, which could yield positive developments for China and its trading partners. "We are now at an interesting stage," says Parson. "The WTO benchmarks have to be honoured and Beijing is under the spotlight as the Olympics near so the authorities know that anti-competitive measures or retention of backdoor barriers to western corporate and banking activity will get picked up on."

Increasingly Islamic

While China presents its own complexities for lawyers, the underlying financing involved is essentially familiar. Yet in the



**Marinichev
at Gide
Loyrette**

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GTR

Middle East, the rise of Islamic finance presents a whole new set of challenges for western law firms. Significant legal input is required to structure these products as the prohibitions on interest and uncertainty means that traditional financing techniques must be adapted to implement these structures. And over the past year more law firms have responded to their client's desires to tap into the highly liquid Islamic market as an additional source of funding. White & Case, for example, in March this year formed a dedicated Islamic finance unit, with 25 lawyers led by Craig Nethercott in London and Mohammed Al Sheikh in Riyadh.

"We've been advising on Islamic financing issues for years but hadn't formalised these capabilities to the outside world," says Nethercott. "With interest in Islamic finance increasing across our client base, we wanted to provide a clearer picture of what we do." One of the biggest deals so

on the relationship between English law and *shariah* structures. "One of the greatest challenges over the last year has been the increasing interest in Islamic finance and the need for creative solutions to use English legal principles to implement financing structures in a *shariah*-compliant fashion," says Lacey. "This has been assisted by the earlier decision of the courts that an English law agreement will be construed under English law without regard to the *shariah* even in circumstances where it is put in place as part of a *shariah*-compliant structure. This has given finance providers the comfort of using a well-established legal system while enabling those who require finance to obtain it in a manner consistent with the principles of the *shariah*."

Latin America rides the tide

The influence of high commodity prices has provided for a successful past year for Latin America and most noticeably

11,076/2004, governing the warehousing of agricultural products and the issuance of certificates of deposit (CDAs) and warrants (WA) in respect thereto," he says. "Also, there was the enactment of a new bankruptcy law in Brazil, with a significant impact in credit aspects of transactions involving Brazilian parties. I would also highlight the regulatory modifications enacted by the central bank in the Brazilian foreign exchange regulations and controls." The issues at play in Latin America, and most noticeably Brazil, are those that face participants in transactions elsewhere.

"In terms of bank clients, it is the simple fact that there is great liquidity in the market, especially in Brazil, and that the banks are therefore being squeezed very hard in terms of pricing," says Johnson.

"In terms of borrower clients, as well as the obvious desire to secure the best possible pricing, the main concern is not to allow themselves to be bound too tightly by restrictive covenant packages – borrowers increasingly want to make sure that they give themselves flexibility going forward."

There are some signs that the coming year will be a busier one for litigators involved in Latin American trade finance. "We expect 2006 to be a very different story," says Ramos. "The appreciation of the real and the decline in the prices of certain grains are producing a major negative impact in the economic condition of certain regions and specific producers. Should this situation continue, the financial and credit condition of grain producers will tend to deteriorate and the likelihood of litigation will increase more and more." Whether this price pressure will remain isolated or will spread and see the top coming off the global commodities markets will play a major role in deciding the outlook for the coming year for lawyers involved in trade and export finance.



Fellows at Richards Butler

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“ In the Middle East, the rise of Islamic finance presents a whole new set of challenges for western law firms ”

far featuring Islamic finance was the recent US\$9.9bn petrochemicals plant for Saudi Aramco and Sumitomo Chemicals in Saudi Arabia. The deal features a US\$600mn Islamic facility – the biggest long-term Islamic project financing to date. "The deal is significant in a number of respects," says Nethercott. "It's the first time, to my knowledge, that a significant long-tenor Islamic tranche has participated in a multisourced financing in Saudi Arabia – where the Hanbali school of Islamic jurisprudence is followed." The growth of the market has been aided, from a legal perspective, by greater clarity

in Brazil. "In Brazil there has been a considerable relaxation in terms of the tightness of structures as the lending market has become increasingly liquid and the credit of some of the major exporters has continued to improve, with companies such as Petrobras and CVRD now at investment grade," says Charles Johnson, senior associate at Clifford Chance in Brazil.

The past year has also seen plenty of action in terms of trade and export finance laws, according to De Lima Ramos. "In Brazil, the scenario was particularly interesting because of the enactment, late in December 2004, of Law



Williams at Thomas Cooper and Stibbard

Higher commodity and, in particular, oil prices have led banks and financial institutions to instruct us more to improve their security arrangements to cover the increased exposure