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WE NEED TO TALK

IFLR gives lawyers at Europe's top investment banks and financial advisory firms a platform for candid debate on the issues that matter most to them

Lucy McNulty, managing editor

The past five years have been something of a rollercoaster ride for Europe's capital markets lawyers – thanks, largely, to sustained volatility across regional securitisation, equities and debt capital markets, and the ensuing regulatory drive to reform the system.

While the 2014 outlook for European capital markets looks altogether rosier, those that have survived the tough times must now learn to operate in a much-changed environment.

Indeed, capital markets counsel today need not only negotiate a renewed emphasis on transparency and disclosure, a swathe of new regulatory standards and harsher sanctions for non-compliance. They need also determine how to tackle a market rebound in the aftermath of extensive cost-cutting initiatives.

Against this backdrop, IFLR's contacts have long called for a platform for candid discussion on the key issues for today's market.

IFLR has thereby developed its Bankers' Counsel Poll series to provide the region's top banks with a forum to debate developing transactional best practice in an altered operational landscape.

The poll was refined with the help of Davis Polk & Wardwell's corporate partner Will Pearce and corporate associate Dan Hirschovits, and was sent to the 20 largest investment banks and financial advisory firms in Europe. Seventy-five percent agreed to take part, answering questions on key pressure points as frankly as possible in return for complete anonymity.

Here are the results of IFLR's 2013 Bankers' Counsel Poll: European capital markets.

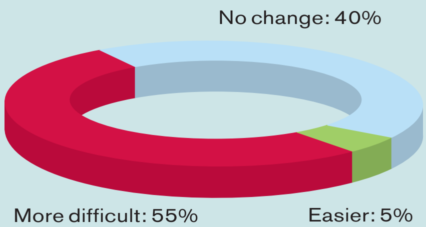
Dealing with auditors

A majority of 55% of respondents say their interactions with auditors had become more difficult in the past five years. While, a further 40% stated service standards had not improved over the same time period.

The increasing time and legal costs required to negotiate engagement letter provisions particularly concern the in-house counsel surveyed. "It feels like we're reinventing the wheel on every transaction," says one ECM execution director at a US investment bank. "It would be helpful if the process were not so unwieldy."

Over the last three years, some – but not all – of Europe's larger auditing firms have taken steps to agree standard positions with the region's bulge brackets on the terms included within their UK engagement letters.

Have accountants become easier or more difficult to work with over the past five years?



Standardising forms in this manner can prove a laborious process. Even so, many poll participants believe more auditors need to invest in such initiatives to ensure more sophisticated execution of ECM transactions.

"In the UK, forms and standards are now better formalised and adhered to," says the counsel at one international investment bank. "It's the same in France and Germany."

"It would be beneficial for certain continental and emerging jurisdictions to follow this trend towards increased sophistication," adds another poll participant. "Developing a common platform among regional law firms and banks as to what accountants' documents and contracts should look like would be extremely helpful."

Where no standard forms exist, counsel complain of a constant pressure to modify comfort letters to improve auditors' position bases by changes to their internal policy.

The Financial Reporting Council's Richard Fleck believes it is inevitable that as the regulatory landscape becomes ever more complicated, accountants will want their forms to reflect the changed circumstances.

But he warns that is not the same as constant tinkering to obtain a less burdensome engagement, or to secure additional protection by reducing the level of assurance provided. "Changes to achieve such results are, I think, undesirable," he says.

He agrees there are certain provisions in the UK engagement letter that lend themselves to standardisation, such as the description of the statutory and regulatory requirements to be complied with.

"If these provisions were to become standardised, clients would be better able to focus on the differences in the other aspects of the arrangements being offered by different firms, while, at the same time, having confidence that the services being offered are in fact the same," he explains.

Fleck believes the best route to such harmonisation would be through a professional body in conjunction with those representing the counterparties, such as the Association of British Insurers (representing investors) or the Confederation of British Industry (representing companies).

SAS72

Poll participants cite US forms as a model to strive for.

For capital markets transactions with a US offering, the SAS72 comfort letter effectively provides a market standard.

"Most banks would want a US disclosure letter which does tend to be very standardised across the board, thanks primarily to the fact it's driven by clear US regulations," says one counsel at an international investment bank.

But Fleck warns against any initiative to standardise entire letters. "That would imply a lack of differentiation in the market and an increasing move towards to the commoditisation of the assurance market," he says.

Certainly, standardisation cannot be viewed as a panacea.

Even where standard forms are widely accepted, such as in the UK, banks and auditing firms are still spending a significant amount of time debating the terms of engagement and scope of work of reporting accountants on corporate finance transactions.

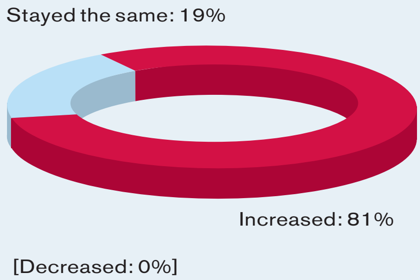
"Clients always ask why we cannot just start from the end point agreed on previous transactions, and make the necessary changes from there," complains the ECM execution director at a US investment bank. "I understand their frustration. Starting from a standard form each time and subsequently entering into a protracted discussion on previously-agreed provisions is an unproductive use of everybody's time."

"It's something auditors need to be more pragmatic about," he adds.

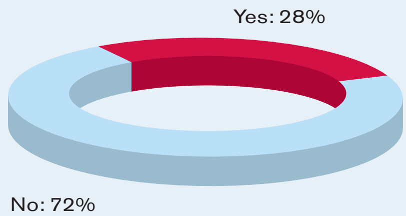
Another respondent says issues often emerge on foreign company listings in the UK, when there is no link-up between the accountant's London and local offices. "In such scenarios, there is sometimes tension

New responsibilities

Have your responsibilities increased, decreased or stayed the same over the past five years?



Have changes to the way your institution manages regulatory capital affected your role?



> **It is very difficult for a firm not on our pre-approved list to get work from us**

Sponsor supervision concerns

A sweeping majority of 97% of respondents tell IFLR they now spend more time dealing with sponsor supervision concerns via internal processes, regulatory liaison and work on transactions, compared to five years ago.

Counsel say this was particularly notable on deals with a UK nexus, given recent efforts by regulators in the country to ramp up their focus on sponsors.

In 2012, the UK's then Financial Services Authority (FSA) put forward a number of changes to the country's sponsor regime. These included extending the circumstances when a sponsor would be required to include smaller related party transactions, and strengthening the rules for sponsor communications with the regulator.

The move was perceived as a reaction to the controversial May 2011 enforcement action against the accounting firm BDO, for its failure to act with due care and skill as sponsor. In that case, BDO even agreed in its letter of engagement not to engage with the FSA. At the time, the UK Listing Authority's (UKLA's) department head, Marc Teasdale said: "BDO failed in its responsibilities as a sponsor...and we are sending a clear message...about the importance we attach to the sponsor role."

Today, most banks agree that where they are acting as sponsor under the UKLA Listing Rules, they now face an increased burden of compliance, for example in terms of preparing for visits from London's new market regulator the Financial Conduct Authority (FCA), and follow-up enquiries. "The UKLA is now far more proactive at monitoring the performance of sponsors and the requirements of the UKLA sponsors are more onerous," says one ECM counsel.

"I now spend about 60% more time focused on our governance of sponsor transactions as an institution, through increased training, manual, and committees among other requirements," another counsel adds.

Hirschovits tells IFLR the sponsor regime changes brought in through CP12/25 moved the goal posts for banks. "All financial institutions active in this market have taken the rule changes seriously," he says.

"Banks' corporate finance legal teams have spent lots of time assessing internal policy, record-keeping obligations, and rewriting general procedures, as a result," he adds. "And the FCA keeps clarifying the standard of care expected in this regard."

Internal approval committees

While respondents were reluctant to reveal exact details on the structuring and timing of their internal approval committees, the majority concede that these committees are now taken more seriously, thanks in part to changes to the UK's sponsor regime as well as the fact that financial institutions are now operating in an environment in which regulators are more likely to clamp down hard on any indiscretions.

"Our committees have become much more formalised in nature, and the processes have become more embedded within the organisation," says the counsel at one bulge bracket in the City.

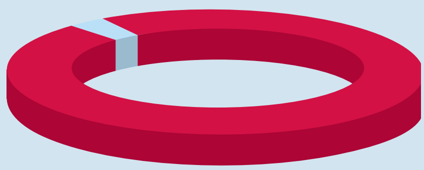
"We've created some additional committees too: issues pertaining to the sponsor role and franchise are now dealt with in separate meetings, for example," he adds. "Previously these were factors that would have been dealt with as part of a broader underwriting committee."

Others speak of a ramped-up focus on the substance of such meetings as opposed to box-ticking processes, as well as more direction on when and how to have internal committee meetings and calls.

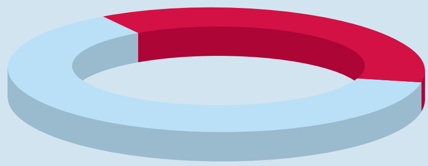
"Of course, it varies according to the deal specifics and our role on the deal, but by way of example, we'd likely meet before taking on a mandate; again to vet any reputational, legal, or regulatory risk issues before a mandate, if any are identified; before the bank is named publicly in connection with the deal; before taking on the sponsor role; as well as before launch, pricing and final UKLA submissions," says on ECM in-house counsel.

"There's more focus than ever before on getting internal approvals right. Risk and compliance are now far more involved," another poll participant reveals. "Committees in relation to sponsor or authorised nominated advisor roles are more robust, and there's more focus on price, fees and position in the syndication within ECM committees."

Do you spend more time dealing with sponsor supervision concerns now as compared to five years ago?



What general changes have you noticed in the structure of internal approval committees in the past five years?



The quality of legal advice seems to vary more greatly than it did five years ago

as to which office should take the lead and that does little to streamline the process."

According to Davis Polk & Wardwell's Will Pearce, concerns around regulatory requirements and risk management also have a part to play in lengthening negotiations.

Of course, banks do not have the same regulatory obligations when advising on transactions involving standard listings or standard listed companies, as they have as sponsor to a premium listed company or premium listing. For standard listings, banks therefore focus on potential reputational risk and common law liability for any disclosure document. Even so, they often expect similar comfort to be provided by accountants as for premium.

"Accountants are often happy to prepare comfort letters and reports for standard listings with the same scope and to the same standard as for premium listings," explains Pearce. "But issuers may often be unwilling to pay for the extra work given it is not required to support regulatory obligations."

On a standard listing, banks therefore often end up compromising and agreeing an approach that lies somewhere between the bare minimum that could be done for a standard listing and the more extensive approach adopted on a premium listing.

Adhoc meetings, convened outside of the usual time slots or to address specific transactional concerns, have also become more common

While for the more volume business on the debt side, email-voting systems have been implemented within a number of banks participating in this poll.

"For basic approvals in DCM, we have a streamlined email voting system which is used as and when decisions are required to be made in a few hours," says one DCM counsel at a regional investment bank.

"An email will go to various senior people in a number of functions, including legal, credit, operations, and risk management," he explains. "Every recipient has to vote as to whether or not they approve the transaction. There is also the option to include a caveat or raise concerns about a deal at this stage, if the recipient would like to do so."

A lot of in-house counsels' time is thereby now being taken up with filling in forms in preparation for, and follow-up to, these committee meetings. But in the current regulatory environment, it is difficult to argue that time is not time well spent.

"The busier we are, the more scrutiny there is on internal process, and the more important it becomes to make sure we are applying the appropriate quality controls and maintaining the standards expected of us," says an ECM director at one bulge bracket.

"Banks now have to be pretty careful not to attract enforcement actions from the regulator," says Pearce. The time and staffing investment that requires could present a problem for some, going forward.

In October, the FCA issued further guidance on adequacy of resourcing by sponsors in its FCA Primary Market Bulletin No 7. "If deal volumes pick up significantly in 2014, it could prove quite challenging for the leaner, more junior in-house legal and banking teams to satisfy FCA requirements on adequacy of resource," explains Pearce.

"In-house teams need to ensure deal teams are not spread too thinly on transactions," Hirschovits adds. "Doing so would negate their ability to comply with the FCA's clear expectations."

It's perhaps unsurprising, therefore, that some respondents raise concerns that the increasingly arduous UK regime might prompt some existing sponsors to decide it was not worth their while to continue to offer this service. "I wouldn't be surprised to see some law firms taking on the role of UKLA sponsor under the listing rules in the future," says one counsel.

However Pearce believes that if the larger investment banks were to walk away from the sponsor regime, it would be more likely for smaller boutiques and accountancy firms to step into the breach.

"For a sponsor to adequately fulfill its role, it needs to know the [Listing] Rules inside out, be in a position to really challenge a company's disclosure and know how to do an in-depth analysis of a company's working capital position," he says. "I'm not sure law firms are well-equipped to examine working capital."

"If the larger banks were to get to the point where they no longer wished to take on the increasingly process-heavy role of sponsor, the Big Four auditing firms would be best-placed to take their place," he says. "They already have the record-keeping and reporting capabilities that the role now requires."

Another market participant tells IFLR there is no imminent danger that banks would abandon the sponsor role entirely. But he believes enough have been put-off by the recent changes to the sponsor regime, that it is not an eventuality that can be ruled out in the long-term.

"It is felt too much responsibility has been offloaded onto the shoulders of sponsors," he adds.

Liability caps

Reporting accountants' increasing imposition of liability caps on their UK capital markets work is a further pressure point in the process.

In 1996, the London Investment Banking Association (LIBA) agreed a moratorium with the then Big Six auditing firms that stipulated London-based auditors would not seek to impose liability caps on any public reports required to be included in disclosure documents, or for work done in support of statements made in such documents.

For work on premium listings, this gentlemen's agreement still holds firm. For work on standard listings, however, there has been a movement away from the moratorium wherever possible.

"It started around two years ago," says one counsel at a European investment bank. "Initially, we were successfully able to resist it, but now it's resulting in an argument more and more often."

Another poll participant noted that accountants were also increasingly unwilling to extend LIBA moratorium practices to new areas that technically fell outside the original agreement – for example, funds.

Of course, the profession's desire to limit liability has been around for decades.

> We look quite closely at associates' skillsets when selecting a firm

Indeed, it is accepted market practice elsewhere in the region. "The starting point for the non-UK engagement letters of some of the larger auditing firms is to include a cap on their liability for their reports," explains Davis Polk & Wardwell's Dan Hirschovits.

Fleck thereby believes it is reasonable for accountants to now seek to limit their liability on UK capital markets transactions. "It would be better for the liability of accounting firms to be agreed by contract at a level that is realistic, but high enough to be a real stimulus of quality," he says.

"Liability caps are permitted by law, but they only become effective if all parties agree to the cap," he adds. "So it's an area where in-house counsel can have a direct effect."

But respondents argue that accountants' increased risk liability management has led to longer and more complex engagement letters and comfort packages.

To most institutions, it is critical that they have the ability to use the comfort package obtained from the accountants as protection against third party accusations of insufficient levels of diligence or inaccurate public reporting.

In light of that, in circumstances where the liability cap debate cannot be resolved to the satisfaction of an underwriting bank, some banks have resorted to seek access to the relevant report on a non-reliance basis.

"This enables the bank to sidestep the debate about liability caps, but provides it with a degree of comfort that the necessary work has been undertaken," explains Hirschovits. "This approach is intended to enable the bank to use the fact of the relevant report as a shield against any third party claim if not as a sword to bring a claim against the accountants."

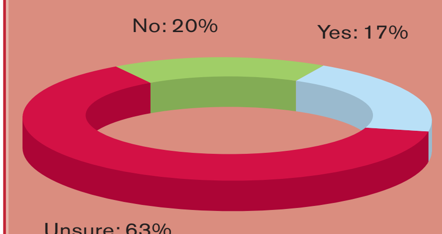
"In certain circumstances, a number of banks would rather have the option to see proof the work has been done, than sign up

London's attractiveness as a listing venue

In November, the UK's FCA released rules designed to enhance the effectiveness of London's listing regime and reinforce protections for minority shareholders.

Known as CP13/15, the FCA's response to its October 2012 consultation paper contained draft 'near final rules' for premium listed companies with controlling (30% or more) shareholders.

Will the changes proposed to the UK Listing Rules help enhance London's attractiveness as a listing venue?



The tightening of the rules has been seen as a move to rehabilitate London's reputation as a financial hub and stem the flow of business to rival centres. It follows high-profile scandals involving two poorly governed emerging market mining groups, Eurasian Natural Resources Corp and Bumi, which were nevertheless presented as premium stocks on the London Stock Exchange.

ECM counsels' reactions to the rules were muted, however. Many are hopeful the changes will have an impact on London's attractiveness as a listing venue, but believe it is probably too early to tell either way.

"CP13/15 removed some of the more controversial elements of previous proposals which is a good thing. But some of the issues are still a bit muddled and need to be clarified," says one ECM counsel. "Until then, it is hard to say whether or not these rules will markedly change issuer perception of the City."

After all, listing in London remains the 'holy grail' for companies thanks to the fact that listing enables the possibility of FTSE index inclusion. "People remain prepared to pay for that," says Pearce.

The proposed changes will draw an even clearer distinction between the UK and US rules on controlling shareholders, he adds. "In the US, the market accepts you can control a company as a shareholder and have more voting rights, as long as that is disclosed. In the UK, the market is increasingly moving away from that," says Pearce.

DCM counsel were more vocal on the impact of the new rules, however. "We are already seeing public debt issuers move to Luxembourg and Dublin, in particular, as a result of the perceived overly prescriptive approach of the UK regime," says the counsel at one regional bank.

But as Hirschovits explains, the choice of listing venue on the DCM side is driven more by cost considerations and ease of listing process, with the rationale for obtaining a listing often being driven by tax reasons as opposed to anything else.

to a formal comfort letter with associated liability caps," he adds.

It is an approach that is gaining traction, not just in investment banks' interaction with accountancy firms, but also in their interactions with specialist service providers or competent persons – such as property valuers or mineral experts – where third party public reporting is required.

But while poll respondents focus on auditors' failings, Pearce tells IFLR that lawyers are not completely innocent in all this. "Reporting accountants have various regulatory obligations and have to follow industry-wide guidance when performing their work: they can't always agree to perform their work in a particular way," he says.

"Marking up the accountants' engagement letter is an aspect of an ECM transaction that is quite often handed to junior lawyers within big law firms," he continues. "Inexperienced lawyers, particularly those that have never read the SIRs [the guidance for reporting accountants], often make unnecessary changes to standard terms."

"It is important to take the time to train up junior lawyers within City firms to better handle and understand the issues," he adds.

Choosing external counsel

Certainly, questions regarding outside counsel's involvement in regional capital market transactions prompted a mixed response.

Just over half of the banks surveyed say law firms' transactional responsibilities have increased in conjunction with an expanding regulatory framework and the downsizing of many institutions' legal teams post-crisis.

"Outside counsel now take a more substantive role on transaction execution, and particularly in relation to the transaction sponsor," says the counsel at one investment bank in the City. "I now rely on them much more than I did previously."

This greater reliance has brought with it a greater scrutiny of the service external counsel provide. "Law firms now have to be even more plugged in to banks' regulatory risk issues and advise as much on them as do the heavy lifting on legal and auditor due diligence, disclosure and legal agreements," explains an ECM counsel at one bulge bracket.

Another respondent tells IFLR that regulatory and litigation expertise has become a key differential. "When I look for outside counsel, I am considering the strengths of the firm in these areas along with their capital markets teams," he says.

While a number agree that magic circle firms have effectively adjusted their established methodology and practices in response to banks' increased demands, concerns were raised as to the increasing variation in service quality. "The quality of legal advice seems to vary more greatly than it did five years ago," says the counsel at one international investment bank.

"The levels of competence, reliability, responsiveness and experience can vary widely between individuals and teams at the same firm, as well as between different law firms," another counsel agrees.

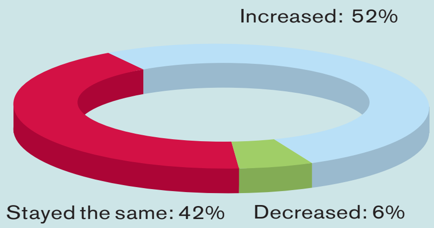
This is thanks in part to the continued downward pressure on legal fees, borne out of the post-crisis slump in regional deal activity.

"Certain law firms under pressure to bring in more work are now prepared to take on deals at heavily discounted fees that do not reflect the amount of work required," explains Pearce. "The risk with low fees can often be its impact on service levels, as partners step back and try to avoid large internal write-offs."

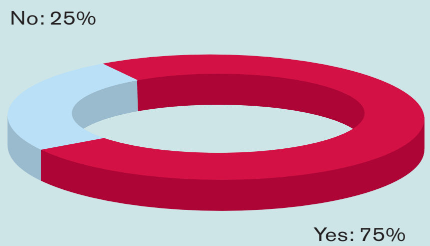
This can be further exasperated on some private equity-backed initial public offering (IPO) exits where, says Pearce, in-house

"More time is now being wasted than ever before on pre-agreeing underwriting agreements before they are pitched

Has the role played by your outside counsel in connection with capital markets transactions increased, decreased or stayed the same in the current market and regulatory environment?



Have law firms adequately adjusted to the evolving needs of financial institutions?



> **There's more focus than ever before on getting internal approvals right**

counsel may often find that the choice of external counsel is made for them.

Indeed, according to Hirschovits, the downward pressure on fees for underwriters' counsel is particularly noticeable on financial sponsor led IPOs, where financially-astute private equity firms see legal fees as a cost straight to their exit proceeds.

Associates are thereby increasingly left to manage workstreams. This can cause significant issues in the ECM space in particular, where the recent drop-off in trades has created something of a vacuum in transactional experience at certain levels of the legal profession.

"Certain counsel do not realise that times have moved on from 2007 in the ECM space as far as banks are concerned," says one ECM legal director. "They grandstand on points for the sake of them with little understanding as to the implications of doing so, and no thought given as to why a bank may have evolved its practice as a result of regulatory and other change."

"The crisis caused many firms to cut their ECM capacity," he adds. "As these smaller teams now get busier, it is critical that partners ensure their associates are well-equipped, know the right points to raise and do not just pick up the last precedent and mark it up."

While banks may be happy to pay lower fees for less risky, simpler transactions, they do want proper coverage and partner involvement on more complex deals.

This has prompted many to reduce the number of law firms they use regularly. "The more banks rely on external counsel on transactions, the more the law firms involved need to be a trusted circle of advisors," says Hirschovits. "It is much more about the individual relationships than just the law firm brand."

As one respondent explains, two developments have adversely affected law firms in the past couple of years. Firstly, larger underwriting syndicates have required external counsel to build stronger relationships with a greater number of banks. Secondly, financial institutions have started creating set lists of firms that are 'pre-approved'.

Those firms that have failed to focus on the bigger picture have had issues building relationships. "It is very difficult for a firm not on our pre-approved list to get work from us," one ECM counsel says.

Firms making the list need to have demonstrable US and European capital markets expertise at partner level, as well as a good bench of quality associates ready to step into the breach when partners are too busy, another respondent reveals. "In light of that, we look quite closely at associates' skillsets when selecting a firm," he adds.

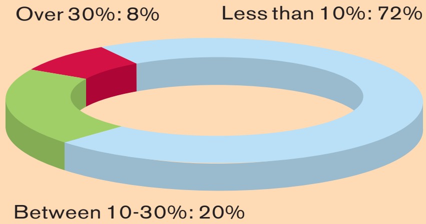
Streamlining ECM trades

As banks tend to use the same pool of law firms as underwriters' counsel, it follows that they should get comfortable with the model documentation used by those firms as a starting point. The law firms should be able to determine the typical pressure points within that documentation too, and to ascertain how certain banks may wish to negotiate on certain provisions.

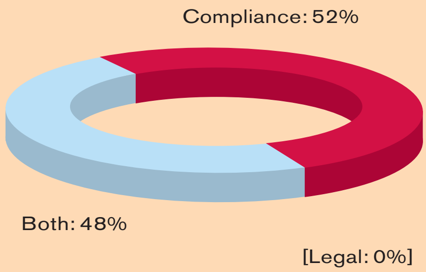
And yet, a significant majority of respondents complain of inefficiencies of process with regards to ECM forms.

Wall-crossing and pre-marketing concerns

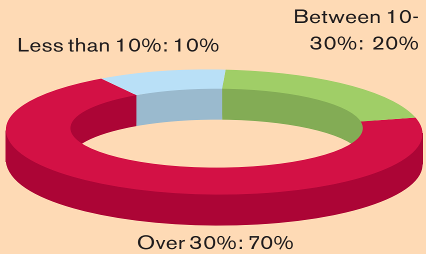
How much of your time is spent on wall-crossing concerns?



At your institution is wall-crossing primarily within the jurisdiction of the legal department or compliance department?



How much of your time is taken up by pre-marketing concerns?



The lengthening of underwriting agreements was a particular concern, with one counsel noting forms were growing longer each year. Of course, this is thanks in part to the introduction of increasingly complex rules and regulations governing transactions. But for simpler listings, there is little reason why the documentation can't be shorter.

"Underwriting agreements should be short and sweet," explains one ECM counsel at an international investment bank. "But they are getting longer because people keeping adding in excessive boilerplate provisions, such as reps and warranties that don't matter."

Almost all banks surveyed believe independent financial advisors' increasing involvement in the negotiation of

General solicitation

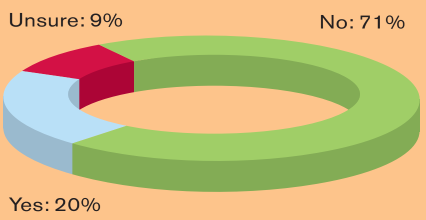
The US Jumpstart Our Business Startups Act (Jobs Act) introduced increased flexibility for issuers doing a Rule 144A transaction out of London to advertise into the US on a less restrictive basis. But the majority of banks surveyed reveal they have yet to take advantage of the reduced restrictions on marketing.

"Ultimately issuers are still only able to sell to institutional investors in the US," explains Hirschovits. "There is no incremental upside to marketing to people, they would not otherwise be selling to."

There is also still an ongoing debate as to whether the Securities and Exchange Commission's rule change applies on a broader basis than pure Rule 144A transactions. "It is still a little early to tell how these changes will impact drafting for law firms and banks," says Hirschovits.

And there are still conversations to be had with the regulator on this, says Pearce. "Hopefully, as people start to work with the rule, the interpretation of them becomes clearer, the rule change will be a more positive step forward," he adds.

Has the elimination of the restriction on general solicitation in the US changed your institution's approach to publicity in connection with unregistered offerings of securities in any material respect?



agreements was to blame. "These advisors have really carved out a niche for themselves as independent advisers to the issuer," says one poll participant. "They advise on the auction and selection process and generally make the role and job of the joint global coordinators and bookrunners significantly harder."

"Financial advisors are becoming irrational and difficult," another counsel adds. "They think up all sorts of creative stuff to clog up the process."

By way of example, many respondents cite one emerging – and especially polarising – trend; advisors' growing tendency to serve up pre-deal term sheets for underwriting agreements and request these be negotiated or agreed upon at the outset of an IPO.

"Even before being selected, banks are increasingly being forced into 'take it or leave it' positions on engagement terms and underwriting agreement terms, which is obviously sub-optimal," says one frustrated ECM counsel.

"I suspect they believe it is in the best interests of their clients to crack some of the more difficult nuts upfront," says the ECM execution director at an investment bank in the City. "But in reality, it's just inappropriate to enforce a set of terms on both the syndicate and lead underwriters at the start of transactions, before we've even got legal counsel involved."

From the perspective of those pushing this trend, a pre-deal underwriting agreement term sheet puts the investment banks under pressure to agree to provisions that they might otherwise not ordinarily be prepared to agree to, such as more restrictive liability caps, proposals on syndicate fees, a narrower scope of warranties and indemnity, and so on. "The independent financial advisers see it as leveling the playing field somewhat," explains Hirschovits.

But counsel complain negotiation can often feel like a duplicative process as a result, with a number of provisions agreed on in a short-form term sheet likely to be revisited as the more detailed drafting process evolves and the parties' different interpretations of terms are fleshed out.

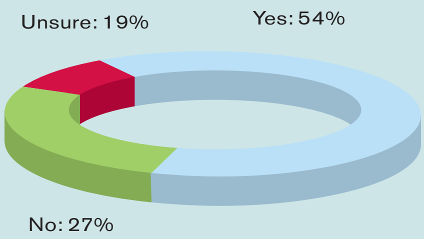
> **Financial advisors are becoming irrational and difficult**

"More time is now being wasted than ever before on pre-agreeing underwriting agreements before they are pitched," adds one ECM counsel at an international investment bank. "It's not only a colossal waste of legal fees to spend time negotiating stuff at one side that may not come to pass, but it is also not right for financial advisers to be putting pressure on banks via their legal teams," he adds.

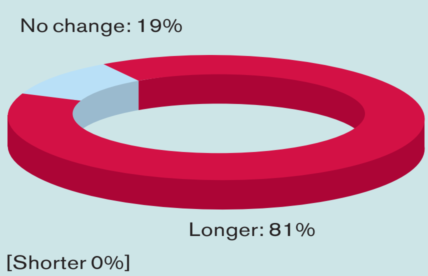
Respondents call for a middle ground to be found. "Of course, I don't object to big picture discussions, but this trend is ludicrously counterproductive and getting worse," says one.

But Hirschovits warns there is no easy solution to resist having to negotiate or accept a pre-deal underwriting agreement term sheet when one is presented. "One option is to agree to the drafting of a full-form underwriting agreement sooner in the transaction process than may be typical, but that ultimately comes down to the willingness of the parties involved to agree to such an approach," he says.

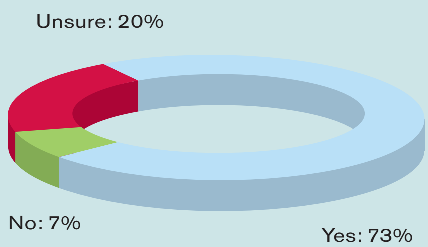
Are you using the Afme standard form block trade agreement and agreement among underwriters as a starting point for documenting such arrangements?



Are underwriting agreements longer or shorter than they were five years ago?



Are financial advisors becoming more demanding in the negotiation of underwriting agreements?



Even so, several banks believe the US example might present a solution. "The only certainty is that ECM has got more bespoke, and complex in nature from product-to-product and country-to-country in terms of the documentation, marketing, legal, listing and regulatory requirements than previously when a US model for execution prevailed throughout EMEA," says one respondent.

"In the US, the underwriting agreement is not a document that is negotiated on at length. It is a standardised form that market participants have come to know well," adds another ECM counsel. "I struggle to understand why it is something that needs to be negotiated *ad nauseum* in EMEA."

I now spend about 60% more time focused on our governance of sponsor transactions as an institution

But, says Pearce, while the introduction of a standardised plain English, short-form underwriting agreement would be nice, it would be near impossible to attain the required agreement on provisions to implement such an initiative.

Standardisation is not necessarily the right approach to every transaction, Hirschovits explains. "Arguably, one runs the risk of over-engineering an industry-wide standard form, if you have too many lawyers from across the City contributing to it," he says.

However, almost all banks surveyed agree standardisation makes sense for short-form placing agreements – such as those used on legally intensive block trades, where there may be little time available to negotiate transaction documentation.

To that end, the Association for Financial Markets in Europe (Afme) launched the region's first model placing agreements for block transactions in October, following 18 months of consultation with over 20 international law firms active in EMEA ECM, as well as legal and commercial representatives from the bulge bracket members of Afme's ECM working group.

The models aim to streamline trades across EMEA and into the US by combining the typical contractual terms used by both sell-side and buy-side on EMEA block transactions into two standardised agreements – one with a built-in backstop underwriting commitment, and one without.

Afme's ECM division managing director William Ferrari tells IFLR the forms sought solely to provide a reasonable starting point for negotiations for all parties involved on block trades in the region. They should not be viewed as fixed forms with mandatory terms.

"As the market's understanding of these models develops over time, participants can decide which aspect of the agreements they agree with, which they don't, and negotiate from there," he says. "The two agreements should therefore assist both sides in arriving at an agreement quicker and on a more cost-effective basis."

Just over 50% of the banks surveyed say the forms are now viewed as the market standard. "We use the Afme forms as the usual starting point on block trades 90% of the time," says one counsel at a regional bulge bracket. "We hope the sell-side market uses it as a basis for short-fuse blocks (with tracked changes to show their amends if any) to speed up the response time on short-fuse evening trades."

"Banks and law firms are all using them as a starting point," adds another poll participant. "We expect them to become more and more unequivocally the prevailing forms, as the New York standard AAU [Agreement Among Underwriters] and the International Capital Market Association (ICMA) standard DCM forms."

Almost a third of respondents still favoured their own standard forms, however. "Where we can propose a starting point, we always use our own forms," says the counsel at one international investment bank. "Only where the decision is issuer-led or a consortium of banks are involved, will we use the Afme standard as a starting point."

"There tend to be two main camps; the banks that are using the Afme form more often and the block trades managed by financial advisory firms which use more bespoke documentation," explains another counsel. "I will sometimes ask a firm to start with the Afme AAU, but I tend to defer to other syndicate banks if they have their own form."

The Association of British Insurers and Confederation of British Industry did not respond to IFLR's request for comment.

Methodology

IFLR's Bankers' Counsel Poll was compiled with the help of the poll's sponsor firm – Davis Polk & Wardwell.

With input and insight from the firm's corporate partner Will Pearce and corporate associate Dan Hirschovits, poll questions were refined and targeted to best address the issues in European capital markets in 2013.

Using recommendations of in-house counsel from the editorial team and Davis Polk & Wardwell, the poll was distributed to counsel at over 20 of the largest investment banks and financial advisory firms in Europe. In the end, 75% responded with an agreement to participate.

To ease the concerns of the participants, anonymity was guaranteed to all respondents. To that end IFLR will not even name the banks that replied with questionnaires and agreed to interviews.

Ultimately, some respondents only wanted to discuss issues in an interview, while other sent multiple responses from their banks.

Having collated a number of questionnaires and written responses to the survey, interviews were conducted with contacts at a selection of banks. While the more structured responses in the questionnaires provided interesting statistics, a real sense of the concerns of in-house counsel emerged from the supplementary interviews. The topics raised in those interviews formed the basis of the conclusions drawn out of the main body of IFLR's analysis.

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IFLR Q&A: UKLA's Marc Teasdale

Market participants say changes to the UK sponsor regime could prompt some existing sponsors to decide it is not worth continuing to offer this service. Do you agree this is a development likely to arise? Broadly, what benefits would you hope to arise from changes to the sponsor regime?

The sponsor regime is a key distinguishing feature of the UK's premium listing segment, and is in many ways fundamental to its proper operation. As it sits within our domestic Listing Rules, a key focus of ours is to ensure the regime remains fit for purpose and responsive both to market developments, and our own observations of market practice.

The most recent changes to the sponsor regime – in 2012 – were a response to developments we'd seen in certain transactions and during on-site reviews. A key characteristic of these changes was to make explicit some basic assumptions which are central to ensuring the regime operates properly.

"Retail investors should be able to understand the documentation relating to a product they are being offered

For example, due diligence has always been an important aspect of the sponsor regime, and to that end there's been a requirement that sponsors keep proper records. With the 2012 changes, we made this requirement much more explicit. We also made explicit the requirement for a sponsor to act with integrity, and clarified that where a sponsor uses expert third parties (such as lawyers or accountants), the sponsor responsibility nonetheless stays with the sponsor firm and does not pass to the third party. In each of these cases it's difficult to see how the sponsor regime could operate effectively if the opposite were the case.

Some of the changes were positively welcomed by the sponsor community, as they helped them to discharge a role which we recognise at times can be very difficult. For instance, we clearly articulated the concept of 'regulatory conflict', recognising that there can be circumstances where an issuer simply doesn't want to follow the advice a sponsor is providing. Our rules clarified that in circumstances where this conflict can't be managed, a sponsor must resign. By making this point clear, and by subjecting issuers to a complementary requirement to cooperate with sponsors to enable them to discharge their responsibilities to us, the consistent feedback we have received is that sponsors are finding their ability to manage these difficult (if relatively infrequent) situations significantly enhanced.

So on the one hand, we are seeking to change market practice in certain areas where behaviour has been perceived to have fallen below acceptable standards. On the other hand, we are seeking to implement requirements that are fundamental to a well-functioning regime. If sponsors don't keep records properly, for example, then the regime cannot operate as it should. Our focus is to clarify where useful, and change where necessary. These are not reforms that should polarise.

Are we in danger of pushing people away from wanting to do the role, through the changes we've introduced? I'd argue, the answer is no.

To a lot of market participants, such amendments weren't controversial. Rather, they were seen as a more explicit articulation of what they had already assumed to be the case. For others the rule changes might have required a relatively significant change of practice, but I would argue for these firms the change was necessary to ensure the regime operated effectively, as in some cases we had observed that market practice had been slipping.

That said, we have had some sponsor firms raise the point that we need to be careful that the risk/reward of the sponsor role remains appropriately balanced. We're still seeing a good through-put of potential new applicants to the sponsor list, and recent removals from the list have been motivated by general inactivity rather than a more fundamental desire to step away from the role. What is clear though is that our reforms have caused sponsors to consider more explicitly the value to the issuer of the sponsor role. As a result, I'd expect more specific negotiation from sponsors around fees in light of the clear responsibilities it involves, and I think it increasingly unlikely that the role will be carried out as 'loss-leader'. On recent deals, we have already started to see some developments in this direction.

Fundamentally, I don't think the changes we introduced were unreasonable or too high a level of regulation. I would expect the vast majority of sponsor firms would agree with that basic premise. If members of the community do not, however, and if certain sponsors believe that this basic level of expectation is set too high, then maybe the role isn't for them.

DCM lawyers have said that the UKLAs proscriptive approach is encouraging debt issuers (such as, public debt issues off an MTN programme) to other exchanges (predominantly Dublin, Luxembourg). Are any initiatives under way to encourage such issuers back to the UK? To what extent do you see preferences for other EU exchanges on the DCM side to be a concern?

The EU Prospectus Directive requires all prospectuses to be 'easily analysable and comprehensible', having regard to the nature of the investor that is being targeted. That is to say, if an instrument is targeted at retail investors for example, the documentation should be capable of being easily understood by that investor base.

This agenda has generated a lot of reaction in the market recently. But most of our efforts here are focused on the nascent retail markets rather than established wholesale markets.

We understand that some market participants may have expected these new markets could be grown using practices prevalent in existing wholesale markets. But we think – and we are backed up by EU law here – that retail investors should be able to read and understand the documentation relating to a product they are being offered.

Clearly, we recognise there is a European aspect to this debate and we are in dialogue with European regulatory colleagues on this.

Our overall aim is to ensure that the small but growing retail market for corporate debt securities develops in a way which is sustainable, and therefore more likely to be successful on a long-term basis. And to that end, we are working to more broadly educate debt market participants as to what is required and why. More specifically, we are consulting market participants (both formally and informally) on this requirement to make sure they understand what is required, and the underlying policy and legal considerations.

I believe what we're asking is neither unreasonable, difficult to achieve, nor inconsistent with EU law.

Do you have any comment around the removal of 'international competitiveness' from the UKLA's objectives? In particular what does this mean in practice for the UKLA? Is it something that worries you?

Prior to the changes to FSMA [Financial Services and Markets Act] that created the Financial Conduct Authority (FCA), we had to 'have regard' to the international competitiveness of the UK's listed market. That is to say, the international competiveness of the UK's listed market was not an objective under the previous statutory regime, but it was one of the things we had to consider when exercising our regulatory functions. In simple terms, we were required to consider the impact of our decision-making on the attractiveness of the UK market in a broader international context.

Under the new regime, this 'have regard' has been removed, although in practical terms it is hard to think of many situations where this is likely to make a significant difference. We are still required under the new regime to act in a proportionate manner, and that regime also requires us to have regard to the desirability of sustainable growth in the UK economy in the medium or long term.

More importantly, I would say that if we are doing our job properly, then we should be creating a market that is attractive to a broad range of participants anyway. I don't accept the view that there is a necessary conflict between maintaining high standards of investor protection on the one hand, and keeping a market competitive on the other. Certainly our experience of the appeal of the premium listing regime (which contains a series of investor protections that are additional to those required by European law) seems to bear that out.

What are your views on eligibility versus suitability? Could more be done to assess the suitability of a company for listing in the future?

The Listing Rules contain a series of stringent, but objective, conditions for listing. Although there is a degree of judgement in determining whether the more substantive eligibility conditions have been met, once they have, the issuer is eligible for listing.

This contrasts with a suitability approach, which would be far more subjective. We don't, for instance, when listing a company, form a view on the quality or viability of its business model, or whether the company is offering a good investment proposition.

One of the things that the market really values is transparency, consistency and predictability. We may still disagree with an issuer as to whether or not it complies with a certain condition, but the rules of the game remain clear and that's important. Issuers know what to expect when applying for a listing in the UK.

More fundamentally, the UK's system of primary market regulation is based primarily on principles around the importance of disclosure. Our regulatory regime seeks to ensure that investors are given sufficient information to enable them to make investment decisions on a properly informed basis. It does not seek to make those decisions for them. There would need to be a really strong case to change the system in such a fundamental way, and I'm not sure that case is there.

Would the UKLA consider focusing more on individuals within organisations, interviews going forward and direct supervision of listed issuers?

This in a sense is an extension of the previous question, and similar considerations apply. The FCA acting in its capacity as a listing authority does not supervise listed issuers, and does not satisfy itself that the directors or owners of listed companies are fit and proper.

If concerns about companies, their owners or their directors are relevant to the investment decision that investors are being asked to take, our regime requires those concerns to be clearly disclosed. Except in extreme cases though, consideration of these matters does not form part of the listing process itself.

To move to a different system would be a significant change to the nature of the UK's securities market, and would ultimately be a matter for government. I would note in this context though that when HM Treasury consulted recently on whether we should be given powers to enable us to commission 'skilled persons' reviews of listings-related matters in issuers, the proposal was not proceeded with as it was seen to take us too far in a 'supervisory' direction perceived to be at odds with our role as a securities regulator.

There's a school of thought that in drafting the new Listing Rules, the UKLA might have missed an opportunity to re-educate the institutional investor community. Do you have comment on this viewpoint?

I don't like the idea of the UKLA re-educating institutional investors, because it suggests a view that we already know all the answers and should be in 'telling mode'. I think we should always be keen to listen to the views of market participants, and be ready to consider that we might ourselves have useful things to learn!

Our most recent consultation document on the premium listing regime was the result of 18 months of discussions with market participants, and our engagement with institutional investors and pension funds was a crucial part of that process.

During the course of those discussions, I felt the terms and focus of the debate shifted relatively significantly. Initially conversations centred on questions around free float, indexation and the relative merits of domestic and foreign companies. We felt, however, that the crux of the issue was really one around voting power, and about how to ensure the minority voice has an appropriate place in the governance of a listed company, particularly where a controlling shareholder is present. We didn't think changing the free float requirements was a proportionate or appropriate response to the issues we were discussing. We also felt that discussions about indexation criteria were a matter for FTSE rather than ourselves.

The rules that we are currently consulting on seek to ensure that all shareholders (whether controlling or minority shareholders) are able to play an appropriately active and engaged role in the governance of the companies they own. I hope the discussions that we had with market participants, including institutional investors, have been successful in garnering a broad degree of support for these proposals.

More broadly, what opportunities/challenges do you expect within UK ECM in 2014?

We are already seeing increased initial public offering (IPO) volumes and that looks set to continue in 2014. That presents both an opportunity and a challenge for the market.

For us as a regulator, the challenges ahead remain in a sense the same – ensuring we remain responsive to market feedback, but also true to our basic regulatory principles and objectives. Often those who shout the loudest do not reflect the market view as a whole – this requires us to ensure we strike the right balance between responding to feedback from specific market participants on the one hand, and operating a regime that appropriately balances competing interests and objectives on the other.