

WINSTON
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the
in year
preview
2009

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Winston & Strawn is pleased to present our second annual *Year in Preview*, which focuses on some of the most critical and rapidly changing issues affecting business today—from changes in the financial markets to changes in the U.S. administration, from tax regulations to antitrust enforcement, from energy initiatives to patent reform. Our goal is to give you a better understanding of what lies ahead and provide insights into how you can use this information to strengthen your business during these challenging times.

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2009

Profound changes await us. In these pages, we try to understand what they will mean for executives...

In 2008, companies and individuals alike found themselves continually changing plans to keep up with one astounding turn of events after another. By year's end, the world was a very different place than it had been just 12 months earlier.

The year saw several currents converging to redraw the business and political landscape. There was the credit crisis, the decline of stock markets, the global economic slowdown. There were the responses to those problems, from government bailout packages to cutbacks in corporate budgets and headcounts.

At the same time, there was the U.S. presidential election—a historic event that brought the nation's first African-American president to office—and the ensuing changing of the guard in agencies across Washington. Perhaps more than most presidential transitions, this one has brought a fundamental shift to policies and legislation, a shift that is still taking shape.

These events have left us with a fast-moving, constantly changing picture, and we have all had to adjust and adapt. The new administration and Congress have had to devote the lion's share of their energies to economic issues, and companies have had to change strategies. This publication is no exception. With so many issues in play as we crossed into 2009, Winston & Strawn decided to delay its forward-looking analyses until some degree of stability returned to the political and economic scenes.

It seems clear that profound changes still await us. In the following pages, we try to understand how these will play out—and what they will mean to executives as they try to navigate through largely uncharted waters.

Undoubtedly, the economy will continue to be a focus of attention as stimulus and recovery efforts work their way through the system. Efforts to rethink regulation will not be far behind, as events of the past year have so clearly tied the financial services industry to the common good in the public mind. “The problems that began... in the subprime mortgage markets and quickly spread to the credit markets and across our economy are just the latest stark reminder that capital markets don't matter just to

Wall Street,” Thomas J. Donohue, president and CEO of the U.S. Chamber of Commerce, wrote last year. “Every citizen, family and business has a critical stake in ensuring that our nation is home to the strongest, fairest and most efficient markets in the world.”

Beyond the economy, the coming year will see a number of other developments affecting business. The Obama administration has promised to bring significant change to the health care and patent systems. The new political landscape is likely to lead to increased antitrust enforcement and changes in tax laws. Several Supreme Court decisions will have an impact on business—and the court itself may be seeing change, with the potential for one or more justices

to retire. New energy and environmental legislation will make energy efficiency a strategic issue across industries.

The problems confronting us are not small, but in facing them, it is important to maintain perspective and remember that business and government are not without ideas and resources. As *Wall Street Journal* columnist Peggy Noonan recently noted, “While terrible challenges face us...we are building from an extraordinary, brilliant and enduring base.”

In the coming year, we will need to draw on that base to search for answers—and business needs to have a voice in that effort. “Business leaders need to...propose solutions that benefit the entire country,” Bill George, a professor of management practice at Harvard Business School and former CEO of Medtronic Inc., wrote in *BusinessWeek*. “Either we get engaged, or we'll suffer unintended consequences from well-intentioned new programs that don't work in the real world.” We hope that the insights in the following pages aid in that discussion, and help executives understand and prepare for this changing world.

The problems confronting us are not small, but in facing them, we need to remember that business and government are not without ideas and resources.

With a weak economy and more spending, Congress will look for **revenue-neutral tax changes.**

“There is enormous pressure to move sooner rather than later. The administration has the wind at its back...and that means getting started over the next several months.”

The reform of U.S. corporate tax laws has been talked about for some time, but a number of observers have wondered if significant change will now be slowed by larger concerns about the economy—and a reluctance to recast the rules while businesses are struggling. Perhaps, but any such delays are likely to be short, says James Miller, a partner at Winston & Strawn.

“There is enormous pressure to move sooner rather than later,” Miller explains. With solid Democratic majorities in Congress and high levels of political goodwill in hand, “the Obama administration has the wind at its back and is likely to want to accomplish significant tax changes over the next year or two—and that means getting started over the next several months.”

One area of possible consensus is already evident: lowering the U.S. corporate tax rate, which tops out at 35 percent and when combined with state taxes, gives the United States a 39.3 percent rate. That is the second-highest corporate tax rate in the world, behind Japan’s, and more than 12 percent higher than the average rate across Organization for Economic Cooperation and Development countries—which many critics say impairs U.S. companies’ competitiveness in a global economy.

The Obama team has said that it wants to “cut corporate taxes for firms that invest and create jobs in the United States,” and many in Congress appear

to agree. Representative Charles Rangel of New York, the chairman of the House Committee on Ways and Means, has pushed for significant tax changes in the past, including a reduction of the corporate tax rate to 30.5 percent, and he has said that he is interested in reform in 2009.

At the same time, of course, there is the weak economy, a growing deficit and more spending programs being planned by the new administration—not to mention a number of tax breaks included in the recent economic stimulus package. As a result, Congress is going to be looking for changes that are revenue-neutral. The question is, how will lawmakers pay for a cut in the corporate rate?

Closing the loopholes

One likely starting point is the closing of corporate loopholes, which was a recurring theme in Obama’s 2008 campaign. For his part, Rangel said last fall that “we don’t have to reinvent the wheel. All we have to do is wipe out a lot of the fat that’s in the corporate code and redirect it to dramatically [reduce] the corporate rate.” It seems likely that tax breaks for oil and gas companies, such as special expensing rules, will be eliminated. But some other industries will probably be spared, as one person’s loophole is another’s incentive.

“Some of the biggest corporate tax breaks are the low-income housing tax credit, the renewable energy tax credits,

and the R&D credit,” says Miller. “These breaks are designed to prompt corporate investment in these areas, and they are used by corporations to reduce their effective corporate tax rate. They have wide support, and President Obama is not going to eliminate those.” In fact, the administration has said that it hopes to move the R&D credit and the renewable energy production tax credit for wind out of their current temporary status and make them permanent in order to encourage longer-term investment in these areas.

There are several other areas that are likely to be targeted relatively soon in the search for revenue. For example, Obama has made it clear that he wants to raise the capital gains tax from 15 percent to 20 percent. In a related vein, says Winston & Strawn partner Alex Zakupowsky, Congress will probably tackle carried interest, which is the share of a private investment fund’s profits used for much of a fund manager’s compensation. Carried interest is taxed at the capital gains rate of 15 percent, but Congress has made attempts in the past to tax it at the higher ordinary income tax rates. Those previous attempts were dampened by the threat of a presidential veto, but with a new administration, Congress is fairly certain to revisit the issue soon.

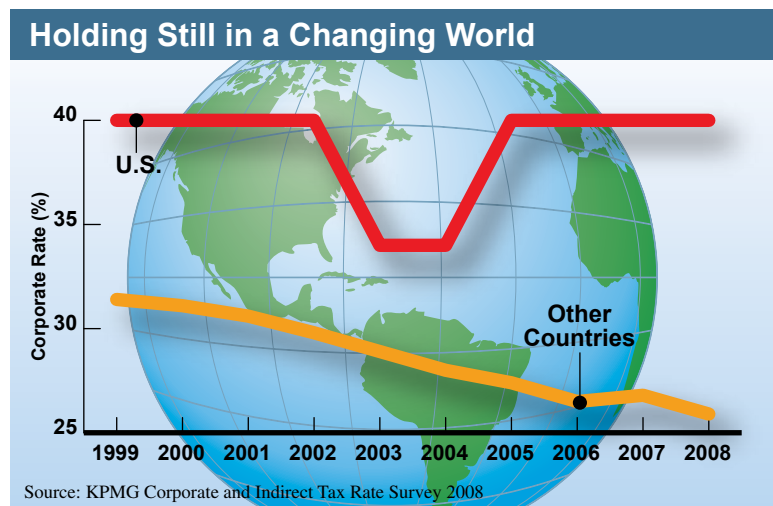
Another likely target: publicly traded financial companies that are set up as widely held partnerships. Currently, income at these firms is taxed at the individual partner level, not the corporate level. “We may see a change that treats those partnerships as C corporations, which pay corporate taxes, and then when dividends are paid to a partner, the partner is taxed like a shareholder,” says Zakupowsky. “Right now, there’s just one

level of taxation; this would introduce a two-level approach.”

To keep corporate tax changes neutral, however, the administration will have to cast a wider net—and based on Obama’s emphasis on bolstering the middle class and employment, that will mean targeting U.S. companies doing business internationally. In a long-term budget blueprint released in February, for example, the administration outlined proposed increases to U.S. multinationals’ foreign income, which would bring in an additional \$25 billion per year by 2014, according to White House projections.

Here again, the president and Congress are more or less in sync. As Senate Finance Committee Chairman Max Baucus from Montana pointed out last fall, “Simply put, I do not intend to allow U.S. multinationals to sidestep their fair share of taxes by moving income offshore. Rather, they should...start to bring their income onshore, along with as many jobs as possible for American workers.”

“Tax policy can be a powerful tool for reducing the incentive to move work overseas, and the administration is going to be attacking tax policy in a way that it thinks will create jobs in the United States.”



The U.S. cut corporate taxes significantly in the '80s, giving it a relatively low rate. Since then, despite a brief drop in 2003-04, the U.S. has held steady. But other countries have cut their taxes, leaving the U.S. with one of the highest rates in the world.

Tax havens and transfer pricing

“Tax policy can be a powerful tool for reducing the incentive to move work overseas, and the administration is going to be attacking tax policy in a way that it thinks will create jobs in the United States,” says Miller. “So, the Obama team is going to be looking at reforming the tax laws that encourage U.S. companies to engage in foreign direct investment in countries with low corporate tax rates,

such as Ireland.” Tax havens, too, are likely to be targeted. Obama once co-sponsored legislation called the Stop Tax Haven Abuse Act, and he wants to make it less attractive to park profits in areas where there are no corporate taxes, such as the Cayman Islands.

Another specific practice likely to land in the administration’s sights is transfer pricing, in which companies allocate the costs of transferred assets internally, an approach used by multinational companies to shift profits from one part of the organization to another to reduce their taxable income in countries with higher tax rates. “It seems that the president would like to essentially end the practice of transfer pricing,” says Miller. “He would do that probably by forging agreements between the U.S. Treasury Department and other countries’ treasury departments, where they would come up with a tax formula that would prohibit companies from manipulating prices within their corporate groups to avoid taxes in one place or another.”

When tax laws are being changed, there are often strongly differing views regarding what should be done, and with the Democratic majority in the Senate falling short of the 60 members needed to limit debate, that raises the possibility of filibusters slowing revisions to a crawl. But some changes may find their way in through another route, says Miller. He explains that tax changes that relate to budget matters may be handled as part of a budget reconciliation bill, as opposed to a tax bill—and the budget reconciliation process does not allow filibusters. Says Miller, “I think the reconciliation process is probably the place where we will see a lot of the Obama tax program being advanced.”

Derivatives: A Clearer Tax Picture?

Over the past decade, the use of derivative financial instruments—forward contracts, swaps, exchange-traded notes and so forth—has grown dramatically. Congress and the IRS have responded with numerous rules for taxing those derivatives, but the results of those efforts have been somewhat limited, says Ed Cohen, a partner at Winston & Strawn.

“The taxation of derivative instruments has been murky,” Cohen says. “There are a variety of rules, but the rules are not consistent across types of financial instruments, and not all rules have been implemented.” And it’s complicated. The tax on a derivative is determined by factors such as the nature of the derivative and its underlying property, the purpose of transaction and even the identity of the taxpayer. In essence, the burgeoning use of derivatives has outstripped the tax policy’s ability to keep up. For many, this murkiness has made these investments attractive from a taxation standpoint.

That’s likely to change in the coming year, however, with increased scrutiny on the taxation of derivatives coming from several directions. “There is a strong feeling that unregulated derivatives caused the financial meltdown, so people will be regulating derivatives—and one form of that will be tax regulation,” says Cohen. At the same time, he says, the IRS has announced its intention to take a close look at its enforcement of tax regulations on these instruments. In addition, Congress is showing an increased interest in addressing “tax avoidance” practices as it tries to balance revenues and spending, and some of that will focus on derivatives.

“I certainly think there will be both legislative and regulatory changes that will affect the tax consequences of derivative ownership,” says Cohen. “It’s hard to say exactly what that change will be—but things are very likely to be different for investors and institutions that use these instruments, and businesses will need to watch these changes closely.”

In the wake of **the financial meltdown**, “we will have a very different regulatory landscape.”

Last fall, in a hearing before the House Committee on Oversight and Government Reform, Representative

Henry Waxman, the committee chairman, asked Alan Greenspan, the former Federal Reserve chairman, about mistakes that had led up to the 2008 financial meltdown. Greenspan responded: “I made a mistake in presuming that the self-interest of organizations, specifically banks and others, was such as they were best capable of protecting their own shareholders.” The message was clear: Something was wrong with the U.S. financial regulatory system, and more oversight was needed.

That was, and is, a widely shared view, as people have watched the stock market decline, credit tighten up, and foreclosures and layoffs increase. “Despite the talk about Wall Street versus Main Street, people realize that it’s all interconnected,” says Christine Edwards, a partner at Winston & Strawn. “It affects the mortgage market, the housing market, the ability to buy automobiles, the ability of people to retire, so there is a strong demand for new regulation.”

In late 2008 and early 2009, Congress and regulators focused on a number of rapid responses to the downturn, from emergency changes to rules on short selling stocks to the Troubled Asset Relief Program and the economic stimulus package. As these measures worked their way through the legislative process,

and when some degree of economic stability takes hold, Congress is likely to take a deeper look at reforming the regulation of the country’s financial system, says Edwards. The depth of the economic downturn and its broad impact on the country, she says, will open up an opportunity to truly rethink regulation and to implement a framework that is both more effective and more efficient. “It won’t happen in the next few months,” she says, “but I think that, ultimately, we will have a regulatory landscape that is quite different from what we have now.”

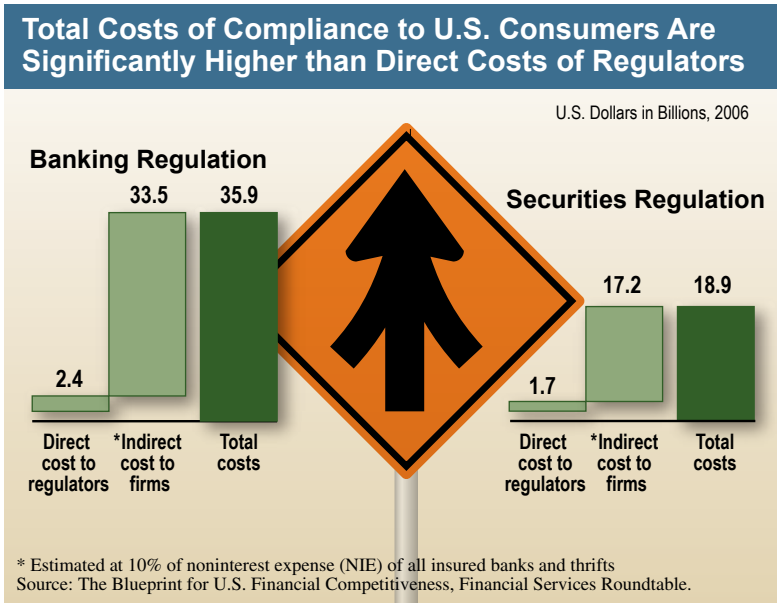
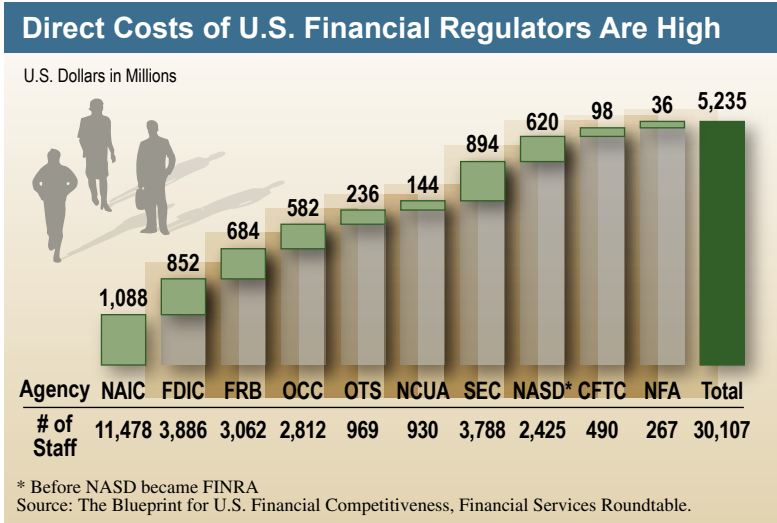
Three themes of regulatory change

The interest in regulatory change is not an entirely new development. In recent years, members of Congress, academics and organizations ranging from the U.S. Treasury Department to the U.S. Chamber of Commerce and the Financial Services Roundtable have put forth guidelines and proposals for a new financial regulatory system. The specifics of how these concepts will translate into regulatory reality will be hammered out in the coming months, but there are three broad themes that will shape reform efforts: improving regulatory coordination, expanding the regulatory umbrella and managing systemic risk.

1. Improving regulatory coordination

Today’s regulatory framework is

“Despite the talk about Wall Street versus Main Street, people realize that it’s all interconnected.... So, there is a strong demand for new regulation.”



fragmented; for example, federal bank regulators are covering banks, federal securities regulators have responsibility for broker-dealers and investment advisors, and insurance regulators across 50 states are evaluating insurance companies. “One thing this crisis has said to us is that we can no longer have balkanized regulation, which is essentially what we have right now,” says Edwards. “Financial regulators need to be able to have a full picture of risk in order to adequately examine or coordinate examinations for banking, securities and insurance activities.”

The simple fact is that today’s financial activities overlap industries in a number of ways, and the regulatory framework needs to reflect that. For example, the areas regulated by the Commodity Futures Trading Commission (CFTC) were historically separate from the securities regulated by the Securities and Exchange Commission (SEC). Now, however, instruments like credit swaps, index futures and securities futures essentially transform securities into commodities, and neither agency has full control or even a full view of such instruments.

“Every few years somebody proposes merging the two agencies, but nothing has happened,” says Edward Johnsen, a partner at Winston & Strawn. “Now, I think that’s changing. People are recognizing that futures aren’t just contracts on oil and pork bellies anymore. There are futures on financial products and the like, and these marketplaces have really converged in a way that the regulatory structure no longer properly reflects.” Johnsen adds that in the past year the heads of both the SEC and the CFTC have suggested ways of integrating their activities, and while an out-and-out merger could still pose problems, one possible scenario is to

Many proponents of regulatory reform are calling for a more integrated, streamlined approach—not just more regulation. Today, the regulation of the U.S. financial industry involves a number of agencies providing a patchwork of oversight. Observers say that this can create inefficiencies and limit the effectiveness of that oversight—and drive up costs for government. It also translates into increased costs for business and consumers.

have the two agencies become separate divisions of one overarching regulatory agency. “Of course,” says Johnsen, “with the new chairperson of the SEC, Mary Schapiro, having also been the chairperson of the CFTC, a merger of the two agencies may be more likely.”

2. Expanding the regulatory umbrella

As Congress looks at reforming financial industry regulation, it seems very likely that it will want to include areas that have traditionally seen little or no federal oversight. “There are a number of entities that are outside the regulatory structures that will be brought into it,” says Winston & Strawn partner Paul Pilecki. “Just about any firm involved in financial markets trading and investing is likely to be brought under the umbrella, and perhaps commercial finance companies that currently aren’t regulated and various types of private investment vehicles.”

Another particularly likely target, it appears, is hedge funds, which have grown dramatically in number and size during the past decade. In hearings last fall, Representative Waxman noted this expanding role and the lack of oversight of the industry, pointing out that “regulators aren’t even certain how many hedge funds exist or how much money they control.”

Credit rating agencies, which many observers fault for missing the loan problems underlying the recent economic turmoil, may also find themselves placed under this larger umbrella. These agencies “failed to provide accurate information to the market,” says a recent U.S. Chamber of Commerce report. “We support responsible regulation of this industry, including eliminating conflicts of interest and ensuring a high level

of professionalism and competency in assigning ratings.”

The insurance industry is also likely to see increased oversight. Here, lawmakers might be inclined to take a hybrid approach, says Edwards. States not only regulate the industry within their respective borders, but also maintain surety pools as a backup in case companies run into financial trouble. That works well enough if a problem is limited to one or two smaller companies, but those resources can be inadequate if there is a problem with

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Fallout: More Litigation Coming

While the U.S. Congress works on regulatory change, financial services firms face significant challenges on another front, as well, as regulators and investors pursue their own solutions through the courts.

“When there are disasters like this, regulators tend to get more aggressive, partly because they have been somewhat embarrassed by what has occurred,” says Stephen Senderowitz, a partner at Winston & Strawn. “So, we’ll probably see much more legal action by the SEC, the CFTC and others.” Already, he says, companies are dealing with lawsuits related to everything from auction rate securities and collateralized debt obligations to the manipulation of natural gas and cotton markets.

Companies may also see lawsuits related to the Bernard Madoff scandal and other similar cases, as defrauded investors could sue intermediary financial institutions that may have introduced them to such investments. “Madoff is the largest of these, but it is not the only Ponzi scheme that’s been uncovered. There have been several,” says Senderowitz.

In addition, the courts will probably see more securities class action suits than they have in recent years, “simply because there have been more failures,” Senderowitz continues. “In connection with that, people obviously look for the deep pockets, so they generally will go after financial institutions that handled transactions, large accounting firms, banks—anybody involved that seems like they might have money.”

Overall, sums up Senderowitz, “what you are basically seeing is the fallout from a bunch of failed investments, with everyone now trying to find a way to recoup their losses. And it looks like the courts are going to be spending some time sorting it all out.”

“If Congress gets on a roll, it may look at things like credit card practices.... There may be a move for more straightforward disclosure.”

a large company that has investments across the financial services spectrum. “A good approach might be to leave in place the 50 state insurance regulators for institutions where that is appropriate,” says Edwards. “But for national insurance companies or international financial institutions with insurance operations in the United States, you could have a federal insurance regulator in Washington, which, of course, we don’t have now. So, there would be complementary federal and state regulation, similar to what we currently have with banking.”

If momentum is strong enough, such discussions could extend to the world of consumer credit. “If Congress gets on a roll, it may look at things like credit card practices, such as how interest is calculated on balances,” suggests Pilecki.

Some observers, he explains, believe that credit card policies need to be more open, so that consumers can have a better understanding of what they are getting into. “There may be a move for more straightforward disclosure,” he says. “That could end up limiting the options in terms of what a credit card issuer can build into the offering and result in very uniform products in the industry.”

3. Managing systemic risk

When the headline-grabbing financial problems at AIG unfolded last year, most officials were caught off-guard by the scope of the problem, because the fragmentation of the regulatory landscape meant that there was no clear overview of how bad things were getting, or how far problems would ripple through the industry. That situation pointed to a fundamental problem: As Steve Bartlett, CEO of the Financial Services Roundtable, told Congress last fall, “No single agency or entity is officially empowered to monitor all markets and all financial services firms and raise a red flag when practices or policies need to be adjusted or modified to minimize systemic risk... Congress should empower some agency or authority to keep abreast of market developments, and help foresee, and forestall, a repeat of this crisis.” In the current environment, it seems likely that Congress will take that kind of action fairly soon.

“One of the biggest issues to come out of the recent crisis is, how does the financial regulatory system grapple with overall risk management?” says Edwards. “We don’t really have a way to look at collective risk to the system.” A potential solution, she says, is to create an overall federal financial regulator that would look at the entirety of the financial system—

Private Equity: Moving In?

In the coming year, fallout from the economic downturn may provide some opportunities for private equity firms that are interested in the financial services industry.

For example, last fall, the U.S. Office of the Comptroller of the Currency began allowing “shelf charters,” which allow a group without a bank charter to bid on troubled banks, with a charter to be granted after a successful bid. This effectively broadens the potential pool of bidders to include private equity firms. “There are a number of private equity firms interested in acquiring failed banks,” says Paul Pilecki, a partner at Winston & Strawn. “They would be in position to establish a new bank that would basically be starting fresh with new funding, the acquired deposits of the failed bank and very little in the way of debt, so there is a real potential for private equity to create significant new bank franchises that can start out without a lot of problems on their books.”

The future may also see more private equity firms simply buying an interest in banks. The U.S. Treasury Department has provided a great deal of capital to a number of banks, which comes with a number of conditions. “Banks are likely to want to get out of a situation where the government is an owner,” says Pilecki. “They will want to redeem that capital from Treasury, and private equity will probably be a substantial source of funds for those redemptions.”

across banking, insurance, capital markets and hedge funds—to identify major risks. “Regulation could be left to the individual regulatory regimes such as banking or securities or insurance,” she says. “But the overall risk monitoring would be done by the federal regulator.”

Many observers see this as a critical element in regulatory reform. In February 2009, Representative Barney Frank, chairman of the House Financial Services Committee, said that creating such broad oversight was a priority on the reform agenda. He also proposed that the Federal Reserve be given that role—an idea backed last year by then-Treasury Secretary Henry M. Paulson Jr. Some critics, however, worry that such a move would concentrate too much power with the Fed, or perhaps overload it with new responsibilities. An alternative might be to create a separate new entity to take on the role. For example, the Committee on Capital Markets Regulation, an independent research organization, recently proposed the creation of an “independent United States financial services authority” that would “regulate all aspects of the financial system, including market structure and activities and safety and soundness for all financial institutions.”

Taking the time to get it right

With such fundamental changes under consideration, many observers see an opportunity to correct long-term problems. Much of the current regulatory framework dates back to the 1930s, with a patchwork overlay of additions and modifications added over time. The opportunity, then, is to create a coherent, transparent and up-to-date regime—and getting it right is critical. As Edward Carr,

Executive Pay: Back in the Spotlight

Executive pay has once again come to the forefront, as government-funded bailout efforts for the financial industry put a variety of conditions on compensation. These conditions apply only to financial firms receiving emergency aid—but they are likely to have a much broader impact.

“Many of the compensation provisions in the stimulus legislation will probably become best practices for the rest of corporate America,” says Michael Melbinger, a partner at Winston & Strawn. “Already, some of the original provisions of the TARP and CPP legislation have been adopted as best practices by non-financial public companies.”

For example, Melbinger explains, a number of corporations have embraced a rule that says that companies receiving federal assistance must provide assurances that executive compensation does not encourage executives to take excessive risks. “Compensation committees have always thought that it was a good idea to incentivize officers to produce outstanding results, but now they are going back to make sure they aren’t creating too much of an incentive to create too great a result,” he says. Another provision that may become a widespread practice is “say on pay,” in which shareholders vote on executive compensation—with the result being non-binding, but sending a powerful message nonetheless.

There are also conditions that are not likely to become broader best practices. “Things such as preventing any bonus payments or severance payments—those are just plain punitive, and they don’t make a lot of sense in the real world,” says Melbinger.

Finally, it’s not just government bailouts that will be affecting executive compensation in the coming year. Melbinger explains that Section 409A of the Internal Revenue Code, which took full effect at the end of 2008, has turned out to have some unintended consequences. “It was supposed to apply to deferred compensation. Everybody understands that,” he says. “The problem is that the way it was drafted, it applies to any promise of severance, promise of equity awards, and any promise of compensation in a later year—things that no one ever thought of as deferred compensation, but which are defined as such under the statute. So now, with almost every agreement with an employee, you have to think about 409A issues. That’s going to create a lot of ongoing havoc.”

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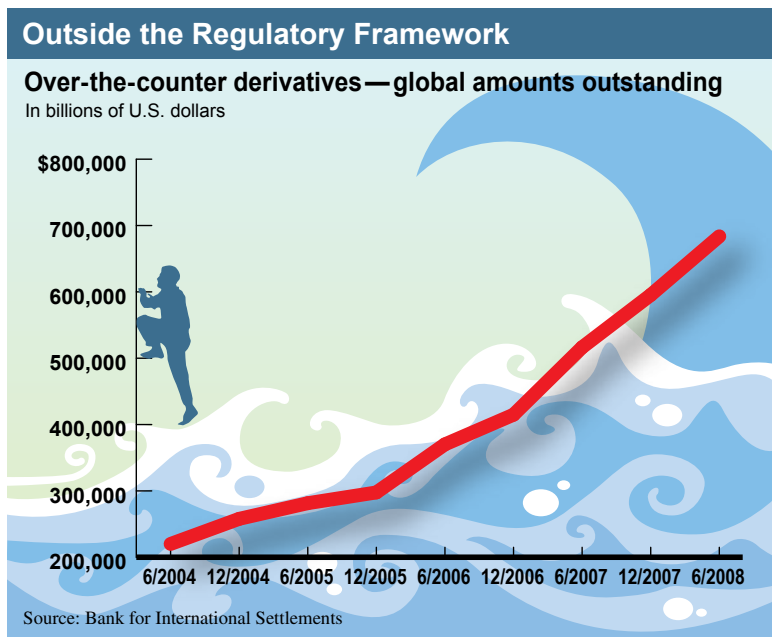
business affairs editor at *The Economist*, recently wrote, “Just now, many people will criticize regulation for being too lax. But remember that regulation can also be costly and distorting. And who will suffer if finance works badly? One thing that became agonizingly clear in 2008 is that we all will.”

For its part, the U.S. Chamber of Commerce recently outlined several principles to guide the effort. Among other things, it recommended more comprehensive regulation that eliminates duplication and layering of effort. It also called for “forward-looking regulation” that focuses on addressing tomorrow’s realities, rather than retroactively punishing wrongdoers for the errors of the past. And it notes that regulation needs to

reflect the increasing internationalization of capital markets and work in alignment with regulatory frameworks in other countries. Overall, the committee reported, “we must be careful not to embrace changes that fail to fix real problems and avoid undermining those capital markets functions that work well.”

Doing so will not be simple—it will take time and careful analysis. The question is, will that kind of diligence be politically feasible? “In so-called normal times, regulatory change is a deliberate process driven by changing trends in the market and the results of significant enforcement proceedings,” says Johnsen. Now, the broad impact of the credit crisis and market downturn has made public opinion a much larger factor. “The demand for new rules is being driven much more by emotion and headlines and by people posting statements on the Internet,” he says. That, in turn, has the potential to drive rapid and perhaps not well thought out change, which could lead to new regulations that create burdens without really solving problems.

The point, says Johnsen, is that financial services companies need to make sure that they understand the issues and are part of the discussion—monitoring rules proposals, participating in roundtables, talking to representatives. Business, he says, can bring a critical, practical perspective to the table. “You need to look not just at what the rule is, but at how it is going to work,” he explains. “Sometimes, a rule is well-intentioned, but the people who actually have to live with it find that it’s difficult or expensive and doesn’t really accomplish what you want. In the coming year, there will be significant change in the regulatory structure, and business needs to be involved in that discussion to help shape solutions that are effective.”



A number of observers believe Congress will work to bring previously unregulated financial instruments under the regulatory umbrella. One concern is that the amount of trading and development activity taking place in such instruments has been growing rapidly. For example, the total value for largely unregulated over-the-counter derivatives, such as credit default swaps and interest rate contracts, has more than tripled in the past four years.

The conventional wisdom may not apply; a more nuanced **approach to antitrust** can be expected.

Conventional wisdom says that a new Democratic administration in the White House is likely to bring about a shift from several years of light antitrust activity to a much more proactive approach. And as a presidential candidate, Barack Obama made it clear that antitrust enforcement would pick up under his administration.

“We’re going to have an antitrust division in the Justice Department that actually believes in antitrust law,” Obama said during the primaries. “We haven’t had that for the last seven, eight years.” Elsewhere, his campaign noted Obama’s intention to “reinvigorate antitrust enforcement, which is how we ensure that capitalism works for consumers.”

But that’s not all Obama or his aides said. The topic of antitrust—which is not usually fodder for campaign speeches—actually came up fairly often in the 2008 race. And Obama’s comments suggest that the conventional wisdom may not apply and that a more nuanced approach can be expected in the years ahead.

“Yes, there is going to be a general philosophy of more vigorous enforcement, but in several ways, President Obama appears to take a centrist view of antitrust,” says John Gibson, a partner at Winston & Strawn. “He has said that he will take steps to ensure that antitrust law is not used as a tool to interfere with robust competition.”

“Reinvigorated” activity

Gibson says that this centrist approach may show up in the definition of what is and what isn’t a monopoly. “President Obama made the statement that we live in a different world, where sometimes American businesses have to be enlarged to compete effectively in an international market, for example. So, I think we’ll see a very studied approach that says, ‘Let’s look at which companies are really

Taking a centrist view, President Obama “has said he will take steps to ensure that antitrust law is not used as a tool to interfere with robust competition.”

Overlaps: A Changing World

As the Obama administration tackles its agenda, questions about monopolies are likely to come up in a number of areas and take antitrust oversight into complicated territory.

For example, there is a great deal of interest in health care reform in Washington, and many observers see expanded cooperation across providers as a way to increase efficiency and quality. “The health care industry already feels like the guidelines for how they can collaborate with each other to improve quality and clinical integration aren’t too clear, and they have been pushing for clarification,” says Michael Sibarium, a partner at Winston & Strawn. “Now, if health care reform calling for greater cooperation comes along, what impact, if any, will that have on antitrust?”

Similar issues may arise with the \$700 billion-plus financial services industry bailout. “To the extent that the federal government takes equity stakes in banks, what does that mean for antitrust as a practical matter?” asks Sibarium. “How is enforcement going to work with a company in which the government owns a 20 percent stake? There are some significant potential question marks out there.”

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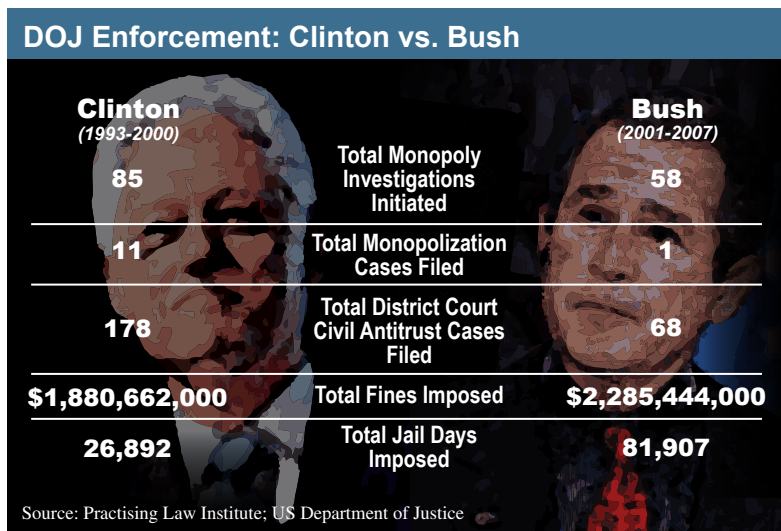
impacting competition unfairly, not just at who is big and successful.’ This is not an administration that is going to declare total war on the Fortune 500.” With a troubled economy, the new administration may also find that political realities trump ideology, and be more open to large mergers if they seem likely to preserve industries and jobs.

That said, increased antitrust activity is, in time, almost inevitable, and there are a number of issues that are likely to see “reinvigorated” activity under the new administration. In his Senate confirmation hearings, U.S. Attorney General Eric Holder said that antitrust is “a critical part of what the Justice Department does.... And so, antitrust enforcement will be something that we will devote a lot of attention to. We’ll get an assistant attorney general who understands the mission of that division, the historic mission of that division, and I expect it will be more active.”

“The choices for President Obama’s antitrust team certainly suggest more aggressive action,” says Michael Sibarium, a partner at Winston & Strawn. For example, he says, Jon Leibowitz, the new chairman of the Federal Trade Commission, has been a member of the commission for several years, and has tended to favor strong enforcement. And for assistant attorney general for the antitrust division of the Department of Justice—the position Holder mentioned—the president picked Christine Varney. As an FTC commissioner during the Clinton administration, she worked to expand merger analyses to include companies’ research into future products, not just existing or about-to-be-released products. Later, as a private lawyer for Netscape, she encouraged the Justice Department to pursue its antitrust case against Microsoft.

“In the area of consumer protection, for example, I think you’ll see investigations by the FTC ratchet up significantly,” says Mark McCareins, a Winston partner. In addition, he notes that President Obama has expressed interest in scrutinizing media industry mergers to ensure a diverse range of viewpoints and the use of regulation to ensure open Internet access.

There is also likely to be action in the area of unilateral conduct, in which individual, dominant companies take certain actions that might limit competition in their industries. One such issue involves minimum resale price maintenance agreements—those in which manufacturers require retailers to sell their products at a certain price. For almost a century, such agreements were automatically considered an antitrust violation. But in 2007, the U.S. Supreme Court ruled that they are not always illegal, and instead have to be considered on a case-by-case basis.



U.S. Department of Justice enforcement activity is expected to increase under the Obama administration, following a relative lull during the Bush years. It is worth noting that fines and imprisonments did not decline under Bush, and are not likely to do so under the new president, underscoring the importance of effective compliance programs.

Opponents say that this change will drive up prices for consumers, and a number of businesses are also displeased, says Sibarium. “Companies have had to navigate through this and figure out how to respond to the change in the law, while dealing with a variety of state laws that still consider these agreements to be per se illegal,” he says. In 2007, then-Senator Joe Biden co-sponsored the Discount Pricing Consumer Protection Act, which was designed to restore the previous treatment of such agreements. It did not make it to the Senate floor, but in early January 2009, the bill was reintroduced—clearly indicating that the issue is still in play.

Beyond such specific issues, more fundamental changes are likely to increase enforcement activity in the long run. For example, in recent years, the FTC has been more aggressive and the Justice Department less aggressive in enforcement, but with new Obama appointees, the agencies are likely to operate with more of a shared perspective. In addition, President Obama has the opportunity to name a number of judges early in his term, thanks in part to several Bush court appointments that were delayed by Congress. Says Gibson: “Over the next couple of years, these things are likely to have a meaningful effect on the antitrust environment.”

The coming years are also likely to see increased coordination between federal and state antitrust authorities, which had declined over the last eight years, says Sibarium. He adds that greater cooperation between antitrust authorities in the United States and other countries is also likely. “There has been a trend toward greater coordination internationally on antitrust, and that trend will probably continue, with coordination on a range of enforcement

actions, such as mergers and criminal cartel work,” he says.

The motivation for this cooperation is, in large part, a growing interest in antitrust globally, with more and more countries adopting laws to help ensure competition. China, for example, put an “antimonopoly law” in place last year, Sibarium says. “Where the United States historically took a lot of the lead in pursuing antitrust, you may see more big cases coming out of places like Asia,” he says. “The growth of antitrust around the world will continue to be a significant story.”

Vigilance: An Ounce of Prevention

The vast majority of business activity does not involve antitrust issues, but companies still need to be vigilant—especially with a new administration that promises greater enforcement. “The penalties for antitrust violations, both in terms of fines and jail time, can be severe, so it’s very important to maintain a strong internal antitrust compliance program,” says Winston partner Mark McCareins.

Companies need to follow several rules of thumb for an effective program. For example, such efforts need to be ongoing. “It’s not simply a matter of taking the vaccine once and then being fine,” McCareins says. “It takes continuing commitment, both to update people and to make sure new employees are on board.” In addition, he says, such programs need to extend beyond U.S. borders, because antitrust is now a global issue, with increasing action by governments around the world and the increasing flow of executives and business across borders. And they need to be driven from the top down: “Senior management backing the program is essential,” he says. “Otherwise, it is going to be hard to get the rest of the organization to buy in.”

Compliance programs are key to staying out of trouble, but they can also be important when problems do arise. For example, says McCareins, “under the Federal Sentencing Guidelines, companies that have active compliance programs are in a sense given ‘credit’ for those programs.” In addition, the Department of Justice has a program that grants amnesty to companies that voluntarily report internal illegal antitrust activities that they discover. “An ongoing compliance program can be an excellent vehicle for detecting problematic conduct in its infancy, making it possible for a company to avail itself of the amnesty program,” he says.

“Companies will see **energy and climate change** legislation that has a lot of both carrots and sticks.”

“The states [won’t] be quick to give up their ability to set these levels. The question is, to what extent will federal laws trump state laws?”

In a challenging economic climate, corporations have launched an array of cost-cutting efforts—and energy efficiency has become a prime focus. Increasingly, however, energy efficiency is not just a tactical necessity, but a long-term strategic imperative. For one thing, energy prices are expected to rise significantly in the coming years. Just as important is the growing political focus on energy usage, tying it to everything from climate change and national security to a company’s reputation.

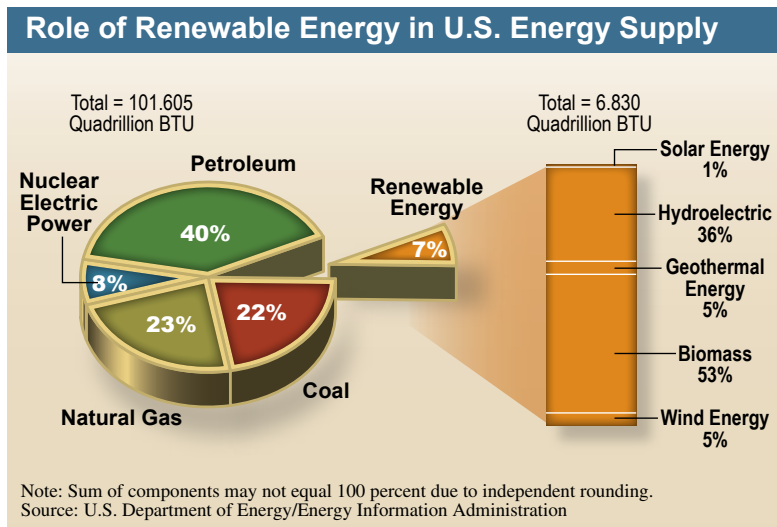
As a result, many businesses are recognizing that green initiatives make good, bottom-line business sense. Wal-

Mart, for example, reports significant savings with efficient “daylight harvesting” systems and LED lighting in its stores. The Dow Jones Sustainability Indexes “expect the demand for sustainability indexing to continue with accelerating speed.” And T. Boone Pickens, the Texas oil billionaire, has famously focused his attention on wind and natural gas transportation projects.

A strategic focus on energy will only become more important for business in the coming year. President Obama has made renewable energy and climate change top priorities. The recent stimulus bill included a range of energy-related items, and his proposed budget called for increased funding of greenhouse gas monitoring and alternative energy research. As this shift in policy works its way through Washington, Winston & Strawn partner Jerry Bloom says, “companies are going to see energy and climate change legislation that has a lot of both carrots *and* sticks.”

In recent years, much of the activity in these areas has occurred at the state and regional level. Most noticeably, California law now calls for returning greenhouse gas emissions to 1990 levels by 2025, and for having 33 percent of the state’s energy coming from renewable sources, such as solar and wind generation, by 2020. About half the states have some sort of renewable portfolio standard (RPS) that requires a certain percentage of electricity generation to come from renewable sources.

It appears that the U.S. Congress is



The percentage of renewable energy sources in the energy mix is relatively small, but should increase—though traditional fuels will still play a big role. While renewables now account for 8.5% of electricity generation, by 2030 that figure will reach 14.1%.

going to weigh in on the topic with a comprehensive energy bill this year. Based on recent proposals, Bloom says that legislation might call for an RPS of 10 percent of U.S. electricity coming from renewable sources by 2012, and 25 percent by 2025. Or, he adds, Congress might take a more flexible approach that recognizes that many states simply do not have the wind, solar or hydro resources to meet high renewables targets. “Rather than a renewable portfolio standard, Congress could create a green portfolio standard,” Bloom suggests. “This would mandate a reduction in carbon footprints, rather than percentages of renewable energy, which could then be achieved through a combination of energy-efficiency measures and investment in renewal resources and clean, efficient, fossil-fuel generation.”

Congress is also likely to pass climate-change legislation, but that may wait until 2010, given the current focus on economic issues, says Winston partner Eleni Kouimelis. It’s too early to know just what the details of such a bill would include, she says, but it seems likely that it will establish a cap-and-trade system, which puts increasing limits on greenhouse gas emissions and then allows companies to trade emissions credits so that the overall limits are met. The administration’s outline budget included provisions for such an approach, she says, adding that “the new head of the EPA, Lisa Jackson, is a big proponent of cap-and-trade.”

All this legislation will raise some fundamental questions, Kouimelis continues. “How are the state and federal efforts going to fit together?” she asks. “The states aren’t going to be quick to give up their ability to set these emissions and levels of renewable sources. The

question is, to what extent will federal laws trump state laws?”

But one thing is clear: The coming changes will contribute to increased energy costs. Some of that will stem from the need for new infrastructure, such as on-site equipment at companies and more-sophisticated transmission networks. In addition, says Bloom, “renewable power is expensive.” With coal and natural gas-fired generation, it costs about 4 cents to produce 1 kilowatt hour of electricity. With photovoltaic solar power, that can be as high as 30 cents. “As electricity prices go up to reflect costly additions to traditional resource generation mixes, companies will need to keep their costs down—which brings you right back to the continued importance of energy efficiency,” he says.

The U.S. government is expected to provide incentives for companies making the transition to this new world. A number of these are already in place. With the administration’s focus on energy, such breaks are likely to increase, says Andrew Ratts, a Winston partner. “The government historically uses tax policy to help implement desired social policy, and energy efficiency is one such policy,” he explains. “Energy efficiency and tax incentives to get there will be a continuing theme. So, businesses will have an opportunity to use the tax code to get help in managing the rising cost of energy.”

However, adds Bloom, “those dollars will not be endless.” As more energy-efficient technologies are installed, incentives will tail off with the declining need. “You need to position yourself for when these incentives become available, so you can take advantage of them as they emerge,” he says. “But this is complicated and not something you figure out overnight. You really need to start planning for it now.”

“Businesses will have an opportunity to use the tax code to get help in managing the rising cost of energy.”

There are no headline-grabbing business cases before the **Supreme Court**, but several will have an impact.

Preemption “is an important issue for a lot of businesses that would prefer to have a single federal regulation to deal with...rather than 51 different regulations.”

A few years ago, Eugene Volokh, a law professor at the University of California, Los Angeles, pointed out that the U.S. Supreme Court tends to have a gradual impact. In the coming years, as he told *The New York Times*, “the changes are likely to be incremental. We are not going to see a radical reordering of society.”

As it turns out, that is an apt description of the business-related cases being heard in the court’s current term. There are no headline-grabbing business cases that will bring sweeping change, but there are several that will have a real impact on business.

One set of these cases focuses on the concept of preemption. Federal law preempts state law when it comes to lawsuits over products that have met federal safety standards. “This is an important issue for a lot of businesses that would prefer to have a single federal regulation to deal with, even if it is not ideal from their standpoint, rather than 51 different regulations,” says Gene Schaerr, a partner at Winston & Strawn.

So far, businesses may not be getting the clarity they want. The court has already ruled in one preemption case, *Altria Group v. Good*. This involved the question of whether state consumer fraud laws could be used to sue cigarette companies for making claims about low tar and

nicotine—and the court has said that federal law does not preempt state law in that case. And the court recently reached a similar conclusion, although in a different context, in *Wyeth v. Levine*, in which a jury found that an FDA-approved drug led to gangrene and the amputation of a Vermont woman’s arm. The court ruled that federal labeling requirements do not necessarily preempt state laws in that area.

How willing to impose arbitration?

A number of other cases focus on arbitration. “The general issue in these cases is how strictly is the Supreme Court going to enforce the Federal Arbitration Act and to what extent is it going to be willing to impose arbitration on people who don’t want to be subject to it?” says Linda Coberly, a Winston partner. For example, *14 Penn Plaza v. Pyett* will determine whether arbitration required as part of a collective bargaining agreement limits an individual’s right to bring claims in court. “In contracts, unions will often say that if one of their workers has a dispute with the employer, the worker must go to arbitration, rather than file a lawsuit,” Coberly explains. “The question is whether the union can validly bind its members that way. This is important because, obviously, if unions can’t combine their members that way, the collective bargaining agreement becomes much less valuable to both

employers and unions.”

Further out on the court’s calendar is *Andersen v. Carlisle*, which will determine whether, in some situations, a company can compel a party to comply with an arbitration agreement when the company itself was not part of the agreement. For example, says Schaerr, “a company might have a contract with an employee that requires arbitration, but what happens if that company is bought by another company? The question is, can the second company take advantage of the arbitration clause that was negotiated by the first?”

Finally, the current term has several cases that will address environmental issues that could affect business costs and plans. For example, in *Entergy v. Environmental Protection Agency*, the court will determine whether the U.S. Clean Water Act allows the EPA to perform a cost-benefit analysis when identifying environmentally friendly cooling-water intake structures that should be used at power plants. The case will also address whether the EPA can regulate structures at existing plants, as well as at new plants.

In two cases involving the U.S. government versus Shell Oil and two railroads, the court is reviewing the environmental law that calls for “joint and several liability.” This law essentially says that when a contaminated Superfund site is cleaned up, every companies that has had something to do with the site can be held liable for the full cleanup costs, not just the company that owns the site. This includes those that sold or transported hazardous products there, and even those that subsequently purchased the property. In this particular event, the owner of such a site went out of business, Shell and the railroads were charged for the cleanup and they have gone to court to challenge these charges.

Meanwhile, in *Summers v. Earth Island Institute*, the court is deciding in which situations environmental groups have standing to challenge environmental regulations, as opposed to challenging a given project that is subject to those regulations. That is, when are they being harmed sufficiently to warrant the filing of a lawsuit? “Often, the federal regulations do not have much of an actual impact on environmental groups, but they still want to be able to go to court,” says Schaerr. “So, the case will address how much of an impact on their members they have to demonstrate in order to have standing.”

Appointments: New Justices, New Court?

Many observers have noted that President Obama is likely to have an opportunity to appoint at least one, and perhaps as many as three, Supreme Court justices in his first term. It also seems clear that he will consider justices who tend to be liberal, which could create a more liberal court overall. But that shift may not be as dramatic as some think, says Winston & Strawn partner John Gibson.

“There’s a lot of speculation that one or two of the justices will retire now that there’s a new president to nominate like-minded replacements,” Gibson says. “But the fact is that it is difficult to predict exactly who will retire when.”

While health or personal issues can prompt a sudden retirement from the court, justices have historically preferred to stay on as long as they can—and political considerations typically take a back seat. Supreme Court Justice Ruth Bader Ginsburg, who had surgery for pancreatic cancer in February, underscored that view last fall, when she told an audience about Justice Louis Brandeis. “He remained on the bench until age 83,” she said. “My hope and expectation is to hold my office at least that long.” That would put her retirement some time in 2016.

Demographics, too, come into play, with the more liberal justices, John Paul Stevens and Ginsburg, being the two oldest on the court, and Anthony Kennedy, known as a swing-vote justice, being tied for third-oldest with Antonin Scalia. “You can’t go by age alone,” says Gibson. “But if the oldest retire first, President Obama could actually be replacing liberal justices with other liberal justices initially, and it may not be that dramatic a change overall.”

Events may be dampening the sense of urgency for congressional action **on patent reform.**

The Obama campaign called for more “predictability and clarity in our patent system” and changes that would “reduce the uncertainty and wasteful litigation that is currently a significant drag on innovation.”

Patent Reform: Evolution, Not Revolution

Many observers see a need to reform U.S. patent law, but doing so has proven to be difficult. A year ago, this publication noted that patent legislation was more or less stalled in Congress. Now, a year later, the patent landscape looks much the same, with a patent reform bill having been approved by the Senate Judiciary Committee last spring, only to fail to make it to the floor.

That does not mean that the issue is dead. During the presidential race, the Obama campaign called for more “predictability and clarity in our patent system,” and for changes that would “reduce the uncertainty and wasteful litigation that is currently a significant drag on innovation.” And in early 2009, Senator Patrick Leahy, chairman of the Judiciary Committee, indicated that patent reform was a priority in the current session of Congress.

But there is some question as to how far legislative efforts will go. “In general, it seems unlikely that there is going to be any kind of consensus in the next year around patent reform,” says Michael Brody, a partner at Winston & Strawn. For one thing, he explains, the economy is still commanding much of the energy and attention of Congress. In addition, some stakeholders tend to see patent reform as a move that might stifle economic activity. A

joint letter sent in February 2009 and signed by more than 130 U.S. manufacturers said that many of the changes that had been proposed in previous reform legislation would create “a disincentive to invest and employ more Americans.” In the current climate, says Brody, such views may make elected officials reluctant to act quickly to change the law.

At the same time, many of the issues that have stymied past reform bills do not seem to have been resolved. For example, changes that raise the bar for infringement tend to be viewed by high-tech companies as a way to reduce baseless lawsuits, and by pharmaceutical companies as a restriction on their ability to protect their intellectual property.

Events on several fronts may also be dampening the sense of urgency for congressional action. For example, the number of patent litigation cases—which is sometimes cited as an indicator of problems with the system—has leveled off. Meanwhile, a number of court decisions have altered the patent landscape considerably.

In recent years, the U.S. Supreme Court has restricted the use of injunctions in patent cases, limited the awarding of treble damages for infringement and reinforced the non-obvious standard for determining what can be patented. And in October 2008, the U.S. Court of Appeals for the Federal Circuit’s decision in the *Bilski* case limited the patenting of business

methods—an area seen as problematic by proponents of reform. (In early 2009, *Bilski* was appealed to the Supreme Court.) In the coming year, says Brody, “the courts are likely to continue to play a lead role in changing the patent system, as they consolidate and clarify these positions.”

IP Online: From Conflict to Cooperation

For years, protecting intellectual property (IP) on the Internet was a highly contentious issue with no simple solutions in sight. Last year, however, signs were beginning to emerge that the struggle that pitted content owners against content users was beginning to give way to discussion and compromise. And that trend continued over the last year. “There has been a greater sense of partnership,” says Winston partner Michael Elkin.

Elkin points to agreements such as the one in April 2008 that saw the MySpace social networking site join forces with several record companies to create MySpace Music, a service that sells music and concert tickets. Moreover, he adds, the Recording Industry Association of America has said it is shifting away from its widely discussed strategy of suing individuals who share music over the Internet. “Now, it has turned its sights on Internet service providers to limit illegal downloads,” he says.

Elkin also cites a set of User Generated Content Principles that was created to help content owners and users work together in order to keep content available while protecting intellectual property. These principles are supported by companies on both sides of the issue, including CBS Corp., Fox Entertainment

Group, Microsoft Corp., MySpace, NBC Universal, Sony Pictures Entertainment, Veoh Networks, Viacom and The Walt Disney Company. “At one point, people expected to see companies beating on each other in court over these things,” Elkin says. “Instead, they have put together a set of principles that were created with the idea of having the respective players cooperate and abide by certain concepts.” The principles aren’t legally binding, but many companies are working to adhere to them, he adds.

That is not to say that no one is taking online IP issues to court. For example, Cablevision was sued two years ago by several TV networks and movie studios over a proposed system that lets customers store content on its central servers, rather than a set-top box. That case has now been appealed to the U.S. Supreme Court, and many observers think that the court will hear the case.

The courts will no doubt continue to play a role in shaping online IP protection as businesses try to hammer out what is a very important issue. However, says Elkin, “I think we will tend to see more and more cooperation, and that we will see less activity in terms of enforcement this coming year.”

For one thing, he says, the downturn in the economy and budget constraints are likely to dampen interest in pursuing what can be lengthy and complex IP litigation. But more important, perhaps, is a growing sense that when it comes to protecting both content and users in a fast-moving world, cooperative solutions can often be more effective than conflict. Says Elkin: “There is an interest in stemming the tide of piracy online while recognizing the respective interests and rights of all the parties involved.”

The Recording Industry Association of America has “turned its sights on working cooperatively with Internet service providers to educate users and limit illegal downloads.”

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Key Conferences

FINANCIAL SERVICES

June 2009

Managed Funds Association Forum 2009, Chicago, IL—Brings together investment and hedge fund managers, brokers and service providers who support the industry

June 2009

ALM General Counsel East Conference, New York, NY—Gathers in-house counsel to discuss navigating the pitfalls of doing business with the tumultuous financial markets

September 2009

15th Annual Reuters LPC Loan Conference, New York, NY—Draws more than 500 investors, lenders, financial sponsors and borrowers in the commercial loan market

October 2009

Turnaround Management Association 2009 Annual Convention, Phoenix, AZ—Unparalleled gathering of leading turn-

around, restructuring and distressed investing professionals from across the country for education, networking and best practice sharing

October 2009

LSTA 13th Annual Conference, New York, NY—Promoting the orderly development of a fair, efficient, liquid and professional trading market for corporate loans originated by commercial banks and other similar private debt

ENERGY

April 2009

24th Annual Global Power Markets Conference, Las Vegas, NV—Brings together power industry leaders to discuss issues crucial to the development of electric power markets

June 2009

REFF Wall Street, New York, NY—The latest policy developments across the major renewable energy sectors as well as the increasing involvement of big energy and agribusiness

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