Goettingen Journal of International Law 4 (2012) 1, 177-197

Have Measures Adopted by States to Cope With the Global Financial Crisis Been in Accordance With Their Obligations Under International Investment Law?

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doi: 10.3249/1868-1581-4-1-hocke

Abstract

International investment law guarantees broad protection. The following article examines how measures against the Global Financial Crisis, e.g. the acquisition of shares or the refusal to help particular financial institutions, affected those standards. However, the article argues that due to public policy reasons the measures have been in accordance with all protection standards.

A. Introduction

Foreign investors enjoy special protection under Bilateral Investment Treaties ("BITs") or Free Trade Agreements ("FTAs"). For this reason, numerous investors were able to sue Argentina for the measures adopted by it during its economic crisis in 2001 – 2002.[1] Although no investor has started arbitral proceedings against the Host State for measures adopted against the global financial crisis of 2007 – 2010 yet, this is not unlikely to happen.[2] Due to the transnational connections in today's commercial world, many internationally acting businesses have been seriously affected by the impact of the global financial crisis, which caused an estimated loss of $ 32 trillion for global equity markets.[3] Foreign investors could potentially sue their Host States for their losses due to the bankruptcy of Lehman Brothers Inc., or because their shares have been acquired by a government.

The following work has the ambition of assessing, whether the protection standards for foreign investors under BITs and FTAs have been violated by States when they adopted measures to cope with the global financial crisis and what potential claims might therefore result. For this purpose, the common standards of investment protection shall be described briefly (B.). Eventually, the compliance of exemplary measures, taken by the world's major economies during the global financial crisis, with the standards of investment protection shall be discussed. In respect of the

1 See for a brief description: C. Brown, 'Investment Arbitration as the New Frontier', 28 *The Arbitrator & Mediator* (2009) 1, 59, 60-61.

2 A. van Aaken & J. Kuntz, 'The Global Financial Crisis: Will State Emergency Measures Trigger International Investment Disputes?', *Columbia FDI Perspectives*, No. 3 (23 March 2009), available at http://www.vcc.columbia.edu/documents/Perspective3-vanAakenandKurtz-FINAL.pdf (last visited 26 April 2012).

3 K. Rudd, 'The Global Financial Crisis', *The Monthly*, February (2009), 20, 21.

scope of this work, the focus will be on the measures taken by selected major economies such as China, Germany, Switzerland, the UK and the USA. The measures are categorized in respect of their target and their character. Therefore, the measures will be separated into measures adopted to stabilize financial institutions (C.), omissions to stabilize financial institutions (D.), acquisition of properties in order to regulate financial institutions (E.) and direct stimulations of domestic economies (G.).

B. Standards of Investment Protection

Notwithstanding other international law sources, the protection of foreign investors depends on the specific formulation of a BIT or a FTA. In these treaties, States agree to confer certain protective rights on investors of the treaty partner's nationality. The effect is that foreign investors no longer have to seek legal protection through diplomatic and juridical actions of their home State, but can directly initiate proceedings against their Host State, usually before an arbitral tribunal.[4] Treaty parties frequently agree on the International Centre for the Settlement of Investment Disputes ("ICSID"), as the forum for investment arbitration.[5] Established as a separate institution of the World Bank Group by the ICSID Convention in 1965, ICSID provides facilities for investment arbitration, administers the proceedings and has fixed procedural rules.[6]The award itself, however, is issued by an independently constituted tribunal and ICSID's function is solely administrative.[7]

In 2009, over 2,800 BITs and FTAs have been recognized.[8] Although scope and protection standards can differ from one treaty to another, the treaties are surprisingly similar in structure and content.[9] They usually confer five major protection rights on an investor against a Host State. The traditionally most important standard is the prohibition of expropriation of foreign investments, or measures with an equivalent effect, without

4 C. Brown, *supra* note 1, 61.

5 Art 25 para. 1, ICSID Convention.

6 *Convention on the Settlement of Investment Disputes between States and Nationals of Other States*, opened for signature 18 March 1965, 575 UNTS 159 (entered into force 15 October 1966) (ICSID Convention).

7 A. Reinisch & L. .Malintoppi, 'Methods of Dispute Resolution', in P. Muchlinski, F. Ortino & C. Schreuer (eds), *The Oxford Handbook on International Investment Law* (2008), 691, 698.

8 A. Newcombe & L. Paradell, *Law and Practice of Investment Treaties* (2009), 57.

9 *Id.*, 1.

compensation.[10] In addition, Host States do not merely have to accept foreign investments once they were made, but also have to treat foreign investors in a fair and equitable way.[11] This obligation may cover more specific obligations, such as consistent conduct, respect of the investor's reasonable expectations, lack of arbitrariness, due judicial process and transparency.[12] In order to ensure fair competition within their territories, Host States especially have to treat foreign investors in a non-discriminative way.[13] This comprises two separate protection standards: First, the Host State must not discriminate *against* foreign investors, but treat them as nationals are treated.[14] Second, there must not be any discrimination *between* foreign investors. Every investor therefore has the right to the so-called Most-Favored-Nation Treatment.[15] Finally, not only Host States' authorities itself can be a threat for investors, but also the population of Host States and economic circumstances within the Host States. Therefore, Host States have to ensure foreign investors' full protection and security against third parties.[16]

It appears that during the financial crisis, four standards of investment protection might have been breached by States: The prohibition of expropriation without appropriate compensation, the fair and equitable treatment standard, the standard of national treatment and the standard of full protection and security. When assessing, whether investors have claims for breaches of these standards, a three-step test should be taken. First, is the person concerned an investor of its home State and his business an investment under the relevant investment agreement and the ICSID convention? Second, has the Host State acted in accordance with the standard of investment protection in question? Third, if not, is a potential

10 C. Schreuer, 'Introduction: Interrelationship of Standards' in A. Reinisch (ed.), *Standards of Investment Protection* (2008), 1.

11 I. Tudor, *The Fair and Equitable Treatment Standard in the International Law of Foreign Investment* (2008), 132.

12 K. Yannaca-Small, 'Fair and Equitable Treatment Standard: Recent Developments' in August Reinisch (ed.), *Standards of Investment Protection* (2008), 111, 118.

13 P. Acconci, 'Most-Favoured-Nation Treatment' in P. Muchlinski, F. Ortino & C. Schreuer (eds), *The Oxford Handbook on International Investment Law* (2008), 363, 364.

14 R. Dolzer & C. Schreuer, *Principles of International Investment Law* (2008), 178.

15 A. R. Ziegler, 'Most-Favoured-Nation (MFN) Treatment' in A. Reinisch, *Standards of Investment Protection* (2008), 59, 60.

16 C. McLachlan, L. Shore & M. Weininger, *International Investment Arbitration: Substantive Principles* (2007), 247.

breach of an investment protection standard justified by a defense? This test procedure shall be the course of the following observation.

C. Stabilization of the Financial System

The global financial crisis reached its peak in fall 2008. With a credit squeeze ballooning into the biggest financial crisis since the Great Depression after 1929, States suddenly faced the threat of the breakdown of the whole global financial system.[17] It is said to have been one of the most threatening moments for the global economy in modern times.[18] As a consequence, States adopted measures in order to stabilize struggling financial institutions. As it will be shown, these measures have been merely adopted for domestic banks. Therefore it shall be examined, whether foreign banks could claim compensation for this disadvantage

I. Measures Adopted

From the handling of the global financial crisis in the world, three different types of measures appear to have been adopted in order to ensure the vitality of banks. Banks received direct liquidity, guarantees and the opportunity to trade highly risky assets to States.

The first country to directly help one of its major banks was the UK in September 2007. Following an announcement about financial support from the Bank of England on 13 September 2007, customers of the UK retail bank Northern Rock plc started a run on their bank's offices. As a consequence, the UK government fully guaranteed all of the bank's retail deposits.[19] Half a year later, the Bank of England decided to allow UK banks to swap their high quality mortgage-backed and other securities for UK Treasury Bills.[20]

17 'Economic Crisis and Market Upheavals', *The New York Times Online*, available at http://topics.nytimes.com/top/reference/timestopics/subjects/c/credit_crisis/index.html?8qa&scp=1-spot&sq=&st=nyt (last visited 23 April 2012), para. 10.

18 S. Wilske, 'The Impact of the Financial Crisis on International Arbitration' 65 *Dispute Resolution Journal* (2010) 1, 82, 83.

19 J. Goddard, P. Molyneux & J. O.S. Wilson, 'The financial crisis in Europe: evolution, policy responses and lessons for the future', 17 *Journal of Financial Regulation and Compliance* (2009) 4, 362, 363.

20 Bank of England, *Special Liquidity Scheme: Information*, notice of 21 April 2008, available at http://www.bankofengland.co.uk/markets/sls/sls-information.pdf (last visited 26 April 2012).

Whereas the Federal Reserve Bank of America and the Reserve Bank of New York managed to arrange takeovers of the major American banks Bear Stearns Inc. and Merrill Lynch & Co. Inc., Lehman Brothers Inc. filed for bankruptcy relief on 15 September 2010. On 16 September, the Federal Reserve Bank of America accepted a bailout of $ 85 billion for AIG Inc.[21] As a consequence, US Congress passed the Emergency Economic Stabilization Act of 2008[22] on 3 October 2008. Under section 101 of this act, the Troubled Asset Relief Program was established, so that assets and equity for up to $ 700 billion from financial institutions that were regulated under US law and had significant operations in the USA could be purchased. Eventually the US Department of the Treasury directly transferred almost $ 200 billion to US financial institutions in return for preferred shares.[23]

The German government first guaranteed all retail deposits in Germany on 5 October 2005.[24] Eventually the Financial Market Stabilization Act[25] was passed, which established a fund that provided € 80 billion of liquidity as well as € 400 billion of guarantees for German banks.[26] Germany is fully liable for this fund. It was not until 23 July 2009, however, that German financial institutions were allowed to trade their highly risky assets.[27]

In the meantime, UK government decided to guarantee up to £ 250 billion of UK incorporated banks' obligations and approved that the struggling HBOS plc was taken over by Lloyds TSB plc, although Lloyds TSB plc consequently acquired a market share of one third in UK savings

21 A. Shah, 'Emergency Economic Stabilization Act of 2008' 46 *Harvard Journal on Legislation* (2008) 2, 569, 573.

22 Emergency Economic Stabilization Act of 2008, Division A Public Law 110-343, 122 Stat. 3765, enacted 3 October 2010.

23 T. C. Baxter Jr. & D. Gross, 'The Federal Reserve's response to the Crisis: Doing whatever it takes within its legal authority' in M. Giovanoli & D. Devos (eds), *International Monetary and Financial Law* (2010), 293, 296.

24 'Merkel und Steinbrück im Wortlaut: Die Spareinlagen sind sicher', *Spiegel Online*, 5 October 2010, available at http://www.spiegel.de/wirtschaft/0,1518,582305,00.html (last visited 26 April 2012).

25 'Act on the implementation of a package of measures to stabilize the financial market (Gesetz zur Umsetzung eines Maßnahmenpakets zur Stabilisierung des Finanzmarktes), 17 October 2008, BGBlI 1982.

26 *Id.*, Article 1 § 2 (1). In the end only € 128 billion of guarantees have been issued.

27 B. Krauskopf, 'Legislative measures to support financial market stability: The German example and its European context' in M. Giovanoli & D. Devos (eds), *International Monetary and Financial Law* (2010), 329, 352.

and mortgage markets. It even supported the takeover through a capital injection of £ 17 billion, almost the same amount of money the Royal Bank of Scotland plc received.[28]

The Swiss government did not even announce a general program, but merely offered direct help to UBS AG and Credit Suisse AG. Whereas Credit Suisse AG successfully managed to approach private investors,[29] UBS AG finally had to receive CHF 5.4 billion from the Swiss Confederation.[30]

II. Affected Foreign Investments

The disadvantaged of the measures described could be *foreign* financial institutions, which did not receive any bailout from States. As a first requirement of their investment claims, it has to be established that a foreign investment has been affected by the situations above. In the globalized world, no market merely contains domestic investors. Especially, contemporary financial institutions engage in businesses throughout the world. They trade physical assets, shares and derivatives in foreign venues and direct their business at foreign customers. For investment claims, these businesses have to be classified as investments under the relevant BIT or FTA and under the ICSID Convention. Whereas the former determine the scope of their material protection standards and usually cover any kind of *asset*,[31] Art. 25 (1) ICSID Convention requires an undefined investment for the admissibility of an arbitral claim before ICSID.

Although there is no rule of precedence in investment arbitration,[32] the course of arbitral awards under the ICSID convention established the following trademarks of an investment: A significant duration, an element of risk, a commitment of the investor and a significant contribution to the Host State's economy.[33] Whereas some tribunals regarded these criteria as

[28] Goddard *et al.*, *supra* note 19, 364.

[29] L. Thévenoz, 'The Rescue of UBS' in M. Giovanoli & D. Devos (eds), *International Monetary and Financial Law* (2010), 378, 383.

[30] *Id*., 388.

[31] McLachlan *et al.*, *supra* note 16, 171.

[32] C. Schreuer & M. Weiniger, 'A Doctrine of Precedence?' in P. Muchlinski, F. Ortino & C. Schreuer (eds), *The Oxford Handbook on International Investment Law* (2008), 1188, 1189.

[33] *Fedax N.V. v. Republic of Venezuela*, ICSID Case No. ARB/96/3, Decision on Jurisdiction, 11 July 1997, (2002) 5 ICSID Reports 186, 199;

fixed requirements,[34] others adopted a more intuitive method applied the criteria as merely indicating characteristics.[35]

A participation of a foreign investor in a State's financial markets certainly involves a risk to lose assets and can therefore be regarded as a commitment. An appropriate duration can at least be approved for a business of two years.[36] The issue, however, is, whether a foreign investor's participation in financial markets constitutes a significant or positive[37] contribution to a Host State's development. For this purpose it appears useful to separate financial activities into services for customers and independent transactions between financial institutions. The provision of loans and investment opportunities for consumers and entrepreneurs ensures the supply of liquidity for an economy's participants.

In contrast, consumers and entrepreneurs do not seem to obtain any benefits from highly risky interinstitutional transactions. However, these transactions are an important factor of a financial institution's profitability. This profitability ensures the ability to provide services for customers. Providing liquidity for customers thus requires interinstitutional transactions. Since the provision of liquidity is therefore a contribution to a Host State's economy, financial institutions must meet all the significant criteria of an investment under Art. 25 (1) ICSID Convention. They are consequently allowed to commence arbitral proceedings before ICSID.

III. Compliance with National Treatment Standard

The measures adopted to bailout financial institutions could have breached the national treatment standard. The national treatment standard

SaliniConstruttoriSpAetItalstradeSpA v. Kingdom of Morocco, ICSID Case No. ARB/00/4, Decision on Jurisdiction, 23 July 2001, (2003) 42 ILM 609, para. 53.

34 *Victor Pey Casado and President Allende Foundation v. Republic of Chile*, ICSID Case No. ARB/98/2, Award, 8 May 2008, para. 232, cited by E. Gaillard, 'Identify or define? Reflections on the evolution of the concept of investment in ICSID practice' in Christina Binder *et. al.* (eds), *International Investment Law for the 21st Century – Essays in Honour of Christoph Schreuer* (2009), 403, 411. The tribunal, however, disclaimed the fourth requirement.

35 *CSOB v. The Slovak Republic*, ICSID Case No. ARB/97/4, Decision on Jurisdiction, 24 May 1999, (1999) 14 ICSID Review – Foreign Investment Law Journal 251, para. 90; *M.C.I Power Group, L.C. and NEW Turbine Inc. v. Republic of Ecuador*, ICSID Case No. ARB/03/6, Award, 31 July 2007, available at http://ita.law.uvic.ca/documents/MCIEcuador.pdf (last visited 26 April 2012), para. 165.

36 *Salini v. Morocco*, *supra* note 33, para. 54.

37 Gaillard, *supra* note 34, 415.

ensures that foreign investors shall be treated no less favorable than national investors.[38] In practice, this standard is restricted to situations where foreign and national investors are in like circumstances.[39] States required companies to be incorporated under their domestic law or have their seat in their territory in order to be eligible for State help, if they did not even drafted their measures for specific domestic banks. Foreign banks explicitly received no direct help from their Host States, but were treated less favorable than national banks. This leads to the question of like circumstances. On the one hand, foreign financial institutions undertake exactly the same business as national investors and could therefore come under even the toughest formal test.[40] They were in the same *de facto* situation, as *van Aaken* and *Kuntz* phrase it.[41]

On the other hand, however, as stated by the Tribunal in *S.D. Myers Inc. v. Canada*, the assessment of like circumstances should take reasonable policy grounds into consideration.[42] Although most investment agreements do not explicitly provide it, differentiations between foreign and national investors can be justified on rational grounds.[43] There appear to be two policy grounds to justify the focus on domestic banks while handling the global financial crisis. First, national banks are more important for the provision of liquidity within the domestic economy. Although foreign bank equivalently provide customer services, domestic institutions dominate the markets of financial services. Since the goal of the measures adopted against the global financial crisis was to keep the economy alive by ensuring the

38 See for example: 'Treaty between the Government of the Italian Republic on the Kingdom of Saudi-Arabia concerning the protection and the recivprocal protection of investments' (*Tra Il Governo della Repubblica Italiana e dil Regno dell' Arabia Saudita sulla Reciproca Promozione e Protezione Degli Investimenti*), opened for signature 10 September 1996, available at http://www.unctad.org/sections/dite/iia/docs/bits/italy_saudiarabia_it.pdf (last visited 26 April 2012) Art. 3 (2), '(…) [C]iascuna Parte Contraente accorderà agli investimenti (…) degli investitori dell' altra Parte Contraente un trattamento non meno favorevole di quello accordato agli investimenti degli (…) dei suoi investitori.'

39 Dolzer & Schreuer, *supra* note 14, 179.

40 See for this test *Marvin Roy Feldman Karpa v. United Mexican States,* ICSID Case No. ARB(AF)/99/1, Award, 16 December 2002, 18 ICSID Review – Foreign Investment Law Journal (2003) 2, 488, para. 171.

41 A. van Aaken & J. Kuntz, *supra* note 2, para. 9.

42 *S.D. Myers Inc. v. Canada,* Partial Award, 13 November 2000, (2001) 40 ILM 1408, para. 250.

43 Dolzer & Schreuer, *supra* note 14, 181. Indeed, the tests of breach of a standard and its justification seems merged for this standard.

provision of liquidity, it were the domestic banks that had to be rescued. In regard of the extraordinarily high costs of the bailouts, it can be regarded as a legitimate policy ground, that the costs shall be absolutely necessary for the domestic economy.

Second, it seems highly practical that States all over the world concentrate on their own financial institutions. Since every government was aware of the global financial crisis and considered possible measures to solve it, each financial institution was focused on by its home government. The alternative – each government focuses on the domestic market participants instead of the national institutions – involves the difficulty to assess each participant’s market share in the domestic market and stabilize it according to this share. In an emergency situation like in fall 2008, this seems highly ineffective. The efficiency of the handling of the global financial crisis, however, was intrinsic for the vitality of the world’s economy. The tribunal in *GAMI v. Mexico*, even held that the solvency of an local sugar industry was a legitimate goal of policy.[44] The effectiveness of the handling of the global financial crisis should be a legitimate goal of policy *a fortiori*. In conclusion, the distinction between foreign and national banks was justified by the enormous costs and the effectiveness of bailouts. Therefore, foreign and national banks were not in like circumstances and States did not breach the national treatment standard.

D. Rejection of Help for Financial Institutions

The incident that turned the so-called subprime mortgage crisis into the global financial crisis was the breakdown of the US investment bank Lehman Brothers Inc. Having taken over the two government sponsored loan providers Fannie Mae and Freddie Mac on 6 September 2010, the US government refused a bailout for Lehman Brothers Inc. for fiscal reasons. The bank went bankrupt and was sold to Barclays plc for $ 20 billion less than its assets were worth.[45] The issue, to what extent eventual rescue packages could have been avoided without the insolvency of Lehman Brothers Inc. shall not be the topic of this observation. It shall be

[44] *GAMI Investments Inc. v. United Mexican States*, Award, 15, November 2004, available at http://www.state.gov/documents/organization/38789.pdf (last visited 26 April 2012), para. 114.

[45] S. Lubben & C. Bowles, ‘The sale of the century and its impact on asset securitization: Lehman Brothers’, 27 *American Bankruptcy Institute Journal* (2009) 10, 1.

concentrated on the direct effects for share- and stakeholders of this refusal. Could foreign owners and creditors of Lehman Brothers Inc. seek damages from the USA, for breach of investment protection standards? The refusal of a bailout for Lehman Brothers Inc. will be examined in regard of the fair and equitable treatment standard and the full protection and security standard.

I. Affected Foreign Investments

Directly affected by the bankruptcy of Lehman Brothers Inc. have been creditors on the one hand and shareholders of Lehman Brothers Inc. on the other. The former are barely covered by the investment definitions in BITs and FTAs. Usually physical property, intellectual property, equity participation or special public law rights are required.[46] Mere contractual claims against entities incorporated under the law of another State, however, do not seem to be covered. This appears to be in accordance with the criteria for an investment under Art. 25 (1) ICSID Convention. In contrast to an equity participation, a contractual claim does not involve participation of the creditor in another's business or a commitment for further action. Although creditors certainly bear a risk when entering into a contract, they conceptually have no need for active conduct in order to satisfy their claims. Equity participation, in contrast, involves the necessity to actively develop the equity in order to obtain profit.

The holding of shares in companies, notwithstanding their amount, is usually mentioned as an investment in BITs and FTAs.[47] Art. 25 (2) (b) ICSID Convention only addresses the case of control by a foreign investor. Whether a minority shareholding in a local company constitutes an investment, however, is left unaddressed by the ICSID Convention. The usual authority for the approval of minority shareholders' claims is the case *CMS v. Argentina*, where the tribunal allowed a US minority shareholder of an Argentine company to claim under the US-Argentine BIT.[48] It relied on

[46] See for example: *Treaty between the United States of America and the Government of the Republic of Croatia concerning the encouragement and reciprocal protection of Investment*, opened for signature 13 July 1996, available at http://www.unctad.org/sections/dite/iia/docs/bits/croatia_us.pdf (last visited 26 April 2012), Art. 1 (d).

[47] Dolzer & Schreuer, *supra* note 14, 57.

[48] *CMS Gas Transmission Company v. Argentine Republic*, ICSID Case No. ARB/01/8, Decision on Jurisdiction, 17 July 2003, 42 ILM 788 (2003), para. 51.

the fact that ownership of shares was submitted as a specific example of an investment during the negotiation of the ICSID Convention.[49] Since shareholders are virtually owners of a company and therefore undertake their business through that company, this can be approved. If a local company would constitute an investment, what an essential bank like Lehman Brothers Inc. certainly does, than its shareholders should be seen as acting through this local investment and therefore constituting the investment. Even if not every small minority shareholding should constitute an investment, it could be argued that the bigger the business of the local company is, the smaller the minority shareholding needs to be. In respect of a major bank, such as Lehman Brothers Inc., this would allow any shareholder to be classified as an investor.

II. Compliance with Fair and Equitable Treatment Standard

When assessing, whether the rejection of a bailout for Lehman Brothers Inc. was a breach of the fair and equitable treatment of the foreign shareholders of Lehman Brothers Inc., the analysis shall not be merely concentrated on the reasonableness of the rejection. This argument is subject to a very deep economic investigation. The legal argument is, whether the US government's rejection was arbitrary and discriminatory. The obligation to avoid arbitrary and discriminatory conduct is usually expressly mentioned together with the fair and equitable treatment standard and therefore regarded as one of its aspects.[50] Although the prohibitions of arbitrariness and discrimination are sometimes assumed to be identical, their separate listing suggests that each must be accorded its own significance and scope.[51]

1. Discrimination

Why is discrimination at this stage assessed under the fair and equitable treatment standard? The reason lies within the nature of the treatment of Lehman Brothers Inc.: Neither was Lehman Brothers Inc. sent into bankruptcy because of the shareholding of foreign investors, nor were foreign investors, or investors from a certain country particularly affected by the bankruptcy. French investors in Lehman Brothers Inc., for example, suffered just as badly as investors form the US or investors from the UK.

49 *Id*., para. 50.
50 Tudor, *supra* note 11, 177.
51 Dolzer & Schreuer, *supr*a note 14, 173.

The discrimination could, however, lie in the fact that investors of rescued Wall Street banks did not suffer as much. This variety of potential discrimination is independent from nationality and therefore distinct from national or Most-Favored-Nation treatment. The discrimination could thus be, that the Troubled Asset Relief Program of the US Treasury Secretary helped struggling banks, while there was no bailout for Lehman Brothers Inc.[52]When assessing, whether financial assistance was discriminatory, it has to be focused on the leading case of *Saluka Investments v. The Czech Republic*. In this case, Saluka acquired the majority of shares in IPB, one out of four major Czech State banks. As a consequence of the State management during the Cold War, all of the four major banks struggled. IPB, the only bank now owned by a foreign investor, was the only bank not to receive any financial assistance from the Czech Republic. Saluka successfully claimed damages for violation of the fair and equitable treatment standard.[53]

However, there are major differences between the situations of Saluka Investments and Lehman Brothers Inc.: First, Saluka Investments inherited the debt problems from the Czech Republic. Lehman Brothers Inc. has always been privately managed in contrast. Second, when help for IPB was rejected by the Czech Republic, the other major Czech banks received financial assistance *at the same time*. The impression of discrimination of Lehman Brothers Inc. however arises out of eventual bailouts. The handling of the US government was rather a gradual decision-making process where the reasoning continuously developed.

Finally, it is an intrinsic feature of an investment, that the investor bears the insolvency risk. There is no general bailout right, merely because some institutions were regarded as essential for the economy and bolstered. The circumstances of insolvency do not impose any obligation on States. The prohibition of discrimination, however, is rather designed for situations of natural State involvement. For this reason the classification of financial assistance as discriminatory should be applied only in a limited manner.

52 Shah, *supra* note 21, 573-574.

53 *Saluka Investmens v.The Czech Republic*, Partial Award, 17 March 2006, available at http://www.pca-cpa.org/upload/files/SAL-CZ%20Partial%20Award%20170306.pdf (last visited 26 April 2012), para. 498.

2. Arbitrary Conduct

The literal meaning of 'arbitrary conduct' is interpreted by tribunals as 'action founded on prejudice or preference rather than on reason of fact'.[54] Arbitrary measures therefore lack a rational decision-making process.[55] There cannot be found any sufficient evidence, that the Treasury Secretary and other US authorities did not sufficiently consider the relevant arguments during their conduct in September 2008. Arbitrary conduct is therefore unlikely to be argued.

III. Compliance with Full Protection and Security Standard

A violation of the full protection and security standard can be rejected as well. Most investment agreements contain clauses promising full protection and security.[56] Besides the protection from physical harm to an investment, this standard of investment protection also covers the availability of the judicial and administrative system.[57] The tribunal in *Siemens v. Argentina* even extended this to the stability of the legal system as a whole.[58] But it was not the legal system that caused the breakdown of Lehman Brothers Inc. If any, there were economic circumstances. Following the argument concerning a potential discrimination, there can be no reason, why a non-profitable business should have a claim against its State to be protected. Bankruptcy perspectives belong to a business as exorbitant profits do. In addition, it is not the purpose of the full protection and security standard to protect an investment from threats to which it contributed. Therefore, the rejection of a bailout was no breach of the full protection and security standard against shareholders of Lehman Brothers Inc.

54 *Lauder v. Czech Republic*, Award, 3 September 2001, (2005) 9 ICSID Reports 66, para. 221.
55 *CMS v. Argentina*, *supra* note 48, para.158.
56 Dolzer & Schreuer, *supra* note 14, 149.
57 G. Cordero Moss, 'Full Protection and Security' in A. Reinisch (ed.), *Standards of Investment Protection* (2008), 131, 144.
58 *Siemens AG v. Argentine Republic*, ICSID Case No. ARB/02/8, Award, 6 February 2007, para. 303, cited by Moss, *supra* note 57, 145.

E. Acquisition of Properties

The German bank Hypo Real Estate AG has been extraordinarily threatened in 2008. Eventually it became an example of an expropriated company. Due the important position of this bank in the European financial system, it received guarantees for more than € 100 billion from the German government. As the situation of the Hypo Real Estate Holding AG barely improved by March 2009, it was decided to totally acquire the bank's shares. The idea was that the bank might be supervised more effectively as a State enterprise.[59] As a consequence, a statute was drafted that allowed an expropriation of shareholders.[60] Having acquired over 90 per cent of the shares of Hypo Real Estate AG after a public takeover proposal and the issue of new shares,[61] the German government initiated a squeeze-out for the remaining shareholders. The American investor J. Christopher Flowers unsuccessfully campaigned against this expropriation and finally sought legal protection before German courts.[62]

I. Affected Foreign Investment

The shareholding in the major German bank of J.C. Flowers & Co. LLC can be regarded as foreign investment.[63] Therefore the issue arises, whether the American entity, J.C. Flowers & Co. LLC, are particularly protected by foreign investment standards.

59 S. Kaiser & Antje Sirleschtov, 'Warum die HRE nicht Pleite gehen darf', *ZEIT Online*, 4 May 2009, available at http://www.zeit.de/online/2009/08/hypo-real-estate-staatshilfe/komplettansicht (last visited 26 April 2012).

60 'Act on the Rescue of Enterprises to Stabilise the Financial Market' (Gesetz zur Rettung von Unternehmen zur Stabilisierung des Finanzmarktes), 7 April 2009, [2009] BGBl. I 725, 728, Section 1.

61 'Bund kann HRE verstaatlichen', *Handelsblatt Online*, 3 June 2009, available at http://www.handelsblatt.com/unternehmen/banken-versicherungen/bund-kann-hre-verstaatlichen;2320797 (last visited 26 April 2012).

62 'Flowers macht bei HRE mit Klage Ernst', *Handelsblatt Online*, 11 October 2009, available at http://www.handelsblatt.com/unternehmen/banken-versicherungen/flowers-macht-bei-hre-mit-klage-ernst;2467652 (last visited 26 April 2012).

63 *CMS v. Argentina*, *supra* note 48, para. 51.

II. Compliance with Expropriation Standard

Investment protection between the USA and Germany is not ensured by a sole investment agreement, but by the extensive US-German Treaty concerning Friendship, Trade and Shipping of 1954.[64] Although this treaty provides court proceedings instead of arbitration, the protection of investors' properties is similar to BITs. Expropriations of foreign investors may only take place for a public purpose,[65] in a non-discriminatory way[66] and with prompt, adequate and effective compensation.[67]

1. Non-Discriminative Expropriation for a Public Purpose

The acquisition of shares in Hypo Real Estate Holding AG constituted a direct expropriation of the shares of J.C. Flowers & Co. LLC. The protection standard in question is consequently concerned. The expropriation took place in order to prevent the necessity of further aid from the German government for the private bank. Given that the public purpose of an expropriation is barely questioned,[68] the purpose to prevent further expenses is admissible. Although J. Christopher Flowers argues that there was discrimination, because Commerzbank AG, Germany's second biggest private bank, received capital from the German State without the obligation to be controlled, there is broad consensus that Hypo Real Estate Holding AG was in much worse, rather than in like circumstances.

2. Adequate Compensation

The final requirement of a lawful expropriation of J.C. Flowers & Co. LLC is therefore an adequate compensation. The compensation of shareholders was with € 1,30 per share in accordance with the market price. However, the investors purchased the shares for ten times the price. Mr. Flowers was satisfied that the share price would rise soon

64 'Treaty concerning Friendship, Trade and Shipping between the Federal Republic of Germany and the United States of America' (*Freundschafts-, Handels- und Schiffahrtsvertrag zwischen der Bundesrepublik Deutschland und den Vereinigten Staaten von Amerika*), opened for signature 29 October 1954, [1956] Bundesgesetzblatt II 487 (entered into force 14 July 1956).

65 *Id*., Section 5 (4), sentence 1.

66 *Id*., Section 5 (3).

67 *Id*., Section 5 (4), sentence 2.

68 Dolzer & Schreuer, *supra* note 14.

after there was sufficient help for Hype Real Estate Holding AG. This submission leads to the issue, how expropriated shares should be valuated, especially concerning prospects.

As pointed out by Sergey Ripinsky and Kevin Williams in a study concerning damages in international investment law, the term ‘value’ refers to the price brought by property in a fair and competitive market.[69] An active market, such as a stock exchange, is an adequate forum for such a valuation.[70] Since an existing market is the venue, where necessities, expectations and information come together, this seems reasonable. If the market already takes all the relevant aspects of a property’s price into account, why should an arbitral tribunal consider the prospect of the market price? It is the expropriated property itself that is decisive for the relevant compensation. Therefore only its prospect can be important. Since prospects of a share are already considered by the market price, there is no further need to derive from this price. Therefore, J.C. Flowers & Co. LLC was also adequately compensated and has no claim against the Federal Republic of Germany for breach of a standard of investment protection.

F. Stimulus Packages

From fall 2008 onwards, the global financial crisis soon developed into an economic crisis. Facing recessions, numerous States announced stimulus packages for their economies. Since these are especially targeted at domestic economies, they are likely to discriminate against foreign investors and thus enable them to claim damages for breach of the national treatment standard.

I. Measures Adopted

Soon after the breakdown of Lehman Brothers Inc. and the prospect of a decrease in economic growth, European states adopted economic stimulus packages in order to bolster their economies. Germany was one of the first countries to spent approximately € 100 billion on benefits for households, infrastructure, company support and environmental measures. The first enormous stimulus package was announced in November 2008 by China, which intended to spend more than $ 580 billion on a wide area of national

69 S. Ripinsky & K. Williams, *Damages in International Investment Law* (2008), 182.

70 *Id.*, 189.

infrastructure and social welfare programs.[71] This amount was even outnumbered by Barack Obama's plan from early 2009 to spend $ 787 billion on programs for infrastructure, renewable energy projects, education and tax reductions.[72]

II. Affected Foreign Investments

Aiming at their domestic economies in general, the economic stimulus packages also concern foreign investments.

III. Compliance with National Treatment Standard

1. Breach of the Standard

Depending on the public procurement practice in each particular State, foreign and local investors may be treated differently. This depends on each case as a matter of fact. However, even if foreign and national investors are not treated alike, they have to be in like circumstances for a breach of the national treatment standard to occur.

As with the bailout of financial institutions, public policy reasons could distinguish apparently similar investors. In regard of the enormous costs of the stimulus packages, governments have a high interest in the benefit of their domestic enterprises and population. Nevertheless, the situation appears to be a different than the situation of the bailout of financial institutions: Whereas the aim of the rescue packages for banks was to immediately stabilize them, economic stimulus packages are not designed for primary beneficiaries, but to initiate a constant process of economic activity. If the primary beneficiary of a construction project, for example, is a foreign investor, this initiation can be just as useful. Since the nationality of an investor has no influence on its employees and suppliers, the benefit of a project cannot be directed by the nationality of the primary beneficiary.

In addition, since the targets of economic stimulus packages are not the primary beneficiaries, there is no practical need, as in the bailout of

[71] B. Barboza, 'China plans $ 586 billion economic stimulus', *The New York Times Online*, 9 November 2008, available at http://www.nytimes.com/2008/11/09/business/worldbusiness/09iht-yuan.4.17664544.html?_r=1 (last visited 26 April 2012).

[72] 'Economic Stimulus', *The New York Times Online*, available at http://topics.nytimes.com/top/reference/timestopics/subjects/u/united_states_economy/economic_stimulus/index.html (last visited 26 April 2012), para. 16.

banks, for every State to concentrate on its domestic enterprises. In the contrary, the protective measures for the national economy may even have a negative influence on the overall economic growth as the national focus during the world economic crisis after 1929 revealed.[73]For these reasons, there are no public policy grounds for not declaring foreign and national investors to be in like circumstances concerning stimulus packages. Only in circumstances of a domestic investor's exceptional importance for the domestic industry, could there be a justification. Therefore, the national treatment standard will be breached, if foreign investors are treated differently when applying for stimulus projects.

2. Justification of a Potential Breach

This breach could however be justified. As Hermann Ferré and Kabir Duggal recently proposed, treaty obligations under BITs and FTAs might have been temporarily suspended during the Global Financial Crisis. The argument derives from Art. 62 S. 1 Vienna Convention on the Law of Treaties.[74] The article mentioned provides a withdrawal from a treaty if essential circumstances have changed and transformed the extent of obligations.[75] However, even if such an argument might be basically followed, the extent of the obligation at issue has not been affected. As shown above, in the particular situation of economic stimulus packages there was no essential necessity to privilege primarily domestic investors. Hence, a potential breach will not be justified. As it is an accepted principle that treaty breaches give rise to damages,[76] foreign investors could therefore claim damages.

73 See further A. J. Schwartz, 'Understanding 1929-1933' in K. Brunner (ed.), *The Great Depression Revisited* (1981), 1, 21-24.

74 *Vienna Convention on the Law of Treaties*, opened for signature 23 May 1969, 1155 UNTS 331 (entered into force 27 January 1980) (Vienna Convention).

75 H: Ferré & K. Duggal, 'The world economic crisis as changed circumstance', *Columbia FDI Perspectives*, No. 43 1 August 2011, available athttp://www.vcc.columbia.edu/files/vale/print/Ferre_and_Duggal_-_1_Aug_2011_FINAL.pdf (last visited 26 April 2012), para. 5.

76 *Case Concerning the Factory at Charzów (Merits) (Germany v. Poland)*, [1928] Publications of the Permanent Court of International Justice A17, 47; *CMS v. Argentina*, *supra* note 48, para. 410.

G. Conclusion

As the observation of exemplary measures that have been adopted to cope with the financial crisis shows, it will be difficult for disadvantaged foreign investors to sue their Host States. Most measures have appeared to be in accordance with standards of investment protection. Although the bailouts of financial institutions were nationally focused, this seems to be justified by public policy reasons. So was the refusal of help for Lehman Brothers Inc. by the US government. J. Christopher Flower's investment fund has been adequately compensated, when the German government lawfully expropriated its shares. The only remaining prospect of claims of foreign investors concern the States' handling of economic stimulus packages. If these packages prove to be solely for the benefit of domestic businesses, foreign investors will have possibilities to claim damages for breach of the national treatment standard.