THE GLOBAL FINANCIAL CRISIS AND INTERNATIONAL ECONOMIC LAW

ANNE VAN AAKEN* AND JÜRGEN KURTZ+

EXECUTIVE SUMMARY

Economists and political scientists have begun to isolate the causes and implications of the spread of the global financial crisis in late 2008. Critical attention – often accompanied by strident disagreement – has also focused on the efficacy of various domestic plans implemented in response to the crisis. International lawyers have contributed little to these debates. Our analysis aims to partly redress this gap by examining whether and how international economic law might act as a credible constraint on state tendencies towards domestic preference when formulating emergency responses to the crisis.

We begin by offering a typology of the typical emergency measures implemented by states that are at the greatest risk of breaching commitments under international economic law. Our focus here is not on classic embodiments of protectionism, such as increases in tariffs and the resort to unjustifiable trade remedies (especially anti-dumping measures). We examine instead the tendencies towards nuanced forms of preference, embedded within regulatory responses to the crisis. This covers, for example, governmental provision of liquidity support, purchase of banking assets, inter-bank (wholesale) lending activities and increases in retail deposit guarantees. There is considerable evidence of discrimination directed at foreign investors operating in the finance sector, across a range of these emergency interventions.

The question we then address is whether international economic law will operate to constrain these nuanced forms of protectionism. International economic law comprises a variety of sources, most notably commitments on trading relations (especially under the World Trade Organization) and the treatment of foreign investors. We argue that international investment law is, in the short-term, more likely than any other area of international economic law to give rise to complaint and initiation of legal action. There are three critical factors that might trigger international investment litigation where states have regulated in a discriminatory fashion against foreign investors in the aftermath of the crisis. First, the scope of most investment treaties is typically broader than instruments of trade law (and especially the WTO). This is particularly apparent in the relative absence of exceptions for state conduct under most investment treaties, compared to the detailed and elaborate carve-outs in the WTO. Second, the right to initiate a WTO dispute is vested only in states that are members of the WTO. This has important limiting effects in the context of the current crises as states may rationally refrain from invoking their legal rights against each other given their own (discriminatory) attempts to respond to the crisis and the possibility of attracting retaliatory litigation. Investment treaties displace this default position by conferring standing on a private party, foreign investors of a signatory state. The foreign investor has the right to initiate action against a host (signatory) state in a range of institutional fora, including the

* Max-Schmidheiny Tenure Track Professor of Law and Economics, Public Law, International and European Law at the University of St. Gallen, Switzerland, Guisanstrasse 36, CH-9010 St. Gallen, Email: anne.vanaaken@unisg.ch.

+ Director, International Investment Law Research Programme, Institute for International Law and the Humanities, University of Melbourne Law School, Australia. Email: j.kurtz@unimelb.edu.au.
World Bank’s Convention on the Settlement of Investment Disputes Between States and Nationals of Other States (ICSID). There is thus no political filter at play in this system; a foreign investor will consider only the commercial imperatives for initiating action and there is no possibility for the state party to retaliate through cross-claim or invocation of the system. Third and perhaps most crucially, international investment law is characterized by a range of hard, enforceable remedies adding further incentive to commencement of international litigation. In investment arbitration, the remedy nearly always consists of monetary compensation for loss suffered by the foreign investor. Significant monetary awards have been issued against states under this system, including Argentina who was found to be in breach of investment treaty obligations in the aftermath of its 2001-2 financial crisis.

Even with these institutional differences in mind, there is still the question of whether the surveyed forms of discrimination are likely to constitute breach of particular investment treaty commitments. We focus on two key treaty obligations being the specific protection against discrimination of foreign investors in the obligation of national treatment, as well as the broader guarantee of fair and equitable treatment. Both of these legal obligations have been the subject of varying and sometimes conflicting interpretation by adjudicatory tribunals. We find a strong case for breach of the obligation to accord national treatment and a possible (but far weaker) case on the guarantee of fair and equitable treatment. We conclude by surveying the remote possibility that states might escape liability through prudential carve-outs and security exceptions in operative treaty instruments.
I. Introduction

Economists and political scientists have begun to isolate the causes and implications of the spread of the global financial and economic crisis in late 2008. Critical attention – often accompanied by strident disagreement – has also focused on the efficacy of various domestic plans implemented in response to the crisis. International lawyers have contributed little to these debates. Our analysis aims to partly redress this gap by examining whether and how international economic law might act as a credible constraint on state tendencies towards domestic preference when formalizing emergency responses to the crisis.

International economic law comprises a variety of sources, most notably commitments on trading relations and the treatment of foreign investors. The former – international trade law - encompasses bilateral free trade agreements, regional instruments such as the North American Free Trade Agreement and the multilateral World Trade Organization (WTO). In comparison, the latter – international investment law – is largely confined to a network of bilateral investment treaties but also includes key aspects of customary international law.

We believe that international investment law is, in the short-term, more likely than any other area of international economic law to give rise to complaint and initiation of legal action. This may, in turn, act as some constraint against the protectionist tendencies evident across state responses to the crisis. There are three critical factors that might trigger international investment litigation where states have regulated in a discriminatory fashion against foreign investors in the aftermath of the crisis. First, the scope of most investment treaties is typically broader than instruments of trade law (and especially the WTO). This is particularly apparent in the relative absence of exceptions for state conduct under most investment treaties, compared to the detailed and elaborate carve-outs such as the prudential exception in the Annex on Financial Services of the WTO General Agreement on Trade in Services. Second, in traditional systems dispute settlement at international law (such as in the WTO), the right to initiate a dispute is vested only in state signatories to the relevant treaty. This has important limiting effects in the context of the current crises as states may rationally refrain from invoking their legal rights against each other given their own (discriminatory) attempts to respond to the crisis and the possibility of attracting retaliatory litigation.\(^1\) Investment treaties

\(^1\) Although the Brazilian Foreign Minister Celso Amorim said that Brazil may challenge the legality of a "Buy American" clause in the recently approved U.S. economic stimulus package at the World Trade Organization,
displace this default position by conferring standing on a private party, foreign investors of a
signatory state. The foreign investor has the right to initiate action against a host (signatory)
state in a range of institutional fora, including the World Bank’s Convention on the
Settlement of Investment Disputes Between States and Nationals of Other States\(^2\) (ICSID).
There is thus no political filter at play in this system; a foreign investor will consider only the
commercial imperatives for initiating action and recouping loss caused by state conduct and
there is no possibility for the state party to retaliate through cross-claim or other invocation of
the system. Third and perhaps most crucially, international investment law is characterized
by a range of hard, enforceable remedies adding further incentive to commencement of
international litigation. In investment arbitration, the remedy nearly always consists of
monetary compensation for loss suffered by the foreign investor. Significant monetary
awards have been issued against states under this system, including Argentina who was found
to be in breach of investment treaty obligations in the aftermath of its 2001-2 financial crisis.\(^3\)

We begin our analysis in the next Part II by offering a typology of the typical emergency
measures implemented by states to date that are at the greatest risk of breaching commitments
under international economic law. We focus here on the early evidence of discrimination
directed at foreign investors in the financial sector in the emergency plans of a number of
developed states. These varied forms of discrimination are highly likely to constitute breach
of obligations of states under international investment law. To fully contextualize our
analysis, we briefly consider in Part III select areas of international trade law. Our primary
focus is, however, international investment law which we turn to in Part IV. There we review
the various forms and sources of international investment law including treaties of friendship
commerce and navigation, bilateral investment treaties (BITs), customary international law
(CIL) as well as the OECD National Treatment Instrument. We identify potential violations
of investment law norms across the different categories of surveyed measures. We focus here
on two key treaty obligations being the specific protection against discrimination of foreign
investors in the obligation of national treatment, as well as the broader guarantee of fair and
equitable treatment. We also assess the remote possibilities of escaping liability through

---

\(^2\) Covenant on the Settlement of Investment Disputes between States and National of Other States, signed in

\(^3\) UNCTAD, Latest Developments in Investor-State Dispute Settlement, IIA Monitor No. 1, 10 (2008) (detailing
that, in 2007 alone, five investment tribunals awarded foreign investors a total of US$615 million in damages
against Argentina).

---
prudential carve-outs and security exceptions in (some) BITs or CIL. Part V ties these lines of inquiry together and concludes.

II. A Typology of Emergency Measures taken by States

States have taken different measures in order to save their financial sector and to mitigate the economic downturn. Almost all of those measures were introduced in a very short time period and are often subject to continuing changes. Many measures are codified in law but delegate significant discretion to the executive branch. As these laws are often imprecise and without implementing regulation, the regulatory landscape resembles a “moving target”. Nevertheless, we will try to categorize the most frequently taken measures with specific relevance to state commitments under international economic law.

These emergency measures can be grouped into three broad categories: 1) measures designed to bolster the stability of the financial services industry; 2) measures directed at the financial services industry but structured to increase the availability of credit to other sectors of the economy; 3) measures targeting select and strategic industries (including the automotive industry). We set out below an analysis of individual state measures highlighting evidence of discrimination against foreign actors before examining whether and how this might attract liability under international economic law.

1. Category 1: Measures Directed at the Financial Services Industry

The extensive measures undertaken in this first category are designed to increase the confidence of various market participants and to ensure the continuation of bank funding. They encompass liquidity support, recapitalisation (through nationalisation or otherwise), purchase of specific assets (including “toxic” bank assets), inter-bank (wholesale) lending guarantees and increases in retail deposit guarantees. We find firm evidence of discrimination directed at foreign investors across these various state measures.

---

Australia, for example, introduced an insurance scheme both for retail deposits and wholesale lending in early October 2008. The coverage of both guarantees was initially limited to Australian-owned banks and credit unions and Australian incorporated subsidiaries of foreign institutions. Branches of foreign banks – such as Citibank, Credit Suisse and UBS – were excluded from the insurance scheme. This exclusion triggered flight of wholesale capital from foreign bank branches to domestic guaranteed institutions. Australia is not alone in building adverse incentives for regulatory arbitrage in this area. Ireland has also temporarily guaranteed deposits, covered bonds, senior and dated subordinated debt but only in the six biggest banks of that country, reportedly leading to shifts in deposits to the perceived safety of those guaranteed institutions.

Germany has established a fund to stabilize the financial market by overcoming liquidity shortages and by creating framework conditions for strengthening the capital base of financial institutions. The Act covers only financial institutions with their seat in Germany, thereby excluding foreign branch operations. It enables the executive to take various measures, inter alia, to assume liabilities accrued by financial-sector enterprises up to an amount of 400 billion Euro and to guarantee liabilities of special purpose vehicles which have assumed risk positions of a financial-sector enterprise. Furthermore, the fund may recapitalize financial-sector firms by acquiring shares or silent participations. It may also overtake risk positions, that is, buy toxic assets, such as receivables, securities, derivatives, rights and obligations from loan commitments. Finally, the Federal Administrative Court is the first and last instance court that can adjudicate on disputes under the Act (except measures with constitutional implications).

The program in the United Kingdom has a broader scope by covering subsidiaries of foreign institutions (as authorized deposit takers). In contrast, Switzerland has elected to only bail-out specific institutions taken to be of systemic importance for the financial place.

---

5 Financial Systems Legislation Amendment (Financial Claims Schemes and Other Measures) Act 2008 (Cth); Banking Amendment Regulations 2008 (No.1) (Cth).
9 Sec. 6 para 1of the Financial Market Stabilization Act.
10 Sec. 7 para 1of the Financial Market Stabilization Act.
11 Sec. 8 para 1of the Financial Market Stabilization Act.
12 Sec. 15 of the Financial Market Stabilization Act.
Switzerland. To date, the benefits of this ad hoc program have only been extended to a national bank – UBS - with a promise to do the same for another, Credit Suisse.

Finally, the position under U.S. law and practice is more nuanced. Early proposals put forward by Secretary of Treasury Henry Paulson excluded foreign banks from the coverage of the U.S. bailout plan. Following concerted lobbying, the Emergency Economic Stabilization Act of 2008 now authorizes purchase of distressed assets (especially mortgage-backed securities) in financial institutions if they have “significant operations” in the U.S. The face of the Act then allows for the possibility of foreign bank participation in the U.S bailout scheme. This absence of formal differentiation though should be seen in light of the significant discretion vested in the Treasury Department under the Act. Early reports suggest that domestic U.S institutions are the majority if not exclusive recipients of capital injections under the scheme. Similarly, the “Public-Private Investment Programme” within the Troubled Assets Relief Program foresees the buying of “toxic assets” up to 1 trillion USD but also limits access to institutions with “significant operations” in the US. If this trend continues, there may be differentiation against foreign institutions as a matter of fact, even if not on the face of the law.

2. Category 2: Conditional Measures – Provision of Credit

The second type of measures also addresses the banking industry but is meant to foster credit to the non-financial industry. The UK as well as Germany stress in their bail-out plans that the provision of credit to national industry, especially SMEs is one of the conditions to be imposed on banks if they take the benefit of the type 1 measures. Given scarce credit availability, lending to foreign industry may well be restricted. In Switzerland, the Swiss

---

14 Botschaft zu einem Massnahmenpaket zur Stärkung des schweizerischen Finanzsystems of November 5, 2008, at 8969. They are well aware of the creation of competitive disadvantages (also of Swiss banks in other countries) but maintain that supporting measures are only available to Swiss banks.
15 Public Law 110-343.
17 The development of bond prices of those institutions receiving aid by the state show the immediate effect – their prices go up. This might well be used as a proxy for refinancing costs, crucial for competitive conditions of the market.
18 HM Treasury, Statement to the House of Commons on Bank Lending, January 19th, 2009: „support small and medium businesses“; „The government could now own up to 70 per cent of RBS (Royal Bank of Scotland). In return for this, we have agreed with them an extension of lending commitments to large companies, and an increase in lending over £6bn in the next 12 month….These agreements will be specific – covering both the quantity and the type of lending made available to people and businesses across the country….“
19 Sec. 10 para 2 (1). Financial Market Stabilization Act.
Federal Banking Commission (SFBC) has agreed with Credit Suisse and UBS to raise current capital adequacy requirements by 2013. The banks will have to comply with a leverage ratio in addition to their risk-based capital adequacy requirement but critically, domestic lending activities are exempted from the leverage ratio. This exemption for domestic lending activities sets strong incentives for preferring domestic debtors and potentially shifts available credit away from foreign firms. These various biases towards domestic lending also have a broader spillover effect. Developing countries now face a severe financing shortfall as investors (including foreign banks) pull resources out of emerging markets to either meet home country conditions or take advantage of lower risk, newly guaranteed markets in developed states.

3. Category 3: Measures Targeting “Strategic” Sectors

The third category of measure is the most recent and targets strategic industry sectors. In the U.S for instance, there are proposals to limit production subsidies for the automotive sector to sites that have been in operation for at least twenty years. This condition has the effect of confining those subsidies to the ‘Big Three’ American automakers (along with one production facility maintained by Toyota in California) since all other production sites of foreign carmakers have been in operation for less than twenty years. Such differential effect may constitute impermissible discrimination under international investment law if foreign car makers who have invested in the U.S do not – as a class – qualify for those subsidies.

---

20 The leverage ratio defines the proportion of core capital to total assets and it will be set for both banks at a minimum of 3% at group level and at 4% for the individual institutions.
23 “Energy Independence and Security Act of 2007”; SEC. 136. ADVANCED TECHNOLOGY VEHICLES MANUFACTURING: INCENTIVE PROGRAM. (g) PRIORITY.—The Secretary shall, in making awards or loans to those manufacturers that have existing facilities, give priority to those facilities that are oldest or have been in existence for at least 20 years. Such facilities can currently be sitting idle.”
24 Measures like car premiums to buy new cars are not discriminatory if they do not put any conditions on the origin of the new car, as is done by Germany, see http://www.bafa.de/bafa/de/wirtschaftsfoerderung/umweltpraemie/index.html
Furthermore, the recently passed U.S stimulus package - the American Recovery and Reinvestment Act of 2009 (ARRA)\textsuperscript{25} – forbids the use of public funds for projects involving public works “unless all of the iron and steel used in the project is produced in the United States”.\textsuperscript{26} Similarly, Sec. 604(a) of that Act provides that “(e)xcept as otherwise provided ..., funds appropriated or otherwise available to the Department of Homeland Security may not be used for the procurement of [specified items of clothing or equipment] if the item is not grown, reprocessed, reused, or produced in the United States”. These measures have been amended - at the insistence of President Obama in the face of threatened trade litigation - so that they “shall be applied in a manner consistent with United States obligations under international agreements”.\textsuperscript{27} Even with this legal amendment, there is evidence that the actual implementation of this program continues to preference government purchases of domestically-produced goods.\textsuperscript{28}

III. Potential Violations of International Trade Law

International trade law comprises the multilateral treaty instruments of the WTO as well as a variety of bilateral and regional trade agreements. We expect this body of treaty law to act as a firm limit on resort to traditional and identifiable forms of protectionism, such as increases in tariffs above bound levels and resort to unjustifiable trade remedies (especially anti-dumping measures). It is far more difficult to predict the likely influence of trade law on the nuanced forms of protectionism surveyed in Part II above. This is both due to the hidden or embedded nature of the discrimination practiced and the complexity of the trade instruments in question. We identify below some of these complexities in two key instruments, being the WTO General Agreement on Trade in Services (GATS) and the WTO Agreement on Subsidies and Countervailing Measures (SCM). These are not the only WTO commitments that might apply\textsuperscript{29} nor is our analysis intended to be comprehensive. The next part distills a set of critical issues surrounding the application of these WTO instruments as part of a comparative exercise to identify the potentially broader scope of operation of international investment law, dealt with in Part IV.

\textsuperscript{25} Public Law 111-5, signed into law by President Obama 17\textsuperscript{th} Feb. 2009.
\textsuperscript{26} Sec. 1605(a).
\textsuperscript{27} Sec. 1605(d) and Sec. 604(k).
\textsuperscript{28} See Simon Evenett, The Devil is in the Details: The Implementation of Stimulus Packages and their Effects on International Commerce, in this compilation.
\textsuperscript{29} Two further possible candidates include the plurilateral WTO Agreement on Government Procurement and the Agreement on Trade-Related Investment Measures
As a start point, the GATS Agreement is relevant for the category 1 and 2 measures that intervene in the financial services industry. The GATS covers measures that affect “trade in services”, which is defined to include provision of a service through commercial presence. This can encompass foreign investment in the banking and finances sector, regardless of the form and organization of the investment vehicle. The national treatment Article XVII of the GATS enjoins discrimination directed at foreign services and foreign services suppliers. There are, however, a series of limiters that might constrain the likelihood of a dispute being brought before the WTO based on these GATS provisions. For one thing, specific commitments – including the national treatment Article XVII – only apply if a WTO member state has chosen to list the financial services sector as subject to those commitments. Even if this requirement is satisfied, there is a specific Annex on Financial Services in the GATS that preserves the ability of States to adopt and maintain measures for prudential reasons, including those for the stability of the financial system. This exception may offer a safe harbour for those state measures (such as the Swiss intervention) that are justified publicly on systemic and stability grounds.

Secondly, the various guarantees and government benefits in the category 1 to 3 measures may potentially violate the disciplines on the provision of domestic subsidies in the WTO SCM Agreement. A “subsidy” is defined as encompassing four basic elements: (i) a financial contribution, (ii) by a government or any public body within the territory of a Member, (iii) those are, e.g., grants, loans, equity infusions, loan guarantees, fiscal incentives, the provision of goods or services, the purchase of goods.

---

30 See Art. XXVIII (d) GATS: “commercial presence” means any type of business or professional establishment, including through (i) the constitution, acquisition or maintenance of a juridical person, or (ii) the creation or maintenance of a branch or a representative office, within the territory of a Member for the purpose of supplying a service.”

31 Annex on Financial Services, para 2 (a): “Notwithstanding any other provisions of the Agreement, a Member shall not be prevented from taking measures for prudential reasons, including for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system. Where such measures do not conform with the provisions of the Agreement, they shall not be used as a means of avoiding the Member’s commitments or obligations under the Agreement.”

32 One should bear in mind however that the prudential exception is limited by certain good faith requirements including that “such measures shall not be used as a means of avoiding the Member’s commitments or obligations under the Agreement”. Ibid. This exception has not been adjudicated in the case law but the good faith qualifications are similar to parts of the chapeau to GATT Article XX. On this latter point, see Eric Leroux, Trade in Financial Services under the World Trade Organisation, 36 Journal of World Trade 2002, pp. 413-442, 430 et seq.

33 This applies not only to measures of national governments, but also to measures of sub-national governments and public bodies such as state-owned companies. If newly nationalized banks give credit to domestic firms which they would not have obtained otherwise in the market, these actions would be included. Furthermore, Art. 1.1. SCM Agreement distinguishes between direct and indirect subsidies. In the latter the funds are channeled through private institutions, thus a link to a government agency needs to be found. Type II measures could constitute indirect subsidies.
which confers a benefit\(^\text{35}\) (iv) to a specific recipient.\(^\text{36}\) All of these elements must be satisfied in order for a subsidy to exist. The SCM Agreement distinguishes between prohibited and actionable subsidies.\(^\text{37}\) Prohibited subsidies are those which are conditional on export performance or upon local content requirements\(^\text{38}\), while actionable subsidies require a complaining country to prove that the measure has caused it “adverse effects” (which includes material injury to domestic industry or serious prejudice to the state’s interests)\(^\text{39}\). Depending on implementation, some of the benefits and guarantees extended by states responding to the crisis might constitute actionable subsidies. There are strategies however by which states can protect themselves from liability in this area. For example, measures which target consumption (and not production) leaving consumers free to choose the goods and services that they purchase, are unlikely to violate the SCM Agreement.\(^\text{40}\)

Under the SCM Agreement, a country can use the WTO’s dispute-settlement procedure to seek the withdrawal of the subsidy or the removal of its adverse effects (the multilateral avenue). Alternatively, the country can launch its own investigation and charge extra countervailing duty on subsidized imports that are found to be hurting domestic producers (the unilateral avenue).\(^\text{41}\) To do so, a member state must show the existence of a subsidies scheme, an injury to its domestic industry producing a like product and a causal link between the two. A threat of injury suffices for a lawfully imposed countervailing duty.\(^\text{42}\) There may however be important extra-legal and political economy factors that restrain use of these legal avenues. There is widespread use of subsidies in the various emergency measures adopted by a significant proportion of the WTO membership. A choice of a given member to initiate either a WTO complaint or a unilateral response might in turn trigger retaliatory action on the part of the targeted state. This potential for reciprocity of legal action inherent in international

\(^{35}\) Often the existence of a benefit and its valuation will be clear. This is especially the case in the Type 1 Measures. In case of doubt, the Appellate Body uses the private investor test, that is, the existence of a benefit is to be determined by comparison with the market-place (i.e., on the basis of what the recipient could have received in the market); see Canada – Aircraft, WT/DS70, Report of the Appellate Body.. Art. 14 SCM Agreement provides some guidance with respect to determining whether certain types of measures confer a benefit.

\(^{36}\) There are four types of “specificity” within the meaning of the SCM Agreement, of which two are of interest here: (i) enterprise-specificity where a government targets a particular company or companies for subsidization; or (ii) industry-specificity where a particular sector or sectors is targeted for subsidization.

\(^{37}\) Non-actionable subsidies no longer exist, Art. 8 SCM Agreement. They included subsidies for environmental purposes, to make up for regional inequalities, and the promotion of R&D. They were included on a provisional basis for five years ending 31 December 1999, (Art. 31 SCM).

\(^{38}\) A detailed list of export subsidies is annexed to the SCM Agreement;

\(^{39}\) Art. 5-6 SCM Agreement.

\(^{40}\) Report to the TPRB, supra note 4, para 8.

\(^{41}\) Those forms of relief may not be used simultaneously. See footnote 35 to the SCM Agreement.

trade law is largely absent in international investment law. Investment treaties instead confer standing on foreign investors (of a signatory state) to bring legal action against another signatory state and there is no possibility for retaliation by the targeted state. This critical difference may leave investment treaties as the most likely and promising forum to challenge discriminatory state measures.

IV Potential Violations of International Investment Law

We now turn to the likely implications that might flow under international investment law from these various differentiations between foreign and domestic actors. It is difficult to formulate a single answer given the heterogeneity of the legal instruments in the field. There are, for instance, important textual differences in the formulation of key protective norms, such as “national treatment” and “fair and equitable treatment”. Moreover, certain investment treaties include exceptions for national security and prudential regulation, while these are absent in other instruments. Last, but not least, the jurisprudence on the relevant norms is often fractured and conflicting, which may again impact on a given reading. With these factors in mind, we set out below a survey of the key forms of international investment law.

1. OECD National Treatment Instrument

We will deal first with the OECD National Treatment Instrument. This forms part of the OECD Declaration on International Investment and Multinational Enterprises together with an OECD Council Decision obliging adhering countries to notify their exceptions to the Instrument.

The OECD Instrument defines national treatment as the “commitment by a country to treat enterprises operating on its territory, but controlled by the nationals of another country, no

---

43 Adhering to it are the thirty OECD member countries and eleven non-member economies: Argentina (22 April 1997), Brazil (14 November 1997), Chile (3 October 1997), Egypt (11 July 2007), Estonia (20 September 2001), Israel (19 September 2002), Latvia (9 January 2004), Lithuania (20 September 2001), Peru (25 July 2008), Romania (20 April 2005) and Slovenia (22 January 2002).

44 Although the Instrument is not binding, states have consented to a procedure of notification and negotiation of their exceptions, thus fostering transparency. The exceptions are periodically examined by the Investment Committee. These examinations result in a decision by the OECD Council, which formulates proposals for action by the country concerned. The results of the examinations are published in the series OECD Reviews of Foreign Direct Investment. Typically, the exceptions cover sectors like mining, transport, fisheries, broadcasting and telecommunications as well as real-estate. Exceptions to national treatment cannot be found in the banking sector concerning stabilizing measures, just as there are no exceptions concerning state aid for finance and automotive sectors.
less favourably than domestic enterprises in like situations\textsuperscript{45}. The exceptions to be notified are classified and encompass mechanisms like “official aids and subsidies”, “government purchasing” and “access to local finance”. Differential treatment of national and foreign investors concerning state aid and government procurement thus seem to be accepted by the OECD states (together with eight non-member countries) as contrary to the National Treatment Instrument.\textsuperscript{46}

With this in mind, the explicit differentiations based on nationality evident throughout categories 1 to 3 are likely to violate the Instrument. A notification of exceptions now, would also breach a standstill agreement.\textsuperscript{47} These breaches will not give rise to justiciable disputes, as the instrument is non-binding. Investors must rely on their home countries to raise these issues in the OECD Investment Committee. The Instrument is, however, likely to have a broader impact than this initial modest output. It may well inform a common understanding of the OECD states (and the eight non-member countries) of the scope of national treatment protection, as the wording of the OECD Instrument is almost identical to many investment treaty formulations. Indeed, the Instrument has been pivotal in a number of investor-state cases in guiding the interpretative choices of arbitral tribunals, which we examine later in the paper.\textsuperscript{48}

\textbf{2. Treaties of Friendship, Commerce and Navigation}

Most modern bilateral investment treaties (BITs) are signed between developed and developing states. On first view, this typical country pairing might preclude claims by foreign investors of OECD states against other OECD countries, even though a significant proportion of global financial transactions take place within the OECD grouping. There are however two possibilities that might allow for a claim by this class of investor against an OECD state. First, an investor of an OECD state may partly structure their business operations through a

\textsuperscript{46} To put this slightly differently, as these measures would be a violation of the Instrument, member states would be obliged to notify them as exceptions.
\textsuperscript{47} In 1988, an unanimous pledge of all adhering countries to refrain from introducing new exceptions (“standstill pledge”).
\textsuperscript{48} For example, see SD Myers, Inc. v Canada, UNCITRAL Award under the NAFTA (13 November 2000, at para 248; Pope & Talbot Inc v Canada, UNCITRAL Award under the NAFTA (10 April 2001), at para 78 (and footnote 73)
developing country to take advantage of select BIT protections. Secondly, older investment commitments – including Friendship, Commerce and Navigation treaties (FCN) – remain in operation across a range of OECD states. For example, the U.S has FCN treaties in operation with both Germany and Japan. These treaties usually allow disputes to be brought before the International Court of Justice and, at least in the case of the U.S, may be self-executing as a matter of U.S constitutional law giving investors of a state party the ability to initiate claims before U.S courts. This latter aspect may be particularly pertinent for (German and Japanese) foreign investors who are excluded from the “Buy American” procurement conditions of the American Recovery and Reinvestment Act 2009 as it offers them a potential avenue of compliant within the U.S judicial system. The primary FCN provision involved in actions of this sort would be the obligation of national treatment, a norm shared with modern investment treaties. We examine that legal obligation of non-discrimination more fully in the next part.

3. International Investment Agreements

There are approximately 2800 bilateral and regional investment treaties (including investment chapters in free trade agreements) in operation across the globe. The ability of an investor to

49 While this is a commonly accepted strategy within the jurisprudence, it has occasionally elicited criticism by arbitral tribunals. For example, see Phoenix Action, Ltd. v Czech Republic, ICSID Case No. ARB/06/5, Award (15 April 2009).

50 After the Second World War, the so-called Modern FCN Treaty Series contained provisions on MFN status and national treatment, but also on the protection from expropriation without prompt, adequate, and effective compensation, see Andreas Paulus, Treaties of Friendship, Commerce and Navigation, Max Planck Encyclopedia of Public International Law available at: www.mpepil.com.


52 Signed at Tokyo April 9, 1953, entered into force October 30, 1953.

53 As, e.g. Case concerning Elettronica Sicula S.p.A (ELSI) (United States of America v Italy) [1989] ICJ Rep 15.


55 For example, Art. Article XVII of the Japan-US FCN treaty provides:

1. Each Party undertakes (a) that enterprises owned or controlled exclusively by its Government, and that monopolies or agencies granted exclusive or special privileges within its territories, shall make their purchases and sales involving either imports or exports affecting the commerce of the other Party solely in accordance with commercial considerations, including price, quality, availability, marketability, transportation and other conditions of purchase or sale: and (b) that the nationals, companies and commerce of such other Party shall be afforded adequate opportunity, in accordance with customary business practice, to compete for participation in such purchases and sales. 2. Each Party shall accord to the nationals, companies and commerce of the other Party fair and equitable treatment, as compared with that accorded to the nationals and commerce of any third country, with respect to: (a) the governmental purchase of supplies, (b) the awarding of concessions and other government contracts, and (e) the sale of any service sold by the Government or by any monopoly or agency granted exclusive or special privileges.

56 UNCTAD, Recent Developments in International Investment Agreements, IIA Monitor No. 3 2, 6-7 (2007).
successfully initiate and conclude a claim under any part of this extensive network of investment treaties will, however, depend on three key issues.

First, both the claimant and the measure in question must fall within the jurisdiction and scope of operation of the treaty instrument. On this fundamental question, we find a critical difference between U.S investment treaty practice and those of other states. Most U.S treaties – including the investment Chapter 11 of the NAFTA – exclude the provision of “subsidies or grants” from the scope of national treatment protection. In contrast, the investment treaties of other states such as Germany and the U.K contain no such exclusion. This would, on first view, appear to offer some protection for the U.S against potential complaint by foreign investors for exclusion from the provision of U.S government benefits. It is important however to reiterate that this is only a limited exclusion. It does not prevent claims based on other provisions (such as the fair and equitable standard).

A second fundamental issue requires identification of the key substantive obligations of investment treaties that might be breached by the measures surveyed above. We examine this in Parts 3(a) and (b) below and confine our analysis to two key obligations being the requirement that states accord both “national treatment” and “fair and equitable treatment” to foreign investors. Select and larger-scale nationalization of shares in banks may also raise issues surrounding investment treaty guarantees of compensation in the event of expropriation.

Finally, there is the issue of whether an exception might apply to shield state conduct from liability under an investment treaty. Some BITs contain carve outs for certain sectors or explicitly allow for prudential regulation of the finance sector. Furthermore, some instruments contain national security clauses which might also be invoked as an exception. We examine these various but limited exceptions in Part 3(c) below.

(a) National Treatment

---

58 See, for example, the model German and UK BITs extracted in Campbell McLachlan, Laurence Shore and Matthew Weiniger, International Investment Arbitration: Substantive Principles 2007, at pp. 379-385 and 417-422.
National treatment proscribes “less favourable treatment” of a foreign investor that stands “in like circumstances” or in “like situations” with a domestic actor. There are three critical interpretative questions that have occupied arbitral tribunals in interpreting this obligation of non-discrimination. First, when will a foreign investor stand “in like circumstances” or “in like situations” with a domestic actor? Second, what will constitute “less favourable treatment” of a foreign investor? Thirdly and perhaps most critically, is adverse purpose on the part of the regulating state required as a condition of breach and if so, what indicia should be used to evidence or construct such purpose?

As a start point, most of the early cases – including SD Myers v Canada (NAFTA, 2000), Pope & Talbot v Canada (NAFTA, 2001), Feldman v Mexico (NAFTA, 2002); and ADF v USA (NAFTA, 2003) – endorse some form of competition as a condition of likeness in a national treatment inquiry. Under this line of reasoning, a foreign investor will be “like” a competing domestic investor. This jurisprudential line is disrupted by the awards in Occidental v Ecuador (U.S-Ecuador BIT, 2004) and Methanex v U.S (NAFTA, 2005). The Occidental Tribunal adopted a much broader approach by ruling that a foreign investor involved in oil exports was “like” domestic companies exporting non-oil related goods such as flowers and seafood products. The broad Occidental test remains largely an outlier in the jurisprudence, with only one later case adopting other parts of that award. The later Methanex Tribunal also opposed a role for competition in a likeness inquiry but offers a much narrower approach requiring identification of an “identical” comparator to the foreign investor. This narrow test also has not found reflection in later case-law, which has largely returned to a competition-based reading of national treatment.

60 For a review of NT clauses in BITs, see Dolzer, R., & Stevens, M. (1995). Bilateral Investment Treaties. The Hague: Nijhoff, pp. 63-65 and for a short survey on the meaning and jurisprudence of NT, see Dolzer, R., & Schreuer, C. (2008). Principles of International Investment Law. Oxford: Oxford University Press, p. 178 et seqq. As an example, NAFTA’s provision is quoted: Article 1102(2). “Each Party shall accord to investments of investors of another Party treatment no less favorable than that it accords, in like circumstances, to investments of its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.” (Article 1102(1) is the same except that it refers to “investors” rather than to “investments of investors;” under Article 1102(3), the obligation applies to state/provincial governments as well.

61 Occidental Exploration and Production Company v. Ecuador, Award, LCIA Case No UN 3467, IIC 202 (1 July 2004), para 173.

62 Siemens A.G. v Argentina, ICSID Case No. ARB/02/8, Award (6 Feb. 2007), at paras 320-1.

63 Methanex Corporation v USA, UNCITRAL, Final Award (3 Aug. 2008), at Part IV, Chp B, para 17.

64 Corn Products International, Inc. v Mexico, ICSID Case No. ARB(AF)/04/01, Decision on Responsibility (15 Jan. 2008), at paras. 120-122.
With this in mind, we expect arbitral tribunals to adopt a robust method that looks to whether foreign investors in the finance sector as a whole are disadvantaged vis-à-vis competing domestic actors. It is unlikely that arbitral tribunals will endorse a narrow view that differentiates between different corporate actors (such as investment banks, wholesale banks or other investment vehicles) simply on their organizational structure. In any event, certain laws already define the type of financial sector industry or the automotive sector qualifying as potential institutions for supporting measures. In those cases, foreign investors falling within the definition (but not included merely because of their nationality and/or judicial organization), will have a strong claim for breach. The more difficult cases involve narrowly tailored definitions such as the Swiss measure targeting only banks that pose a systemic risk to the Swiss economy. Even here, other financial institutions can make credible claims for a broad basis for comparison, since as we have seen, arbitral tribunals have looked to competitive interactions as a necessary condition of finding that domestic and foreign investors operate “in like circumstances”.

The second fundamental interpretative issue involves the determination of “less favourable treatment” of foreign investors and their investments. There is broad consensus that not only de iure (in law) discrimination but also de facto (in fact) discrimination amounts to a breach of the national treatment guarantee. This is in line with WTO jurisprudence and also with most constitutional interpretation in different states. In other words, origin-neutral measures that pose a greater adverse burden on the foreign investor than “like” domestic investors may be in breach of the national treatment obligation.

There are various examples of de iure discrimination in the measures surveyed above, not least the new Australian and Irish guarantees of retail and/or wholesale deposits that are explicitly limited to domestic institutions. In cases involving origin-neutral measures, there is the difficult issue of determining what level of less favourable treatment of domestic investors is an appropriate requirement of breach. One possibility is that national treatment entitles a foreign investor to the best treatment afforded to “like” domestic investors. Provided that

---

65 E.g. Sec. 2 of the German Financial Market Stabilization Act.
66 For example, the NAFTA Tribunal in Feldman v Mexico ruled clearly that “de facto difference in treatment is sufficient to establish a denial of national treatment under Article 1102.” Marvin Feldman v Mexico, ICSID Case No. ARB(AF)/99/1, Award, (16 Dec. 2002), at para 169.
there is a single “like” domestic actor who is treated more favourably by the regulating state, there will be “less favourable treatment” of the foreign claimant. Under this broad approach, it is irrelevant that there may be other “like” domestic actors who are treated equally to, or indeed worse than, the foreign claimant. This broad approach has found reflection in the jurisprudence, most notably in Pope & Talbot v Canada (NAFTA, 2001). 68 It has also been affirmed in successive cases, including Methanex v U.S (NAFTA, 2005) 69, parts of UPS v Canada (NAFTA, 2007) 70 and most recently, ADM v Mexico (NAFTA, 2007) 71. If this test were to be applied, many if not all of the origin-neutral measures surveyed above are likely to constitute “less favourable treatment” of a foreign claimant. Significant competitive advantages flow to domestic banks and institutions from these measures including much lower refinancing costs through guarantees, recapitalization or liquidity support, and allowing supported banks to offer better interest rates than those actors which compete normally. 72

Our third and final interpretative issue concerns the role (if any) of protectionist purpose in assessing breach of national treatment Some tribunals have held that discriminatory intent is not a necessary element for the breach of national treatment. Following the Occidental award 73, the Siemens v. Argentina Tribunal (Germany-Argentina BIT, 2007) held that “intent is not decisive or essential for a finding of discrimination, and that the impact of the measure on the investment would be the determining factor to ascertain whether it had resulted in non-discriminatory treatment”74. Under this effects-based approach, the mere presence of less

68 Pope & Talbot v Canada, supra note 48, at paras 39-42.
69 Methanex v U.S, supra note 63, at paras 20-1.
70 Arbitrator Cass ruled in his Separate Statement: “It is, as UPS urges, enough to establish that a NAFTA Party has given one or more of its investors or investments more favorable treatment.” United Postal Service of America Inc. v Canada, ICSID, Award on the Merits (24 May 2007), Separate Opinion of Arbitrator Cass, at para 60.
71 Archer Daniels Midland Company and Tate & Lyle Ingredients Americas, Inc. v Mexico, ICSID Case No. ARB(AF)/04/05, Award, at para 205.
72 The perceived security of state guaranteed banks or bank bonds is mirrored in the spread of credit default swaps, which diminished considerably for those institutions getting help, see only Cash, Gesicherte Bankanleihen bieten attraktive Renditen of 14th May 2009, available at: http://www.cash.ch/news/newsletter/gesicherte_bankanleihen_bieten_attractive_renditen-795407-440. See also Stijn Claessens, The Financial Crisis and Financial Nationalism, p. 6.
73 E.g. Occidental, supra note 62. para 177: „In the present dispute the fact is that OEPC has received treatment less favorable than that accorded to national companies. The Tribunal is convinced that this has not been done with the intent of discriminating against foreign-owned companies. [...]However, the result of the policy enacted and the interpretation followed by the SRI in fact has been a less favorable treatment of OEPC. “
74 Siemens AG v. Argentina, Award and Separate Opinion, ICSID Case No ARB/02/8, 6 February 2007, para 321. Similarly, the NAFTA Tribunal in Thunderbird v. Mexico did not require the claimant to show that the less favorable treatment was motivated by nationality. See International Thunderbird Gaming Corp. v. Mexico, Award, NAFTA under UNCITRAL, January 26, 2006, para 177: “It is not expected from Thunderbird that it show separately that the less favourable treatment was motivated because of nationality. The text of Article 1102 of the NAFTA does not require such showing. Rather, the text contemplates the case where a foreign investor is
favourable treatment of a foreign investor will be sufficient for breach. For example, the U.S subsidies for the ‘Big Three’ American automakers - which de facto excludes non-American car producers (except for one Toyota plant in California) – would breach the national treatment obligation of an operative investment treaty.75

Other awards adopt a very different approach to this interpretative question. These tribunals have explored – with different emphases - whether the distinction is based on legitimate policy grounds and justifiable or solely as a means of conferring protection to domestic actors and thus impermissible. For example, the 2000 NAFTA Pope & Talbot Tribunal strongly endorses competition as a necessary condition of likeness in a national treatment inquiry76 but also requires evidence of protectionist purpose as a condition of breach.77 Under this competing approach, differentiation between foreign and domestic actors is permissible if rational grounds are shown for it. This may have particular relevance for interventions such as the Swiss bail-out of Credit Suisse and UBS which were publicly justified on systemic grounds. The problem however is that the investor-state arbitral tribunals have not clearly defined what will constitute “rational” grounds for differentiation. The 2004 NAFTA GAMI Tribunal found that the Mexican measure - nationalization of potentially insolvent sugar refiners - did not breach national treatment because it was motivated by a legitimate public policy goal, namely keeping the sugar industry in the hands of solvent enterprises.78 But in the Saluka award, the Tribunal looked at a range of different criteria in assessing the legitimacy of the exclusion of a bank with foreign shareholding from a program of state financial assistance to stabilize the Czech banking system.79 The Tribunal surveyed criteria such as the systemic importance of the bank, its business strategy and liquidity positions.80 It held that none of these features provided rational grounds for differentiation with domestic banks that

treated less favourably than a national investor. That case is to be proven by a foreign investor, and, additionally, the reason why there was a less favourable treatment.”77

75 Of course, the likely complainants in such an action will be German and Japanese investors in the automotive industry in the U.S. However, neither Germany nor Japan has executed modern investment treaty protection with the U.S. As we noted earlier however, both those states have older FCN treaties with the U.S which may be an alternate avenue of complaint. See CSR Report for Congress: U.S.-Japan Economic Relations: Significance, Prospects, and Policy Options, 9 July 2007, p. 20 et seqq., available at: http://www.fas.org/sgp/crs/row/RL32649.pdf.
76 Pope & Talbot, supra note 48, at para 78.
77 Ibid. at para 79 (ruling that difference in treatment must ‘be justified by showing it bears a reasonable relationship to rational policies not motivated by preference of domestic over foreign owned investments’).
78 GAMI v. Mexico, Award, NAFTA under UNCITRAL, 15 November 2004, para 114.
80 Ibid. at para 327 et seqq.
took the benefit of the assistance program. With this in mind, even those measures adopted formally for reasons of systemic concern may be in risk of breach of the national treatment obligation.

(b) Fair and Equitable Treatment

The obligation to accord fair and equitable treatment (FET) will cover, at a minimum, three possible grounds of breach: (i) discriminatory conduct on the part of a regulating host state; (ii) an absence of due process (including the failure of a state to act in a transparent manner) and (iii) denial of justice especially in offering foreign investors access to forms of judicial review.

As a start point, the FET standard has often been held to include protection against discrimination. The Tribunal in *Eureko v. Poland* for example has linked “discriminatory conduct” with a finding of breach of the FET standard. This, however, raises a fundamental interpretative issue that has largely been ignored in the jurisprudence to date. The type of discrimination caught under the FET standard must be something different to that covered by national treatment otherwise we face the problem of redundancy. Most recent awards simply and bluntly conflate national treatment and the FET standard, where discrimination is at issue in the latter. This is an untenable outcome given the need to give separate effect to each treaty provision.

In our view, the type of discrimination caught by national treatment is purposeful protectionism, defined as a desire of a host state to protect a domestic actor vis-à-vis a competing foreign investor. There is then the question of what other forms of discrimination might be caught by the FET standard. Few arbitral awards have examined this in any detail, given the tendency to conflate national treatment and the FET standard. One possibility is a type of hostile “singling out”; the foreign investor is targeted for disadvantage by the host state simply because of their foreignness (rather than any desire to tilt the competitive scales

---

81 For example, on liquidity, the Saluka Tribunal held that it “is not convinced that different liquidity ratios warranted different treatment with regard to the provision of State financial assistance in order to overcome the bad debt problem”. Ibid. at para 345.
82 See also Separate Opinion Wälde in Thunderbird, supra note 74 Error! Bookmark not defined., para 103.
83 See for example Siemens, supra note 62, at paras 318-321 (drawing on NAFTA national treatment jurisprudence in interpreting the treaty prohibition of “arbitrary or discriminatory measures”).
in favour of a domestic actor).\footnote{We can trace a concern with this type of hostile discrimination in customary international law (which is incorporated into particular FET standards such as NAFTA Article 1105) together with intriguing hints in this direction in the decision of the ICJ Chamber in \textit{ELSI}. See \textit{ELSI}, supra note 53.} If this is to be the type of discrimination caught by the FET standard, there is little evidence of hostile singling out at play in the measures we have surveyed. To put it bluntly, we are dealing with classic protectionist measures, rather than any desire to harm or evict foreign actors, \textit{per se}.

As a second possibility, the failure to act in a transparent matter in administrative decision-making has been used by arbitral tribunals to ground breach of the FET standard.\footnote{Metalclad Corp. v. Mexico, ICSID Case No. ARB(AF)/97/01 See for more details: Akira Kotera, Regulatory Transparency, in: Muchlinski/Ortino/Schreuer, Oxford Handbook of International Investment Law, 2008, 617-636. But note that the NAFTA Free Trade Commission issued a binding statement in 2001 concerning the interpretation of Fair and Equitable Treatment. See “Free Trade Commission Clarifications Related to NAFTA Chapter 11,” July 31, 2001, at http://www.ustr.gov/regions/whemisphere/nafta-chapter11.html. It held that this provision equals only Minimum Standard of Treatment and does not contain any transparency requirements for states. However, this instrument is not applicable for cases involving investment treaties other than the NAFTA.} In \textit{Metalclad} for instance, the Tribunal relied on a reference to transparency in part of the NAFTA in its analysis of the FET standard\footnote{Ibid. at para 99.} while the \textit{Tecmed} Tribunal drew on the notion of good faith in finding transparency to be component of the FET standard.\footnote{Tecnicas Medioambientales TECMED S.A. v. Mexico, ICSID CASE No. ARB (AF)/00/2, para 154: “The Arbitral Tribunal considers that this provision of the Agreement, in light of the good faith principle established by international law, requires the Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations.”} States have to some degree acted in a transparent manner in promulgating many of the emergency measures surveyed. Those measures have largely been enshrined in law (rather than simple administrative practice) and often published immediately on government websites. Nevertheless, there is still considerable uncertainty as to the eligibility of foreign actors to benefit from certain measures. For example, the U.S interventions do not clarify what constitutes “substantial business activities” and whether or not foreign branches are included, or what is meant by “government owned”.\footnote{Public Law 110-343, 12 USC 5202, Sec. 3: “Financial institution.--The term ‘financial institution’ means any institution, including, but not limited to, any bank, savings association, credit union, security broker or dealer, or insurance company, established and regulated under the laws of the United States or any State, territory, or possession of the United States, the District of Columbia, […] and having significant operations in the United States, but excluding any central bank of, or institution owned by, a foreign government.”} It is however too early to offer a definitive assessment of breach here given the likelihood that the executive branch will offer guidance or regulation on these different criteria.
Finally, the FET standard will be breached where foreign investors have been denied justice (usually in the domestic court systems of host states). In Germany\textsuperscript{89} as well as in the United States,\textsuperscript{90} special procedures have been foreseen in the emergency laws. Both countries restrict the review mechanisms usually available against state actions, but they do not entirely exclude judicial review. As there is no complete denial of due process, it is unlikely that a violation will be found on these current trends.

(c) Exceptions

There are exceptions for host state conduct in the event of a finding of liability for breach of an obligation in an applicable investment treaty. Given the heterogeneity of this field, there are three possible categories of exemption that might apply depending on the instrument in question. First, certain newer investment treaties – especially those concluded as part of a free trade agreement – offer qualified exemption for prudential regulation of the financial services industry (modelled on the similar carve-out in the GATS)\textsuperscript{91} or specific exemption for the application of national treatment to the financial services sector\textsuperscript{92}. These are, on the whole, likely to offer safe harbour for state conduct otherwise in breach of an investment treaty obligation.\textsuperscript{93} Second, certain states have amended their model bilateral investment

---

\textsuperscript{89} Sec. 15 and 16 of the Financial Market Stabilization Act.
\textsuperscript{90} 12 USC 5229, Sec. 119.
\textsuperscript{91} For example, the US-Uruguay BIT of 2006 contains a prudential carve-out in Art. 20 (1): “Notwithstanding any other provision of this Treaty, a Party shall not be prevented from adopting or maintaining measures relating to financial services for prudential reasons [...]”. Similarly, Canadian 2004 Model Foreign Investment Protection and Promotion Agreement (FIPA), Article 10 (2), available at http://www.sice.oas.org/Investment/NatLeg/Can/2004-FIP/Amodel-en.pdf (accessed 7 May 2009): “2. Nothing in this Agreement shall be construed to prevent a Party from adopting or maintaining reasonable measures for prudential reasons, such as: (a) the protection of investors, depositors, financial market participants, policyholders, policy-claimants, or persons to whom a fiduciary duty is owed by a financial institution; (b) the maintenance of the safety, soundness, integrity or financial responsibility of financial institutions; and (c) ensuring the integrity and stability of a Party’s financial system.”
\textsuperscript{92} For example, some US BITs contain MFN/NT exceptions for the financial sector. The 1994 Argentinian-US BIT includes exceptions to national treatment in a Protocol to the BIT: “(2) With reference to Article II, paragraph 1, the United States reserves the right to make or maintain limited exceptions to national treatment in the following sectors: [...] banking; insurance [...]”. The 1994 US-Bulgaria BIT and 1990 US-Turkey BIT contain similar clauses. The 1996 Ukraine-US BIT explicitly excludes financial services from MFN/NT: “The U.S. portion of the Annex contains a list of sectors and matters in which, for legal and historical reasons, the federal government or the States may not necessarily treat investments of nationals or companies of the other Party as they do U.S. investments or investments from a third country. The U.S. exceptions from national treatment are: [...] banking; insurance [...].” However, none of the Swiss, the German or UK BITs contain prudential carve outs or MFN/NT exceptions for the financial service sector.
\textsuperscript{93} A direct carve out on national treatment in the financial services sector will offer a substantive defence based on national treatment, leaving only a second and possibly marginal claim on FET. If there is only a prudential carve-out, much will depend on how this carve-out is interpreted by an arbitral tribunal. As a point of comparison, the GATS prudential carve-out has not to date been interpreted by a WTO panel. See Mamiko Yokoi-Arai, GATS’ Prudential Carve Out in Financial Services and Its Relation with Prudential Regulation, 57 International and Comparative Law Quarterly 2008, pp. 613-648.
treaty to ensure that any invocation of a treaty exemption for, *inter alia*, “essential security interests” is a matter of competence for signatory states alone. This shift towards auto-interpretation precludes any role for an adjudicator in assessing whether the constituent elements of the treaty exception have in fact been proven. In general, both these categories of exemption are relatively rare and reflect new trends in investment treaty rule-making.

In contrast, older investment treaties will only typically exempt measures “necessary” to maintain “public order” or to protect “essential security interests”. This form of exemption is not explicitly self-judging and indeed has been adjudicated in a range of cases brought against Argentina in the aftermath of its 2001-2 financial crisis. We should, however, exhibit some caution in relying on this case-law. Early arbitral awards – including *CMS*, *Enron* and *Sempra* - engage in a questionable interpretative methodology of conflating the terms of the treaty exception with the stringent customary plea of necessity (represented by Article 25 of the International Law Commission’s Articles on the Responsibility of States for Internationally Wrongful Acts).

This then raises our first interpretative question of whether the effects of financial crisis might somehow engage a state’s “essential security interests”. Of the few cases that have avoided the error of conflating the treaty defence with the customary plea, the *Continental* award offers especially pertinent guidance on this question. That Tribunal was prepared to accept that the grave economic and social dislocations of the Argentine financial crisis were sufficient to engage that state’s “essential security interests”. Ultimately however, the likely success of this defence may turn more so on whether an adjudicator will find that the particular measures chosen by the state are indeed “necessary” to protect such “essential security interests”. The necessity component of the treaty exception asks a question of the closeness or fit between the chosen means and the asserted regulatory purpose of the state in question. There are various methods of engaging in means-end inquiry, with the *Continental* Tribunal electing to endorse a “reasonable less restrictive means” test. This approach requires an adjudicator to assess whether there any reasonably available alternatives to the chosen measure that have less restrictive effects on the rights of foreign investors. On the

---

95 See eg, Art. XI of 1991 U.S-Argentine BIT.
98 Ibid. at pp. 87-8.
whole, it is unlikely that the current measures will fall within the exemption. It will be
difficult to make the argument that discrimination directed against foreign bank institutions
(with domestic depositors) was indeed “necessary” to protect those “essential security
interests”.

Finally, one should keep in mind that in most investment treaties contain a most favored
national clause (MFN). Even if the relevant treaty provision at issue restricts a possible claim
by an investor, that investor may be able to use the MFN clause to invoke more favorable
protections in other investment treaties ratified by the host state. The exceptions surveyed
above, if used to shield the host state from suits concerning measures in the financial sector,
might therefore be rendered obsolete through this legal manoeuvre.

V. Conclusion and Outlook

We draw two tentative and sobering conclusions from this analysis.

First, there is clear evidence of both overt and factual discrimination directed at foreign actors
(and goods) in the laws we have surveyed. This is not confined to any individual state or
select grouping; it is a marked characteristic of emergency responses to the financial crisis
across a significant proportion of the globe. This then is a timely reminder to revisit the
lessons associated with the outbreak of protectionism leading to the Great Depression in the
inter-war period. Protectionism is the result of a prisoner’s dilemma understood in game
theory terms. Cooperation would make every state better off, but it is individually rational for
states to pursue their self-interest (and protect domestic industry) at least in the short run.
While protectionist instincts are now more nuanced, it is difficult to escape the conclusion
that states are failing to cooperate in the current crisis, with possible cascading consequences.
One pertinent example is the sharp contraction in credit availability across Eastern Europe,
where much of the banking sector is controlled by Western European banks who now have
strong incentives to lend only within their home countries. This leads to our second, tentative
assessment. The framers of the post-Second World War architecture of international law
-especially the GATT, the forerunner of the WTO), were deeply influenced by the lessons of
the inter-war period. They had drafted those rules hoping to embed a loose form of
cooperation and constrain the freedom of states to resort to short-term protectionist measures.
The preparedness and rapidity by which states are now moving in that direction raise serious
questions of whether our existing system is in fact a sufficient check against these problematic and destructive tendencies.

Ultimately however, these complex issues may be addressed – at least in the short-term - in legal rather than diplomatic fora. The 2001 Argentine financial crisis triggered a wave of international investment litigation against that state. There is good reason to expect foreign investors will similarly seek to use their rights under international investment law to combat discrimination embodied in state responses to the current crisis. The likely success of such litigation – with the possibility of award of significant monetary compensation - should act as some constraint against risk-adverse governments continuing to resort to short-term protectionist measures.