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Could Some European Countries Initiate A State-To-State Investment Arbitration Against Switzerland For Abruptly De-Pegging The Swiss Franc From The Euro?

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In the 2000s, mortgages in Swiss Franc (CHF) were very popular among consumers in Central, Eastern and Southeastern Europe for the acquisition of both private and commercial properties, as the CHF was a stable and reliable currency and offered lower interest rates than loans in Euro or in local currencies. When on 15 January 2015 the Swiss National Bank (SNB) suddenly decided to de-peg the CHF from the Euro, the move took by surprise the world central banking system, a market where slow and predictable decisions are of the essence. As a result of the de-pegging, the CHF drastically surged and considerably appreciated against the Euro and all the region's currencies, making the CHF mortgages far more expensive to repay for hundreds of thousands of Central, Eastern and Southeastern European borrowers with incomes in local currency (in some cases, the principal sum as well as the monthly repayments owed doubled or even tripled up), thus throwing countries like Romania, Poland, Croatia, Montenegro, Serbia, and Bosnia-Herzegovina into a financial turmoil. Borrowers in these countries – struggling to repay the CHF mortgages – began pressuring their respective governments to artificially fix those loans at a lower exchange-rate.

Consequently, many of these countries implemented or consider implementing a forced conversion of the CHF loans into loans denominated either into national currency or in Euro, at historical exchange rates (meaning prior to 15 January 2015), to allow population to repay the installments of those loans. Namely, Croatia and Montenegro passed a law to this effect. Whereas Poland and Romania – that at first wanted to adopt a forced conversion bill from CHF to zlotys and lei at the expense of the banks – got cold feet fearing the reaction of German, Austrian and Italian banks.

Indeed, should any of these States enact a law forcing the conversion of housing loans made in CHF into the local currency or Euro at the currency fluctuation on the day these loans were disbursed, banks will suffer capital losses amounting to billions of Euros. That is why the drafting of these loan conversion acts is shaking the financial sector and investment arbitrations are looming against these States either to repeal or to compensate for these regulatory measures, being the first of these arbitrations already launched against Croatia and Montenegro. Arguably, foreign banks invoking bilateral investment treaties may well claim the breach of the FET standard, because of the retroactive effect of these measures converting the CHF loans at the exchange-rate they were originated at the expenses of the lenders, thus threatening the principle of legal certainty and, accordingly, impairing investors' legitimate expectations.

Luckily enough, these counties might turn the tables on Switzerland by resorting to the same instrument wherefrom the problems seem to come, in other words, by commencing one or multiple State-to-State investment arbitrations. Before exploring this exciting avenue, it is necessary first to understand what a currency peg is and the implications of its snap termination.

A currency peg takes place when a government fixes its currency's value to that of another country. By pegging the exchange-rate between countries, such monetary policy serves the purpose of creating a stable trading environment, which allows for accurate long-term predictability for business planning, especially in the import-export sector (whose operators will be able to know beforehand exactly what exchange-rate to expect, accordingly reducing uncertainties inherent to international transactions). A government achieves a currency peg by committing its central bank to either buy or sell its own currency on the open market to maintain the fixed exchange-rate, which has been previously set. The SNB introduced the exchange-rate peg in 2011 holding the CHF at 1.20 to the Euro, by promising to buy unlimited quantities of foreign currencies, thus forcing down its value to foster exports.

To any investment arbitration practitioner, the elements surrounding the pegging of a currency to another – i.e. the creation of stable trading conditions built upon the commitments of a state's organ to ensure a predictable climate favorable to the operation of enterprises and to the flow of capitals and goods – should already ring a bell as they depict the recurring backdrop of a FET violation, where such elements stop being upheld by the State in question. Elements and evidence in support of a FET violation in this case are:

– the breach of specific representations made on 18 December 2014 by the president of the SNB, Thomas Jordan, who reaffirmed SNB's commitment to the minimum exchange-rate of CHF 1.20 per Euro by continuing to enforce it with the *utmost determination* (just for breaking his promise the month after, on 15 January 2015);

– the breach of another (more specific) rule of international law that comes into play through Art. 31.2.c of the VCLT, *videlicet* Art. IV of the Articles of Agreement of the International Monetary Fund that imposes upon the Contracting Parties (like Switzerland) the obligations to promote economic stability through a monetary system that does not produce erratic disruptions (like the one at end), and to notify the Fund promptly of any changes in its exchange-rate policy.[1)];

– an interview of the Managing-Director of the IMF – that may well serve as a witness/expert deposition as to the breach of the IMF Articles – where Ms. Lagarde states that she had not been notified about the CHF/Euro de-pegging ahead of time, which she found "a bit surprising" (by using a euphemism).

– a study of 2009 conducted under the auspices of the SNB on the CHF lending across Europe, proving that the SNB was aware of the widespread use of the CHF loans all over Europe, so it could not be unaware of the dire spill-over effects of an offhand revaluation.

As to the attribution of the wrongful conduct, attribution under art. 4 of the Articles on State Responsibility of the SNB's action to the Swiss State should be no problem as the Swiss Constitution devotes article 99 to the SNB itself, making it arguably a full-fledged State organ.

Romania, Poland, Croatia, Montenegro, Serbia, and Bosnia-Herzegovina have all concluded a BIT with Switzerland providing for an FET provision and a dispute settlement provision between the

Contracting Parties to the treaty regarding its interpretation and (more importantly for our purposes) its application. Such a State-to-State dispute settlement provision, whose scope covers the application of the BIT itself, means that it will encompass divergences concerning the compliance of the actions or measures taken by the Contracting Parties with the terms and purposes of the BIT.[2)] Hence, each one of these States may effectively invoke the international responsibility of Switzerland by giving notice to the Swiss government of its arbitration claim, wherein it alleges that Switzerland violated, under the applicable BIT, the obligation to afford FET with respect to the Claimant-State and its actual and potential investors by abruptly de-pegging the CHF from the Euro and, accordingly, thwarting friendly-investments constant conditions. To be clear, what constitutes a FET violation is not having de-pegged the CHF, but how such action was taken, *videlicet* without any prior notice to the Fund and, if this wasn't enough, by issuing a misleading statement – just few weeks before the de-pegging occurred – where the SNB assured that it would have kept the CHF pegged to the Euro at 1.20. The failure to notify in time the Fund about the de-pegging, prevented other central banks' governors from taking the necessary steps to avoid or mitigate the damages. Each Claimant-State may also be free to enact a forced conversion law whereby it converts the CHF-denominated loans into local currency and labels such act as a countermeasure against the internationally wrongful act committed by Switzerland to shield itself from international liabilities and the threat of foreign banks.

In the arbitration claim, every Claimant-State should pursue a declaratory relief[3)], asking for satisfaction as form of reparation, modeled after Mexico's claim in the 2000 NAFTA case *Mexico v. United States of America*, because in that way the Claimant-State would not have to prove that a particular national investor or investment had been affected by the sudden CHF/Euro de-pegging. Instead, it should simply tackle the measure or action adopted by the Respondent-State that it deems in violation of the BIT, i.e. the abrupt CHF/Euro de-pegging itself[4)]. By doing so, every problem concerning the territoriality requirements of a specific impaired investment would be avoided. Further, the Claimant-State could always reason its position by maintaining that such an abrupt revaluation of the CHF against the Euro, as well as, its currency is harmful for a stable economic environment *per se*.

Finally, it would be a unique opportunity for the whole system of investment arbitrations because it would be probably the first time that an investment arbitration be deployed to justify a regulatory measure adopted by several States (the forced loans conversion act), rather than undermining States' regulatory powers. In this way, some of the harsh criticisms regarding the legitimacy of investment arbitrations could be softened.

The views expressed in this article are those of the author and DO represent those of the law firm Bottega DI BELLA.

References

?1 In this regard, see also the Decision No. 5712-(78/41) of the IMF of 23 March 1978 concerning art. IV of the IMF Agreement and emphasizing the importance of a prior notification to the Fund of all changes in the peg. Please see Erik Denters and Annamaria Viterbo (2015), International Monetary Fund (IMF), Second Edition, Wolters Kluwer

?2 UNCTAD, 2003, Dispute settlement: State–state, 14.

?3 See Nathalie Bernasconi-Osterwalder, State–State Dispute Settlement in Investment Treaties, October-2014, The International Institute for Sustainable Development,7-8.

?4 See *Mexico v. United States*, Final Report of the Panel, February 6, 2001, para. 292

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