Kluwer Arbitration Blog

Does Investment Arbitration Threaten the Effectiveness and Integrity of EU Bank Resolution?

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Background

In early June 2017, Banco Popular Español S.A. ('Popular') was placed into resolution under the European Union's ('EU') Bank Recovery and Resolution Directive ('BRRD') and the Single Resolution Mechanism Regulation ('SRMR'). It was the first – and only, to this day –case where the Single Resolution Board ('SRB'), as the European resolution authority, intervened on public interest grounds to prevent another bailout. Popular was sold to Santander for one euro, whilst losses were covered through the use of the bail-in tool on shareholders and junior subordinated debtholders.

On 23 August 2018, a group of Mexican investors affected by the June 2017 resolution initiated two parallel arbitrations against Spain under the Mexico-Spain Bilateral Investment Treaty ('BIT'). The two arbitrations were later consolidated and are now being heard by a single arbitral tribunal operating under the UNCITRAL Arbitration Rules 2013. The case, *Antonio del Valle Ruiz et al. v. Kingdom of Spain (PCA Case No. 2019-17)* (hereinafter '*Antonio del Valle Ruiz v. Spain*'), is being administered by the Permanent Court of Arbitration ('PCA'). In their Notice of Arbitration, the claimants allege that they lost "their entire original investment, which […] was of more than € 470 million",[1] as a result of the resolution. The claimants argue that this was the result of Spain's "acts and ommissions" in precipitating Popular's "liquidity crisis and the using it to justify the bank's resolution and 'sale' to Santander".[2] The claimants consider these actions violated several of Spain's obligations under the BIT, including the obligation to provide fair and equitable treatment and not to engage in an unlawful expropriation of the claimants' investment.[3]

This is a case of first impression in two ways: (i) it concerns the first EU sanctioned resolution of a *failing or likely to fail* financial institution under the BRRD and the SRMR; and (ii) it constitutes the first ever investment treaty arbitration directly arising out of the application of the EU's new regulatory resolution framework for systemic banks that was promulgated in response to the 2008 financial crisis.

Scholarly discussions on investment claims as a corollary to bank resolution have so far focused on the purported conformity of the resolution process to investment protection standards of treatment, the availability of state defenses against such claims and on whether liabilities subject to bail-in

could fall under the definition of *investment* under the relevant investment treaty and the ICSID Convention.[4)] Evidently, as discussed in a previous Kluwer Arbitration Blog post, *Antonio del Valle Ruiz v. Spain* has also touched on salient transnational litigation issues, such as the availability and extraterritorial reach of discovery applications under Section 1782 of the United States Code.

Opposing Dynamics in EU Integration

Other than reaffirming the notion that investment treaty claims can indeed arise out of a BRRD/SRMR bank resolution, the case's nascent stage does not allow us to draw any conclusions on how such claims would play out in practice. Instead, we would argue that this case could highlight the lingering tension between two of the EU's most ambitious integration efforts in the post-Lisbon era: (i) shaping an EU international investment policy (Article 207(1) of the Treaty on the Functioning of the European Union ('TFEU')) and (ii) establishing a single resolution mechanism as a fundamental pillar of the Banking Union (Article 114 TFEU).

The EU's international investment policy relates to the EU and its Member States' shared competence to conclude Investment Protection Agreements ('IPAs') with non-EU states pursuant to Article 4 TFEU. Recent examples of such treaties include the EU-Singapore IPA and the EU-Vietnam IPA. Following the Court of Justice of the European Union's judgment in *Achmea* on 6 March 2018 which found the international dispute settlement provisions in the Netherlands-Slovakia BIT to be incompatible with EU law, intra-EU investor-state arbitration is now precluded under EU law. This was reaffirmed in the CJEU's Opinion 1/17 of 30 April 2019 concerning the EU-Canada Comprehensive Economic and Trade Agreement ('CETA'). In the field of investor-state dispute settlement, the EU is pushing for the ultimate replacement of the current regime by a Multilateral Investment Court system with an Appellate Mechanism.

In the context of the BRRD/SRMR, investors affected by the resolution tools can seek limited recourse to domestic courts (*cf.* Articles 85 and 86 BRRD) and can instead only challenge the resolution decision taken by the SRB before the CJEU (Article 86 SRMR) – as is the case with Popular. This is in line with the EU policies behind the BRRD/SRMR and the EU Banking Union more generally. But again, all such claims need to be justified on the basis of the *no creditor worse off* principle ('NCWO'), meaning that investors should not be treated in resolution worse than they would have in national insolvency as the default alternative option to resolution. Proving damages on the basis of the NCWO is challenging given the technical and complex nature of the underlying valuations as well as the assumptions built into the assessment of the counterfactual, namely of liquidation. Therefore, investment arbitration could well have a role to play in allowing individuals affected by resolution to bring forward claims that would be inadmissible before the CJEU or national courts.

The Significance of *Antonio del Valle Ruiz v. Spain*

In our view, *Antonio del Valle Ruiz v. Spain* raises a normative conflict between two aspects of EU integration. Investors from non-EU states affected by the Popular resolution can – and for the first time, have – avail(ed) themselves of the investment treaty protection regime, alleging that Spain

violated its international law obligations, initially by contributing to the bank runs experienced by Popular and later on by raising its liquidity provision requirements to unprecedented levels and using the mandatory EU law framework of the BRRD to engineer the sale of Popular to Santander or another large bank. Essentially, given the difficulties attached to a direct challenge of the resolution actions, *Antonio del Valle Ruiz v. Spain* illustrates the case that challenging the resolution of a bank in arbitration can occur indirectly by challenging the circumstances that led to the resolution and not the mechanics of the resolution *per se*. A successful outcome for the claimants could significantly affect the integrity of the resolution process by legitimizing damages beyond those provided on the basis of the NCWO standard described above.

Meanwhile, it is now trite EU law that this avenue would not be available to EU investors. We consider this result to be the victim of an unforeseen externality of the *Achmea* judgment with severe effects for both EU investors and the EU as a whole. Not only are EU investors placed in a less favorable position than their non-EU peers – which can hardly be seen as a welcome outcome from an EU investment policy perspective – but the EU's policy under the BRRD/SRMR is also in danger of being displaced since Spain could plausibly be held accountable for complying with a mandatory EU law obligation instead of opting for a bailout.

Ironically, while not a classic intra-EU case, *Antonio del Valle Ruiz v. Spain* could have major consequences for EU law and policy by placing a higher standard of accountability for Member States hosting banks undergoing resolution, while creating more legal uncertainty as to the finality of resolution actions. Indeed, we would not be surprised if the EU Commission – or even the SRB for that matter – attempted to participate in the arbitral proceedings as an *amicus curiae*, bringing this matter to the Tribunal's attention. Regardless, it will be interesting to see how this case unfolds.

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References

?1 *Antonio del Valle Ruiz v. Spain*, Notice of Arbitration, 23 August 2018, para. 10.

?2 *Id.* at 11.

?3 *Id.* at 12.

?4 *See, e.g.*, Michael Wolfgang Müller, "Creditor protection in bank resolution: a case for international investment arbitration?" (2015) 10(3) *Capital Markets Law Journal* 276; Maurice Mendelson QC and Martins Paparinskis, "Bail-ins and international investment law: In and beyond Cyprus", *in* Christian J. Tams, Stephan W. Schill and Rainer Hofmann (eds.), *International Investment Law and the Global Financial Architecture* 193 (Edgar Elgar, 2017); Phoebus Athanassiou, "BITs and pieces: Reflections on the relevance of BITs in resolution-related litigation", *in* Christian J. Tams, Stephan W. Schill and Rainer Hofmann (eds.), *International Investment Law and the Global Financial Architecture* 240 (Edgar Elgar, 2017).

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