Profiting from Crisis

How corporations and lawyers are scavenging profits from Europe's crisis countries

Amsterdam/Brussels, March 2014

Published by the Transnational Institute and Corporate Europe Observatory

Executive summary

Profiting from Crisis is a story about how corporations, backed by lawyers, are using international investment agreements to scavenge for profits by suing governments from Europe's crisis countries. It shows how the global investment regime thrives on economic crises, but is very uneven in who it benefits. While speculators making risky investments are protected, ordinary people have no such protection and – through harsh austerity policies – are being stripped of basic social rights.

For a long time, European countries were left unscathed by the rising global wave of investor-state disputes which had tended to target developing countries. In the wake of the global financial crisis, however, corporations and investment lawyers have turned their eyes to potential pickings in Europe. An investment regime, concocted in secretive European board rooms, and that gives corporations powerful rights to sue governments, has finally come home to roost.

The report first explores the history of investor-state lawsuits as a result of economic crises across the world from Mexico in 1994 to Argentina in 2001. As crises struck these nations scrabbled desperately to protect their rapidly sinking economies; the measures they took have since come under systematic attack from corporations. Countries have been sued for measures to revive a domestic financial system or the freezing of public services' tariffs to keep them affordable for their people. Some measures, such as sovereign debt restructuring (renegotiating terms with creditors) are even required as part of debt deals, yet have been similarly challenged by investment lawsuits.

The legal bases of these lawsuits are the over 3,000 international investment treaties in existence to date. They contain far-reaching protections of private property enshrined in catch-all clauses such as "fair and equitable treatment" and "protection from indirect expropriation". The trouble is that these clauses have been interpreted so broadly that they gave a carte blanche to corporations to sue states for any regulations that could be deemed to affect current or future profits. Moreover, investment treaties grant corporations rights to protection, without giving equivalent rights to states to protect their own citizens.

Profiting from Crisis looks closely at how corporate investors have responded to the measures taken by Spain, Greece and Cyprus to protect their economies in the wake of the European debt crisis. In Greece, Postová Bank from Slovakia bought Greek debt after the bond value had already been downgraded, and was then offered a very generous debt restructuring package, yet sought to extract an even better deal by suing Greece using the Bilateral Investment Treaty (BIT) between Slovakia and Greece. In Cyprus, a Greek-listed private equity-style investor, Marfin Investment Group, which was involved in a series of questionable lending practices, is seeking €823 million in compensation for their lost investments after Cyprus had to nationalise the Laiki Bank as part of an EU debt restructuring agreement. In Spain, 22 companies (at the time of writing), mainly private equity funds, have sued at international tribunals for cuts in subsidies for renewable energy. While the cuts in subsidies have been rightly criticised by environmentalists, only large foreign investors have the ability to sue, and it is egregious that if they win it will be the already suffering Spanish public who will have to pay to enrich private equity funds.

Profiting from Crisis reveals how:

- **The public bailout of banks that led to the European debt crisis could be repeated with a second public bailout, this time of speculative investors.** Corporate investors have claimed in arbitration disputes more than 700 million euros from Spain; more than one billion euros from Cyprus and undisclosed amounts from Greece. This bill, plus the exorbitant lawyers' fees for processing the cases, will be paid for out of the public purse at a time when austerity measures have led to severe cuts in social spending and increasing deprivation for vulnerable communities. In 2013, while Spain spends millions on defending itself in lawsuits, it cut health expenditure by 22 per cent and education spending by 18 per cent.
- **Many of the investment lawsuits under way against European crisis countries are being launched by speculative investors.** They were not long-term investors but those which invested as the crisis first emerged and were therefore fully cognisant of the risks. Yet rather than paying the costs of risky investments, investment agreements have given them an escape clause and are being used to extract further wealth from crisis countries. Poštová Bank, for example, bought bonds in early 2010 at the same time that Standard & Poor's categorised Greece's debt as "junk". In Spain, out of 22 companies involved in lawsuits, 12 invested after 2008 when the first restrictions to feed-in tariffs for solar energy were introduced; eight more continued to invest in the country despite the 'threats' to their investments.
- **The investors involved in lawsuits have profited considerably despite the 'threat' to their investments by the crisis countries.** Pos ˇtová Bank reported a net profit of 67.5 million euros in 2012; renewable energy investor Abengoa SA reported a 17% increase in revenues to 5.23 billion euros in the first nine months of 2013. It has been a very different story for the citizens of the countries being sued. Greeks, for example, are on average almost 40% poorer than they were in 2008 and there has been a drastic rise in homelessness. One in three children (around 600,000) are now living under the poverty line.
- **Corporate investors have been supported and encouraged by highly paid investment lawyers who continuously and actively identify litigation possibilities.** In a few cases, arbitration firms suing cash-strapped countries were also advising the very same companies when they made the risky investments in the first place. UK-based law firm Allen & Overy, now counsel to investors in five out of seven known claims (at the time of writing) against Spain relating to subsidy cuts in the energy sector, advised some of these investors in their original acquisition of the power plants. The corporate lawyers' marketing has paid off with a boom in cases and healthy profits and income for these elite firms. UK-based Herbert Smith Freehills, hired to represent Spain in at least two cases, for example, is retained at a fee of 300 euros an hour and could earn up to 1.6 million euros for the cases.
- **Investment lawyers and corporations are using the threat of legal cases to try to change policies or prevent regulation that threaten profits.** In an October 2011 client briefing paper, US-based law firm K&L Gates, for example, recommended investors should use the threat of investment arbitration as a "bargaining tool" in debt restructuring negotiations with governments. Similarly, UK-based firm Clyde & Co suggested using the "potential adverse publicity" of an investment claim as "leverage in the event of a dispute with a foreign government".
- **The European Commission (EC) has played a complicit and duplicitous role, effectively abetting this wave of corporate lawsuits battering crisis-hit countries.** Some of the lawsuits have arisen due to debt and banking restructuring measures that were required as part of EU rescue packages. Moreover, while the EC has been critical of BITs (Bilateral Investment Treaties) between EU member states (known as intra-EU BITs), they continue to actively promote the use of investor-state arbitration mechanisms worldwide, most prominently in the current negotiations for the controversial EU-US trade agreement (TTIP). Defending corporate protection while denying social protection is a disturbing indictment of current priorities in European trade and economic policies.
- **The investment arbitration regime provides VIP treatment to foreign investors and privatises justice.** Foreign investors are granted greater rights than domestic firms, individuals or communities, even when these are just as affected by the measures that led to the dispute. The cases are judged by a tribunal of three private, for-profit lawyers who get to decide on policies that affect the welfare of millions of people. Some of them have ignored international legal principles that allow for states to violate their international obligations when it is necessary to protect the interests of their citizens, especially in crisis situations.

The deepening crisis in the European periphery has attracted more and more circling vultures, scavenging for profits. In 2012, New York-based Greylock Capital argued that buying Greek bonds was "the trade of the year". At the time, investors were paying 19 to 25 cents for bonds for every dollar worth of bonds.

In April 2013, US-based law firm Skadden which represents Cyprus Popular Bank (Laiki) in a looming multibillion-euro investment treaty dispute against Greece praised the "increasing appeal and novel use of Bilateral Investment Treaties". The firm noted, "the appeal of BIT tribunals, coupled with the economic uncertainty of recent times, has triggered an increased use of BITs to resolve disputes in ways that previously had not been encountered by arbitral tribunals, and we expect this trend to continue." The experience of Argentina, which faced 55 investor lawsuits in the aftermath of its crisis in 2001, shows that claims keep coming some time after a crisis. The cases listed in this report are almost certainly just the beginning of a new wave of investor-state lawsuits against European countries.

These investor-state disputes are part of a broader pattern that has become deeply evident since the economic crisis broke; one where corporations are protected from risky investments while citizens are told that cuts are inevitable; where corporate losses are socialised and taxpayers pay the bill; where corporations have recourse to justice while citizens' human rights are sidelined.

The European and American public were understandably angry about bailout of the banks. It is time now to turn a spotlight on the bailout of investors and call for a radical rewrite of today's global investment regime.

As a first step, we believe EU governments should seek to terminate existing investment agreements. In particular, European citizens and concerned politicians should demand the exclusion of investor-state dispute mechanisms from new trade agreements currently under negotiation, such as the proposed EU-US trade deal. A total of 75,000 cross-registered companies with subsidiaries in both the EU and the US could launch investor-state attacks under the proposed transatlantic agreement. Europe's experience of corporate speculators profiting from crisis should be a salutary warning that corporations' rights need to be curtailed and peoples' rights put first.