

## ‘Black’s Bank’ and the Settlement of Investment Disputes

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### I. Introduction

The organization referred to in the title of this contribution is the International Bank for Reconstruction and Development (the IBRD or ‘the Bank’). Its constituent treaty was drawn up at the United Nations Monetary and Financial Conference held in 1944 at Bretton Woods, New Hampshire.<sup>1</sup> The treaty, the Articles of Agreement of the IBRD, came into force at the end of 1945.<sup>2</sup> The Bank began operating the following year. Already then, it was being referred to informally as the ‘World Bank’, a sobriquet that the institution eventually adopted officially.<sup>3</sup>

The purposes of the Bank, as set forth in its Articles of Agreement, include assisting in the reconstruction of the economies of members destroyed or disrupted by war, and in the development of productive facilities and resources in less developed

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\* This short contribution on an aspect of the prehistory of the International Centre for Settlement of Investment Disputes is offered as an all-too-modest tribute to Charles N Brower, prominent in many ICSID cases, first as an eminent advocate and then as an illustrious arbitrator and ad hoc committee member.

<sup>1</sup> See Final Act of the Bretton Woods Conference (22 July 1944) in *United Nations Monetary and Financial Conference: Bretton Woods, Final Act and Related Documents 11-27* (US Government Printing Office 1944).

<sup>2</sup> Articles of Agreement of the International Bank for Reconstruction and Development (IBRD) (adopted 22 July 1944, entered into force 27 December 1945) 2 UNTS 134.

<sup>3</sup> See IBRD, *A Guide to the World Bank* (2nd edn, World Bank 2007) 11.

countries.<sup>4</sup> Early in its history, the Bank moved out of the reconstruction field, focusing instead on its other purpose of helping in the development of its developing member countries.<sup>5</sup> It serves the purpose by providing financing, mainly loans, for investment projects and economic reform. The loans are made to, or with the guarantee of, creditworthy developing member countries.<sup>6</sup> Interest charged by the Bank on such loans is only fractionally above its own overall cost of borrowing.<sup>7</sup> The Bank also provides technical assistance to its member countries, undertakes research and training, and administers, on behalf of donors, funds for specific uses.<sup>8</sup>

As the ‘chief of the operating staff of the Bank’ in charge of its ‘ordinary business’,<sup>9</sup> the Bank has a President selected by the Executive Directors of the Bank for a renewable five-year term. The President also serves as Chairman of the Executive Directors, who function as a resident board at the principal office of the Bank (in Washington, DC).<sup>10</sup> The Executive Directors, now twenty-five in number, oversee the general operations of the Bank, exercising powers delegated to them by the Board of

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<sup>4</sup> See Articles of Agreement of the IBRD (n 2) Art I(i).

<sup>5</sup> Richard N Gardner, *Sterling-Dollar Diplomacy: The Origins and Prospects of Our International Economic Order* (McGraw Hill 1969) 303–4 (as quoted in Devesh Kapur, John P Lewis, and Richard Webb, *The World Bank: Its First Half Century*, vol 1 (Brookings Institution Press 1997) 74 (explaining that as the European Recovery Program, commonly known as the Marshall Plan, gained momentum, the IBRD turned from its initial emphasis on assisting with the reconstruction of the war-damaged European countries to the task of helping developing countries)).

<sup>6</sup> See Articles of Agreement of the IBRD (n 2) Art III(4).

<sup>7</sup> Member countries of the Bank subscribe to its capital stock on the basis of their relative economic strength. A small proportion of the subscribed capital is paid in; the rest is subject to call to meet obligations of the Bank. The callable capital supports borrowing by the IBRD in the capital markets to fund its lending operations.

<sup>8</sup> See IBRD, ‘Information Statement’ (September 2013) 22, <<http://treasury.worldbank.org/cmd/pdf/InformationStatement.pdf>> accessed 24 September 2014.

<sup>9</sup> See Articles of Agreement of the IBRD (n 2) Art V(5)(b).

<sup>10</sup> Ibid Arts V(5)(a) and V(9)(a).

Governors, which consists of one Governor appointed by each member and meets once annually.<sup>11</sup>

Since its establishment, the IBRD has had twelve Presidents, all of them nationals of the Bank's largest shareholder, the United States. The third, and longest-serving, President was Eugene R Black, who held the position from 1949 to 1962.<sup>12</sup> A profile of Black on the Bank's website describes as the most striking feature of his presidency

the extent to which Black came to personify the Bank. His tenure of office was so long, the stamp of his personality so strong, and his responsibility for its evolving pattern so clear that the Bank came to be known as Black's Bank.<sup>13</sup>

Black led the institution from

tentative beginnings to broad recognition as an important, well- functioning, effective and profitable development institution. He established the Bank's credit in the capital markets of the United States, ensured the acceptability of its bonds to the country's institutional investors, and obtained the highest commercial rating for its paper. He assembled a growing international staff that brought experience and imagination to tackle the demands of an expanding membership. Lending increased rapidly, and covered virtually all sectors relevant to economic progress, including infrastructure, industry, agriculture, and education. In response to the

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<sup>11</sup> In accordance with the Articles of Agreement (Art V(4)(b)(i)), five of the Executive Directors are appointed, one by each of the five members having the largest number of shares (currently France, Germany, Japan, the United Kingdom, and the United States). The other Directors are elected by the Governors of the remaining members, grouped for the purpose in different voting constituencies. The Board of Governors decides on such matters as admitting new members, increasing the capital stock, and amending the Articles of Agreement; see *ibid* Arts V(2)(b), V(4)(b), and VIII.

<sup>12</sup> His predecessors as President were Eugene Meyer, who served in 1946, and John J McCloy, President from 1947 to 1949 (when he left the Bank to become US High Commissioner for Germany). Before becoming President of the Bank in 1949, Black had been the US-appointed Executive Director since 1947; he joined the IBRD from a position as Senior Vice President of Chase National Bank.

<sup>13</sup> Eugene Robert Black, 3rd President of the World Bank Group, 1949–1962, <<http://web.worldbank.org>> accessed 20 August 2014.

changing needs of the membership two major affiliates were created: the International Finance Corporation (IFC) and the International Development Association (IDA).<sup>14</sup>

The website profile points to an additional accomplishment of Black: ‘He established the Bank as an impartial mediator in international disputes.’<sup>15</sup> An overview of the Bank prepared by its staff and published in 1960 described the institution as having been brought ‘logically but unexpectedly’ into this field by its ‘international character, its reputation for objectivity and its expertness in finance’.<sup>16</sup> In addition, Black had a ‘reputation as a reasonable man with extensive experience in financial matters’, which drew many parties to ask him personally to mediate or conciliate their disagreements.<sup>17</sup>

Arbitration in the sense of deciding a dispute in a binding manner was outside the purview of this activity of the Bank.<sup>18</sup> Black insisted as a condition of his or the Bank’s involvement as mediator or conciliator that it was requested by both parties.<sup>19</sup> As to the distinction between cases of the Bank mediating a dispute and Black doing so in his personal capacity, William Iliff, a Vice President of the Bank at the time, explained that

we approach that very empirically. I think Mr. Black really makes up his mind as to whether it’s appropriate that he should do this in his personal capacity. Of

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<sup>14</sup> Ibid. Membership in the Bank grew from forty-five to sixty-seven countries during Black’s presidency. The IFC was established in 1956 and IDA in 1960. The former lends to private enterprises in developing member countries without a government guarantee and makes equity investments in such enterprises, whereas the IBRD cannot lend to such enterprises without such a guarantee; and while the IBRD lends to creditworthy borrowers at non-concessional rates, IDA provides concessional credits to poorer countries.

<sup>15</sup> Ibid.

<sup>16</sup> Eugene R Black, *The Diplomacy of Economic Development* (Harvard University Press 1960) 61, 70 (Appendix: A Note on the World Bank).

<sup>17</sup> Jochen Kraske, William H Becker, William Diamond, and Louis Galambos, *Bankers with a Mission: The Presidents of the World Bank, 1946–91* (Oxford University Press 1996) 95.

<sup>18</sup> World Bank Oral History Program, Interview with Eugene R Black (6 August 1961) 51.

<sup>19</sup> Ibid 43.

course, he's really doing it as President of the World Bank, but institutionally the Bank is not involved.<sup>20</sup>

The next section of this chapter looks at two experiences of Black's Bank, and Black personally, with the settlement of investment disputes. Aron Broches, who as General Counsel of the Bank was to lead the staff work on the establishment of the International Centre for Settlement of Investment Disputes (ICSID), agreed that these experiences 'rang the bells that started [him] thinking about ICSID'.<sup>21</sup> The two 'forerunners . . . were . . . Black's conciliation role with the City of Tokyo bonds, and the Bank's mediation between the Suez Canal Company and Egypt'.<sup>22</sup>

## II. The City of Tokyo Bonds and Suez Canal Company Cases

The first case concerned French holders of bonds issued by the City of Tokyo in 1912 to help finance the development and expansion of the city's electrical tramways and lighting undertakings. Service on the bonds had been suspended in 1928 as funds remitted for the purpose were being attached by bondholders complaining, in the wake of a substantial depreciation of the franc in relation to sterling, that the bonds were envisaged to be payable in the franc equivalent of their sterling value, rather than in francs at their franc face amount. There were conflicting court rulings on the question in France and Japan. Negotiations were started between representatives of the parties to overcome the resulting deadlock. The negotiations produced a settlement in the late 1930s effectively raising the franc face value of the bonds. War intervened to prevent implementation of the settlement, which the bondholders later argued should be disregarded. Eventually, in 1958, representatives of the bondholders and the City of Tokyo concluded a conciliation

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<sup>20</sup> World Bank Oral History Program, Interview with William Iliff (16 August 1961) 64. Iliff conceded, however, that this was a 'sort of fiction', *ibid*. In a book about the World Bank commissioned by the Bank, James (now Jan) Morris quipped that when Black performed these missions in his personal capacity it 'means that he was accompanied by only one vice-president of the Bank and two heads of departments': James Morris, *The Road to Huddersfield: A Journey to Five Continents* (Pantheon Books 1963) 213.

<sup>21</sup> World Bank Oral History Program, Interview with Aron Broches (18 April 1984) 29.

<sup>22</sup> *Ibid*.

agreement pursuant to which Black was asked ‘to draft a concrete and workable plan for settling in a fair and feasible manner the controversy between the parties’.<sup>23</sup> In 1960, Black delivered a plan to the parties for the resumption of payment of principal and interest on the bonds. The plan was based on the pre-war settlement while providing for the bondholders to be compensated for losses due to the delay in carrying out the settlement as contemplated by its provisions. Black’s plan led to a resolution of the controversy after another two years.<sup>24</sup>

The dispute regarding the Suez Canal Company was over the amount of compensation to be paid to its mainly French and British shareholders by the Egyptian Government following the government’s nationalization of the company in 1956. Egypt had offered to pay the shareholders compensation on the basis of the price of the shares on the Paris Bourse on the day before the nationalization; the offer was inadequate to the shareholders as concern over the situation in Egypt during the previous months had resulted in the stock falling to an artificially low figure.<sup>25</sup>

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<sup>23</sup> World Bank Press Release (4 April 1960). The explicit mandate from the start for Black to draw up terms of settlement perhaps accounted for the use by the parties of the term ‘conciliation’ as opposed to ‘mediation’. Cf Nigel Blackaby and Constantine Partasides with Alan Redfern and Martin Hunter, *Redfern and Hunter on International Arbitration* (5th edn, Oxford University Press 2009) 46: ‘Parties who have failed to resolve a dispute for themselves turn to an independent third person, or mediator, who will listen to an outline of the dispute and then meet each party separately—often ‘shuttling’ between them—and try to persuade the parties to moderate their respective positions . . . The terms “mediation” and “conciliation” are often used as if they are interchangeable; and there is no general agreement as to how to define them. Historically, a conciliator was seen as someone who went a step further than the mediator, so to speak, in that the conciliator would draw up and propose the terms of an agreement that he or she considered represented a fair settlement. In practice, the two terms seem to have merged.’

<sup>24</sup> On this case, see *In re City of Tokyo 5 Per Cent Loan of 1912—Plan for Resumption of Payment of Principal and Interest on the French Tranche of the Loan*, 1 April 1960, 29 ILR 11. See also the discussion in Michael Waibel, *Sovereign Defaults before International Courts and Tribunals* (Cambridge University Press 2011) 83–4.

<sup>25</sup> See Iliff Interview (n 20) 33.

Through UN Secretary-General Dag Hammarskjold, the Egyptians and the representatives of the shareholders asked Black to lend the good offices of the Bank to the negotiations.<sup>26</sup> Black accepted the request, designating Iliff to handle the matter on behalf of the Bank. At Black's suggestion, Iliff was assisted in the negotiations, which lasted most of the first half of 1958, by George D Woods, Chairman of the First Boston Corporation, as a financial consultant.<sup>27</sup>

Iliff and Woods started off talks with the Egyptians in Cairo and the representatives of the shareholders in Paris before convening a meeting of both sides in Rome. They then 'went back and forth from Rome to Cairo, Cairo to Paris, Paris to Rome, and finally got to a point where we had narrowed the gap very, very considerably'.<sup>28</sup>

A figure acceptable to both sides was reached after a personal intervention of Black. Under the subsequently concluded settlement agreement, the Bank agreed to act as fiscal agent for the transfer of the periodic compensation payments to be made by the

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<sup>26</sup> See *ibid* 34.

<sup>27</sup> See *ibid* 36; IBRD, *Thirteenth Annual Report 1957–1958* (IBRD 1958) 6. Woods was later to succeed Black as President of the World Bank.

<sup>28</sup> Iliff Interview (n 20) 41. An anecdote of Iliff regarding one of their meetings with the Egyptians is revealing of the Bank's (or perhaps rather of Woods's) persuasive powers: 'The Egyptians had been very difficult on this particular morning, and they had been chiseling a lot at certain proposals that we had put up to them as, in our view, an appropriate approach to this problem. Mr Woods had listened to them very patiently for about three quarters of an hour, and he suddenly got up from the table where he and I were sitting, and he walked over into a far corner of the room, and he put his hand underneath the lapel of his coat and he scratched his shoulder, in a very characteristic gesture of his which always indicates that some devastating remark is about to come out. He came back to the table and he sat down, and he looked at the Egyptians on the other side of the table and he said, "Look here, gentlemen, don't you realize that you have made the greatest steal in history since the Dutch bought Manhattan from the Indians for 20 bottles of gin? Stop your chiseling!" And the Egyptians did stop their chiseling. That was one of the breaks that we had in this particular situation . . .' (*ibid* 42).

government.<sup>29</sup> The Bank eventually also agreed to provide financing for improvements of the canal.<sup>30</sup>

### III. A ‘Special Forum’ for the Settlement of Investment Disputes

In the later years of Black’s presidency, increasing attention was being given in various fora, notably at the Organisation for Economic Co-operation and Development (OECD), to the contribution that private foreign investment could make to the development of developing countries. Perceptions of political risk, in particular the risk of expropriation, were seen as a major deterrent to investment in these countries. Measures under consideration to address the problem included the elaboration of a ‘code of conduct’ for host states in their treatment of foreign investment and the possible establishment of a multilateral organization to offer foreign investors insurance against political risks. In 1959, Germany introduced into the OECD’s predecessor organization a draft of the ‘code of conduct’ as a proposal for a multilateral treaty that might be adhered to by members and non-members alike. This was the famous Abs-Shawcross Draft Convention, which combined substantive protections of investment with provisions on the arbitral settlement of disputes, including investor-state disputes. Despite later iterations at the OECD, however, this project never progressed beyond the draft stage.<sup>31</sup> As to the investment insurance possibility, the Development Assistance Group of the OECD asked the Bank in

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<sup>29</sup> IBRD (n 27) 6.

<sup>30</sup> IBRD, *Fifteenth Annual Report 1959–1960* (IBRD 1960) 29.

<sup>31</sup> On the Abs-Shawcross Draft Convention (named for the leaders of the private initiative that produced it, Hermann J Abs of Deutsche Bank and Hartley Shawcross, a former British Attorney-General) and the OECD drafts based on it, see Georg Schwarzenberger, *Foreign Investment and International Law* (Stevens & Sons 1969) chs 8 and 10. After producing the first of its redrafts in 1962, the OECD asked the Bank if it would take over the project. The Bank declined to do so, believing that it could not bridge the gap between industrial and developing countries in this contentious area and still produce a meaningful document; cf World Bank Oral History Program, Interview of Aron Broches (23 May 1984) 30.

1961 to prepare a study of the possibility. The Bank acceded to the request without, however, committing itself to the ‘usefulness or feasibility’ of the idea.<sup>32</sup>

Embraced more warmly by the Bank was a third possibility examined in a report issued by the UN Secretary-General in 1960. This was to create by treaty a separate arbitration agency to which foreign investors might have independent access for the resolution of disputes with their host states. Given the difficulty of reaching agreement on a broader ‘code of conduct’, this could be ‘at least an intermediary solution’.<sup>33</sup> The report added that the separate arbitration mechanism might actually provide greater protection than a code of conduct; the former might be made to cover all investment disputes, while the protection of the latter would normally be limited to the rules that the parties had agreed in the code.<sup>34</sup>

The Bank’s previous experience with the settlement of investment disputes not only helped to persuade it to pursue this apparently more modest option; it also influenced the Bank’s design of it in providing for conciliation as well as arbitration given ‘that the Bank’s . . . experience . . . has indicated the value of conciliation’.<sup>35</sup>

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<sup>32</sup> See IBRD/IDA, Summary Proceedings, 1961 Meetings of the Board of Governors (Annual Address of Eugene R Black) (1961) 8. The Bank delivered its report to the OECD in 1962 and took no further action on the proposed scheme until it was asked by the OECD in 1965 to work towards the establishment of an international investment insurance agency along the lines indicated in a further report of the OECD. In response, the Bank commenced work on a charter of an international investment insurance agency. Successive drafts were prepared and discussed with the Executive Directors and member countries. Disagreements surfaced over key issues. Eventually, with broad support for the idea seemingly gone, the Bank ceased work on it in 1976. The creation under World Bank auspices of a globally operating investment guarantee scheme had to await the establishment of the Multilateral Investment Guarantee Agency in 1988. On this history, see Ibrahim F I Shihata, *MIGA and Foreign Investment* (Martinus Nijhoff 1988).

<sup>33</sup> The Promotion of the International Flow of Private Capital: Progress Report by the Secretary-General, United Nations Economic and Social Council, E/3325 (26 February 1960) 79.

<sup>34</sup> *Ibid.*

<sup>35</sup> Note by Aron Broches to the Executive Directors on the Settlement of Disputes between Governments and Private Parties (28 August 1961) 3, reprinted in ICSID, *History of the ICSID Convention*, vol 2 (ICSID 1968) 1.

Although Black regarded helping in the resolution of economic and financial disputes as an important part of the Bank's service to its membership,<sup>36</sup> he often remarked how arduous and time-consuming the task could be.<sup>37</sup> The new agency could help to relieve the Bank of such 'extra-curricular burdens'.<sup>38</sup>

These themes were brought together in Black's address to the annual meeting of the Board of Governors of the Bank in September 1961. In it, he observed that the settlement of disputes between governments and private investors was often mentioned in connection with promoting increased flows of investment to developing countries. He continued:

As most of you know, the Bank as an institution, and the President of the Bank in his personal capacity, have on several occasions been approached by member governments to assist in the settlement of financial disputes involving private parties. We have, indeed, succeeded in facilitating settlements in some issues of this kind, but the Bank is not really equipped to handle this sort of business in the course of its regular routine. At the same time, our experience has confirmed my belief that a very useful contribution could be made by some sort of special forum for the conciliation or arbitration of these disputes. The results of an inquiry made by the Secretary-General of the United Nations show that this belief is widely shared. The fact that governments and private interests have turned to the Bank to provide this assistance indicates the lack of any other specific machinery for conciliation and arbitration which is regarded as adequate by investors and governments alike. I therefore intend to explore with other institutions, and with our member governments, whether something might not be done to promote the establishment of machinery of this kind.<sup>39</sup>

Work soon began at the Bank, under the inspired leadership of Broches, on drawing up what would become the ICSID Convention. The work included the discussion of

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<sup>36</sup> Kraske et al (n 17) 96.

<sup>37</sup> See, eg, Black interview (n 18) 50.

<sup>38</sup> Note by A Broches to the Executive Directors on the Settlement of Investment Disputes (19 January 1962) 2, reprinted in *History of the ICSID Convention*, vol 2 (ICSID 1968) 6.

<sup>39</sup> IBRD/IDA, Summary Proceedings (n 32) 8.

successive drafts of the Convention by the Executive Directors, by legal experts designated by governments to participate in four regional consultative meetings, and, after the Board of Governors had formally requested the Executive Directors to formulate a text of the Convention for submission to member governments, by a legal committee of representatives of member governments convened to assist the Executive Directors in that task.<sup>40</sup> The work was completed by 18 March 1965 when the Executive Directors approved the final text of the Convention and submitted it to member governments for consideration with a view to signature and ratification. In accordance with its terms, the Convention came into force on 14 October 1966, thirty days after its twentieth ratification.

Today, almost fifty years later, 150 countries are parties to the Convention, and ICSID has a staff of sixty and a total cumulative caseload of over 470 investor-state cases. Appropriately enough, the Bank has largely shed its role as an ‘international mediator’ of investment disputes, ICSID having separately ‘institutionalize[d] the positive aspects of the 1950s mediation experiences’.<sup>41</sup> To that extent, ICSID might be viewed as a legacy of Black’s Bank.

As explained earlier, the conciliation procedure of ICSID certainly is such a legacy. Perhaps underestimating how uniquely effective the Bank or its head could be as a conciliator or mediator, there was disappointment at ICSID to see, almost from the start, the contrastingly low level of interest in its conciliation procedure. In its first twenty years, ICSID registered twenty-three arbitration cases and just two conciliations. Only seven more conciliation cases have been registered since.<sup>42</sup> On the other hand, many of the arbitration cases end as a successful conciliation might end, with an amicable

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<sup>40</sup> For a more detailed summary of these steps, see Report of the Executive Directors on the Convention on the Settlement of Investment Disputes between States and Nationals of Other States, reprinted in Doc ICSID/15, ICSID Convention, Regulations and Rules (April 2006) paras 6–8.

<sup>41</sup> Kapur et al (n 5) 13, 1191.

<sup>42</sup> See ICSID, The ICSID Caseload-Statistics (Issue 2014-2) 8.

settlement by the parties of their dispute.<sup>43</sup> The recent adoption by the International Bar Association of its Rules for Investor-State Mediation,<sup>44</sup> which can be used in an ICSID conciliation, may help to spark renewed interest in the ICSID procedure. Another step was taken in this direction recently, when a new list of designees of the Chairman of the ICSID Administrative Council to the Centre's Panels of Conciliators and of Arbitrators included, for the first time, a full complement of ten separate designees to the Panel of Conciliators.<sup>45</sup>

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<sup>43</sup> Cf Stephen M Schwebel, 'Is Mediation of Foreign Investment Disputes Plausible?' (2007) 22 ICSID Rev—FILJ 237, 240.

<sup>44</sup> Available at <<http://www.ibanet.org>> accessed 20 August 2014.

<sup>45</sup> See ICSID News Release, 'Designations to the ICSID Panels of Conciliators and of Arbitrators by the Chairman of the ICSID Administrative Council' (15 September 2011).