

**Legal proceedings
regarding the Greek PSI
before the Greek Council of State
(Conseil d'Etat)**

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Historical background

On 22nd of March 2013, the Greek Council of State (Highest Administrative Court) in plenary session has discussed 28 petitions for the annulment of:

- a) the decision of the Council of Ministers for the enactment of the PSI process,
- b) the Council of Ministers' decision for the approval of the Greek Government Bonds' (GGB) swap, implementing also application of Collective Action Clauses (CACs); and
- c) the Bank of Greece Act confirming the results of the GGBs holders voting process.

Classes of Petitioners

- Natural and legal persons (Greek and Foreign bondholders)
- Public legal persons and Social Security Funds, whose assets were part of the Common Fund of Public Law Legal Persons and Pension Funds ("Common Fund"), under the management of the Bank of Greece
- Suppliers of the Greek State (especial pharmaceutical companies) who received GGBs as repayment of the Republic's debts for pharmaceutical products delivered to public hospitals
- Former employees of Olympic Airways who received GGBs as a "compensation" within the meaning of labour law, after their labour contracts wereterminated within the framework of the privatisation of the national carrier

Main legal grounds for the annulment

- Breach through the Law introducing the CACs of individual rights arising from the Greek Constitution (GC) and especially
 - Property rights
 - The principle of equality
 - The justified trust in a fair public sector
 - The proportionality principle
 - The freedom of contract
- Breach of the European Convention of Human (ECHR) rights (article 1 of the First Additional Protocol) and the EU Charter of Fundamental Rights (EUCFR)
- Bad use of discretionary power (in conjunction with breach of the principle of equality)

Jurisdictional grounds of rebuttal – incompetence of the Highest Administrative Court

- Private (and not administrative) Law nature of the challenged acts
- The Hellenic Republic as GGB issuer no different than any other corporate issuer in distress and not in the exercise of public power
- Bank of Greece acted in the whole PSI process as “fiscus” (like any other private sector CSD) and not as authority exercising public power (received orders of participation to the PSI program, calculated and affirmed participation percentages, erased the initial bonds from the accounts of its System and registered the New Bonds)

Breach of freedom of contract and economic freedom:

The issue: CACs activation as measure of state intervention or as recovery measure in the framework of restructuring procedures?

➤ **Bondholders' Arguments**

- Illegal intervention by the legislator, by means of the insertion of CACs in pre-existing contracts (bonds) without the consent of the bondholders
- CACs change the terms of pre-existing contracts *retrospectively*

Breach of freedom of contract and economic freedom (cont)

➤ *Counter arguments*

- No retroactive imposition of CACs, but voluntary nature of CACs insertion
- The exchange of old bonds to new bonds was “voluntary” as:
 - Holders of Eligible Titles were invited to tender any and all Eligible Titles in exchange for New Titles
 - The modification of the bonds’ terms through the insertion of CACs was in essence a change in the way decisions are made (majority rule). The bondholders decided to accept the majority rule and exchange the old bonds with new bonds in accordance with the democratic principle:
- Amendment of decision-making rules of a collective body by way of law is not uncommon

Breach of freedom of contract and economic freedom

(cont - 2)

- **Necessity and proportionality (stricto sensu) of CACs**
 - Free rider and holdout issues / moral hazard:
 - CACs updated old-fashioned loan schemes and delimited possible speculative actions
 - Without CACs consenting bondholders would have to pay a higher price

Deprivation of property against the principles of the Constitution demanding full compensation upon Court Decision and the Human Rights Convention ?

➤ Rebuttal:

- No deprivation by means of public act, rather a change of GGB's terms through contractual means
- Bondholders' qualified majority decision to change the contractual relationship' structure of the bondholders with the issuer
- If restructuring failed, the bondholders would probably lose more (if not all) of the value of their bonds, especially in the likely case of a Greek “bankruptcy” or exit from the Eurozone.
- Haircut not harmful to the bondholders' interests, given the rather unlikely perspectives of the issuer to fulfill its obligations without such restructuring

Property rights arguments (cont.)

In any case:

- a. measures prescribed by law (fulfilled with the enactment of Law 4050/2012),
- b. in the public interest
- c. in accordance with the proportionality principle
- d. fair compensation:
 - New Bonds delivered to the bondholders constitute ‘adequate, prompt and effective’ compensation because:
 - the property of the bondholders has not been reduced or unfairly reduced : new bonds had in essence at least the same market value as the old ones on the day when the exchange took place and a better rating

Property rights arguments (cont.)

- The valuation method and procedure was reasonable, since the respective decision was taken by the supermajority of bondholders and, thus, had to be considered fair, given the circumstances
- Bondholder's interest was protected, considering the consequences of a possible disorderly insolvency on the value of the old bonds
- Thus: PSI and CACs procedure are fully balanced and justified taking into account the superior public interest involved which prevail over individual rights to property

Breach of principle of equality?

➤ **Breach of obligation of similar treatment of essentially similar cases ?**

Arguments:

- bondholders lifted the burden of the Hellenic Republic' s deficit while
 - depositors were protected (non their involvement in any hair cut scheme) and
 - banks were protected against their losses through recapitalization schemes
- Central Banks were exempted from the hair cut procedure
- Treasury bills were exempted

Breach of principle of equality? (cont.)

- **Breach of obligation of different treatment of essentially different cases?**
- Main argument:
 - bondholders - natural persons acted as depositors and not as investors and therefore should have been exempted and not treated the same way as the remaining bondholders / investors
- Rebuttal
 - No discriminatory treatment: provisions applied equally and without exception to all eligible bonds
 - Exemption of the Eurosystem and the Treasury Bills fully justified

Specific grounds arising from the particularities of special categories of bondholders

- **Pharmaceutical companies' arguments**
 - “special purpose” GGBs: not acquired for investment purposes but issued for the repayment of outstanding debts of the Republic for services and products already delivered : a different treatment imposed by the Constitution
- **Argument of former employees of Olympic Airways who were terminated, when the company was privatised**
 - “special purpose” GGBs: not acquired for investment purposes but issued as “compensation” (in the sense of Labour Law) of the former employees of Olympic Airways : a different treatment imposed by the Constitution

➤ **Arguments presented by public legal persons (e.g. Chamber of Commerce) and Pension Funds, whose funds were deposited to the Common Fund concerning the BoG decision to vote for the bonds' swap**

- Common fund: pool of assets managed by the Bank of Greece by law
- Assets invested by law exclusively in GGBs

Rebuttal

- Bank of Greece, as manager of the Common Fund, acted not in the exercise of public power but as a private entity
- The BoG's decision as Common Fund manager to accept the bonds' swap fully justified

➤ **German bondholders invoked the protection of Bilateral Investment Treaty between Greece and Germany on mutual promotion and protection of investment capitals**

Summary

- The Greek Law on the PSI and the CACs not a confiscation tool neither a measure of state intervention, rather a private law driven restructuring / recovery tool
- Equal treatment of all beneficiaries of GGBs, governed by Greek Law, without differentiation of the incentives for the GGB's acquisition
- The bondholders justifiably treated as investors and not as depositors
- The holding system of GGB's made impossible the identification of the end / ultimate bondholders
- The free transferability of the bonds would made a different treatment of specific GGB's classes unfounded
- It can be strongly and solidly argued that the Greek Law on the PSI and the CACs and the Ministerial Decisions, as well as the BoG Act, issued so far on the basis of such Law are not in violation of hierarchically supreme rules of law, such as the Greek Constitution or the European Convention on Human Rights.