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31 August 2001

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Professor Dr. Jochen Abr. Frowein
Professor Mathias Krafft
Professor Paul Lagarde
Professor Albert Jan van den Berg
Arbitration Tribunal Established Pursuant to Article XV
of the Agreement signed at The Hague on 20 January 1930

Notice of Arbitration

Members of the Tribunal:

On behalf of First Eagle SoGen Funds, Inc. ("First Eagle"), we submit this Notice of Arbitration pursuant to Articles 3 and 4 of the Rules for Arbitration Between the Bank for International Settlements and Private Parties (the "Rules").

1. *Demand.* Subject to the reservation of all jurisdictional objections, First Eagle demands arbitration of the dispute set forth in this Notice, which arises from the cancellation on or about 8 January 2001 by the Bank for International Settlements (the "Bank" or "BIS") of the registration of shares of the Bank held by First Eagle.

2. *Parties.* Claimant First Eagle SoGen Funds, Inc., is a U.S.-registered mutual fund group organized under the laws of the State of Maryland, United States of America. First Eagle is managed by Arnhold and S. Bleichroeder Advisers, Inc., a U.S.-registered investment adviser. First Eagle has its address and principal place of business at 1345 Avenue of the Americas, New York, New York 10105. Its telephone and telecopy numbers are 1-212-698-3200 and -299-4400, respectively. First Eagle invests on behalf of more than 100,000 individual investors and their savings, education, and retirement accounts.

Respondent Bank for International Settlements was established pursuant to the Hague Agreements of 20 January 1930, and chartered under the laws of Switzerland as a company limited by shares. It has its address and headquarters at CH-4002 Basel, Switzerland. Its telephone and telecopy numbers are 41-61-280-8080 and –8100, respectively.

3. *Arbitration provisions.* In an action initiated by First Eagle against the Bank in the United States District Court for the Southern District of New York, the Bank has taken the position that the disputes set forth in this Notice are subject to arbitration under Article 54 of the Statutes of the Bank for International Settlements (the "Statutes").

Article 16 of the Rules provides that the Tribunal has jurisdiction to determine its own jurisdiction. First Eagle reserves its position on all questions of jurisdiction. In particular, First Eagle reserves its right to raise the question whether Article 54 may be enforced when all Members of the Tribunal have been appointed by governments that own central banks (a) whose officials, sitting as directors of the Bank, took the actions at issue, and (b) whose own shares will be affected in value by the actions First Eagle challenges.

4. *Agreement or relationship from which the dispute arises.* As of 8 January 2001, First Eagle owned 9085 shares of the Bank for International Settlements, or approximately 12.51% of its publicly traded shares. On that date, the Bank purported to cancel the registration of those shares and all other publicly traded shares, in exchange for compensation determined by its Board in the amount of CHF 16,000 (approximately USD10,500) per share.

5. *Nature and circumstances of the dispute.* The compensation paid by the Bank for First Eagle's and all other publicly traded shares is dramatically lower than their true value. The Bank's actions in cancelling these shares and offering in exchange inadequate compensation constituted fundamental breaches of its statutory, contractual, and fiduciary obligations to First Eagle, depriving First Eagle of valuable property rights and unjustly enriching the remaining shareholders.

a. *The Bank's establishment.* The establishment of the Bank in 1930 implemented one of the principal recommendations of the Young Plan, the product of a committee of experts that was charged with addressing the recurring financial problems created by the collection of World War I reparations. The Bank was created as and remains a banking institution that would earn and distribute profits.

The Young Plan was implemented by the Agreement Regarding the Complete and Final Settlement of the Question of Reparations, signed at The Hague on 20 January 1930 ("the Reparations Treaty"). On the same day, the United Kingdom, Belgium, France, Italy, Japan, and Germany, on the one hand, and Switzerland, on the other, signed a Convention regarding the Bank for International Settlements ("the Bank Convention"). Under Article 1 of the Bank Convention, Switzerland undertook to grant a Constituent Charter to the Bank. Later, on 10 January 1987, the Bank entered into a Headquarters Agreement with the Swiss Federal Council.

The Charter formed part of the Convention, provided for the incorporation of the Bank and its initial capitalization, and granted the Bank limited immunities from taxation and expropriation. It contained the Statutes of the Bank, which, pursuant to Article 2 of the Charter, governed the Bank's "constitution, operations and activities." The Charter and Statutes of the Bank are attached to this Notice as Exhibit 1.

b. *The Bank's capitalization.* Under Article 1 of its Statutes, the Bank is constituted "a company limited by shares." The Bank was capitalized, in part, by offerings of shares to the public.

The subscription of the original authorized capital of 200,000 shares was guaranteed in equal parts by the founding institutions of the Bank: the central banks of Belgium, France, Germany, Great Britain, Italy, and Japan and, as reflected in the Charter, "a banking group including Messrs. J.P. Morgan & Company of New York, the First National Bank of New York, New York, and the First National Bank of Chicago, Chicago." In 1930, each of the seven guarantors subscribed to an equal portion of a block of shares totaling more than half the authorized number, and two years later the remaining shares were sold to other central banks or subscribed, again in equal portions, by the seven guarantors. The United States was not a party to the Reparations Treaty or the Bank Convention, and its central bank, the Federal Reserve Bank, did not originally and has not since subscribed to the Bank's shares.

Article 15 of the Statutes permitted "[a]ny subscribing institution or banking group [to] issue or cause to be issued to the public the shares for which it has subscribed." The U.S. banking group resold a majority of the shares of the U.S. tranche to U.S. public investors, ensuring widespread distribution of the Bank's shares in the U.S. financial market. The shares underwritten by the U.S. banking group were distributed for resale to approximately 100 U.S. financial institutions. A portion of the Belgian and French tranches were also sold to public shareholders.

All shares were sold at the same price. No distinction was made in pricing based on whether the shares were subscribed by a central bank or underwritten by a banking group for resale to the public.

In 1969, the Statutes were amended to authorize second and third tranches of 200,000 shares each. The second tranche was offered to existing shareholders, including those who held publicly traded shares, while the third tranche was reserved for central banks.

Since 1969, the Bank has sold shares to numerous central banks. In setting a price for the shares, it appears to have valued the shares by reference to the net asset value of the Bank, but then sold the shares at a discount from that value. The basis for that discount has not been disclosed.

Until the Bank's cancellation of the publicly traded shares, the U.S. and Belgian issues traded on the Swiss Exchange and the French issue on the Paris Bourse.

c. *The Bank's shares.*

The Bank has only one class of shares, and, in its own words, all shares "carry identical property rights." Specifically, under Article 13 of the Statutes, all shares "carry equal rights to participate in the profits of the Bank and in any distribution of assets," including by liquidation. Article 52 expressly confirms that the equality of property rights encompasses the reserve funds. Conversely, under Article 14, none of the shares carries voting rights.

Prior to their amendment on 8 January 2001, the Statutes contained no provision for cancellation, redemption, or mandatory repurchase of the Bank's shares.

d. *The Bank's governance.*

Under Article 26 of the Statutes, administration of the Bank is vested in its Board, and under Article 40, the Board is authorized to appoint management. The Governors of the central banks of Belgium, France, Germany, Great Britain, Italy, and the United States serve as ex-officio members of the Board, and they are authorized to appoint other central bankers as members of the Board. Article 30 prohibits other government officials from serving on the Board.

Under Article 14, the right of representation and voting at the general meeting of the Bank is exercised by central banks or their nominees "in proportion to the number of shares subscribed in each country."

e. *The Bank's exclusion of its public shareholders.*

By a "Note to Private Shareholders" dated 15 September 2000 ("the Note"), the Bank announced that it had determined that the presence of shareholders that were not central banks was incompatible with the objectives it wished to pursue. According to the Bank, the existence of such shareholders, "whose interest is essentially financial," was "no longer seen to be in line with the international role and future development of the organization." Hence, the Bank further announced, it would amend its Statutes to (a) restrict ownership of shares exclusively to central banks; (b) "exclude" present shareholders who were not central banks against compensation of CHF 16,000 per share;

and (c) "provide for the redistribution of the shares withdrawn from the public to central-bank shareholders of the BIS." A copy of the Note is attached to this Notice as Exhibit 2.

The Note acknowledged that the Bank must pay "fair compensation" to the excluded shareholders. It also provided a summary of a valuation report prepared by J.P. Morgan & Cie S.A. "on behalf of the BIS and in agreement with the latter as to the valuation methods chosen and assumptions used," on which the Bank relied to justify the compensation offered.

Notwithstanding the status of each of the members of the Board as an official of a central bank whose shares would increase in value if the excluded shareholders were undercompensated, the Bank did not appoint an independent committee charged with protecting the interests of the public shareholders or take any other steps to ensure a disinterested determination. Nor did the Note attempt to describe J.P. Morgan as independent. As a bank subject to regulation by one or more of the central-bank shareholders with an interest in the result of its valuation, J.P. Morgan could not have been credibly so described. Instead, the Bank claimed that it had obtained "confirmation by an independent expert" of J.P. Morgan's valuation in the form of what it described as a fairness opinion by Barbier Frinault & Associés. This accounting firm did not do its own valuation, but merely opined that the recommended compensation was fair because J.P. Morgan's methodologies were "suit[able]," its assumptions "realistic," and its discounts "reasonable."

According to the Note, J.P. Morgan relied primarily on a dividend perpetuity model for its valuation, a method that attempts to estimate the present value of future flows of dividends. In setting that value, J.P. Morgan was instructed to assume that the Bank would pay a level of dividends that was "only a small fraction of profits." The assumed rate represented a lower ratio of dividends to profits than the Bank had historically paid.

The Note also advised that J.P. Morgan had taken account of the Bank's adjusted net asset value, or "NAV," which it calculated at USD 19,099 (that is, nearly twice the level of compensation determined by the Bank). The Note stated, however, that the assets of the Bank should properly be viewed as "a cushion for the international financial system," rather than, apparently, the property of the shareholders. The Note then advised that, based on lack of voting rights, limited marketability, and limited liquidity of the shares, "it was deemed appropriate to apply a discount estimated at 45% to the NAV."

From the point at which it learned of the Bank's proposed actions, First Eagle has challenged those actions and sought basic information. On one occasion, the Bank permitted representatives of First Eagle to review the J.P. Morgan report, but it has steadfastly refused to provide First Eagle with a copy. It has also steadfastly refused repeated requests for the underlying information that would allow it to assess properly J.P. Morgan's methods and results and the Board's action in approving both the exclusion of First Eagle and other shareholders and the level of compensation. For example, the information provided by the Bank does not permit First Eagle to perform even a rudimentary independent calculation of the Bank's net asset value, to assess adequately the sources of its profits and losses, or to make an independent determination of its future profitability.

On 8 January 2001, at an Extraordinary General Meeting, the Bank approved the actions described in the Note. The exclusion of First Eagle and the other shareholders who had bought their shares on the public markets was effected by the amendment of the Statutes to add Article 18(A), which was described as a "transitional provision."

On 11 June 2001, First Eagle tendered its shares in exchange for the determined compensation on the basis of the Bank's representation that tendering shareholders did not waive the right to challenge the transaction or the compensation.

f. *The dispute.*

Put simply, the compensation provided to the Bank's public shareholders upon their involuntary "exclusion" from the company is grossly inadequate. A share of a company such as the Bank represents an ownership interest in the company, and a shareholder is an owner. The Bank cannot solicit and use its shareholders' capital to amass its considerable assets and then tell certain shareholders that it is not only forcing them out, but giving them less than their proportionate share of the company. It cannot sell shares that carry identical property rights with all others and then, upon excluding certain owners of those shares, tell those owners that their shares are worth less than those of all remaining owners.

Fair compensation for First Eagle's shares cannot be less than its proportionate share of the value of the Bank as a whole, and that value cannot be less, though it should be more, than the Bank's net asset value. As the Bank acknowledged in the Note, the Bank's NAV "represents [its] intrinsic value." Net asset value is a particularly reliable indicator of value in the case of a financial institution, whose assets and liabilities are readily measured, and even more so in the case of a financial institution, like the Bank by virtue of Article 25 of its Statutes, that is charged to pay particular regard to maintaining liquidity. Indeed, net asset value must be considered the *minimum* value, because it does not take account of the value of the business as a going concern.

There is no justification for the discounts to NAV applied by the Bank. Each of the characteristics identified by the Bank – that the shares do not carry voting rights and that they have limited marketability and liquidity – apply equally to *all* of the Bank's shares. If anything, the shares held by central banks are less liquid than those publicly traded. Implicit in the Bank's position is the notion that, notwithstanding the guarantee in the Statutes that all shares carry identical property rights, the Bank has two classes of shareholders: the privileged, central-bank shareholders, and the disfavored, now excluded, shareholders who bought their shares on the public markets.

The inadequacy of the compensation can also be measured by the effect of the transaction on the remaining shareholders. The Bank acknowledges that, to the extent the compensation paid the excluded shareholders is less than NAV, it represents less than those shareholders' proportionate share of the intrinsic value of the Bank. Hence, by operation of the exclusion of the public shareholders, the value of the remaining shares has been increased by at least that difference. In other words, by forcing out the public shareholders at compensation measured at less than NAV, the central-bank shareholders have enriched themselves by appropriating at least that marginal value. Using the Bank's own figures, the value that the central-bank shareholders have transferred to themselves exceeds USD 600 million.

Finally, there is a procedural dimension to fair compensation, of which two essential components are disinterested decisionmaking and full disclosure. Here, the process must be considered fatally flawed when each of the directors who approved the transaction is an official of a central bank that also owns Bank shares and hence has a direct financial interest in the level of compensation provided to the excluded shareholders. Yet no steps were taken to address that conflict of interest, a failure that constituted a fundamental breach of the solemn duty of loyalty owed by directors to *all* shareholders – including, here, those the Bank wished to exclude. Equally, the compensation cannot be considered fair when the excluded shareholders have been denied the information on the basis of which J.P. Morgan made its recommendations and the Board acted.

In sum, the Bank's action in cancelling the registration of the publicly traded shares in exchange for compensation that is dramatically less than their true value breached (a) its own Statutes and governing instruments; (b) time-honored principles of law governing the duties of corporate directors and the rights of corporate shareholders; and (c) general principles of law barring unjust enrichment.

6. *Relief sought.*

Subject to questions of jurisdiction, First Eagle respectfully requests that this Tribunal issue an award

(a) declaring that the Bank must provide First Eagle full disclosure concerning the basis of the Board's action reflected in the Note of 15 September 2000 and the amendment to the Statutes effected at the Extraordinary General Meeting of 8 January 2001;

(b) declaring that the Bank has an obligation to pay First Eagle the full value of its proportionate interest in the Bank as a whole, which must equal, at a minimum, the Bank's net asset value, adjusted upward for dilution caused by prior sales at less than full value;

(c) declaring that the Bank must pay First Eagle consequential damages resulting from the Bank's unlawful actions;

(d) declaring that the Bank must disgorge to First Eagle the full value by which the remaining shareholders have been unjustly enriched by the cancellation of First Eagle's shares;

(e) granting First Eagle damages in an amount to be determined at the hearing, but in excess of USD 75 million;

(f) granting First Eagle interest on compensation paid by the Bank and sums awarded by the Tribunal calculated from 8 January 2001;

(g) granting First Eagle the costs of the arbitration; and

(h) granting First Eagle such further relief as the Tribunal deems just and proper.

7. *Appointment of representatives.* First Eagle hereby appoints as its representatives Debevoise & Plimpton, by John H. Hall and Donald Francis Donovan, 919 Third Avenue, New York, New York 10022 U.S.A. (telephone: 1-212-909-6000; telecopy: -6836).

Respectfully submitted,

Donald Francis Donovan

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