From Creditor Protection to Preventing Holdouts: Mapping the Evolution of the Law on Sovereign Debt Defaults and Restructurings

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Abstract

The law on sovereign debt defaults and restructurings is heavily fragmented. The norms applying to sovereign debt are scattered across several legal regimes and interpreted by a broad array of jurisdictions, leading to a highly contradictory case-law. At the scholarly level, sovereign debt is seldom treated holistically. Commentators tend to focus on either the domestic law aspects of the debt relationship, or its international law aspects. In addition, sovereign debt as a of legal studies topic is heavily under-theorised.

The purpose of this thesis is to provide a global framework to systematise the law on sovereign defaults and restructurings, both at the domestic and at the international level. This framework makes sense of the contradictions plaguing the legal study of sovereign debt. It also contextualises the changes which recently occurred within the law, and allows mapping the whole impact of legal norms on sovereigns and their creditors. The result is a better understanding of how the law on sovereign debt incentivise stakeholders within the debt relationship.

This thesis understands the evolution of the law on sovereign debt since the 1970 as a succession of two paradigmatic regulatory models: the creditor protection model and the anti-holdout model. Under the first model, norms on sovereign debt sought to incentivise the extension of credit to sovereigns by providing creditors with access to independent courts and efficient judicial remedies. From the 1990s onwards, these remedies enabled vulture funds and retail investors to heavily disturb restructuring processes, often at the cost of the debtor’s population. In response to these inefficiencies the anti-holdout model was developed. Its purpose it to disincentivise litigation on sovereign debt to facilitate the restructuring of unsustainable debts. This new model relies on majority-based restructuring decisions, a limitation of remedies available to holdout creditors, and the provision to the sovereign of liquidities to facilitate its return to debt sustainability.

Understanding that these changes are united by a paradigmatic vision of how sovereign debt should be regulated creates a clearer picture of the blind spots in the current regulation of sovereign debt. Notably, this thesis will show that the recent legal changes lead to an increase in the risk of fragmentation of the regime, creates a system that heavily disfavours retail holders of sovereign debt, and does little to incentivise sovereigns to restructure unsustainable debts.

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Author's Declaration

"I declare that, except where explicit reference is made to the contribution of others, that this dissertation is the result of my own work and has not been submitted for any other degree at the University of Glasgow or any other institution."

Printed Name: Alexandre Belle

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1. Introduction

1.1 Background

1.1.1 Ubiquitous indebtedness and a changing regulatory environment

Sovereign debt, in the 21st century, is quasi-universal. Most States regularly access capital markets in order to borrow the amounts necessary to the pursuit of their public mission[1]. Sovereign bonds[2], the financial instrument underlying most of the world's sovereign debt, heavily feature in many a financial portfolio, from those of retail investors, to the holdings of pension or other investment funds, as well as on the books of most of the world's banks[3].

Sovereign defaults and restructurings[4] have also been a near constant feature of the recent years. The early 2000s and 2010s were marked by two high profile sovereign debt crises, Argentina's and Greece's, leading to the two largest recorded sovereign debt reductions in history[5].

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[1] A recent IMF study finds data on sovereign borrowing since the 1950s in at least 190 States. Samba Mbaye, Marialuz Moreno Badia and Kyungla Chae, 'Global Debt Database: Methodology and Sources' (2018) 18 IMF Working Paper.

[2] Bonds, traditionally, are defined as 'negotiable debt securities'. Philip R Wood, *International Loans, Bonds and Securities Regulation* (Sweet & Maxwell 1995) 9., quoted in Michael Waibel, *Sovereign Defaults before International Courts and Tribunals* (Cambridge University Press 2011) 13 <http://ezproxy.lib.gla.ac.uk/login?url=http://dx.doi.org/10.1017/CBO9780511974922> accessed 12 November 2015. A sovereign bond is a negotiable debt security issued by a sovereign, or on behalf of a sovereign, by a bank. Bonds 'evidence the obligation of the borrower to pay to their holder, an agreed interest on the loan, the principal at maturity, and to amortize the issue in a specified manner.' Edwin Borchard and Justus S Hotchkiss, *State Insolvency and Foreign Bondholders: General Principles* (Beard Books 1951) 23. Quoted in Waibel, *Sovereign Defaults before International Courts and Tribunals* 13.

[3] For an overview of sovereign debt holdings see Serkan Arsanalp and Takahiro Tsuda, 'Tracking Global Demand for Emerging Market Sovereign Debt' (2014) 14 IMF Working Paper; 'Sovereign Bond Holdings | Bruegel' <https://bruegel.org/publications/datasets/sovereign-bond-holdings/> accessed 23 January 2020; IMF, 'Sovereign Investor Base Dataset for Emerging Markets' <https://www.imf.org/~/media/Websites/IMF/imported-datasets/external/pubs/ft/wp/2014/Data/wp1439.ashx>.

[4] A sovereign debt restructuring, is understood as the process via which an overindebted sovereign reduces the amount, maturity, or conditions of its current debt, usually in cooperation with its creditors, with the aim of returning to debt sustainability. They usually rely on a voluntary exchange of "outstanding sovereign debt instruments" against "new debt instruments or cash, through a legal process". Udaibir Das, Michael Papaioannou and Christoph Trebesch, 'Sovereign Debt Restructurings 1950–2010: Literature Survey, Data, and Stylized Facts (WP/12/203)' 7.

[5] While these two restructuring processes have occupied the centre of the discussion regarding sovereign debt, both in the press and academia, they are far from the only recent occurrences of defaults and restructuring. Notably, at the time of writing, Venezuela is in the midst of a sovereign default. Similarly, in 2016, Ukraine defaulted on its external debt, Cote d'Ivoire underwent a restructuring in 2011, Nigeria in 2004, etc. See e.g. Lee C Buchheit and G Mitu Gulati, 'How to Restructure Venezuelan Debt (¿Cómo Restructurar La Deuda Venezolana?)' (Social Science Research Network 2017) SSRN Scholarly Paper ID 3006680 <https://papers.ssrn.com/abstract=3006680> accessed 6 December 2018; 'Venezuela in "Selective Default"'

The impact of sovereign debt crises goes beyond the often-mentioned astronomic sums involved in restructurings. Debt crises force sovereigns to juggle between debt repayment, guaranteeing future in-flows of capital, and the very pressing current needs of their population. This fiscal pressure usually results in austerity, often leaving the most destitute at risk[6]. At the time of writing, with the world's greatest recession looming as a result of the coronavirus pandemic, the question of sovereign debt and debt repayment is undeniably pressing[7]. The world's poorest and middle economies may very well, in the coming months, be forced to choose between defaulting today to suffer market sanctions tomorrow, or repaying and sacrifice lives.

Beyond the undeniable impact of restructurings on the debtors' population, the losses restructurings cause to actors within the global financial system can threaten to trigger worldwide crises, as was the case both during the 1980s Latin American crisis[8] and the recent Greek crisis[9]. Losses to banks and other vital financial institutions go beyond loss of share value. Banking crises lead to lending droughts, causing unemployment, recessions and other financial hardships for many[10]. When bonds of a defaulting sovereign are held by retail

(14 November 2017) <https://www.bbc.com/news/world-latin-america-41982069> accessed 7 May 2019. See also, the annexes in Rodrigo Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (Sweet & Maxwell 2009).

[6] Cephas Lumina, 'Report of the Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, Particularly Economic, Social and Cultural Rights (Mission to Argentina)' (UNHRC 2014) A/HRC/25/50/Add.3; Cephas Lumina, 'Report of the Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, Particularly Economic, Social and Cultural Rights (Mission to Greece)' (UNHRC 2014) A/HRC/25/50/Add.1; Cephas Lumina, *Sovereign Debt and Human Rights: Making the Connection* (Oxford University Press 2018) <http://www.oxfordscholarship.com/view/10.1093/oso/9780198810445.001.0001/oso-9780198810445-chapter-10> accessed 7 February 2020; Michael Riegner, 'Legal Frameworks and General Principles for Indicators in Sovereign Debt Restructuring' (2016) 41 Yale Journal of International Law 141, 168; Juan Pablo Bohoslavsky, 'Economic Inequality, Debt Crises and Human Rights' (2016) 41 Yale Journal of International Law 177.

[7] At the time of submission, an embryo of solution has been put forward by the G-20, the IMF and the World Bank. See 'G20 Finance Ministers and Central Bank Governors Meeting 15 April 2020 [Virtual]' <https://g20.org/en/media/Documents/G20_FMCBG_Communiqu%C3%A9_EN%20(2).pdf> accessed 21 April 2020; 'IIF Statement Following the Conclusion of the G20 Finance Ministers and Central Bank Governors Virtual Meeting' <https://www.iif.com/Press/View/ID/3856/IIF-Statement-Following-the-Conclusion-of-the-G20-Finance-Ministers-and-Central-Bank-Governors-Virtual-Meeting> accessed 21 April 2020. For early criticisms of the scheme laid down in these declarations see Patrick Bolton and others, 'Born Out of Necessity: A Debt Standstill for COVID-19' (*Economics for Inclusive Prosperity*) <https://econfip.org/policy-brief/born-out-of-necessity-a-debt-standstill-for-covid-19/> accessed 23 April 2020.

[8] Manuel Monteagudo, 'The Debt Problem: The Baker Plan and the Brady Initiative: A Latin American Perspective' (1994) 28 The international lawyer 59.

[9] Lamont Black and others, 'The Systemic Risk of European Banks during the Financial and Sovereign Debt Crises' (2016) 63 Journal of Banking & Finance 107.

[10] Bohoslavsky (n 6) 186.

investors, restructurings can mean the erasure of hard-earned savings, usually for middle- and lower-class individuals who lacked access to more sophisticated investment vehicles.

On top of this undeniable relevance, the law on sovereign debt has recently been the object of several developments, leading to constant attention by legal commentators over the last ten to twenty years. First, sovereign bonds have been heavily amended to include collective action clauses[11]. The *pari passu* clause, topic of much contention, has been the object of recent re-drafting by the International Capital Market Association[12], following calls for change by the IMF[13] and much of the scholarship on sovereign debt[14]. The domestic legislation on sovereign debt has also faced changes, with Belgium and France enacting special ‘anti-vulture funds’ legislation[15], and with the UK and Belgium enacting dispositions designed to reinforce the immunities of sovereigns facings debt crises[16].

At the international level, norms on sovereign debt faced a quasi-revolution with sovereign bonds being, for the first time, the object of litigation before ICSID Tribunals[17]. At the same time, sovereign debt was the object of high-profile cases before the European Court of Human Rights[18] and the European court of Justice[19], and even litigation before the International Tribunal for the Law of the Sea[20]. This surge in international litigation on

[11] On CACs see e.g. Antonia E Stolper and Sean Dougherty, ‘Collective Action Clauses: How the Argentina Litigation Changed the Sovereign Debt Markets’ (2017) 12 Capital Markets Law Journal 239; Anna Gelpern, Ben Heller and Brat Setser, ‘Count the Limbs. Designing Robust Aggregation Clauses in Sovereign Bonds’, *Too Little Too Late: The Quest to Resolve Sovereign Debt Crises* (Columbia University Press 2016); Mark Weidemaier and Mitu Gulati, ‘A People’s History of Collective Action Clauses’ [2014] Virginia Journal of international law 1.

[12] International Capital Markets Association, ‘Standard Pari Passu Provision for the Terms and Conditions of Sovereign Notes.’ <https://www.icmagroup.org/assets/documents/Resources/ICMA-Standard-Pari-Passu-Provision-August-2014.pdf.> accessed 2 November 2019.

[13] International Monetary Fund, ‘Third Progress Report on Inclusion of Enhanced Contractual Provisions in International Sovereign Bond Contracts’ <https://www.imf.org/en/publications/search?series=Policy+Papers> accessed 2 November 2019.

[14] See notably Rodrigo Olivares-Caminal, ‘Rank Pari Passu or Not to Rank Pari Passu: That Is the Question in Sovereign Bonds after the Latest Episode of the Argentine Saga’ (2009) 15 Law and Business Review of the Americas 745; Lee C Buchheit and Jeremiah S Pam, ‘Pari Passu Clause in Sovereign Debt Instruments, The’ (2004) 53 Emory Law Journal 869; Mark LJ Wright, ‘Interpreting the Pari Passu Clause in Sovereign Bond Contracts: It Is All Hebrew (and Aramaic) to Me’ (2014) 9 Capital Markets Law Journal 259.

[15] Loi du 12 juillet 2015 relative à la lutte contre les activités des fonds vautours 2015 (Moniteur Belge 16/09/2015) 58113; LOI n° 2016-1691 du 9 décembre 2016 relative à la transparence, à la lutte contre la corruption et à la modernisation de la vie économique 2016 (2016-1691).

[16] Debt Relief (Developping Countries) Act 2010; Loi visant à empêcher la saisie ou la cession des fonds publics destinés à la coopération internationale, notamment par la technique des fonds vautours 2008.

[17] *Abaclat and Others v Argentine Republic* [2011] ICSID ARB/07/5; *Giovanni Alemanni and Others v The Argentine Republic (Decision on Jurisdiction and Admissibility)* [2014] ICSID ARB/07/8; *Ambiente Ufficio S.pA and others v Argentine Republic* [2013] ICSID ARB/08/9; *Poštová banka, a.s and Istrokapital SE v Hellenic Republic (Award)* [2015] ICSID ARB/13/8.

[18] *Mamatas et autres v Greece* [2016] European Court of Human Rights 63066/14; 64297/14 and 66106/14.

[19] *Alessandro Accorinti and others v European Central Bank* [2015] European Court of Justice T-79/13.

[20] *The ‘ARA Libertad’ case (Argentine v Ghana)* (International Tribunal for the Law of the Sea).

sovereign debt was accompanied by the publicatio, of two sets of principles by UNCTAD[21] and the UN General Assembly[22].

These developments have been accompanied by a particularly contradictory case-law[23]. Some jurisdictions have characterised sovereign debt restructuring as *acta de iure gestionnis*[24], others as *acta de iure imperii*[25]. Sovereign bonds have both been characterised as investments for the purpose of the ICSID convention by some arbitral tribunals[26], and not by another[27]. A least four different interpretation of the infamous *pari passu* clause have been put forward by domestic courts[28]. There are stark contradictions within the international law on economic necessity[29], and heavy doubts regarding how it would apply to sovereign debt[30]. Finally, there are debates surrounding the normativity and content of the UNCTAD principles and the UNGA resolution on sovereign debt[31].

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[21] United Nations Conference on Trade and Development, 'Principles on Promoting Responsible Sovereign Lending and Borrowing' <http://unctad.org/en/PublicationsLibrary/gdsddf2012misc1_en.pdf>.

[22] United Nations General Assembly, 'Resolution 69/319: Basic Principles on Sovereign Debt Restructuring Processes' <http://www.un.org/en/ga/search/view_doc.asp?symbol=A/RES/69/319>.

[23] On the general state of the law on debt and debt restructurings, Klabbers notes: 'The innocent Martian landing on earth may be forgiven the somewhat bewildered look in her eyes when surveying the situation regarding regulation of international financial matters' Jan Klabbers, 'On Functions and Finance: Sovereign Debt Workouts and Equality in International Organizations Law' (2016) 41 Yale Journal of International Law 241, 241.

[24] *Republic of Argentina v Weltover, Inc* (1992) 504 US 607 (Supreme Court).

[25] *Ordinanza* (2005) 2005 RDI 856 (Corte di Cassazione).

[26] *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17); *Abaclat and Others v. Argentine Republic* (n 17); *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17).

[27] *Poštová banka, a.s. and Istrokapital SE v. Hellenic Republic (Award)* (n 17).

[28] See e.g.: *Elliott Assocs, LP v Banco de la Nacion* [2000] New-York Southern District Court 194 F.R.D. 116; *NML Capital, LTD, et al v The Republic of Argentina* [2012] United State Court of Appeals for the Second Circuit 12-105(L); *Export-Import Bank of the Republic of China v Grenada* [2014] United States Court of Appeals, second Circuit 12–2619–CV.

[29] Michael Waibel, 'Two Worlds of Necessity in ICSID Arbitration: CMS and LG&E' (Social Science Research Network 2007) SSRN Scholarly Paper ID 1566488 <http://papers.ssrn.com/abstract=1566488> accessed 21 March 2016; August Reinisch, 'Necessity in International Investment Arbitration— An Unnecessary Split of Opinions in Recent ICSID Cases?: Comments on CMS v. Argentina and LG&E v. Argentina' (2007) 8 The Journal of World Investment & Trade vii.

[30] August Reinisch and Christina Binder, 'Debts and State of Necessity', *Making Sovereign Financing and Human Rights Work; Bohoslavsky J. P. and Cernic J. L (eds)* (1st edn, Hart Publishing 2018).

[31] Michael Waibel, 'Out of Thin Air?' in Carlos Espósito, Yuefen Li and Juan Pablo Bohoslavsky (eds), *Sovereign Financing and international law* (Oxford University Press 2013) <http://www.oxfordscholarship.com/view/10.1093/acprof:oso/9780199674374.001.0001/acprof-9780199674374-chapter-5> accessed 3 October 2016; Robert Howse, 'Concluding Remarks in the Light of international law' in Carlos Espósito, Yuefen Li and Juan Pablo Bohoslavsky (eds), *Sovereign Financing and international law* (Oxford University Press 2013) <http://www.oxfordscholarship.com/view/10.1093/acprof:oso/9780199674374.001.0001/acprof-9780199674374-chapter-17> accessed 6 October 2016.

1.1.2 The 'non-system'[32] on sovereign debt

Sovereign debt, as a social phenomenon, inherently crosses the traditional boundary between domestic and international law. On the one hand, the legal instrument underlying the debt is contractual, subject to domestic law[33], and the main forum for dispute settlement is often domestic[34]. Thus, failure to pay by the sovereign will be first and foremost treated as a breach of contract. Similarly, debt restructurings are either regulated in contractual instruments or subject to general principles of domestic contract law.

On the other hand, the sovereign nature of the debtor roots sovereign debt within public international law. Questions relative to State debt have been addressed in specific bilateral or multilateral instruments[35]. There is also one multilateral treaty dealing with matters relative to sovereign debt: the 1983 Vienna Convention on the Succession of States in respect to State Property, Archives and Debt[36].

Despite its perpetual relevance, neither custom, nor the general principles of international law seem to have developed *ad hoc* norms applicable to sovereign debt[37]. Indeed, sovereign debt restructurings, despite constituting an important source of State practice, do not seem to have led to the creation of international custom. State practice, to lead to the creation of normative custom needs to be accompanied by a subjective element, the *opinio iuris cive necessitatis*[38]. As sovereign debt restructurings are usually agreed upon on an *ad hoc* basis, it follows that no *opinio iuris* can emerge from sovereign's negotiations during debt workouts[39], thus preventing the development of *ad hoc* custom.

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[32] Anna Gelpern, 'Sovereign Debt: Now What?' (2016) 41 The Yale Journal of international law Online 45, 48. citing José Ocampo, 'A Brief History of Sovereign Debt Resolution and a Proposal for a Multilateral Instrument: The Quest to Resolve Sovereign Debt Crises' (2016) 189–195.
[33] Either the debtor's law or a foreign law elected via choice of law clauses.
[34] Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 63; citing *Case concerning the Payment in Gold of Brazilian Federal Loans Contracted in France (France v Brazil)* (n 133). The competent jurisdiction being either the debtor's courts and tribunals or those elected in *forum* selection clauses.
[35] See e.g. the provisions related to debt in Treaty of Peace with Germany, signed in Versailles 1919; Treaty of Peace (Spain-USA), Paris 1898. On this question see Howse (n 36).
[36] Vienna Convention on Succession of States in respect of State Property, Archives and Debts 1983. This instrument is however of little relevance on debt defaults and restructurings.
[37] Odette Lienau, 'The Challenge of Legitimacy in Sovereign Debt Restructuring' (2016) 57 Harvard International Law Journal 151, 152–153. In general on the applicability of international law to sovereign debt see the discussions in Waibel, 'Out of Thin Air?' (n 31).
[38] *North Sea Continental Shelf Cases, Federal Republic of Germany v Denmark, Federal Repulbic of Germany v Netherlands* [1969] ICJ Rep (International Court of Justice).
[39] Waibel, 'Out of Thin Air?' (n 29); Bradley N Lewis, 'Restructuring the Odious Debt Exception' (2007) 25 Boston University international law Journal 297.

That is not to say that general customary international law and the general principles of international law do not apply to sovereign debt. While defaults and restructurings are not by themselves prohibited in international law, they can lead to international responsibility under other norms. For example, a State's decision not to fulfil its contractual obligations can be tantamount to expropriation, either under the customary standard[40], a Bilateral Investment Treaty provision[41], or a Human Rights Treaty provision[42]. Similarly, a State's conduct surrounding default or restructuring could give rise to international responsibility under a number of other BIT clauses (such as non-discrimination, national treatment or more likely a fair and equitable treatment clause)[43] or a non-discrimination or due process obligation under a human rights treaty[44].

Beyond issues of international regulation, sovereign debt, as an object of study is of particular relevance to international lawyers. The sets of interest at stake when sovereigns default and restructure, are closely linked to those traditionally examined within the field. Sovereign debt restructurings, as opposed to corporate bankruptcies, are not mere exercises in accounting. Restructurings inherently touch upon the ability of States to regulate their own economic matters. Enforcing debt obligations against sovereigns, whether on the basis of contracts or of international law, prevents those sovereigns from deciding for themselves how their external indebtedness should be managed[45]. Moreover, the domestic measures accompanying restructurings, in particular budget cuts and other austerity programs, are usually demands from creditors which tend to run against the desires of the sovereign's population[46]. Thus, as was recently obvious in the Greek and Argentinean cases[47], matters

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[40] On the customary nature of expropriation see: *Case concerning the Factory at Chorzow (claim for indemnity) (merits)* (Permanent Court of International Justice); Krista Nadakavukaren Schefer, *International Investment Law: Text, Cases and Materials* (Edward Elgar Publishing Limited 2013) 195; August Reinisch, 'Expropriation' [2008] The Oxford Handbook of International Investment Law <http://www.oxfordhandbooks.com.ezproxy.lib.gla.ac.uk/view/10.1093/oxfordhb/9780199231386.001.0001/oxfordhb-9780199231386-e-11> accessed 27 August 2018.

[41] *Abaclat and Others v. Argentine Republic* (n 17).

[42] *Mamatas et autres v. Greece* (n 18).

[43] *Abaclat and Others v. Argentine Republic* (n 17); *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17); *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17).

[44] *Mamatas et autres v. Greece* (n 18).

[45] This right to restructure line of thinking is notably echoed in the recent UNGA resolution. United Nations General Assembly, 'Resolution 69/319: Basic Principles on Sovereign Debt Restructuring Processes' (n 22). See Vassilis Paliouras, 'The Right to Restructure Sovereign Debt' (2017) 20 Journal of International Economic Law 115.

[46] See e.g. Cristina Flesher Fominaya, 'European Anti-Austerity and pro-Democracy Protests in the Wake of the Global Financial Crisis' (2017) 16 Social Movement Studies 1; Luís de Sousa, Pedro C Magalhães and Luciano Amaral, 'Sovereign Debt and Governance Failures: Portuguese Democracy and the Financial Crisis' (2014) 58 American Behavioral Scientist 1517; Stephen B Kaplan and Kaj Thomsson, 'The Political Economy of Sovereign Debt: Global Finance and Electoral Cycles' (2017) 79 The Journal of Politics 605.

[47] See notably Anna-Lena Högenauer and David Howarth, 'Unconventional Monetary Policies and the European Central Bank's Problematic Democratic Legitimacy' (2016) 71 Zeitschrift für öffentliches Recht

of sovereign debt are closely tied to ideas of self-determination and to questions about the very nature of sovereignty and democracy[48]. Those questions are not easily understood through a contract law only framework, but rather require the concepts which come more naturally with an international law lens[49].

Understanding sovereign debt, therefore, requires grappling with the contractual norms surrounding repayment, the principles of international law limiting sovereign behaviour during restructuring, and touches upon the core international law notions of sovereignty, self-determination and democracy. Understanding sovereign debt, at today's date, also requires a model which reflects how the legal norms attached to this unique social phenomenon have recently changed, and a way to make sense of the stark contradictions within the case-law on debt and debt restructurings. So far, however, it appears that such a framework is lacking.

This thesis suggests a systematisation of the law on sovereign debt. Its purpose is to present theoretical framework making sense of the sweeping legal changes that sovereign debt has undergone, as well as systematising the contradictory case-law mentioned above. In order to fully map how legal norms impact States and their creditors, the framework suggested by this thesis applies both to the domestic and international aspects of the law on sovereign debt.

<http://orbilu.uni.lu/handle/10993/28059> accessed 11 May 2020; Matthias Goldmann and Silvia Steininger, 'A Discourse Theoretical Approach to Sovereign Debt Restructuring: Towards a Democratic Financial Order' (2016) 17 German Law Journal 709.

48 See Odette Lienau, 'Who Is the Sovereign in Sovereign Debt? Reinterpreting a Rule-of-Law Framework from the Early Twentieth Century' (Social Science Research Network 2008) SSRN Scholarly Paper ID 1143063 63–64 <http://papers.ssrn.com/abstract=1143063> accessed 12 January 2016; Odette Lienau, *Rethinking Sovereign Debt: Politics, Reputation, and Legitimacy in Modern Finance* (Harvard University Press 2014); Odette Lienau, 'Extending the European Debt Discussion to Broader International Governance' [2011] Cornell Law Faculty Publications <https://scholarship.law.cornell.edu/facpub/593>. These issues echo the concerns regarding economic self-determination which have been encapsulated under the label of the 'New International Economic Order'. See United Nations General Assembly, 'Resolution 3281 (XXIX). Charter of Economic Rights and Duties of States' <http://www.un-documents.net/a29r3281.htm>; United Nations General Assembly, 'Resolution 3202 (S-VI). Programme of Action on the Establishment of a New International Economic Order' <http://www.un-documents.net/s6r3202.htm>; Antony Anghie, 'Legal Aspects of the New International Economic Order' (2015) 6 Humanity: An International Journal of Human Rights, Humanitarianism, and Development 145; Lorenz Eitner, *Foreign Debts In The Present And A New International Economic Order* (Routledge 2019).

49 Goldmann and von Bongdandy argue notably that one should understand sovereign debt restructurings as exercises of public authority and not as private transactions. See Armin von Bogdandy and Matthias Goldmann, 'Sovereign Debt Restructurings as Exercises of International Public Authority' in Carlos Espósito, Yuefen Li and Juan Pablo Bohoslavsky (eds), *Sovereign Financing and international law* (Oxford University Press 2013) <http://www.oxfordscholarship.com/view/10.1093/acprof:oso/9780199674374.001.0001/acprof-9780199674374-chapter-3> accessed 3 October 2016; Matthias Goldmann, 'Public and Private Authority in a Global Setting: The Example of Sovereign Debt Restructuring' (2018) 25 Indiana Journal of Global Legal Studies 331.

This framework understands the law on sovereign debt as a succession between two distinct coherent regulatory models: the creditor protection model and the anti-holdout model. The creditor protection models aims to provide creditors with efficient legal remedies as an incentive to lend to sovereigns. These benefits both parties in the sovereign debt relationship as it enables States to borrow under better conditions, while protecting creditors against repudiation. The anti-holdout model is a reaction to the collective action issues which arose in the 1990s and early 2000s and rendered restructurings increasingly difficult. It aims at encouraging creditor participation in sovereign debt restructurings by disincentivising creditors from holding out of reasonable restructuring offers.

Before delving in the methodology behind this project, two clarifications need to be made.

First, this thesis needs to define what it means by sovereign debt and which aspects of the law on sovereign debt it focuses on. Then, it needs to review the current state of the scholarship on sovereign debt, as the gaps within the way lawyers have approached this topic, provide a direct background behind the necessity of developing the framework advanced here.

1.2 Defining and studying sovereign debt

1.2.1 Defining sovereign debt

Traditionally, the scholarship on State's debts has divided sovereign debt into several categories.

Bilateral debt is usually understood as debt lent by one sovereign to another[50]. Multilateral debt, *a contrario*, is usually defined as debt owed by a sovereign to an international organisation, typically the IMF or the World Bank[51].

Sovereign debt has also been traditionally divided between internal and external debt. External debt being "*expressed in foreign currency, typically payable abroad, governed by external law and subject to the jurisdiction of external courts.*"[52] Internal debt, *a contrario,* is payable domestically, in the local currency and adjudicated by the sovereign's domestic

[50] Mauro Megliani, *Sovereign Debt: Genesis, Restructuring, Litigation* (Springer 2015) 97.
[51] ibid 123.
[52] Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 13.

laws and courts. Some authors characterise internal debt as the debt repayable on the territory of the sovereign and external debt as the debt repayable abroad[53]. However, the place of repayment has little impact on the norms applicable to the bonds[54]. At today's date, the distinction between internal and external debt is somewhat artificial[55]. While historically, internal debt was usually borrowed by the sovereign's own population, the rise of modern finance has globalised exposure to 'internal' debt instruments[56]. Furthermore, the development of the Eurozone calls into question the workability of the distinction between internal and external debt. Indeed, member States of the Eurozone typically issue bonds under domestic law but denominated in Euro, a currency over which they have little control.

This thesis, when it mentions sovereign debt focuses only on either internal or external debt, and generally not on multilateral and bilateral debt. The reason for this limit is triple. First, the legal regime on multilateral debt is fundamentally different from the one governing domestic and external debt, as the first is governed by *ad hoc* international legal instruments. Moreover, the creditor-debtor dynamic arising from bilateral and multilateral debt is materially different from the one governing the relationship between sovereigns and their private creditors[57]. Finally, at today's date, the bulk of sovereign indebtedness is emitted either internally or externally to private entities[58], warranting an in-depth analysis of the legal regime governing it.

[53] Hayk Kupelyants, *Sovereign Defaults Before Domestic Courts* (Oxford University Press 2018) 7.
[54] François Gianviti, 'The International Monetary Fund and External Debt', *Academy of international law, Recueil des cours* 234.
[55] Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 13; Megliani, *Sovereign Debt* (n 56) 4, citing François Gianviti, 'The International Monetary Fund and External Debt' (1989) III Academy of international law, Recueil des cours 205, 235.
[56] Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 13.
[57] Bilateral debt is typically restructured through *ad hoc* negotiations at the Paris club and litigation over bilateral loan is rare. Similarly, multilateral debt has not been the object of litigation and is entirely governed by Treaty. On the Paris Club's functioning see Das, Papaioannou and Trebesch (n 4) 9–14; Megliani, *Sovereign Debt* (n 50) 278–307; Ann Vourc'h, 'L'allégement de la dette au Club de Paris' (Organisation for Economic Co-operation and Development 1992) OECD Development Centre Working Papers <http://www.oecd-ilibrary.org/content/workingpaper/380566408014> accessed 23 February 2016; Alexis Rieffel, 'The Paris Club, 1978-1983' (1984) 28 Columbia Journal of Transnational Law 83; Alexis Rieffel, 'The Role of the Paris Club in Managing Debt Problems' [1985] Essays in International Finance 2.
[58] Matthias Schlegl, Christoph Trebesch and Mark LJ Wright, 'The Seniority Structure of Sovereign Debt' (National Bureau of Economic Research 2019) Working Paper 25793 6 <http://www.nber.org/papers/w25793> accessed 23 January 2020.

For similar reasons, this thesis will not focus on debts arising from war reparations or on odious 'debts'[59]. These two regimes, again, are governed by *ad hoc* norms and their analysis sheds little light on the relationship between private creditors and sovereigns[60].

Finally, it should be noted, that this thesis cannot analyse the entire regulation of internal or external sovereign indebtedness, but rather focuses on the law surrounding default and debt restructurings[61]. The main reason for such a narrow focus is that the changes this thesis focus on have essentially occurred within the norms concerning debt repayment *stricto sensu*. In addition, the private-creditor/sovereign-debtor dynamic which is at the centre of much of the scholarly discussion on sovereign debt is essentially centred on those specific norms.

To summarise, when this thesis uses the term 'sovereign debt law' it does so as a short-hand for: the ensemble of domestic and international law norms governing sovereign, internal or external, debt defaults and restructurings.

1.2.2 Ontological fragmentation

As mentioned above sovereign debt, as a social phenomenon, is entangled in both domestic and international legal sources. Understanding it, therefore, requires a theoretical framework explaining both of those legal aspects of the debt relationship. However, the scholarship on sovereign debt has been 'ontologically fragmented'. With the notable exceptions of Megliani's "Sovereign debt: Genesis – Restructuring – Litigation", Lastra and Buchheit "Sovereign debt Management"[62], and Olivares-Caminal's "Legal Aspects of Sovereign Debt Restructurings"[63] few scholarly works have attempted to analyse sovereign debt in a holistic fashion.

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[59] Odious debts traditionally refer to debts inherit from non-democratic regimes, debts of occupation and debts of "subjugation". See Howse (n 35). This characterisation was first advanced in Aleksandr N Sack, *Les Effets Des Transformations Des États Sur Leurs Dettes Publiques et Autres Obligations Financières.* (Recueil Sirey 1927).

[60] For an overview of the law governing war reparations see e.g. Pierre d'Argent, *Les Réparations de Guerre En Droit International Public. La Responsabilité Internationale Des Etats à l'épreuve de La Guerre.* (2002) <https://dial.uclouvain.be/pr/boreal/object/boreal:91715> accessed 1 April 2019. It is undeniable that some 'odious debts' are held by private creditors. See e.g. *Tinoco Claims Arbitration (Great Britain v Costa Rica)* (1923) 1 U N Rep Arbitr Awards 369. However, the questions surrounding odious debt as a topic of legal scholarship focus more of matters of State succession and/or government succession and therefore are materially different from those arising when sovereigns default or restructure for economic reasons. For an overview of the law on odious debt see Lienau, *Rethinking Sovereign Debt* (n 47); Jeff King, *The Doctrine of Odious Debt in international law: A Restatement* (Cambridge University Press 2016); Howse (n 34).

[61] Instead of e.g., the norms regulating the issuance of bonds, or those regulating their holdings.

[62] Rosa Maria Lastra and Lee C Buchheit (eds), *Sovereign Debt Management* (First edition, Oxford University Press 2014).

[63] Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5).

Most commentators on sovereign debt law have rather provided in-depth examinations of specific aspects of the debt relationship. Notably, Waibel's "Sovereign Debt before International Courts and Tribunals"[64] provides an overview of the international litigation on sovereign debt and highlights the trends present in said litigation[65]. Hayk Kupelyants' 2018 "Sovereign Defaults before Domestic Courts"[66] provides an analysis of the domestic British litigation on sovereign debt. Lienau's "Rethinking Sovereign Debt"[67] and King's "The Doctrine of Odious Debt in International law – a restatement"[68] provide the most recent studies of the odious debt doctrine[69]. Recent collective works have focused on the impact of sovereign debt restructurings on human rights[70], on the UNCTAD's principles on sovereign lending and borrowing[71], and on the lack of adequate regulatory structure to manage sovereign debt restructurings[72].

A large swath of the scholarship on sovereign debt has also focused on the 'vulture fund phenomenon', either to analyse its rise and impact, to critique decisions favouring vulture funds, to find solutions to the vulture fund phenomenon, or in rare cases to argue that the actions of vulture funds participate in the good functioning of the sovereign debt market[73]. In the same vein, the *pari passu* clause and its multiple interpretations has, led to many a

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[64] Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2).

[65] There has been earlier attempts to analyse the international law on sovereign debt see e.g. Nicolas Politis, *Les emprunts d'état en droit international* (A Durand et Pedone-Lauriel 1894).

[66] Kupelyants (n 53).

[67] Lienau, *Rethinking Sovereign Debt* (n 48).

[68] King (n 60).

[69] Dee also Howse (n 35); Lee C Buchheit, G Mitu Gulati and Robert B Thompson, 'The Dilemma of Odious Debts' (Social Science Research Network 2006) SSRN Scholarly Paper ID 932916 <http://papers.ssrn.com/abstract=932916> accessed 13 January 2016; Anna Gelpern, 'Odious, Not Debt' [2007] Georgetown Law Faculty Publications and Other Works <https://scholarship.law.georgetown.edu/facpub/1868>; ibid.

[70] *Sovereign Debt and Human Rights* (Oxford University Press 2019).

[71] Carlos Espósito, Yuefen Li and Juan Pablo Bohoslavsky (eds), *Sovereign Financing and international law: The UNCTAD Principles on Responsible Sovereign Lending and Borrowing* (Oxford University Press 2013) <http://www.oxfordscholarship.com/view/10.1093/acprof:oso/9780199674374.001.0001/acprof-9780199674374> accessed 16 November 2015.

[72] *Too Little, Too Late: The Quest to Resolve Sovereign Debt Crises* (Columbia University Press 2016) <https://www.jstor.org/stable/10.7312/guzm17926> accessed 25 April 2019.

[73] See Elisa Beneze, 'Stopping the Circling Vultures: Restructuring a Solution to Sovereign Debt Profiteering Note' (2016) 49 Vanderbilt Journal of Transnational Law 245; Jonathan Blackman and Rahul Mukhi, 'The Evolution of Modern Sovereign Debt Litigation: Vultures, Alter Egos, and Other Legal Fauna' (2010) 73 Law and Contemporary Problems 47; Jill Fisch and Caroline Gentile, 'Vultures or Vanguards?: The Role of Litigation in Sovereign Debt Restructuring' (2004) 53 Emory Law Journal 1043; Mauro Megliani, 'Vultures in Courts: Why the UNCTAD Principles on Responsible Financing Cannot Stop Litigation' (2015) 28 Leiden Journal of international law 849; Marcus Miller and Dania Thomas, 'Sovereign Debt Restructuring: The Judge, the Vultures and Creditor Rights' (2007) 30 World Economy 1491; Marcus Miller and Dania Thomas, 'Sovereign Debt Restructuring: The Judge, the Vultures and Creditor Rights' (2007) 30 World Economy 1491; Tim R Samples, 'Rogue Trends in Sovereign Debt: Argentina, Vulture Funds, and Pari Passu Under New York Law' (Social Science Research Network 2014) SSRN Scholarly Paper ID 2403342 <http://papers.ssrn.com/abstract=2403342> accessed 19 August 2016; Patrick R Wautelet, 'Vulture Funds, Creditors and Sovereign Debtors: How to Find a Balance?' (Social Science Research Network 2011) SSRN Scholarly Paper ID 1994425 <https://papers.ssrn.com/abstract=1994425> accessed 11 February 2019.

take in legal journals. Most of these takes have focused on critiques of the judicial interpretation of the clause[74], on the reason for the clause's presence in sovereign bonds, or on the lack of market reactions to its interpretation[75].

Similarly, suggestions for a Sovereign Debt Restructuring Mechanism (SDRM), and analysis of SDRM proposals have occupied a large space within the recent scholarly debate on sovereign debt[76]. Studies have also focused on specific restructurings and on key moments within the development of the current sovereign debt market. In particular, the scholarship on sovereign debt has heavily focused on the Latin American debt crisis[77] and the Argentinean[78] and Greek[79] restructuring processes.

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[74] Sergio Chodos, 'Fromt the Pari Passu Discussion to the "Illegality" of Making Payments', *Too Little, Too Late: The Quest to Resolve Sovereign Debt Crises; M. Guzman, J.A. Ocampo, J.E. Stiglitz (eds)* (Columbia University Press 2016); Robert A Cohen, 'Sometimes a Cigar Is Just a Cigar: The Simple Story of Pari Passu' (2011) 40 Hofstra Law Review 11; Romain Zamour, 'NML Argentina and the Ratable Payment Interpretation of the Pari Passu Clause' (2013) 38 The Yale Journal of international law Online <http://www.yjil.org/docs/pub/o-38-zamour-nml-v-argentina.pdf>; Taylor Klavan, 'Rock the Boat: How the Conflict between NML Capital and the Republic of Argentina Will Affect International Investment' (2013) 5 Creighton International and Comparative Law Journal 47; William W Bratton, 'Pari Passu and a Distressed Sovereign's Rational Choices' (Social Science Research Network 2010) SSRN Scholarly Paper ID 505942 <http://papers.ssrn.com/abstract=505942> accessed 26 September 2016; Olivares-Caminal, 'Rank Pari Passu or Not to Rank Pari Passu' (n 13); 'Analysis of the Role, Use and Meaning of Pari Passu Clauses in Sovereign Debt Obligations as a Matter of English Law' <http://www.fmlc.org/uploads/2/6/5/8/26584807/79.pdf>.

[75] Mitu Gulati and Robert E Scott, *The Three and a Half Minute Transaction: Boilerplate Andthe Limits of Contract Design* (University of Chicago Press 2013); Lee C Buchheit, 'The Pari Passu Clause Sub Specie Aeternitatis' (1991) 10 International Financial Law Review 11; Buchheit and Pam (n 14); Lee C Buchheit and Jeremiah S Pam, 'The Hunt for Pari Passu Cover Story' (2004) 23 International Financial Law Review 20; Mark Weidemaier, Robert Scott and Mitu Gulati, 'Origin Myths, Contracts, and the Hunt for Pari Passu' (2013) 38 Law & Social Inquiry 72.

[76] See e.g. Anne Krueger, 'A New Approach to Sovereign Debt Restructuring' [2002] IMF Working Paper <https://www.imf.org/external/pubs/ft/exrp/sdrm/eng/sdrm.pdf>; Patrick Bolton and David AJr Skeel, 'Inside the Black Box: How Should a Sovereign Bankruptcy Framework Be Structured Conference on Sovereign Debt Restructuring: The View from the Legal Academy' (2004) 53 Emory Law Journal 763; Jochen R Andritzky and others, 'A Mechanism to Regulate Sovereign Debt Restructuring in the Euro Area' (Social Science Research Network 2016) SSRN Scholarly Paper ID 2845278 <https://papers.ssrn.com/abstract=2845278> accessed 2 April 2019; Charles Mooney, 'A Framework for a Formal Sovereign Debt Restructuring Mechanism: The KISS Principle (Keep It Simple, Stupid) and Other Guiding Principles' [2015] Faculty Scholarship at Penn Law <https://scholarship.law.upenn.edu/faculty_scholarship/1547>; Richard Euliss, 'The Feasibility of the IMF's Sovereign Debt Restructuring Mechanism: An Alternative Statutory Approach to Mollify American Reservations' (2003) 19 American University international law Review <https://digitalcommons.wcl.american.edu/auilr/vol19/iss1/5>; Sean Hagan, 'Designing a Legal Framework to Restructure Sovereign Debt' (2004) 36 Georgetown Journal of international law 299.

[77] Monteagudo (n 8); Philip Power, 'Sovereign Debt: The Rise of the Secondary Market and Its Implications for Futures Restructurings' (1995) 64 Fordham Law Review 2701; Theodore Allegaert, 'Recalcitrant Creditors against Debtor Nations, or How to Play Darts' (1997) 6 Minnesota Journal of Global Trade 429.

[78] Anna Gelpern, 'What Bond Markets Can Learn from Argentina' (2005) 24 International Financial Law Review 19; Rainer Kulms, 'Private Creditors and Sovereign Default: From Argentina to Greece' (2012) 2012 Annals of the Faculty of Law in Belgrade - International Edition 65; Samples (n 73); Klavan (n 74).

[79] Kulms (n 78); Jeromin Zettelmeyer, Christoph Trebesch and Mitu Gulati, 'The Greek Debt Restructuring: An Autopsy' (2013) 28 Economic Policy 513; Lee C Buchheit, 'Restructuring a Nation's Debt Capital Markets: Greek Sovereign Debt' (2010) 29 International Financial Law Review 46; Sebastian Grund, 'Restructuring Government Debt under Local Law: The Greek Case and Implications for Investor Protection in Europe' (2017) 12 Capital Markets Law Journal 253; Alexander Metalinos, 'The Greek Sovereign Debt Restructuring',

If one focuses on international law[80], the competence of arbitral tribunals on sovereign debt cases has led to several usually critical studies[81]. International lawyers have also focused on sovereign immunities and sovereign debt[82], and the recent UNGA and UNCTAD developments regarding sovereign debt have led to a flurry of literature[83]. From these developments has also sprouted a line of articles focusing on the impact of good faith obligations on sovereign debt restructurings[84].

Fundamentally, studies of sovereign debt either focus on its public international law aspects, or on its private, domestic law aspects. The problem with studying sovereign debt by dividing its public/private and its domestic/international aspects, is that the reality of what sovereign debt *is* transcends these traditional legal boundaries. Thus, focusing on one aspect of sovereign debt regulation paints an incomplete picture of the way in which law affects the behaviour of States and their creditors in general.

That is not to say that such approaches are flawed, the in-depth analyses they provide are necessary to understand the details of how certain aspects of the debt relationship are

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Sovereign debt and debt restructuring : legal, financial and regulatory aspects (Globe Law And Business 2013).

[80] Regarding good faith and international law, Bohoslavsky and Goldmann have also recently proposed an 'incremental approach' to sovereign debt restructuring, and analysed sovereign debt restructurings as exercises of public authority. Juan Pablo Bohoslavsky and Matthias Goldmann, 'An Incremental Approach to Sovereign Debt Restructuring: Sovereign Debt Sustainability as a Principle of Public international law' (2016) 41 Yale Journal of international law 13; Bogdandy and Goldmann (n 48). It has also been argued that the recent developments in the law on sovereign debt have led to a right to restructure for sovereign debtors. Paliouras (n 45).

[81] See e.g. Michael Waibel, 'Opening Pandora's Box: Sovereign Bonds in International Arbitration' (2007) 101 American Journal of international law 711; Pietro Ortolani, 'Are Bondholders Investors? Sovereign Debt and Investment Arbitration after Poštová' (2017) 30 Leiden Journal of international law 383; Kei Nakajima, 'Beyond Abaclat: Mass Claims in Investment Treaty Arbitration and Regulatory Governance for Sovereign Debt Restructuring' (2018) 19 The Journal of World Investment & Trade 208.

[82] W Mark C Weidemaier, 'Sovereign Immunity and Sovereign Debt' (2014) 2014 University of Illinois Law Review 67; Beatrice Bonafè, 'State Immunity and the Protection of Private Investors: The Argentine Bonds before Italian Courts' (2007) XVI Italian Yearbook of international law 165; Georges R Delaume, 'Sovereign Immunity and Public Debt' (1989) 23 international lawyer (ABA) 811; Adriana T Ingenito and Christina G Hioureas, 'Carving out New Exceptions to Sovereign Immunity: Why the NML Capital Cases May Harm U.S. Interests Abroad Symposium: Investor-State Disputes' (2015) 30 Maryland Journal of international law 118.

[83] Stephanie Blankenburg and Richard Kozul-Wright, 'Sovereign Debt Restructurings in the Contemporary Global Economy: The UNCTAD Approach' 42 Yale Journal of international law 1; Lee C Buchheit and G Mitu Gulati, 'Responsible Sovereign Lending and Borrowing' (2010) 198 UNCTAD Discussion Papers <http://unctad.org/en/Docs/osgdp20102_en.pdf>; Mauro Megliani, 'Vultures in Courts: Why the UNCTAD Principles on Responsible Financing Cannot Stop Litigation' (2015) 28 Leiden Journal of international law 849; Espósito, Li and Bohoslavsky (n 70).

[84] Matthias Goldmann, 'Good Faith and Transparency in Sovereign Debt Workouts (Paper Prepared for the Second Session of the UNCTAD Working Group on a Debt Workout Mechanism)' <https://unctad.org/en/PublicationsLibrary/gdsddf2014misc3_en.pdf>; Bohoslavsky and Goldmann (n 80); Dania Thomas and Javier Garcia Fronti, 'Good Faith in Sovereign Debt Restructuring: The Evolution of an Open Norm in "localised" Contexts?' [2007] CSGR Working Paper Series.

regulated. However, if lawyers are to fully understand how sovereign defaults and restructurings work, a uniting framework such as the one suggested here is needed.

1.2.2 Methodological fragmentation

A similar disconnect appears in the methodological approaches used by legal scholars when focusing on sovereign debt. From a methodological standpoint, a large number of studies on sovereign debt have been rooted in legal positivism[85] *sensu lato*. These have, on average, attempted to either highlight trends in specific aspects of the case-law on sovereign debt[86] or to provide an explanatory overview of the international and contractual regimes governing sovereign debt[87]. The legal positivist scholarship has focused heavily on the interpretation of legal norms applicable to State debts, either by virtue of contract or in international law[88]. These positivist approaches to sovereign debt have produced a large body of studies which have made sense of an often obscure and contradictory case-law. Reliance on said scholarship is necessary if one wants to try and determine what the content of sovereign debt law has been or currently is.

However, on average, those studies have ignored the economic impacts of regulation on the stakeholders in the sovereign debt relationship. Similarly, they have not engaged with the reasons behind the existence of legal norms. Moreover, these positivist approaches have mostly been *de lege lata*.

Besides black-letter approaches, sovereign debt law has seen a number of 'law and economics' studies on specific issues plaguing the sovereign debt market[89], and offering technical solutions to said issues[90]. These have ranged from studies of an SDRM mechanism,

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[85] And therefore focused on the 'proper' interpretation of the legal norms affecting sovereign debt.
[86] See e.g. Kupelyants (n 53); Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2).
[87] See e.g. Edwin Borchard, Justus S Hotchkiss and William Harris Wynne, *State Insolvency and Foreign Bondholders* (Beard Books 1951); Megliani, *Sovereign Debt* (n 50); Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5); Dominique Carreau and Malcolm N Shaw, 'La Dette Extérieure | The External Debt' <http://referenceworks.brillonline.com/entries/law-books-of-the-academy/la-dette-exterieure-the-external-debt-ej.9789041100832.3_774> accessed 12 October 2016.
[88] See e.g. Zamour (n 74); Buchheit, 'The Pari Passu Clause Sub Specie Aeternitatis' (n 75); Buchheit and Pam (n 75); Waibel, 'Out of Thin Air?' (n 31); Reinisch and Binder (n 30); Waibel, 'Two Worlds of Necessity in ICSID Arbitration' (n 29); Ortolani (n 81).
[89] A number of studies have notably focused on the collective action issues encountered during contemporary debt restructurings. See notably: Lee C Buchheit and G Mitu Gulati, 'Sovereign Bonds and the Collective Will' (2002) 51 Emory Law Journal 1317; Anna Gelpern, 'How Collective Action Is Changing Sovereign Debt Cover Story' (2003) 22 International Financial Law Review 19; Jesse Kaplan, 'Collective Action and the Competence of Courts: The Lessons of NML v. Argentina' (2014) 20 Stanford Journal of Law, Business & Finance 1.
[90] Yan Liu and others, 'Strengthening the Contractual Framework to Address Collective Action Problems in Sovereign Debt Restructuring' [2014] IMF Policy Paper

to studies of the collective action issues arising in the sovereign bond market, as well as several analyses of the impact of legal changes on bond prices[91]. These law and economics studies of sovereign debt provide some of the background assumptions on which this thesis is based. However, it does not appear that any of those studies has produced an overview of the incentives produced by the regulation of sovereign debt defaults and restructurings, as a whole. These studies have often centred on the production of technical solutions to the inefficiencies created by the sovereign debt market and have thus not sought to analyse the reasons behind the legal system creating these inefficiencies, as this thesis seeks to do.

Finally, a lot of the law and economic studies of sovereign debt tend to heavily focus on the reputational aspects of sovereign debt, and on the need of sovereigns to repay. This has led them to treat the State as a 'black box', to quote Lienau, and therefore to ignore the redistributive aspects of the debt relationship, notably the impact of defaults and restructurings on the sovereign's population[92].

When writers have strayed away from positivists or law and economics their approach has, , focused strongly on the political and deontological issues raised by sovereign defaults and restructurings. Notably, several studies have focused on the impact of sovereign debt on the debtor's population's human rights[93]. The scholarship on odious debt, in particular, has

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<https://www.imf.org/external/np/pp/eng/2014/090214.pdf>; Stolper and Dougherty (n 10); Weidemaier and Gulati (n 10); Gelpern, Heller and Setser (n 10); Melissa Boudreau, 'Restructuring Sovereign Debt Under Local Law: Are Retrofit Collective Action Clauses Expropriatory?' (Social Science Research Network 2012) SSRN Scholarly Paper ID 1979238 <http://papers.ssrn.com/abstract=1979238> accessed 19 August 2016; Marieclaire Colaiacomo, 'Eurozone Collective Action Clauses and Specialised Agencies of the United Nations as International Organisations: Do CACs Constitute an Expropriation under international law?' (2013) 2 international law Research <http://www.ccsenet.org/journal/index.php/ilr/article/view/31660> accessed 19 August 2016.

[91] See notably Stephen J Choi, G Mitu Gulati and Eric A Posner, 'Pricing Terms in Sovereign Debt Contracts: A Greek Case Study with Implications for the European Crisis Resolution Mechanism' (Social Science Research Network 2011) SSRN Scholarly Paper ID 1713914 <https://papers.ssrn.com/abstract=1713914.64> accessed 3 December 2019; Albert H Choi and Eric A Posner, 'The Critique of the Odious Debt Doctrine Odious Debts and State Corruption' (2007) 70 Law and Contemporary Problems 33; Gelpern, 'How Collective Action Is Changing Sovereign Debt Cover Story' (n 89); Weidemaier, 'Sovereign Immunity and Sovereign Debt' (n 82); Kris James Mitchener and Marc D Weidenmier, 'Supersanctions and Sovereign Debt Repayment' (National Bureau of Economic Research 2005) Working Paper 11472 <http://www.nber.org/papers/w11472> accessed 18 January 2016.

[92] On this question see Lienau, *Rethinking Sovereign Debt* (n 48); Lienau, 'Who Is the Sovereign in Sovereign Debt?' (n 48).

[93] See inter allia, Daniel Bradlow, 'Can Parallel Lines Ever Meet? The Strange Case of the International Standards on Sovereign Debt and Business and Human Rights' (2016) 41 Yale Journal of international law; Lumina, 'Report of the Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, Particularly Economic, Social and Cultural Rights (Mission to Argentina)' (n 6); Lumina, 'Report of the Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, Particularly Economic, Social and Cultural Rights (Mission to Greece)' (n 6); Lumina, *Sovereign Debt and Human Rights* (n 6); *Sovereign Debt and Human Rights* (n 69); Emily F Mancina, 'Sinners in the Hands of an Angry God: Resurrecting the Odious Debt Doctrine in international law Note' (2004) 36 George Washington international law Review 1239.

framed much of its approach on the morality of imposing debt obligations of dictatorial regimes on successor governments[94]. Finally, a last strand of the scholarship has focused on sovereign debt through a "colonialism" lens[95], or has centred on the redistributive effects, or the legitimacy of the policies put in place during restructurings[96]. In general, these studies have highlighted the 'human cost' of sovereign debt but have failed to grapple with its economics.

The net result of this kaleidoscope of approaches is that, the technical issues that plagued sovereign debtors and their creditors from the 1980s onwards are well understood. Writers on sovereign debt should know that the 'sovereign' in sovereign debt is not a mere abstract, corporate entity but a legal person designed to act as an agent of its population[97], and that said population heavily suffers during restructurings and defaults. A plethora of solutions to these issues has been suggested, and some have led to actual modifications in the law on sovereign debt.

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[94] See Larry Cata Backer, 'Odious Debt Wears Two Faces: Systemic Illegitimacy, Problems, and Opportunities in Traditional Odious Debt Conceptions in Globalized Economic Regimes Odious Debts and State Corruption' (2007) 70 Law and Contemporary Problems 1; Tom Ginsburg and Thomas S Ulen, 'Odious Debt, Odious Credit, Economic Development, and Democratization Odious Debts and State Corruption' (2007) 70 Law and Contemporary Problems 115; Matthew B Masaro, 'Incorporating the Fresh Start into Sovereign Debt Restructuring through Odious Debt Note' (2018) 104 Cornell Law Review 1643; Paul B Stephan, 'The Institutionalist Implications of an Odious Debt Doctrine Odious Debts and State Corruption' (2007) 70 Law and Contemporary Problems 213; Howse (n 35).

[95] See Maria Giannacopoulos, 'Sovereign Debts: Global Colonialism, Austerity and Neo-Liberal Assimilation Troubling Waters: Speaking (of) Forbidden (Legal) Subjects: Special Issue to Commemorate Penny Pether' (2015) 19 Law Text Culture 166; Maria Giannacopoulos, 'Sovereign Debt Crises, Referendums and the Changing Face of Colonial Power' (2017) 31 Continuum 33; Ranabir Samaddar, *A Post-Colonial Enquiry into Europe's Debt and Migration Crisis* (Springer Singapore 2016) <https://www.springer.com/gp/book/9789811022111> accessed 1 May 2020; Faisal Ahmed, Laura Alfaro and Noel Maurer, 'Lawsuits and Empire: On the Enforcement of Sovereign Debt in Latin America' (2010) 73 Law and Contemporary Problems 39; Dan Beeton, '"Give Me Liberty or Give Me Debt!"' (2013) 34 Third World Quarterly 1499.

[96] See Catherine Bonser-Neal, 'Why Fiscal Austerity - A Review of Recent Evidence on the Economic Effects of Sovereign Debt Symposium' (2015) 22 Indiana Journal of Global Legal Studies 543; Howard Karger, 'The Bitter Pill: Austerity, Debt, and the Attack on Europe's Welfare States Special Issue: Austerity versus Stimulus: International Challenges for Social Welfare' (2014) 41 Journal of Sociology and Social Welfare 33; Bonser-Neal; Jo Marie Griesgraber and Oscar Ugarteche, 'The IMF Today and Tomorrow: Some Civil Society Perspectives Understanding Pathways through Financial Crises and the Impact of the IMF - Global Insights' (2006) 12 Global Governance 351; Larry Cata Backer, 'Ideologies of Globalization and Sovereign Debt: Cuba and the IMF' (2005) 24 Penn State international law Review 497; Richard Joyce, 'Sovereignty and IMF Intervention in Cambodia' (2003) 12 Griffith Law Review 166; Daniel Kalderimis, 'IMF Conditionality as Investment Regulation: A Theoretical Analysis' (2004) 13 Social & Legal Studies 103; Devran Unlu, 'Is Conditionality for Loans from International Financial Institutions a Legitimate Way to Influence National Policies' (2013) 6 Ankara Bar Review 187; Hector R Torres, 'Reforming the International Monetary Fund – Why Its Legitimacy Is at Stake' (2007) 10 Journal of International Economic Law 443; Yanis Varoufakis, *Adults in the Room: My Battle with Europe's Deep Establishment* (The Bodley Head 2017).

[97] Lienau, *Rethinking Sovereign Debt* (n 48); Lienau, 'Who Is the Sovereign in Sovereign Debt?' (n 48).

What is missing from this picture is an understanding of 'why' the law on sovereign debt led to incomprehensible outcomes, and an understanding of the logic behind the measures currently put in place to prevent such outcomes from re-occurring again.

The bird's eye view of sovereign debt advanced by this thesis, centred on paradigmatic regulatory models allows for an answer to these questions. As will be exposed *infra*, the models advanced here are rooted in law and economics. They are based on law as a tool of social engineering, designed to influence the behaviour of sovereigns and their creditors. The models, however, go beyond law and economics *stricto sensu*. Thus, the systematisation of the law they enable aims at providing an intellectual model of how the law on sovereign debt can be construed through a diachronic lens. Moreover, the *de lege ferenda* developments, and the critique of the regulatory models this thesis suggests rely heavily on the fact that the impact of restructurings goes beyond issues reaches the very livelihood of indebted sovereign's populations.

1.3 Theoretical and Normative Background

The purpose of this thesis is to systematise the law on sovereign defaults and restructurings into distinct regulatory models, based on the type of behaviour they aim to incentivise in market actors. Then, it aims at analysing what behaviour these regulatory models lead to, in practice, in order to suggest *de lege ferenda* legal reforms. Methodologically therefore, this thesis needs a theory of law's impact on the behaviour of sovereigns and their creditors, which includes a theory of how these market actors behave. Moreover, it also requires a defined set of values against which the effectiveness of norms should be assessed.

The descriptive framework espoused by this thesis is rooted in law and economics. There are several advantages such a methodology.

First, law and economics, is inherently centred on studying how legal norms impact the behaviour of market actors[98]. Moreover, it is not only of use to describe how actors *currently* react to legal norms, but is also prospective, it enables predicting how actors *will* react to a set of norms[99]. This aspect of economics makes it particularly suited to the objectives of this

[98] Joel P Trachtman, *The Economic Structure of international law* (Harvard University Press 2009) 1–3; Robert B Cooter and Thomas Ulen, *Law and Economics: Pearson New International Edition* (6 edition, Pearson 2013) 3.
[99] Cooter and Ulen (n 98) 3.

thesis as the measures analysed in the anti-holdout model are recent and the body of market practice in response to these norms limited.

In addition, the economic analysis of law as a descriptive tool, is politically and philosophically agnostic as it is centred on the actual preferences on the actors involved[100]. *A contrario*, neither legal positivism nor other approaches to law provide the tools necessary for this project. Legal positivism's insistence of treating the law in 'splendid isolation' does not allow for an understanding of where legal norms come from, or what their impact on the 'real world' is[101]. Similarly, when other schools of thought seek to describe where law comes from, they often do so by reference to a pre-agreed deontological, philosophical or political framework.

Second, law and economics, lends itself to the creation of coherent models of human behaviour[102]. Law and economics postulates that the actions of legal actors can be explained and modelled. Such a starting point is necessary for the endeavour pursued by this thesis. If one wants to make sense of the incentives provided by legal norms, one first needs to believe that human behaviour can be understood and predicted.

Finally, the study of sovereign debt is, by nature, the study of a phenomenon rooted in international finance and macroeconomics. Law and economics, as a discipline, particularly befits such topics of legal scholarship as it integrates well with the abundant economic scholarship on sovereign debt, providing this thesis with some elements of interdisciplinarity.

This should not be taken to mean that this thesis ignores the contributions of other methodological approaches. As the next paragraphs will show, the understanding of human and sovereign behaviour on which it relies departs, in part, from *homo economicus* as a

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[100] Trachtman (n 98) 2. See also Richard A Posner, 'Utilitarianism, Economics, and Legal Theory' (1979) 8 The Journal of Legal Studies 103. There have been criticism against this claim, essentially rooted in the fact that efficiency or self-maximisation as a criterion for 'good law' is far from being depoliticised but rather biased in favour of wealth-holders. See Morton Horwitz, 'Law and Economics: Science or Politics?' (1980) 8 Hofstra Law Review <https://scholarlycommons.law.hofstra.edu/hlr/vol8/iss4/2>; Ronald Dworkin, *Law's Empire* (Belknap Press 1986) ch 2; Ronald M Dworkin, 'Is Wealth a Value?' (1980) 9 The Journal of Legal Studies 191; Ronald Dworkin, 'Why Efficiency? - A Response to Professors Calabresi and Posner' (1980) 8 Hofstra Law Review <https://scholarlycommons.law.hofstra.edu/hlr/vol8/iss3/5>. These assertions, are not intellectually flawed, rather, they attach themselves to law and economics as a prescriptive tool rather than a descriptive approach. While it is undeniable that wealth maximisation *de lege ferenda* is a political statement, the economic analysis of law as a descriptive tool, as underlined by Trachtman is not rooted in such values.

[101] Guido Calabresi, *Of Law and Economics and Economic Analysis of Law: The Role of the Lawyer* (Yale University Press) 8 <http://www.universitypressscholarship.com/view/10.12987/yale/9780300195897.001.0001/upso-9780300195897-chapter-1> accessed 6 May 2020.

[102] Trachtman (n 98) 1–3.

heuristic and takes into account both the behavioural critique of rational choice theory and its liberal critique. As such, it fits perhaps better under the label of a ‘new law and economics approach’[103]. At the normative level, this thesis also departs from the traditional law and economics approach in that it measures the efficiency of norms, not against individual preferences, but against a distinct set of values, as will be shown in the last paragraphs of this section.

Before delving more deeply into the methodological underpinnings of this thesis, a number of caveats on the models on which it relies are necessary. The two models presented here should not be understood as empirical representations of the decision-making behaviour of those enacting the legal norms themselves. For example, when this thesis argues that a certain interpretation of the *pari passu* clause fits within the creditor protection model, it does not claim that the judge interpreting the clause intends to favour creditors in order to incentivise lending[104]. Rather, it only focuses on the potential impact of the clause on the behaviour of actors within the sovereign debt market.

What the models do, is providing an intellectual framework via which the norms on sovereign debt and the changes they have undergone can be intellectually systematised. To use an analogy, one could understand the two models which underpin this thesis as similar to what structuralists would refer to as a ‘structure’[105]. In this analogy, creditor protection and anti-holdout models are the dichotomic structure explaining instances of *parole* in sovereign debt law. *Parole* being, for example, the decision to insert a collective action clause in a sovereign bond. That is not to say that the exercise pursued in this thesis is structuralist. As opposed to Koskiennemi’s work in *From Apology to Utopia* or to Kennedy’s *Semiotics of the legal argument*¸ the purpose of this thesis is not to deconstruct[106] the current

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[103] See Michael G Faure and Roy A Partain, *Environmental Law and Economics: Theory and Practice* (Cambridge University Press 2019) 11 <https://abdn.pure.elsevier.com/en/publications/environmental-law-and-economics-theory-and-practice> accessed 12 May 2020. Citing Cento G Veljanovski, *The New Law-and-Economics: A Research Review* (Centre for Socio-Legel Studies 1982).

[104] It would indeed be impossible to empirically verify what the internal decision-making process of a legal actor is.

[105] Martti Koskenniemi, *From Apology to Utopia: The Structure of International Legal Argument* (Cambridge University Press 2006) 11 <http://ebooks.cambridge.org/ref/id/CBO9780511493713> accessed 3 November 2015. On *parole* and *langue* and their uses in legal structuralism see generally Justin Desautels-Stein, ‘Structuralist Legal Histories’ (Social Science Research Network 2015) SSRN Scholarly Paper ID 2591956 <http://papers.ssrn.com/abstract=2591956> accessed 23 November 2015; Duncan Kennedy, ‘The Structure of Blackstone’s Commentaries’ (1970) 28 Buffalo Law Review 209; Duncan Kennedy, ‘A Semiotics of the Legal Argument’ (1991) 42 Syracuse Law Review 75. On *parole* and *langue* in anthropological literature see Ferdinand de Saussure and others, *Course in General Linguistics* (Open Court 1986); Claude Levi-Strauss, *La Pensee Sauvage* (Revised edition, Pocket 1990); Corinne François-Denève, *Mythologies: Roland Barthes* (Bréal 2002).

[106] Here this thesis use Koskenniemi’s definition of deconstructing as “*the attempt to find a centre, or a ‘‘deep-structure’’ to common discourse*”. Koskenniemi (n 105) 10.

discourse on sovereign debt and reduce it to a set of "*conditions of what can acceptably be said within it*"[107]. Rather, like a structuralist's structure, the models are intellectual creations which can be used to explain a variety of social and cultural phenomena, and not an empirical description of the 'real world'[108].

Moreover, when applied to court decisions the models are not predictive of the result of litigation, but rather focus on the interpretation of the norms applied in the case. For example, in the section on necessity, the *French Company of Venezuelan Railroad* case[109] is considered as fitting into the creditor protection model despite the verdict being in favour of the debtor. In that specific case, for example, the interpretation of the necessity defence fits with creditor protection while the facts of the case led to a situation where the debtor's responsibility was absolved.

1.3.1 The impact of law on the behaviour of States and their creditors

Understanding how legal norms impact the behaviour of sovereigns and their creditors requires three elements: the set of preferences they seek to maximise, their mode of behaviour, and a model of the influence legal norms on this behaviour.

1.3.1.1 The preferences of sovereigns and their creditors

The traditional understanding of market actor's behaviour has been fairly narrow. Market actors, according to the classic economic model of human behaviour espoused by Posner and its followers, are rational self-maximisers. They act on the basis of a cost-benefit analysis in order to increase their own utility, expressed in dollars or dollar equivalents[110]. Applied to the sovereign debt market this would mean that States, seek to borrow at the best possible rate, and repay as little as they can while maintaining said rate. Creditors, on the

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[107] ibid 11.

[108] It should also be noted that the central policy tenets underpinning the two models are akin to what Lienau refers to as the 'laws of the market', or 'law in hiding' within the market. They are economic ideas which shape the legal norms on sovereign debt. See Odette Lienau, 'Law in Hiding: Market Principles in the Global Legal Order' (Social Science Research Network 2018) SSRN Scholarly Paper ID 3096060 <https://papers.ssrn.com/abstract=3096060> accessed 29 April 2020.

[109] *French Company of Venezuelan Railroads Case (France v Venezuela)* (1905) X Rep Int Arbitr Awards 285 (Arbitral Tribunal).

[110] See e.g. Richard A Posner, 'Utilitarianism, Economics, and Legal Theory' (1979) 8 The Journal of Legal Studies 103, 119.For an overview of rational choice theory as a behavioural heuristic in the legal scholarship see in general Richard A Posner, *Economic Analysis of Law* (2d ed, Little, Brown 1977); Andrew T Guzman, *How international law Works: A Rational Choice Theory* (Oxford University Press 2008); Joel P Trachtman, *The Economic Structure of international law* (Harvard University Press 2009). Posner, 'Utilitarianism, Economics, and Legal Theory'.

other hand, seek to maximise their revenues, usually by obtaining the best possible interest payment[111].

There are several issues with applying this narrow definition of human behaviour to the sovereign debt market. First, its reading of utility as applied to States appears too limited. While it is true that, in general, sovereigns seek to borrow at the best possible price[112], their preferences are not purely monetarily motivated. Rather, it appears that, in practice, sovereigns within the sovereign debt market pursue two sets of sometimes contradictory interests: the pursuit of financial gain, and the maximisation of their 'jurisdiction' or 'sovereignty'[113]. Sovereigns, thus, seek to strike a balance between the maximisation of revenues that good borrowing conditions allow, and the loss of jurisdiction over their debts that better borrowing conditions generally entails[114].

A potential difficulty with assessing States' preferences arises from the fact that sovereigns, lack agency, and therefore need to act through the intermediary of individuals[115]. Public choice theory[116] and liberal theories readings of sovereign's preferences assume that the individuals acting on behalf of governments seek to further their own preferences rather than those of the public they theoretically represent[117]. Thus, following those theories one cannot

[111] For such an exercise see notably Vinod K Aggarwal, *Debt Games: Strategic Interaction in International Debt Rescheduling* (Cambridge University Press 1996); Kenneth M Kletzer and Brian D Wright, 'Sovereign Debt as Intertemporal Barter' (2000) 90 American Economic Review 621.
[112] See e.g. Michael Tomz, *Reputation and International Cooperation: Sovereign Debt Across Three Centuries* (Princeton University Press 2007) 5–8.
[113] For an analysis of States preferences see Trachtman (n 68) 10–11. To put it simply, States within the sovereign debt market are not purely motivated by the maximisation of their wealth, but seem to also seek to minimise their own loss of jurisdiction. International norms thus arise within the sovereign debt market when the monetary gains States can obtain outweigh the potential loss of jurisdiction over their own debt.
[114] Notably borrowing under foreign law, or in a foreign currency, a clear loss of jurisdiction by a sovereign usually correlates with better borrowing conditions, as seen in chapter 3. See Stephen J Choi, Mitu Gulati and Eric A Posner, 'The Evolution of Contractual Terms in Sovereign Bonds' (2012) 4 Journal of Legal Analysis 131; Marc Flandreau and Nathan Sussman, 'Old Sins: Exchange Rate Clauses and European Foreign Lending in the 19th Century' (Social Science Research Network 2004) SSRN Scholarly Paper ID 511303 <https://papers.ssrn.com/abstract=511303> accessed 3 August 2018; Barry Eichengreen, Ricardo Haussman and Ugo Panizza, 'Capital Controls and Capital Flows in Emerging Economies: Policies, Practices and Consequences', *Capital Controls and Capital Flows in Emerging Economies: Policies, Practices and Consequences* (National Bureau of Economic Research 2007) <http://www.nber.org/chapters/c0150.pdf>.
[115] David Copp, 'On the Agency of Certain Collective Entities: An Argument from "Normative Autonomy"' (2006) 30 Midwest Studies In Philosophy 194, 195; Alexander Thompson, 'Applying Rational Choice Theory to international law: The Promise and Pitfalls' (2002) 31 The Journal of Legal Studies S285, 291.
[116] For an overview on public choice theory see Dennis C Mueller, 'Public Choice: A Survey' (1976) 14 Journal of Economic Literature 395.
[117] Trachtman (n 68) 19. See notably Andrew Moravcsik, 'Taking Preferences Seriously: A Liberal Theory of International Politics' (1997) 51 International Organization 513, 540–544; Anne-Marie Slaughter and Jose E Alvarez, 'A Liberal Theory of international law' (2000) 94 Proceedings of the Annual Meeting (American Society of international law) 240, 516–518. See also Richard E Wagner, 'Debt Default and the Limits of the Contractual Imagination: Pareto and Mosca Meet Buchanan' [2018] Debt Default and Democracy <http://www.elgaronline.com/view/edcoll/9781788117920/9781788117920.00012.xml> accessed 11 May 2020; Jon Elster, 'Introduction', *Rational Choice* (New-York University Press 1986); Robert Powell, 'Absolute

model sovereigns as having preferences of their own. However, following Trachtmann[118], quoting March and Olsen[119], this thesis opts for a generally institutionalist vision of the sovereign. It considers that, as States are institutionally designed to achieve certain set goals, they benefit from a sufficient internal coherence to allow construing them, as having determinable preferences[120].

That is not to say that this thesis considers the liberal critique[121] of institutionalism to be unfounded. An actual empirical determination of how sovereigns behave would probably require the granularity that public choice theories or liberal theories of sovereign behaviour provide[122]. However, the paradigm-mapping exercise pursued here does not require a perfect empirical representation of sovereign behaviour, but rather benefits from a clearer heuristic of how sovereigns behave[123]. Such an understanding is better achieved by opting for an institutional lens rather than a liberal or public-choice theory approach.

Nevertheless, there are instances where the preferences of certain government organs or their agents are easily identifiable and can thus fit with the broader model of State behaviour used here. In such cases, this thesis takes them into account so as to produce as reliable a model of sovereign behaviour as possible[124].

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and Relative Gains in International Relations Theory' (1991) 85 The American Political Science Review 1303, 1305.

118 Trachtman (n 98) 18.

119 See James G March and Johan P Olsen, 'The New Institutionalism: Organizational Factors in Political Life' (1984) 78 The American Political Science Review 734.

120 Trachtman (n 68) 18.

121 It also appears that a realist approach would not particularly benefit this thesis. The worldview pushed by the realist methodology, heavily focused on security concerns and difficult cooperation seems at odds with the subject matter of this thesis. On this see: See e.g. Duncan Snidal, 'Relative Gains and the Pattern of International Cooperation' (1991) 85 The American Political Science Review 701, 702. Citing notably Kenneth Neal Waltz, *Theory of International Politics* (McGraw Hill 1979) 105. See also Hans J Morgenthau, *Politics Among Nations: The Struggle for Power and Peace* (Alfred A Knopf 1973); John J Mearsheimer, 'The False Promise of International Institutions' (1994) 19 International Security 5.

122 Trachtman (n 98) 18.

123 For such an approach see e.g. Aggarwal (n 111).

124 Similarly, this thesis has no problem espousing credible commitment theories which originally required deconstructing the State into its key components, since again, this enables a clear understanding of sovereigns' preferences. On this see: Douglass C North, 'Institutions and Credible Commitment' (1993) 149 Journal of Institutional and Theoretical Economics (JITE) / Zeitschrift für die gesamte Staatswissenschaft 11; Douglass North and Barry Weingast, 'Constitutions and Commitment: The Evolution of Institutional Governing Public Choice in Seveteenth Century England' (1989) 49 Journal of Economic History 803.

It has also been argued that using set and endogenous preferences, as done here, is unrealistic, as actors' preferences change through time[125]. This argument, while founded in other areas of foreign relations, does not seem particularly relevant to the present study.

For sovereigns it seems that maximising jurisdiction and minimising costs remains a relatively constant set of interests. While the relationship between both sets of preferences may change over time, the nature of the preference sought should remain fairly stable[126].

For creditors one can expect that maximising profits remain a stable goal through time. One can reasonably assume that when they acquire debt titles or during a restructuring, private entities are mostly interested in the obtention of an interest rate payment proportional to the risk they take[127]. As noted by Lienau, this does not mean creditor's preferences are systematically homogeneous[128]. Creditor's specific choices may vary while the nature of their preferences remains the same. For example, during restructurings, some creditors might prefer cooperation with sovereigns, while other may desire full payments. As will be shown in chapter 2 and 3, however in those cases all sets of creditors still seek to further their profits, but given their structural differences obtain profits in different fashion.

1.3.1.2 The behaviour of sovereigns and their creditors

Having established, for the purpose of this thesis the set of preferences sovereigns and their creditors seek to further when accessing capital markets, this thesis now needs to turn to the *way* via which sovereigns and their creditors seek to further said set of interests.

Traditional law and economics reads market actors behaviour as furthering their interest through rational means, as argued in classical economics[129]. A more modern framing of this

[125] See notably George Stigler and Gary Becker, 'De Gustibus Non Est Disputandum' (1977) 67 American Economic Review 76. Cited in Duncan Snidal, 'Rational Choice and International Relations.', *Handbook of International Relations, Walter Carlnaes, Thomas Risse, Beth Simons (eds)* (2nd edn, Sage Publication 2012) 100.
[126] Tomz (n 112) 11–13.
[127] In rare cases, profit is not the main driver behind the extension of credit to sovereigns. For example, it could be argued that the purchase of war bonds, as those emitted by heavily indebted sovereigns during the World Wars is more the result of patriotism and a desire to participate in the war effort than an economic decision. However, such cases are rare. Thus, on average, one can argue that lending to sovereign is done for profit purposes. On war bonds see e.g. James J Kimble, *Mobilizing the Home Front: War Bonds and Domestic Propaganda* (Texas A&M University Press 2006); James T Sparrow, '"Buying Our Boys Back": The Mass Foundations of Fiscal Citizenship in World War II' (2008) 20 Journal of Policy History 263.
[128] Lienau, *Rethinking Sovereign Debt* (n 48) 28–29.
[129] For an overview of rational choice theory as a behavioural heuristic in the legal scholarship see in general Richard A Posner, *Economic Analysis of Law* (2d ed, Little, Brown 1977); Andrew T Guzman, *How international law Works: A Rational Choice Theory* (Oxford University Press 2008); Joel P Trachtman, *The Economic Structure of international law* (Harvard University Press 2009).

theory concedes that individual action may vary, but argues that the aggregate of market actors' behaviour matches the result produced by rational choices and that, therefore, one can construe individual behaviour *as if* it were rational[130].

There are several issues with this conception of behaviour, as applied to the sovereign debt market. First, as opposed to classical conceptions of rational choice theory, market actors' opportunities are, in real life, limited by external circumstances[131]. Transaction costs, information asymmetry, and the opportunity cost of time prevent sovereigns and their creditors from behaving optimally. They *bound* their rationality[132].

Moreover, as behavioural economists have shown, individual action is marred by unconscious biases which prevent them from reaching optimal outcomes, even in the absence of the aforementioned external constraints[133]. Those same inefficiencies apply, to actions within the sovereign debt market. Risk aversion might prevent law firms from altering the drafting of bond clauses, even when they lead to sub-optimal results[134]. Endowment effects or sunk-cost fallacies may prevent bondholders from liquidating their positions when restructurings seem unavoidable[135]. Similarly, some research has found that economic actors are biased towards solutions which appear fair or equitable[136] but diverge from the maximisation of their preferences.

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130 See Milton Friedman and Marilyn Friedman, *Essays in Positive Economics* (University of Chicago Press 1953) 21; Klaus Mathis and Deborah Shannon, 'Homo Economicus' in Klaus Mathis and Deborah Shannon (eds), *Efficiency Instead of Justice? Searching for the Philosophical Foundations of the Economic Analysis of Law* (Springer Netherlands 2009) <https://doi.org/10.1007/978-1-4020-9798-0_2> accessed 13 February 2020; Klaus Mathis and Deborah Shannon, 'Economic Analysis of Law' in Klaus Mathis and Deborah Shannon (eds), *Efficiency Instead of Justice? Searching for the Philosophical Foundations of the Economic Analysis of Law* (Springer Netherlands 2009) <https://doi.org/10.1007/978-1-4020-9798-0_4> accessed 13 February 2020.

131 Trachtman (n 68) 26–71; *The Limits of international law* (n 70) 11.

132 The term bounded rationality was originally coined in Herbert A Simon, *Models of Man; Social and Rational* (Wiley 1957). See also Christine Jolls, Cass R Sunstein and Richard Thaler, 'A Behavioral Approach to Law and Economics' (1998) 50 Stanford Law Review 1471.

133 See e.g. Richard H Thaler and Cass R Sunstein, *Nudge: Improving Decisions About Health, Wealth and Happiness* (01 edition, Penguin 2009); *Misbehaving* <https://books.google.com/books/about/Misbehaving.html?hl=fr&id=9EJzAwAAQBAJ> accessed 9 December 2019; Jolls, Sunstein and Thaler (n 132); Richard A Posner, 'Rational Choice, Behavioral Economics, and the Law' (1998) 50 Stanford Law Review 1551.

134 On this see e.g. Gulati and Scott (n 75); Weidemaier, Scott and Gulati (n 75).

135 See *infra*, and Alexandre Belle, 'Mamatas and Others v. Greece: How the European Court of Human Rights Could Change Sovereign Debt Restructuration', *New Voices and New Perspectives in International Economic Law. J. Haskell, A. Rasulov (eds)* (Springer International Publishing 2020).

136 Cass R Sunstein, 'Human Behavior and the Law of Work' (Social Science Research Network 2001) SSRN Scholarly Paper ID 267447 217 <https://papers.ssrn.com/abstract=267447> accessed 13 May 2020; Jolls, Sunstein and Thaler (n 132) 1492; Ernst Fehr, Georg Kirchsteiger and Arno Riedl, 'Does Fairness Prevent Market Clearing? An Experimental Investigation' (1993) 108 The Quarterly Journal of Economics 437. The idea that human behaviour is directed by ideals beyond self-interest is, of course, not the invention of behavioural economists. Smith himself explored similar concepts in: Adam Smith, *The Theory of Moral Sentiments* (H G Bohn 1853) 162. Reconciling the fact that market actors behave in ways corresponding with

If one particularly considers the application of rational choice theory to sovereigns, a rich literature has argued that the collective nature of States prevents the application of rational choice theory to model their behaviour, as said theory is better suited to individuals[137]. Here again it is argued that, because sovereigns lack agency, one should deconstruct the black box that is the modern State and focus on the behaviour of individuals acting as its agents. Understood as such, the actions of sovereigns are less rational, more *bounded*, than those of the individuals who compose them[138].This thesis, to a certain extent, takes into account these preferences of government organs. Notably, in its chapter 4, it argues that short-term electoral interests may prevent sovereigns from behaving optimally by delaying necessary restructurings.

However, following Sunstein[139], this thesis does not embrace a complete rejection of rational choice theory in favour of fully empirical and detailed models of human behaviour, neither does it treat actors as fully 'rational' in the traditional sense of the term. Rather, it understands that behaviour, while generally rational, is limited by external constraints and takes into account market actor biases when they are directly relevant.

1.3.1.3 The impact of legal norms on the behaviour of sovereigns and their creditors

If one assumes that sovereigns and their creditors have set preferences, and that they behave in a predictable way, there are several ways via which norms can impact their behaviour. Here again, the specificity of sovereign debt, as a legal relationship, must be kept in mind. Theories of international law's impact on sovereigns' behaviour abound[140]. However, most

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'morals' *sensu lato*, with the essentially self-interested set of preferences that economists tend to adopt is a complex question, impossible to fully explore within these pages. To put it simply, one can frame the desire for morality as part of market actors' utility function, as Smith does or as a bias in market actor's action, as a behaviourist would. This thesis opts for the latter, as it makes for a simpler modelling of market actor's relationships.

137 Copp (n 115) 195; Thompson (n 115) 291.

138 On collective entities as more prone to biases see notably David G Myers and Helmut Lamm, 'The Group Polarization Phenomenon' (1976) 83 Psychological Bulletin 602; Paul Hart, 'Irving L. Janis' Victims of Groupthink' (1991) 12 Political Psychology 247; Prof Paul t'Hart, *Groupthink in Government: A Study of Small Groups and Policy Failure* (Johns Hopkins Paperbacks Ed edition, The Johns Hopkins University Press 1994).

139 As such, this thesis understands that the contribution of behavioural economics has not been to undermine the idea that people act in a somewhat rational manner, but rather to note that when behaviour predictably deviates from what is expected, it should be modelled. See Cass Sunstein, 'Behavioral Analysis of Law' [1997] Law & Economics Working Papers 1–2 <https://chicagounbound.uchicago.edu/law_and_economics/79> noting, "it it does not follow that people's behavior is unpredictable, systematically irrational, random, rule-free, or elusive to social scientists. On the contrary, the qualifications can be described, used, and sometimes even modelled."

140 A classic argument would be that breaching international norms leads to reputations costs. See e.g. Abram Chayes and Antonia Handler Chayes, *The New Sovereignty: Compliance with International Regulatory Agreements* (Harvard University Press 1995). For an application to sovereign debt see, *infra*, and Tomz (n 112). Another well-known theory states that international law works by enabling State to cooperate, via institutions,

of these theories focus on the behaviour of sovereigns towards other sovereigns and have very little to say about how the law can impact the actions of sovereigns in at arms' length transactions with private entities.

This thesis operates from the postulate that legal norms can affect the behaviour of market actors in three main ways. First, norms shape the market itself. Second, norms tax certain behaviours in order to alter the preferences of market actors. Finally, norms provide legitimacy to certain behaviours.

On the first point, laws provide the structure of the legal relationship between sovereigns and their creditors. Financial markets, like any other market, are essentially created by legal norms enabling market actors to interact with each other[141]. For example, the transferability of bonds has enabled both retail investors and vulture funds to participate within the sovereign debt market by providing them with a legal title over the bonds emitted by sovereigns.

Beyond their roles as gatekeepers, legal norms also structure the behaviour of market players by creating strategic opportunities[142]. They determine the range of possible behaviours within the sovereign debt market. For example, the insertion of collective action clauses in sovereign bonds creates a new strategic opportunity for sovereigns and their creditors, it enables them to restructure entire bond series through a majority vote by bondholders[143].

Second, through enforcement, legal norms incentivise certain behaviours by acting as a pricing mechanism. To put it simply, legal norms render certain types of behaviour more

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in order to reduce transaction costs, and thus functions by being mutually beneficial. See e.g. Robert O Keohane, 'International Institutions: Two Approaches' (1988) 32 International Studies Quarterly 379, 386–387; Terry M Moe, 'Interests, Institutions, and Positive Theory: The Politics of the NLRB' (1987) 2 Studies in American Political Development 236; Duncan Snidal, 'Political Economy and International Institutions' (1996) 16 International Review of Law and Economics 121; Douglass C North, 'Government and the Cost of Exchange in History' (1984) 44 The Journal of Economic History 255. Other arguments base themselves on the fact that sovereigns have to justify their behaviour. See e.g. Louis Henkin, *How Nations Behave* (2nd edn, Columbia University Press 1979).

141 See notably Justin Desautels-Stein, 'The Market as a Legal Concept: Classic Liberalism, Modern Liberalism, Pragmatic Liberalism' [2015] Research Handbook on Political Economy and Law 394 <https://www.elgaronline.com/view/edcoll/9781781005347/9781781005347.00011.xml> accessed 13 May 2019. Citing David Kennedy, *International Legal Structures* (Nomos Verlagsgesellschaft 1987). See also

142 Or, to put it otherwise, legal norms de not merely affect preferences, they can create preferences. See Oren Bar-Gill and Chaim Fershtman, 'Law and Preferences' (2004) 20 Journal of Law, Economics, & Organization 331, 331–332; Sunstein (n 139) 2–3. See also Jules L Coleman and Jody Kraus, 'Rethinking the Theory of Legal Rights' (1985) 95 Yale Law Journal 1335. Citing RH Coase, 'The Problem of Social Cost' (1960) 3 Journal of Law & Economics 1.

143 See *infra* chapter 4.

expensive via sanctions. This indirectly incentivises other types of behaviour[144]. In order to function as incentives, legal norms must provide those injured by the behaviour they seek to disincentivise with legal rights. These legal rights need to be attached to legal remedies, actionable by the injured party[145]. Lastly, remedies need to be of such a nature that, when employed, their impact is sufficient to dissuade the actor against which they are levelled from breaching the norm[146].

Moreover, the content of the obligations contained in the legal norms on sovereign debt, and the remedies attached to their breach, need to be relatively predictable[147], and their enforcement beneficial to the right-holder[148]. In the absence of predictability, actors cannot, *ex ante*, adapt their behaviour to match legal requirements and therefore norms lose their incentivising effect. In addition, in the absence of legal certainty, enforcement by right-holders features an additional risk cost and is thus costlier for the victim.

The impact of the norms which apply to sovereign debt on the behaviour of market actors can also derive from said norms' perceived legitimacy[149]. The legitimacy of legal norms can form part of their pricing effect in that breaching a norm that appears legitimate may lead to additional political or social costs, and *vice versa*[150]. Legitimacy, however, acts beyond

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[144] Oliver Wendell Jr Holmes, *The Path of the Law* (Martino Fine Books 2012); Cooter and Ulen (n 98) 3; Trachtman (n 98) 5–6; Guzman (n 110) 33.; Matthew Adler and Eric Posner, 'Rethinking Cost-Benefit Analysis' (1999) 109 Yale Law Journal 165; Matthew D Adler, Eric A Posner and University of Chicago (eds), *Cost-Benefit Analysis: Legal, Economic, and Philosophical Perspectives* (The University of Chicago Press 2001); Steven Shavell, *Foundations of Economic Analysis of Law* (Harvard University Press 2009) 575–592. For an overview in tort law of how the law can play such a role see e.g. Guido Calabresi, *The Cost of Accidents: A Legal and Economic Analysis* (Yale University Press 2008); Clifton R Musser Professor Emeritus of Law and Economics and Senior Lecturer William M Landes and others, *The Economic Structure of Tort Law* (Harvard University Press 1987).

[145] For a theory of entitlements see Wesley Newcomb Hohfeld, 'Fundamental Legal Conceptions as Applied in Judicial Reasoning' (1916) 26 Yale Law Journal 710.

[146] If they fail to do so, it creates a possibility of efficient breach. Posner, *Economic Analysis of Law* (n 110) 107; Gregory Klass, 'Efficient Breach', *Philosophical Foundations of Contract Law, G. Klass, G. Letsas, P. Saprai (eds.)* (2014); Daniel Friedmann, 'The Efficient Breach Fallacy' (1989) 18 The Journal of Legal Studies 1.

[147] For an illustration of the links between norm's efficiency and predictability see Mario J Rizzo, 'Law amid Flux: The Economics of Negligence and Strict Liability in Tort' (1980) 9 The Journal of Legal Studies 291; Paul H Rubin, 'Predictability and the Economic Approach to Law: A Comment on Rizzo' (1980) 9 The Journal of Legal Studies 319. See also Michael Alstine, 'The Costs of Legal Change' (2002) 49 All Faculty Publications 813; Anthony D'Amato, 'Legal Uncertainty' (1983) 71 California Law Review 1; Jonathan Macey, 'The Internal and External Costs and Benefits of Stare Decisis' (1989) 65 Chicago-Kent Law Review 93; Aurelien Portuese, Orla Gough and Joseph Tanega, 'The Principle of Legal Certainty as a Principle of Economic Efficiency' (2017) 44 European Journal of Law and Economics 131.

[148] Louis Kaplow and Steven Shavell, *Economic Analysis of Law* (1999) 46, 53. Citing Ronald Braeutigam, Bruce Owen and John Panzar, 'An Economic Analysis of Alternative Fee Shifting Systems' (1984) 47 Law and Contemporary Problems 173; Posner, *Economic Analysis of Law* (n 110).

[149] The literature on law's impact and legitimacy is abundant, and a complete overview of the topic is impossible here. As such, this brief section focuses on the impact of legitimacy directly relevant to the current project.

[150] Chayes and Chayes (n 140). See also Bar-Gill and Fershtman (n 142) 332. Citing Louis Kaplow and Steven Shavell, 'Fairness Versus Welfare: Notes on the Pareto Principle, Preferences, and Distributive Justice'

pricing to influence the behaviour of States and their creditors[151]. As mentioned *supra*, market actors are influenced by moral concerns[152]. As such, norms aligning with these concerns are more likely to be followed[153]. As market actors are biased towards acting fairly, norms which are perceived as legitimate logically incentivise certain types of behaviour. For example, if one believes that requiring sovereigns to repay their debts is legitimate since as it aligns with the broadly shared moral principle that promises should be honoured, then, enforcement of sovereign debt contracts against defaulting States is legitimised, and thus incentivised.

Finally, given that sovereign debt is rooted in both contract and international law, it should be noted that the self-serving character of the norms on sovereign debt may play in their favour. As both legal systems are rooted in consent, and as actors within the sovereign debt market are self-interested, it is logical that most of the norms applying to the lawmakers in the sovereign debt relationship will be self-serving. The result of here is that most actors will perceive said consensual norms as legitimate and will thus be likely to follow them[154].

1.3.2 What should the law on sovereign debt do?

After having established how the law on sovereign debt can impact the behaviour of actors within the sovereign debt market, this thesis now needs to determine what type of behaviour a legal system on sovereign debt should encourage, *i.e.* what sets of interests should be protected.

(National Bureau of Economic Research 2003) Working Paper 9622 4 <http://www.nber.org/papers/w9622> accessed 11 May 2020; See also Sunstein (n 139).

[151] Robert Alan Dahl and Charles Edward Lindblom, *Politics, Economics, and Welfare* (Transaction Publishers 1992) 102. Cited in Ian Hurd, 'Legitimacy and Authority in International Politics' (1999) 53 International Organization 379, 388. See also Max Weber, *Economy and Society: An Outline of Interpretive Sociology* (University of California Press 1978) 548; Alexander Wendt, 'Collective Identity Formation and the International State' (1994) 88 The American Political Science Review 384. See also Thomas M Franck, *The Power of Legitimacy Among Nations* (Oxford University Press 1990).

[152] Sunstein (n 136) 217; Jolls, Sunstein and Thaler (n 132) 1492; Fehr, Kirchsteiger and Riedl (n 136).

[153] Multiple empirical studies in criminal law and criminology have found that alignment between norms and shared social values increased compliance. See Tom Tyler and Jonathan Jackson, 'Future Challenges in the Study of Legitimacy and Criminal Justice' (Social Science Research Network 2013) SSRN Scholarly Paper ID 2141322 11 <https://papers.ssrn.com/abstract=2141322> accessed 14 May 2020; Jonathan Jackson and others, 'Why Do People Comply with the Law?Legitimacy and the Influence of Legal Institutions' (2012) 52 The British Journal of Criminology 1051. Lienau also notes 'Perhaps the unique feature of institutions or rules that are considered legitimate is their ability to encourage voluntary compliance—to command a higher degree of support or acquiescence than might otherwise exist in the absence of coercion or selfinterest' Lienau, 'The Challenge of Legitimacy in Sovereign Debt Restructuring' (n 37) 154.

[154] Hurd (n 151) 385. See also Robert Axelrod, 'Effective Choice in the Prisoner's Dilemma' (1980) 24 Journal of Conflict Resolution 3; Jack Citrin and others, 'Public Opinion Toward Immigration Reform: The Role of Economic Motivations' (1997) 59 The Journal of Politics 858; Debra Satz and John Ferejohn, 'Rational Choice and Social Theory' (1994) 91 Journal of Philosophy 71.

Essentially, sovereign debt, as a social phenomenon, aims at providing States with liquidities necessary for the pursuit of their public mission. As such, two clear sets of interests matter within the sovereign debt relationship[155].

First, the interest of creditors ought to be protected by sovereign debt law. Ensuring that sovereign debts protects the legitimate expectations of creditors and strengthens the rule of law. More importantly, protecting creditor's expectations is also necessary to guarantee that creditors will accept to lend to sovereigns[156].

However, when sovereign debts become unsustainable, *i.e.* when a State becomes so indebted that it cannot satisfy its creditors without requiring an alteration of borrowing conditions[157], the law on sovereign debt should provide stakeholders with incentives to reduce said indebtedness. Doing so is economically productive, as it ensures that sovereigns do not default on their debts, thus limiting the damages caused by over-indebtedness on creditors[158]. Moreover, reducing debt burdens limits the negative effects of sovereign debt crises on the debtor's population. Given the well-documented negative impact of said crises on the ability of sovereigns to fulfil the human rights of their population, ensuring that, when necessary, sovereigns can restructure their debt is primordial[159].

Essentially, an 'ideal' legal system on sovereign debt should incentivise States against repudiating their debts, while enabling them to restructure when their debt burdens becomes unsustainable by incentivising creditors to accept reasonable debt proposals[160].

155 Choi, Gulati and Posner (n 91).
156 North (n 124).
157 On debt sustainability see Charles Wyplosz, 'Debt Sustainability Assessment: The IMF Approach and Alternatives' <https://repository.graduateinstitute.ch/record/11765/files/HEIWP03-2007.pdf>.
158 See e.g. Buchheit and Gulati, 'Sovereign Bonds and the Collective Will' (n 89); Sayantan Ghosal and Marcus Miller, 'Writing-down Debt with Heterogeneous Creditors: Lock Laws and Late Swaps' (2016) 6 Journal of Globalization and Development 239.
159 See Lumina, 'Report of the Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, Particularly Economic, Social and Cultural Rights (Mission to Argentina)' (n 6); Lumina, 'Report of the Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, Particularly Economic, Social and Cultural Rights (Mission to Greece)' (n 6); *Sovereign Debt and Human Rights* (n 70).
160 Riegner notes: '*Sovereign debt restructurings are firstly governed by the principles of economy and of sustainability. In general, economy requires public finances to be managed in a way that is purposeful, results-oriented, and cost efficient. With regard to sovereign debt, economy finds expression in the principle of sustainability: Debt must be managed in a way that uses public resources in a manner that is efficient in the longer term and that prevents avoidable financial burdens. This entails a duty to restructure debt if a restructuring is evidently the only way to avoid excessive burdens on public finances.*' Riegner (n 6) 160.

1.4 Structure of this thesis

This thesis, beyond its introduction, is divided in three main chapters. Chapter 2 aims at providing some background on how sovereign debt works. It is divided in two main sections. Its Section 1 provides a brief overview of the main economic theories explaining the creditor/sovereign relationship. Section 2 provides an overview of how this relationship has evolved historically. The purpose of this first chapter is to frame the creditor protection and the anti-holdout model within the economic scholarship on sovereign debt and to explain the development of both models in a historical perspective.

The third chapter of this thesis provides an overview of the creditor protection model. Its first section provides a general theory of the creditor protection model's functioning. It argues that, in order to incentivise lending, the law on sovereign debt needs a combination of three elements: access by creditors to competent courts independent from the sovereign, the recognition by said courts of the sovereign's responsibility [161]; and efficient legal remedies granted by courts to coerce the sovereign.

The second section of chapter 3 analyses how these three components have been implemented in international law. It analyses each components of the creditor protection model in international law separately. The last section highlights the strengths and weaknesses of the creditor protection model. To summarise, it argues that while creditor protection incentivises lending, enhances the debtor's accountability and is predictable, it also incentivises holding out in the contemporary bond market, thus ultimately leading to a situation where unsustainable debts cannot easily be restructured.

The fourth chapter of this thesis turns to an analysis of the anti-holdout model. As with the second chapter, it begins by highlighting the necessary component for the model to function, namely, majority decision-making during restructurings, a limitation of the remedies available to creditors and the provision of additional liquidities to the sovereign debtor. Section 2 then analyses how these components have been implemented in international law. Section 3, highlights the strengths and weaknesses of the second model, *i.e.* the fact that while the anti-holdout model facilitates restructuring, its implementation is detrimental to

[161] Which this thesis has dubbed, following Gathii, the sanctity of creditor's rights. See James Thuo Gathii, 'The Sanctity of Sovereign Loan Contracts and Its Origins in Enforcement Litigation' (2006) 38 George Washington international law Review 251.

retail investors, risks leading to a fragmentation of the law on sovereign debt and does little to encourage early restructurings by the debtor.

This thesis concludes by providing *de lege ferenda* ideas to improve upon the current weaknesses of the anti-holdout model.

2 Understanding Sovereign debt

2.1 Introduction

As underlined by Graeber, in *Debt: the first 5000 years,* a debt relationship presupposes some form of equality between creditors and debtors[162]. Said equality enables creditors to ensure that debtors will eventually repay their debts, usually by providing lenders with remedies designed to protect their rights against borrowers[163].

Starting from these premises, sovereign debt is an oxymoron. Sovereign debtors, historically, have been endowed with regulatory powers[164] and immunity from litigation[165], meaning lending to foreign sovereigns was an endeavour mired with uncertainty[166]. *A contrario*, creditors of a private entity have always been guaranteed that their debtor cannot unilaterally modify the conditions of the debt contract. Similarly, were a private debtor to default or renege upon its debt, creditors can rely on courts and tribunals to obtain payment, either through the attachment of the debtor's assets, or through its liquidation in a bankruptcy process[167].

This puts the creditor of a sovereign in a peculiar position. On the one hand, sovereign lending has been a particularly lucrative activity. A recent study highlights that since 1815

162 David Graeber, *Debt: The First 5,000 Years* (Melville House 2011) 190–191.
163 ibid.
164 Such an ability, as will be exposed in the next section has at today's been greatly diminished. However, regulatory interventions to facilitate sovereign debt restructurings are not unheard of contemporarily. For example, in the early 2000s, Argentina legislated to prevent itself from repaying holdout creditors. More recently, Greece retroactively introduced a Collective Action Clause in its sovereign bonds to facilitate its restructuring process. See on Argentina: Arturo C Porzecanski, 'From Rogue Creditors to Rogue Debtors: Implications of Argentina's Default Symposium: Sovereign Debt Restructuring' (2005) 6 Chicago Journal of international law 311. On Greece, *Mamatas et autres v Greece* [2016] European Court of Human Rights 63066/14; 64297/14 and 66106/14; Astrid Iversen, 'The Future of Involuntary Sovereign Debt Restructurings: Mamatas and Others v Greece and the Protection of Holdings of Sovereign Debt Instruments under the ECHR' (2019) 14 Capital Markets Law Journal 34. Historically such legislative debt repudiations or restructurings were more common. Waibel, notably mentions Peru's 1886 and 1889 legislative restructuring of its debt. See Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 73–74. Commenting on *Canevaro Claim (Italy v Peru), Award* (1912) 6 AJIL 746 (Permanent Court of Arbitration). On the same case see also 'The Canevaro Case at the Hague' (1912) 6 The American Journal of international law 709.
165 See Delaume (n 82); Weidemaier, 'Sovereign Immunity and Sovereign Debt' (n 82).
166 As underlined by Feis, "A loan to a foreign government is an act of faith" Herbert Feis, *Europe The World'S Banker 1870 - 1914* (Yale University Press 1931) 102. Cited in Megliani, *Sovereign Debt* (n 50) 239. Megliani similarly cites Terré noting that: "L'Etat étranger est bien souvent le plus mauvais des payeurs". François Terré, 'Note a Cour d'appel de Paris, Société Bauer-Marchal c. Ministère Des Finances de Turquie' (1957) 84 Journal de Droit International 394; Megliani, *Sovereign Debt* 239.
167 Ugo Panizza, Federico Sturzenegger and Jeromin Zettelmeyer, 'The Economics and Law of Sovereign Debt and Default' (2009) 47 Journal of Economic Literature 651. For a comparison between sovereign and corporate bankruptcies see also Patrick Bolton, 'Towards a Statutory Approach to Sovereign Debt Restructuring: Lessons from Corporate Bankruptcy Practice Around the World' [2003] IMF Working Paper.

the returns on sovereign bonds have on average outperformed the yield granted by their corporate counterparts[168]. The same study shows that, overall, the risk of default of sovereigns has been quite low[169].

On the other hand, in practice, sovereigns have been able to repudiate their debts, or to force creditors into unwanted restructurings[170]. If one thinks, of the 1917 repudiation of the Tsarist debt by Soviet Russia, or of the refusal by Argentina[171] to repay its creditors it is undeniable that States can go rogue[172].

This peculiar position of creditors to a 'puzzle'[173] for both the legal and the economic scholarship on sovereign debt: why would a rational creditor extend credit to a sovereign whilst knowing that the latter can renege on its contractual obligations without facing efficient judicial remedies?[174] Correlatively, why would a rational State ever repay its debts, knowing that the legal consequences of refusing to do so are limited?

This sovereign debt puzzle is not purely theoretical. The creditor protection model can be understood as a direct response to the challenges produced by the specificities of sovereign lending. In order to better understand the context in which the creditor protection model has developed, the first part of this thesis needs to analyse the two main scholarly answers to the sovereign debt puzzle: the reputational theory of sovereign lending and the credible commitment theory. These two theories will be analysed in section 2 of this first chapter.

While creditor protection, as a framework for regulating sovereign debt is easily explained by the economic specificities of sovereign lending, explaining the move away from creditor protection and towards easing debt restructurings necessitates a deeper historical

[168] Josefin Meyer, Carmen M Reinhart and Christoph Trebesch, 'Sovereign Bonds since Waterloo' (National Bureau of Economic Research 2019) Working Paper 25543 <http://www.nber.org/papers/w25543> accessed 12 February 2019. The profitability of sovereign lending, on aggregate, has also been underlined by Peter Lindert and Peter Morton, 'How Sovereign Debt Has Worked', *Developing Country Debt and the World Economy* (University of Chicago Press 1989) <http://www.nber.org/chapters/c7529.pdf>.

[169] Meyer, Reinhart and Trebesch (n 168).

[170] Gulati and Buchheit quote, as foreword to Olivares-Carminal's "Legal Aspects" an 1876 English decision stating that "these so-called [sovereign] bonds amount to nothing more than engagement of honour, binding, so far as engagements of honour bind (…)". *Twycross v Dreyfus* [1876] Tokyo Ika Shika Daigaku Iyo Kizai Kenkyusho Hokoku 177 (Court of Appeal); Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) vi.

[171] For an overview of Argentina's debt restructuring see Amrita Dhillon and others, 'Debt Restructuring and Economic Recovery: Analysing the Argentine Swap' (2006) 29 World Economy 377; Samples (n 73).

[172] Porzecanski (n 164); Samples (n 73).

[173] The 'sovereign debt puzzle' term was coined by Marc Flandreau and Juan H Flores, 'Bonds and Brands: Foundations of Sovereign Debt Markets, 1820–1830' (2009) 69 The Journal of Economic History 646.

[174] Mark C Weidemaier and G Mitu Gulati, 'Sovereign Debt and the "Contracts Matter" Hypothesis' (Social Science Research Network 2014) SSRN Scholarly Paper ID 2511251 2 <https://papers.ssrn.com/abstract=2511251> accessed 27 November 2019.

understanding of how the sovereign debt market has evolved. This historical overview of sovereign lending will be the subject of the third section.

2.2 Competing Theories of Sovereign Lending

In order to understand the importance of the legal remedies granted to creditors, one has first to understand how sovereign lending, as an economic relationship, can be understood. So far, two main theories have been pushed forward in the literature on sovereign debt. The first focuses on reputation, the second on credible commitment devices[175].

This thesis does not argue that either theory is exclusive. Rather, it understands both reputation and credible commitment devices as tools available to States and their creditors to facilitate relationships within the sovereign debt market. Therefore, this thesis understands the relationship between creditors and sovereign debtors as a hybrid between these two models. This hybrid model will be briefly explained in the third section.

2.2.1 Reputation and Sovereign Debt

The current understanding of the reputational model of sovereign lending has mostly been developed by Tomz[176]. It posits that cooperation between lenders and borrowers can be

[175] Some alternative explanations of how sovereign debt 'works' have been put forward in the scholarly literature on debt. Flandreau and Flores, notably has analysed the role of issuing banks as seal of approval for debtors in the early XXth century, see Flandreau and Flores (n 173).. Similarly, much has been written on the role of colonial institutions, to explain why debtors, especially South American debtors, repaid their debts to creditors in imperial powers. See, *inter allia*, Marc Weidenmier, 'Gunboats, Reputation, and Sovereign Repayment: Lessons from the Southern Confederacy' (National Bureau of Economic Research 2004) Working Paper 10960 <http://www.nber.org/papers/w10960> accessed 18 January 2016; Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 29–35. However, as opposed to the theories analysed in this section, these explanations do not provide an explanation of how sovereign debt works across time. They will therefore not be analysed in more details. Other theories of why sovereign repay have been advanced, notably, the role of international sanctions in repayment has been advanced. See e.g. Jeremy I Bulow and Kenneth Rogoff, 'Sovereign Debt: Is To Forgive To Forget?' (National Bureau of Economic Research 1988) Working Paper 2623 <http://www.nber.org/papers/w2623> accessed 18 January 2016; Jeremy Bulow and Kenneth Rogoff, 'A Constant Recontracting Model of Sovereign Debt' (1989) 97 The Journal of Political Economy 155; Mark C Weidemaier and G Mitu Gulati, 'Sovereign Debt and the "Contracts Matter" Hypothesis', 2 (Social Science Research Network 2014) SSRN Scholarly Paper ID 2511251 <https://papers.ssrn.com/abstract=2511251> accessed 27 November 2019. However, this thesis understands sanctions as a credible commitment devices. Finally, a third school argues that States do not repudiate their debt because of the domestic economic consequences of doing so, both economically and politically. Panizza, Sturzenegger and Zettelmeyer (n 167). While the consequences of defaults and the harmful effects of sovereign debt crises on the domestic population of the debtor are well documented, it seems that arguing that States do not opportunistically default because doing so would be too costly fails to explain the cases in which States have actually gone rogue.

[176] Tomz (n 112). Reputational analysis of the sovereign debt relationship seems to have been first developed by Jonathan Eaton and Mark Gersovitz, 'Debt with Potential Repudiation: Theoretical and Empirical Analysis' (1981) 48 The Review of Economic Studies 289.

achieved because both sovereigns and their creditors are repeat players within the sovereign debt market. In Tomz' model, 'good States'[177], those who repay the sums they have borrowed, do so in order to build a good reputation, and thus benefit from better borrowing conditions[178]. *A contrario*, 'bad States', or 'lemons'[179], do not benefit from such a reputation. Therefore, potential lenders may be weary of extending them credit under favourable conditions. This increased perceived risk by foreign lenders does not mean that lending will not occur, but rather that it will be priced-in by investors, resulting in 'lemons' having to borrow with a higher interest rate than their more reliable counter-part[180].

This creates an incentive for States to repay their debts as, ultimately, doing so will enable them to increase their reputation with lenders, and obtain cheaper debt[181]. On the lenders' side, reputation not only enables creditors to perform a more accurate risk assessment[182], but also incentivises lending since creditors know that rational States have no interest in defaulting without good reason[183].

The reputational theory of sovereign debt can provide a key insight in understanding the move between the two models of sovereign debt regulation exposed in this thesis. It shows that judicial enforcement is not the only tool to incentivise States to repay their debts. Therefore, an absence of legal remedies does not automatically lead to risks of moral hazard.

The problem with the reputational theory, from a creditor's point of view, is that it does not provide actual *ex ante* assurances against debt repudiation. This is especially true when the reputational costs of said repudiation are outweighed by the short-term benefits of default[184]. The knowledge that the debtor will be, *ex post*, punished by higher interest rates is of little

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[177] Tomz's typology divides States in three separate categories, depending on their tendency towards repayment: stalwart, fair-weathers and lemons. While this divide into three types is useful in understanding creditors preferences, it is not necessary for a brief overview of the literature on debt and reputation. Tomz (n11) 16-17.
[178] Tomz (n 112) 16. For a critique of these assumptions see notably Lienau, 'Law in Hiding' (n 108) 562–569.
[179] Tomz (n 112) 17.
[180] ibid 23; Laura Alfaro and Fabio Kanczuk, 'Sovereign Debt as a Contingent Claim: A Quantitative Approach' (2005) 65 Journal of International Economics 297; Ugo Panizza and eduardo Borzenstein, 'The Costs of Sovereign Defaults' (2008) 238 IMF Working Paper. The impact of future borrowing costs and market exclusion is heavily debated in the economic scholarship on sovereign debt. For an overview of the arguments see Panizza, Sturzenegger and Zettelmeyer (n 167).
[181] Tomz (n 112) 23. Irani Arraiz, 'Default, Settlement, and Repayment History: A Unified Model of Sovereign Debt' (Social Science Research Network 2006) SSRN Scholarly Paper ID 1455163 <https://papers.ssrn.com/abstract=1455163> accessed 15 January 2020.
[182] As the risk of repudiation is compounded in the bonds interest rate
[183] Tomz (n 112) 23–25; Juan Cruces and Christoph Trebesch, 'Sovereign Defaults: The Prics of Haircuts' [2011] CESinfo Working Papers Series; Lienau, 'Law in Hiding' (n 108).
[184] See North and Weingast (n 124).

comfort to the bondholder who has just seen his investment disappear following an opportunistic default[185].

Thus, the reputational theory can explain why, on average, States are able to borrow, but a sovereign debt market driven purely by reputation does little to protect the creditors of defaulting States or reassure them *ex ante*. Such mechanism are, rather, the domain of the credible commitment model of sovereign lending.

2.2.2 Credible Commitment and Sovereign Debt

The credible commitment theory of sovereign lending was first put forward by North and Weingast in relation to Britain's increased capacity to borrow following the Glorious Revolution[186].

The two authors base their arguments on the constitutional changes which followed the deposition of James II and the coronation of William III of Orange. The Revolution lead to a shift in power away from the Crown and in favour of Parliament. Under the constitutional regime introduced by the Glorious Revolution, Parliament which at the time was appointed by and constituted of wealth holders, gained the ability to regulate the Crown's finance[187]. According to North and Weingast, this created, an environment in which Britain could borrow at much more favourable rates than its European counterparts[188]. Indeed, Parliament, following the Revolution, was not only committed to the protection of property rights, but also had a vested interest in seeing that the government would repay what it had borrowed from private entities. This synergy was further enabled by the fact that, as members of the financial and aristocratic elite of Britain, parliamentarians themselves would often be creditors of the Crown, and part of a growing British *rentier* class[189]. As such the prerogatives granted to parliament rendered the Crowns' creditors themselves responsible for deciding whether it could repudiate on its debts. This meant, in practice, that the British

[185] Bulow and Rogoff, 'Sovereign Debt' (n 175).In order to solve this conundrum, Eaton suggests a model where creditors agree *ex ante* to deny future lending in case of default. Jonathan Eaton, 'Sovereign Debt, Reputation and Credit Terms' (1996) 1 International Journal of Finance & Economics 25.
[186] See: North and Weingast (n 124); North (n 124).
[187] North and Weingast (n 124) 815–817.
[188] North and Weingast (n 124); North (n 124); John Beckett, 'The Glorious Revolution, Parliament, and the Making of the First Industrial Nation' (2014) 33 Parliamentary History 36.
[189] Kenneth Dyson, *States, Debt, and Power: 'Saints' and 'Sinners' in European History and Integration* (Oxford University Press 2014) 112.

government could constrain its future behaviour in such a way as to render debt repudiation unlikely, if not impossible[190].

These factors explain why, compared to its European neighbours, 17th and 18th century Britain was able to borrow at extremely advantageous interest rates[191]. Interestingly, further studies have confirmed North and Weingast's findings by applying them to other historical democratic transitions in Europe[192].

Studies on the role played by the Gold Standard in sovereign lending seems to similarly confirm the idea that the ability of governments to effectively constrain themselves is key in their ability to borrow[193]. According to Bordo[194], the Gold Standard, via which States pegged the value of their currencies to that of gold, acted as a 'good housekeeping seal of approval' as it effectively prevented States from devaluing their currencies. This guaranteed that sums

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[190] North (n 124); David Stasavage, 'Why Did Public Debt Originate in Europe?', *Fiscal Regimes and the Political Economy of Premodern States* (Cambridge University Press 2015); Gary W Cox, 'Was the Glorious Revolution a Constitutional Watershed?' (2012) 72 The Journal of Economic History 567. It should be noted that there has been push-back against North and Weingast theory. Some authors have emitted doubts as to whether the Glorious Revolution actually lead to a measurable increased in Britain's capacity to borrow. See Nathan Sussman and Yishay Yafeh, 'Institutional Reforms, Financial Development and Sovereign Debt: Britain 1690–1790' (2006) 66 The Journal of Economic History 906. Other have argued that the reforms pointed to by North and Weingast had not been the instantaneous result of the Revolution but rather the result of an evolving trend. See Patrick Karl O'Brien, 'Fiscal and Financial Preconditions for the Formation of Developmental States in the West and the East from the Conquest of Ceuta (1415) to the Opium War (1839)' (2012) 23 Journal of World History 513. Despite these criticism, it seems that North and Weingast theory has entered the real of mainstream political economics and is broadly accepted at today's date. For a rebuttal of these critiques see Cox. For a broader analysis of the context and the constitutional changes heralded by the Revolution see John Miller, *The Glorious Revolution* (2nd edn, Routledge 1997).

[191] North and Weingast (n 124) 820–824. That is not to say that other factors have not played a role in the surge in Britain's capacity to borrow after the Revolution. The creation of the Bank of England, acting as the guardian of British monetary policy, is often mentioned as having bolstered the reliability of British bonds. See Der-Yuan Yang, 'The Origin of the Bank of England: A Credible Commitment to Sovereign Debt' <https://escholarship.org/uc/item/11s61814> accessed 18 November 2019; Stephen Quinn, 'Securitization of Sovereign Debt: Corporations as a Sovereign Debt Restructuring Mechanism in Britain, 1694-1750' (Social Science Research Network 2008) SSRN Scholarly Paper ID 991941 <https://papers.ssrn.com/abstract=991941> accessed 18 November 2019. However, it is undeniable that one of the key differences between Britain at the time and other European Nations, *i.e.* France, Austria or Spain, is the fact that the British monarchs following the Revolution ceased to wield the absolute power that had previously enabled them to ignore contractual obligations. For a comparison between 18th century French and British debt see David Stasavage, *Public Debt and the Birth of the Democratic State: France and Great Britain, 1688-1789* (Cambridge University Press 2003). On debt and the Spanish monarchy see James Conklin, 'The Theory of Sovering Debt and Spain under Philip II' (1998) 106 Journal of Political Economy 483; Anne Dubet, 'Les Rois d'Espagne et Leurs Créanciers', *La dette publique dans l'histoire : « Les Journées du Centre de Recherches Historiques» des 26, 27 et 28 novembre 2001* (Comité pour l'Histoire économique et financière 2006).

[192] Kim Oosterlinck, Loredana Ureche-Rangau and Jacques-Marie Vaslin, 'Waterloo: A Godsend for French Public Finances?' (European Historical Economics Society (EHES) 2013) Working Paper 0041 <https://ideas.repec.org/p/hes/wpaper/0041.html> accessed 27 July 2016.

[193] Michael D Bordo, 'The Gold Standard as a `Good Housekeeping Seal of Approval'' (National Bureau of Economic Research 1995) Working Paper 5340 <http://www.nber.org/papers/w5340> accessed 26 February 2016.

[194] ibid.

they had promised to their creditors would retain their value[195], even in times of crisis. Bordo, logically, finds a strong correlation between adoption of the Gold Standard and increased borrowing capacity[196]. Similar conclusions are drawn by Mitchener and Weidenmier regarding 'supersanctions' during the late 19th century[197]. Supersanctions, here refer to the ability of Western powers between 1870 and 1913 to rely on the use of force or to mandate fiscal change for defaulting foreign sovereigns[198], thus constraining those debtors' future behaviour.

The creditor protection model, as understood in this thesis, could be summarised as a judicial application of the credible commitment theory. As will be shown, under the creditor protection model, courts, whether domestic or international, are tasked with effectively binding States to their contractual obligations. As demonstrated by the aforementioned studies, this not only benefits the creditors of sovereigns, but is also beneficial for the sovereign itself.

The strength of the credible commitment theory of sovereign debt, is that, as opposed to the reputational theory, it can explain how sovereign debt works in specific instances. Creditors agree to lend to specific States because they know *ex ante* that these States cannot repudiate their debts. However, credible commitment fails to explain how sovereign debt functions when such devices are lacking[199].

2.2.3 A Hybrid Model of Sovereign Lending

This thesis does not consider credible commitment and reputation to be exclusive ways of understanding how sovereign debt works. Rather, both credible commitment devices and reputation building can be used by States and their creditors to improve the conditions of their access to capital markets.

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[195] A series of judicial cases were brought, most of them by France, on behalf of creditors having extended to states sums repayable in gold denominated currencies. See Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 58–73. Examining *Case Concerning the payment of various serbian loans issued in France (France v Serbia)* (1929) Series A n°20/01 Publ Cour Int Justice 1 (Permanent Court of International Justice); *Case concerning the Payment in Gold of Brazilian Federal Loans Contracted in France (France v Brazil)* (n 34). The Norwegian loan case brought before the ICJ proceeded from a similar factual nexus but was dismissed on the basis of a lack of jurisdiction. *Case of Certain Norwegian Loans (France v Norway)* (1957) 1957 ICJ Rep 9 (International Court of Justice). See also Borchard and Hotchkiss (n 2) 26–42.
[196] Bordo (n 193).
[197] Mitchener and Weidenmier (n 91).
[198] ibid. The use of force, forced monetary policy and the 'quasi-receivership' of foreign sovereign is also analysed in Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 22–88.
[199] Which is for most of sovereign debt's history.

Fundamentally, this thesis understands that favourable access to capital markets is, in the modern world, essentially governed by financial considerations[200]. The interest rate on a sovereign bond is mostly determined by the borrower's current perceived solvency and liquidity, the bond's maturity, the borrower's reputation and the broader market conditions at the time of lending.

This does not mean that the law plays no role in sovereign lending. At the margin, States which are perceived as less reliable can use credible commitment devices to improve their access to capital markets. Recent studies on Greece for example have shown that when the Hellenic Republic's solvability was doubted, Greek bonds issued under foreign laws were treated more favourably than Greek-law bonds with similar maturities[201]. Similarly, the 'original sin' hypothesis analysed in chapter 3 shows that when the solvency of sovereign borrowers is questioned, they can improve their access to capital markets by borrowing in foreign currencies[202]. However, these devices should be understood as tools available to debtors to improve their borrowing conditions, rather than as mandatory conditions for accessing capital markets.

2.3 Sovereign Lending in a Historical Context

2.3.1 Introduction

Another way to understand the rise of the creditor protection model and the subsequent move towards the anti-holdout model, is to place both models in their respective historical contexts. To that end, this section will look at four distinct 'eras' of sovereign lending. First, it will provide a quick overview of how sovereign debt has worked in a more distant past, between the 4th century B.C. and the 19th century. Generally, the purpose of this section is not to aspire to exhaustivity[203], but rather to highlight that mechanisms designed to protect creditors

[200] Several studies on the *pari passu* clause and CACs have notably shown that the insertion of clauses designed to impede enforcement has little effect on borrowing costs of financially stable States. See Ashoka Mody and Barry Eichengreen, 'Would Collective Action Clauses Raise Borrowing Costs? An Update and Additional Results' (Social Science Research Network 1999) SSRN Scholarly Paper ID 630737 <https://papers.ssrn.com/abstract=630737.> accessed 15 January 2020; Anna Gelpern and Mitu Gulati, 'Public Symbol In Private Contract: A Case Study' (2006) 84 Washington University Law Review 1627; Michael Bradley, James Cox and Mitu Gulati, 'The Market Reaction to Legal Shocks and Their Antidotes: Lessons from the Sovereign Debt Market' (2010) 39 Journal of Legal Studies 289. Similar conclusions have been drawn by Weidemaier regarding changes in the law of immunities. See Weidemaier, 'Sovereign Immunity and Sovereign Debt' (n 82).

[201] Choi, Gulati and Posner (n 91).

[202] Eichengreen, Haussman and Panizza (n 114).

[203] This historical section, in general, does not focus on the League of Nations Loans, the role of issuing banks in signalling debtors' credibility in the early XXth century or on borrowings by Northern European Cities via

are not a historical anomaly. As will be shown, creditors have historically benefitted from institutional arrangements, either with the debtor or with their own States, designed to maximise the likelihood of seeing sovereign debts repaid. This hardly comes as a surprise given the role credible commitment plays in sovereign lending. However, and as will be underlined in the first section, while these remedies existed and provided a measure of creditor protection, their nature[204] and effectivity[205] renders them materially different from those analysed under the creditor protection model.

The second section focuses on sovereign debt between the late 19th century and the 1950s. This specific era of sovereign lending deserves specific attention as it provides a direct backdrop for the rise of the creditor protection model in the 1970s. It argues, that the illegality of gunboat diplomacy, and the political risks tied to the exercise of diplomatic protection, combined with a wave of defaults in the 1920s explain why private creditors refrained from lending to developing States during the interwar period, and up to the 1970s.

The third section then focuses on sovereign debt during the 1970s and 1980s, this period not only marks the return of developing States to capital markets, but also marks the rise of the conditions in which the creditor protection model could function, *i.e.* the syndicated loan market.

Finally, the last section analyses the rise of the modern bond market following the Latin American debt crisis, which marks the beginning of the inefficiencies of the creditor protection model and the rise of the restructuring protection model analysed in chapter 4.

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rentes. These questions, while deserving a place in a historical study of sovereign debt are not as useful g to set the background of the creditor protection model. See Margaret G Myers, 'The League Loans' (1945) 60 Political Science Quarterly 492; Manon van der Heijden, 'Renteniers and the Public Debt of Dordrecht (1555-1572)', *Urban public debts, urban government and the market for annuities in Western Europe (14th-18th centuries)*, vol 3 (Brepols Publishers 2003) <http://www.brepolsonline.net/doi/abs/10.1484/M.SEUH-EB.3.1948> accessed 27 July 2016; John H Munro, 'The Medieval Origins of the Financial Revolution: Usury, Rentes, and Negotiability' (2003) 25 The International History Review 505; Flandreau and Flores (n 173). See also for an historical overview of sovereign debt Dyson (n 189); Graeber (n 162); Jean Andreau and others, *La dette publique dans l'histoire : 'Les Journées du Centre de Recherches Historiques' des 26, 27 et 28 novembre 2001* (Comité pour l'Histoire économique et financière 2006).

[204] The fact that they are mostly extra-judicial.

[205] The fact that, often, they failed to provide creditors with an actual shield against foreign sovereigns unwilling to repay their debts.

2.3.2 Early Instances of Sovereign Lending

Sovereign debt has a significant history. The first recorded mention of public entities borrowing from private citizens dates from Ancient Greece, in the 4th century B.C.[206]. Debt, at the time, was mostly used by City-States to quickly raise the liquidities required to hire mercenary armies[207]. Greek city-States only sheltered a small population compared to their larger neighbours, meaning they could hardly spare the men needed to maintain a standing army and had to rely on mercenaries to wage war[208].

The debt of these Greek cities bears witness to the fact that mechanism designed to ensure that sovereigns[209] could not renege upon their debts have historical precedence. Loans to the cities, for example, were secured against the assets of the *polis*[210] itself or by personal guarantees pledged by its wealthy citizens[211]. Enforcement of these secured loans was possible either by seizing the assets pledged as security, by suing individuals within the city themselves, or by recourse to arbitration before a third city[212].

With the first borrowings by public entities came the first defaults. The first recorded mention of sovereign debt focuses on a dispute between Dionysus, tyrant of Syracuse and his foreign creditors[213]. Said creditors accused the tyrant of having willingly debased his own currency to facilitate the repayment of large sums he had borrowed abroad[214].

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206 Léopold Migeotte, 'L'endettement Des Cités Grecques Dans l'Antiquité', *La dette publique dans l'histoire : « Les Journées du Centre de Recherches Historiques» des 26, 27 et 28 novembre 2001* (Comité pour l'Histoire économique et financière 2006).
207 Graeber (n 162) 226; Emily Mackil, 'The Greek Polis and Koinon', *Fiscal Regimes and the Political Economy of Premodern States* (Cambridge University Press 2015); Migeotte (n 206).
208 Migeotte (n 206); Mackil (n 207).
209 'Sovereign', in this section is used in the loosest of sense and not in its modern, post-Westphalian meaning. It simply refers to the fact that the debtor has regulatory capacities, which therefore increase the political and legal risks faced by its creditors. Some authors refer to 'public debt' rather than 'sovereign debt' when discussing the borrowings of pre-modern 'sovereigns'. However, for the sake of clarity, this thesis uses the term sovereign debt throughout its entirety.
210 Often the public buildings themselves or future tax revenues. See the multiple examples mentioned in Léopold Migeotte, *L'emprunt Public Dans Les Cités Grecques: Recueil Des Documents et Analyse Critique* (Les Éditions du Sphinx 1984).
211 For an overview of the contracts of the Greek *polis*, see the documents gathered by ibid.
212 Joseph J Walsh, 'The Disorders of the 170s b.c. and Roman Intervention in the Class Struggle in Greece' (2000) 50 The Classical Quarterly (New Series) 300; Migeotte (n 210) 44; RJ Buck and RM Nielsen, 'Is Nikareta an Exception?' (1989) 21 Prudentia 14; Sheila L Ager, *Interstate Arbitrations in the Greek World, 337-90 B.C* (University of California Press 1996). Later on cities would sometimes submit their arbitral disputes to well regarded foreign intellectuals, Cicero notably served as sole arbitrator of one such dispute. See ibid; Walsh.
213 Charles J Bullock, 'Dionysius of Syracuse. Financier' (1930) 25 The Classical Journal 260.
214 ibid.

The debt of 4th century B.C. Greek city-States clearly highlights the importance of some measure of creditor protection to enable public entities to obtain lending. Those remedies, designed to protect creditors, were quasi-boilerplate clauses present in most of them[215], highlighting their importance.

Due to the lack of surviving written sources, assessing the efficiency of these remedies for creditors is difficult. However, the historical record shows instances of arbitral litigation between foreign creditors and foreign city-States, resulting in repayment of debts to the latter[216]. Similarly, anecdotal evidence suggests that attachment of assess of assets of defaulting debtors occurred[217].

These early instances of sovereign debt would cease after the assimilation of the Hellenic peninsula by the Roman republic. Rome itself seldom borrowed, and never from foreign creditors[218], and whether other antique nations did so is uncertain in the absence of written sources.

Medieval sovereigns, *a contrario*, often relied on credit, either from their subjects or more often from Italian or Jewish bankers. The relationship between those bankers and the crowns of Europe would be fraught with defaults by the latter. Notably, Edward III’s debt repudiation, which arguably caused the downfall of the Florentine Bardi bank[219].

As opposed to the creditors of Greek City-States, Italian and Jewish bankers were not endowed with any legal recourse against defaults[220]. However, while judicial creditor protection is absent in medieval sovereign debt, creditors effectively tied lending to the

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[215] See the study of these clauses by Migeotte (n 210).
[216] For a study of this early quasi-international litigation on sovereign debt see Ager (n 212).
[217] See the examples mentioned in Migeotte (n 210); Migeotte (n 206); Ager (n 212).
[218] There seems to be only two instances where Rome relied on debt to fund itself, respectively during the first and second Punic wars. At both times, the Republic was famously in dire circumstances and on the verge of collapse, leading historians to argue that in those cases the line between actual lending with the intention on seeing repayment and charity is blurred. There are some mentions of Emperors borrowing in their own names, however, given the structure of the Imperial Roman constitution, said debt does not appear to have been attributed to Rome itself. See Jean Andreau, ‘Existait-Il Une Dette Publique Dans l’Amtiquité Romaine?’, *La dette publique dans l’histoire : « Les Journées du Centre de Recherches Historiques» des 26, 27 et 28 novembre 2001* (Comité pour l’Histoire économique et financière 2006).
[219] For an overview of the relationship between the Bardi bank and the English crown see Edwin S Hunt, ‘A New Look at the Dealings of the Bardi and Peruzzi with Edward III’ (1990) 50 The Journal of Economic History 149.
[220] Regarding the latter the repudiation of debts owed to Jewish bankers had been actively encouraged by the IVth Lateran Council in 1213. The reasoning of the Council was that, while Jewish bankers escaped the prohibition of usury required by the Catholic doctrine, their practices were ‘cruel’, ‘treacherous’ and their interest rates ‘excessive’ which justified repudiation of debts and confiscation of the Jewish merchants’ property. See Dyson (n 189) 175; Mark Koyama, ‘The Political Economy of Expulsion: The Regulation of Jewish Moneylending in Medieval England’ (2010) 21 Constitutional Political Economy 374.

obtention of tax-farming competences, or trade in restricted goods. In practice, therefore, creditors could obtain repayment via the obtention of streams of revenues which would otherwise have flown to the sovereign itself.

For example, Italian banks operating in England obtained a monopoly on the trade of English wool in exchange for their loans to the crown[221]. Similarly, the Medici bank obtained, from its loan to the papacy, the right to collect annates[222], and the fees owed by bishops for their instauration[223].

Similar relationships were developed by medieval city-States and their creditors, with the latter obtaining rights to farm taxes on behalf of the city, and to pay themselves with the proceeds of said tax collection[224].

These schemes, for creditors, had the advantage of substituting a debtor immune to enforcement (the sovereign), with a stream of revenue whose originator could effectively be coerced into repayment (the taxpayer). Tax evasion, indeed, could effectively be punished, if needed, by recourse to excommunication[225].

Outside medieval Europe, similar relationships can be found Ottoman Empire's management of its debt from the 16th century onwards[226]. Like its European counterparts, the Sublime Port assigned to its creditors the collection of specific tax-revenues in order to secure lending. Tax farming rights were first granted on the basis of specific individual contracts called *Mukataa*, but from the 16th century onwards, those rights were auctioned off to potential lenders[227].

[221] Meir Kohn, 'Merchant Banking in the Medieval and Early Modern Economy' [1999] Dartmouth College, Department of Economics Working Paper <http://poseidon01.ssrn.com/delivery.php?ID=013084113099072068086101118111086007093015095067062090018078004127125093086088083115004013115118029070026041120031031106072030065125108101124099071091104121124106028097068110007121097114&EXT=pdf>; Janet Burton, Frederique Lachaud and Phillipp Schofield, *Thirteenth Century England XIII: Proceedings of the Paris Conference, 2009* (Boydell Press 2011); Dyson (n 189) 139.

[222] Annates were the yearly fee paid by bishops or other clerics on the revenues of their see.

[223] Raymond De Roover, *The Rise and Decline of the Medici Bank, 1397-1494* (1963) 212; Tim Parks, *Medici Money: Banking, Metaphysics, and Art in Fifteenth-Century Florence* (WW Norton 2005) 47–48.

[224] Michele Fratianni, 'Government Debt, Reputation and Creditors' Protections: The Tale of San Giorgio' (2006) 10 Review of Finance 487; Michele Fratianni and Franco Spinelli, 'Italian City-States and Financial Evolution' (2006) null European Review of Economic History 257.

[225] Fratianni (n 224); Parks (n 223); De Roover (n 223).

[226] Şevket Pamuk, 'The Evolution of Financial Institutions in the Ottoman Empire, 1600–1914' (2004) 11 Financial History Review 7; Dyson (n 189) 106.. Pamuk.

[227] Pamuk (n 226); K Kivanç Karaman and Şevket Pamuk, 'Ottoman State Finances in European Perspective, 1500–1914' (2010) 70 The Journal of Economic History 593.

Assignment of specific tax streams to a debt emission continued well into the 20th century. One can for example mention a 1919 Greek bond, secured by a tobacco tax[228] or the use of guano as a security by Peru during the 19th century[229].

These examples of early sovereign lending practice highlight two fundamental aspects of sovereign lending supporting this thesis. Creditor protection, in one form or another has historically been a key aspect of sovereigns' access to foreign credit. However, the effectivity of the mechanism protecting creditors has usually been limited. Even if medieval bankers obtained the rights to farm taxes, these rights were pointless once repudiated by the debtor. The same goes for tax revenues as a security for sovereign bonds as said rights were of little use against a sovereign deciding to repudiate them[230].

2.3.3 Sovereign Lending Between the 19th Century and the 1950s

The previous section underlined the fact that creditor protection, usually through extra-judicial means, has been a regular feature of sovereign lending throughout history. Similarly, sovereign debt in the 19th and early 20th century was propped up by a series of measures designed to maximise creditor's chances to see that the debts they had extended would be repaid.

Sovereign debt regulation in the early 19th and 20th century is the direct backdrop behind the modern creditor protection model. First, diplomatic protection, leading to lawsuits before arbitral tribunals and later the PCIJ, provides the first examples of modern international litigation on sovereign debt[231]. However, despite this limited recognition of creditor's rights, the competence of international jurisdictions remained uncertain. Debates upon whether creditors of sovereigns, or of entities controlled by sovereigns, possessed remedies for repayment in international law were a recurring occurrence[232]. Thus, while international

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228 Buchheit and Pam (n 14).

229 Catalina Vizcarra, 'Guano, Credible Commitments, and Sovereign Debt Repayment in Nineteenth-Century Peru' (2009) 69 The Journal of Economic History 358.

230 Buchheit and Pam (n 14).

231 See e.g. *French Company of Venezuelan Railroads Case (France v Venezuela)* (n 109); *Case Concerning the payment of various serbian loans issued in France (France v Serbia)* (n 195); *Case concerning the Payment in Gold of Brazilian Federal Loans Contracted in France (France v Brazil)* (n 34); *Canevaro Claim (Italy v. Peru), Award* (n 164).

232 See e.g. *Biens Britanniques au Maroc espagnol (Réclamation 53 de Melilla - Ziat, ben Kiran) (great Britain v Spain)* (1925) 2 UNRIAA 729. Discussed in Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2). Citing David Bederman, 'Creditors' Claims in international law' (2000) 34 international lawyer 235, 329.

litigation on sovereign debt was a possibility, its realisation was often mired with legal uncertainty.

Moreover, as enforcement usually required relying on diplomatic protection by the creditor's national state, enforcement before international tribunals was often denied for political reasons[233].

Creditors, beyond those uncertain judicial remedies could also rely on a series of extra-legal mechanisms to ensure that sovereign debts would be repaid.

The most infamous of these mechanisms, was gunboat diplomacy: the reliance by the creditor's State on military force against sovereign debtors to ensure that debts owed to its nationals would be repaid[234]. There are two caveats regarding the use of gunboat diplomacy as a mean to protect creditors. The first is that, in practice, the use of force to enforce contractual obligations was not a usual mean of settling disputes related to sovereign debt[235].

From a creditor protection standpoint, the second issue tied to gunboat diplomacy is that it relies on some form of espousal of the creditor's claims by their national State. This means that in practice the decision to enforce sovereign debt contracts was not purely a financial one, but also was heavily linked to politics[236]. For creditors this does little to reduce the political risk tied to lending to sovereigns and therefore renders gunboat diplomacy somewhat inefficient as a creditor protection device.

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[233] For a brief overview of the role of diplomatic protection see Waibel, 'Opening Pandora's Box' (n 81) 26. Often governments argued that creditors of sovereigns were aware of the risks tied to sovereign lending and were therefore unwilling to undertake the heavy political costs tied to enforcing contractual claims on behalf of their nationals. In those cases, creditor associations or committees often were left with coordinating the actions of bondholders seeking to obtain payment. On refusals to grant diplomatic protection see notably Weidenmier (n 175). On the arguments surrounding risks tied to sovereign lending see Charles Cheney Hyde, 'The Negotiation of External Loans with Foreign Governments' (1922) 16 The American Journal of international law 523, 523–524. On the role of creditor committees see Marc Flandreau, 'Sovereign States, Bondholders Committees, and the London Stock Exchange in the Nineteenth Century (1827–68): New Facts and Old Fictions' (2013) 29 Oxford Review of Economic Policy 668; Lee C Buchheit, 'Use of Creditor Committees in Sovereign Debt Workouts' (2009) 10 Business Law International 205.

[234] Mitchener and Weidnemier have provided empirical evidence of the short-term efficiency of gunboat diplomacy and other supersanctions to force repayment by sovereigns see Mitchener and Weidenmier (n 91); Weidenmier (n 175).

[235] Martha Finnemore, 'Sovereign Default and Military Intervention', *The Purpose of Intervention: Changing Beliefs about the Use of Force, M. Finnemore (eds.)* (Cornell University Press 2003) 27.

[236] Tomz notably underlined that recourse to gunboat diplomacy was often tied with broader geopolitical objectives and not merely with debt repayment. Tomz (n 112) 152; W Mark C Weidemaier, 'Contracting for State Intervention: The Origins of Sovereign Debt Arbitration' (2010) 73 Law and Contemporary Problems 335, 346.

Moreover, following the Drago-Porter convention, gunboat diplomacy, as an avenue for enforcing sovereign debt contracts, was legally closed[237].

Another central pillar of sovereign lending in the 19th and early 20th century is the reliance on the Gold Standard, mentioned *supra*. For creditors, the Gold Standard provided a check against the ability of States to devalue their currencies to repay their debts. In addition, the Standard acted as a signal for adherence to the traditional liberal values of the time[238]. Indeed, the Gold Standard appeared to be the ideal tool to promote 19th century "*laissez-faire*" principles as it created a common currency system with fixed exchange rate therefore fostering international trade[239].

As previously mentioned, this meant that States who had adopted the Gold Standard usually benefitted from better borrowing conditions than those who had not[240]. This led its adoption globally, starting with Western Europe, then the US, Canada and Australia, until most States chose to follow the trend[241]. Reliance on the Gold Standard would, however, falter with the participants in the first World War abandoning it to fund themselves through the conflict[242].

Following the first World War, all the European participants in the hostilities[243] would default or need a debt restructuring[244]. This was followed in the 1920s and 1930s by defaults from most of Eastern Europe and Latin American States due to the worldwide financial crisis[245]. At the international level, a limited response was heralded by the League of Nations, acting as a facilitator between a series of heavily indebted nations and international banks[246], but the League's intervention remained limited in scope and efficiency.

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[237] Drago Porter Convention (The Hague) 1907.On the Drago-Porter convention and sovereign defaults see Finnemore (n 235).
[238] Bordo (n 193).
[239] Eric Helleiner, 'Denationalizing Money? Economic Liberalism and the "National Question" in Currency Affairs', *International financial history in the twentieth century : system and anarchy* (Cambridge University Press 2003).
[240] Bordo (n 193).
[241] ibid; George Selgin, 'Law, Legislation, and the Gold Standard' (2015) 35 Cato Journal 251.
[242] Convertibility would return, though not for all currencies, after the war, however the dynamic of the inter-war system was materially different from the classical gold standard put in place before the war. See Barry J Eichengreen and Marc Flandreau (eds), *The Gold Standard in Theory and History* (2nd ed, Routledge 1997) 13–16.
[243] Except Finland.
[244] Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 27.
[245] Lindert and Morton (n 168); Barry J Eichengreen and Richard Portes, *Dealing with Debt: The 1930s and the 1980s* (World Bank Publications 1989).
[246] See Myers (n 203); Juan-Huitzi Flores and Yann Decorzant, 'Public Borrowing in Harsh Times : The League of Nations Loans Revisited' (Universidad Carlos III de Madrid Instituto Figuerola 2012) wp12-07 <https://ideas.repec.org/p/cte/whrepe/wp12-07.html> accessed 24 January 2020; Louis W Pauly, 'The League of Nations and the Foreshadowing of the International Monetary Fund' (Social Science Research Network

In general, the bond market of the 19th and early 20th can be characterised as a period of great economic disturbance and near total lack of efficient remedies for creditors, especially post Drago-Porter convention. This combination between a complete lack of reliable remedies by creditors and waves of defaults easily explains why after World War II private creditors were reticent to lend to risky sovereigns, leading them to turn to the Bretton Woods institutions for capital[247].

2.3.4 The 1970s and 1980s sovereign syndicated loan market

As previously mentioned, sovereign debt between the second World War and the 1970s, for developing States, mostly flew from the Bretton Woods institutions and from other States. Private lending only emerged in the 1970s as inflation reduced the IMF capacity to provide for loan arrangements[248] and as Western banks were blessed with fresh capital flows from the Middle East. Historically high oil prices after the 1973 crisis lead to increased deposits by petrol exporting countries into US and European Banks. This increase in liquidities was then recycled by the banks to fund South American States' sovereign debt[249]. This arrangement not only filled the hole left by the decrease in IMF lending, but also allowed developing countries to borrow without being constrained by IMF conditionality[250]. As a result, the debt of Latin American Nations rose massively, an increase that would soon prove unsustainable for the debtors[251].

The sovereign debt market of the 1970s features several peculiarities compared to previous instances of sovereign lending. First, the contractual instruments underlying petro-dollar recycling were syndicated loans[252]. Syndicated loans are loans extended by a group of banks -the syndicate- under the management of a lead or agent bank on a several liability basis[253].

1996) SSRN Scholarly Paper ID 2173443 <https://papers.ssrn.com/abstract=2173443> accessed 24 January 2020.

[247] On the lack of access of defaulting borrowers of 1930s to capital markets see Eichengreen and Portes (n 245) 31; Barry Eichengreen and Richard Portes, 'The Interwar Debt Crisis and Its Aftermath' (1990) 5 The World Bank Research Observer 69, 74.

[248] Aaron L Warren and Ryan E Avery, 'Investors of Prey: Seeking Relief in Distressed Debt Markets' (2010) 18 University of Miami International and Comparative Law Review 213.

[249] A Scheme dubbed the recycling of petrodollars Enrique R Carrasco, 'The 1980's: The Debt Crisis and the Lost Decade of Development E-Book on International Finance and Development: Part One: Pursuing the Good Life: The Meaning of Development as It Relates to the World Bank and the International Monetary Fund (IMF)' (1999) 9 Transnational Law & Contemporary Problems 119; Lienau, *Rethinking Sovereign Debt* (n 48) 158–159.

[250] Warren and Avery (n 248).

[251] Carrasco (n 249).

[252] Robert Devlin, *Debt and Crisis in Latin America: The Supply Side of the Story* (Princeton University Press 2014) 32, 97.

[253] Philip Wood, *Law and Practice of International Finance* (University ed, Sweet & Maxwell 2008) 164.

Syndication provides several advantages for the players involved[254]. The several nature of the loan enables banks to make vast sums of money available to their debtor without one bank shouldering all the default risk[255]. As the liability is several, each bank is individually responsible for making the funds available, while profits are shared pro-rata between the members of the syndicate[256]. Decision making, within the syndicate, is democratic with decisions taken on a majority or qualified majority basis[257]. As the contractual instrument underlying the debt is a loan, and not a security, the contract is not easily transferable, meaning that there was no large-scale secondary debt market[258].

Moreover, the 1970s are characterised by a progressive adoption of the relative doctrine of sovereign immunities, and the loan contracts of the time usually featured immunity waiver clauses[259]. The consequences of such a change will be examined the next chapter. For the purpose of this section, it suffices to underline that this change enabled creditors, for the first time, to enforce sovereign debt contracts before domestic courts.

As the syndicated market involved a limited number of recurrent players, and because of the rules of syndication[260], if a restructuring was needed, creditors usually managed to do so simply by negotiating[261]. Thus, litigation during the syndicated loan era was particularly rare[262].

This lack of litigation can be explained by examining the incentives against litigating for creditors. Large commercial banks, the bulk of the syndicated loan market, are repeat players within the sovereign debt market[263]. As such, they benefit from a return of the debtor to

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[254] For an overview of the syndicated sovereign loan market see: Philip Wood, 'Essay: Sovereign Syndicated Bank Credits in the 1970s' (2010) 73 Law and Contemporary Problems 7.
[255] ibid.
[256] Wood, *Law and Practice of International Finance* (n 253) 97; Wood, 'Essay' (n 254); Lee C Buchheit and Ralph Reisner, 'The Effect of the Sovereign Debt Restructuring Process on Inter-Creditor Relationships International Banking Symposium: Part II. Management of International Bank Exposure' (1988) 1988 University of Illinois Law Review 493.
[257] Wood, *Law and Practice of International Finance* (n 253) 97.
[258] Transferability, if contractually available can be made possible through assignment, novation or sub-participation. Wood, 'Essay' (n 254) 168.
[259] Weidemaier, 'Sovereign Immunity and Sovereign Debt' (n 82).
[260] Wood, *Law and Practice of International Finance* (n 253) 164–165.
[261] That is not to say that syndicated lending is a panacea when it comes to debt restructuring. For the coordination issues between members of a syndicate see: Buchheit and Reisner (n 256).
[262] Only one case seems to have been brought before US courts at the time *Allied Bank v Banco Credito Agricola de Cartago (Rehearing)* [1985] United States Court of Appeal for the Second Circuit 83–7714, 24 No 3 Int Leg Mater 762.
[263] Fisch and Gentile (n 40) 1059.

capital markets, as said return will provide them with the payment of new interests, as well as the obtention of fees during the lending process[264].

In addition, the rules of syndication prohibit the preferential treatment of creditors over other members of the syndicate and enforce a strict equality between members[265]. This, again, limited the incentives towards holding out as the entirety of the syndicate was bound to identical conditions during a restructuring[266].

Similarly, States in the syndicated loan market had an interest in not opportunistically defaulting. Since market access was guarded by a small number of banks, opportunistic defaults could be easily punished, and further market barred[267].

From a game-theoretical point of view, the relationship between States and their creditors at the time can be seen as an iterated version of the prisoner's dilemma. In the classic, one-round version of the prisoner's dilemma, players are incentivised to defect to maximise their profits as defection cannot be punished in subsequent rounds. In the iterated version, since defection can be punished, players are incentivised towards cooperation[268].

In the syndicated loan market, each individual loan is a round of the game between the banks and the sovereign. If the sovereign defaults opportunistically, the banks can punish it in the next round, either by preventing the sovereign from borrowing or by raising the interest rate. Similarly, if one bank defects by deciding to litigate against a sovereign acting in good faith, other banks can punish it by excluding it from future syndicates. In practice, this situation leads to path-dependency between the sovereign and its creditors. Cooperative creditors are rewarded by being able to play future rounds of the game, therefore they have no interest in litigating, unless they are facing a debtor acting in bad faith. A similar relationship is at play between the large banks involved in the negotiation of a restructuring deal themselves[269]. Larger creditors, in charge of assembling a syndicate[270] and negotiating the terms of a restructuring deal constantly deal with each other and therefore play a similar game[271]. This,

[264] Banks in charge of managing the syndication typically charged agency fees or management fees.
[265] Buchheit and Reisner (n 256).
[266] ibid; Wood, 'Essay' (n 254).
[267] Charles Lipson, 'Bankers' Dilemmas: Private Cooperation in Rescheduling Sovereign Debts' (1985) 38 World Politics 200.
[268] Axelrod (n 154); Christian Hilbe, Arne Traulsen and Karl Sigmund, 'Partners or Rivals? Strategies for the Iterated Prisoner's Dilemma' (2015) 92 Games and Economic Behavior 41.
[269] Lipson (n 267).
[270] ibid.
[271] ibid.

again, fosters cooperation between the main lenders, facilitating the restructuring process[272]. Finally, because of the democratic rules of the syndicate, in case of restructuring, decision-making is simplified as restructuring proposals only need to convince a qualified majority of lenders[273].

However, if the club-like nature of the syndicated loan market encourages cooperation in times of restructuring, it also creates the conditions for concentrating sovereign default risks to major players within the financial sector[274].

As previously underlined, there was no widespread secondary debt market during the syndicated loan era of sovereign debt. This meant that the entirety of the default risk of sovereigns sat in the balance sheets of the small number of banks involved in syndicated lending. Moreover, the recycling of petro-dollars at the basis of the syndicated loan market was resting on the perception that “countries don't go bust”[275]. As a result, banks started to lend Latin American countries sums well over their capital-adequacy requirements[276]. *A posteriori*, this appears to have been a recipe for disaster. A small number of major lenders were over-exposed to the credit risk of a limited number of debtors and were not holding the capital required to face an eventual default. The final nail in this coffin was that sovereign lending in the 70s and 80s was mostly extended to Latin American States, leading to fear of a large financial collapse when these countries started defaulting in the 1980s[277].

The crisis began on the 22nd of August 1982, with Mexico declaring that it could not face its external debt obligations[278]. During 1983 fifteen other South American debtors were facing the same situation[279], threatening to bring major US banks down with them[280].

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[272] ibid.

[273] Wood, *Law and Practice of International Finance* (n 253); Wood, ‘Essay’ (n 254); Buchheit and Reisner (n 256).

[274] Monteagudo (n 8). Lienau notes that this concentration is not purely financial, but also geographic, and notes, citing Cassis, that herd instinct might have played a role in this consolidation of major financial players around a sole type of investment. See Lienau, *Rethinking Sovereign Debt* (n 48) 160; Youssef Cassis, *Capitals of Capital: A History of International Financial Centres 1780–2005* (Jacqueline Collier tr, Cambridge University Press 2006) 237 <https://www.cambridge.org/core/books/capitals-of-capital/7B33E46801E22B68F90334F6E5989011> accessed 19 May 2020. See also Vinod K Aggarwal, *International Debt Threat: Bargaining among Creditors and Debtors in the 1980’s* (Institute of International Studies, University of California 1987).

[275] Alexis Rieffel, *Restructuring Sovereign Debt: The Case for Ad Hoc Machinery* (Brookings Institution Press 2003) 289.

[276] Warren and Avery (n 248).

[277] Monteagudo (n 8).

[278] James M II Hays, ‘Sovereign Debt Dilemma, The’ (2009) 75 Brooklyn Law Review 905.

[279] ibid.

[280] For an more in-depth overview of the crisis see Devlin (n 252).

A first step toward preventing this collapse was for the creditors to extend maturities on the loans and to agree to provide extended credit in collaboration with the IMF[281]. The idea was to avoid default while buying the banks more time to increase their capital reserves[282]. However, this delay proved insufficient, prompting the US government to intervene in the crisis with a plan from Treasury Secretary James Baker[283]. The plan involved the cooperation of private creditors and multilateral financial institutions[284]. The aim was to provide new loans, on a voluntary basis, to the most indebted States, amounting to $29 billion ($20 billion coming from the banks, and $9 billion from the IMF and the World Bank)[285]. In exchange, the debtors agreed to open up to foreign trade and investment and liberalize State enterprises[286].

Meanwhile, US banks were creating a secondary market allowing them to swap sovereign loans portfolios to hedge default risks[287]. Basically, a bank would consolidate several loans it held against a specific sovereign and swap them against a similar portfolio from a sovereign deemed more trustworthy[288]. This embryo of secondary market was at the time purely limited to US commercial banks[289]. However, with the crisis worsening, banks opened it to third parties interested in speculating over such portfolios, offered with significant discounts[290]. This also allowed debtor States to buy-back some of their own debt, therefore managing to reduce it, thanks to the low price of the securities on the secondary market[291].

A last step was built on the foundations of this emerging secondary market[292]: the Brady Plan, named after yet another US Treasury Secretary (Nicholas Brady). The new secondary market, in addition to paving the way for securitisation, had allowed banks to amass cash reserves large enough for them to withstand important debt write-offs[293]. The Brady plan relied on voluntary participation from lender banks to provide a third series of loans, as well as the reduction of the old debt. In exchange, the old loans would be securitized and sold to

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[281] Monteagudo (n 44), 59.
[282] ibid.
[283] ibid.
[284] ibid.
[285] ibid.
[286] Gathii (n 97), 256.
[287] Monteagudo (n 44), 59.
[288] Power (n 44), 2709-2714.
[289] ibid.
[290] ibid.
[291] ibid.
[292] Amounting to $273 billion dollars in 1993, compared to a mere $7 billion in 1987. ibid.
[293] Hays (n 278).

the public, backed by US securities[294]. Basically, several loans were tied together and repackaged as bonds, then sold at discount to the secondary market. The benefits of the bond sale were then used to off-set the losses incurred by banks[295].

As will be seen in the following section, bonded sovereign debt is structurally different from syndicated-loan debt. The main difference lies in the transferability of bonds. Bonds, as opposed to loans, are negotiable instruments, and involve a significantly higher number and diversity of creditors[296]. This spreading of the risk across multiple class of actors enabled the financial sector to maintain high levels of lending while spreading default risk away from major financial institutions. However, bonded sovereign debt brought with it another issue, managing restructuring processes across vast numbers of actors with sometimes widely differing motivations[297].

2.3.5 **The Modern Bond Market**

The current sovereign bond market is a direct heir of the Brady plan. The transferability of sovereign bonds, allowing for the creation of a secondary market, has opened up the sovereign debt market to a broader range of creditors, ranging from institutional investors to hedge funds and retail investors[298].

From a systemic risk perspective[299], this broadening of the creditor-base prevents the concentration of the default risk of sovereigns in one single sector of international finance. However, this heterogeneity of creditors shatters the club-like mentality that was reigning during the syndicated loan era, making restructurings more difficult[300].

From a contract law perspective, while syndicated loans feature *ad hoc* provisions enabling creditors to restructure a sovereign's debt via majority votes, historically, bonds did not benefit from such clauses[301]. The lack of mechanisms designed to facilitate restructuring

[294] Gathii (n 97), 256-259.
[295] ibid.
[296] Wood, *Law and Practice of International Finance* (n 253) 160.
[297] Ghosal and Miller (n 158); Harris Dellas and Dirk Niepelt, 'Sovereign Debt with Heterogeneous Creditors' (2016) 99 Journal of International Economics S16.
[298] Dellas and Niepelt (n 297); Ghosal and Miller (n 158); Krueger (n 76); Allegaert (n 77); Fisch and Gentile (n 73).
[299] On systemic risk see. Damiano Sandri, *Dealing with Systemic Sovereign Debt Crises: Fiscal Consolidation, Bail-Ins or Official Transfers?* (International Monetary Fund 2015).
[300] Ghosal and Miller (n 158); Dellas and Niepelt (n 297); Buchheit and Gulati, 'Sovereign Bonds and the Collective Will' (n 89).
[301] At today's date, bonds feature collective action clauses designed to bring majoritarian restructuring to the bond market. These clauses are analysed *infra*.

created a complex game of cooperation between States and their creditors when restructurings were needed[302].

By default, sovereign bonds being contracts, they cannot be modified unilaterally by either party. Restructuring of bonded debt therefore requires changes to be made to each separate bond, with both the debtor and bondholders agreeing to said changes. In practice, the consent of all parties is collected via a bond exchange. During a restructuring, the bonds issued by the sovereign, and that the sovereign wants to be restructured, are offered for a swap against other bonds designed to facilitate repayment[303].

Each individual bondholder during such a process can decide whether to participate in the restructuring, and if they hold out, the original bonds they hold remain completely untouched by the process and are thus enforceable. This means that, in the bond market, for restructurings to be successful, States need to provide an offer that will garner the approval of a critical mass of creditors[304].

Against that background, the heterogeneity of creditors and their investing strategies became from the 1990s onwards, a source of collective action issues. Indeed, some bondholders have no economic incentives towards a quick return of the State to capital markets[305]. To come back to the prisoner's dilemma analogy, while large banks or institutional creditors are playing a repeated version of the game, some bondholders are playing a single round version. Therefore, they are incentivised towards refusing restructuring proposals from the sovereign, and use any available remedy in order to obtain payment knowing that they cannot be punished in subsequent rounds.

Two main categories of bondholders fit this description: retail investors and vulture funds. Retail investors generally invest in sovereign bonds for savings purposes. Their positions

[302] Ghosal and Miller (n 158); Dellas and Niepelt (n 297); Buchheit and Gulati, 'Sovereign Bonds and the Collective Will' (n 89); Anna Gelpern, 'How Collective Action Is Changing Sovereign Debt Cover Story' (2003) 22 International Financial Law Review 19.
[303] Das, Papaioannou and Trebesch (n 4) 7; Steven L Schwarcz, 'Idiot's Guide to Sovereign Debt Restructuring Conference on Sovereign Debt Restructuring: The View from the Legal Academy' (2004) 53 Emory Law Journal 1189, 1193. Alternatively, debt restructurings can involve debt buy-backs, via which a sovereign repurchases its own bonds, thus cancelling the debt.
[304] Dellas and Niepelt (n 297); Ghosal and Miller (n 158); Gelpern, 'How Collective Action Is Changing Sovereign Debt Cover Story' (n 302).
[305] Buchheit and Gulati, 'Sovereign Bonds and the Collective Will' (n 89); Gelpern, 'How Collective Action Is Changing Sovereign Debt Cover Story' (n 89); Kaplan (n 89); Krueger (n 76); Lee Buchheit and Elena Daly, 'Minimizing Holdout Creditors: Carrots', *Sovereign debt management. R. Lastra, L. Buchheit (eds.)* (Oxford University Press) 4–5.

are usually less diversified than their institutional counterparts'[306], meaning that they are more exposed to the default risk of specific sovereigns. Individuals do not benefit from a return of the debtor to the capital market. The debtor is not one of their clients, future interest payment will not flow in their directions and they are not in a position where future bond issuance will yield to the payment of fees. Thus, it is hardly surprising to notice that litigation of sovereign debt restructurings by retail investors is a growing phenomenon[307].

Vulture funds, on the other hand, have developed their trading strategies based on the legal remedies available to them under the creditor protection model. These funds rely on a risky, but potentially highly rewarding investment strategy: buying debt instruments from distressed sovereigns at a steep discount and either pressuring the creditor's government or suing in order to be paid on the full value of the debt[308].

Economically, this strategy can be read as a form of arbitrage. Arbitrage is usually defined as "*the simultaneous purchase and sale of the same, or essentially similar, security in two different markets for advantageously different prices*"[309]. Sovereign bonds, effectively trade at two different prices: their market price, at which they are bought and sold on the secondary market, and their judicial price, the value that can obtained before courts and tribunals[310]. Effectively, vulture funds purchase their bonds at a discounted market price and realise them at their judicial price.

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306 William N Goetzmann and Alok Kumar, 'Diversification Decisions of Individual Investors and Asset Prices' 64; Brad M Barber and Terrance Odean, 'Chapter 22 - The Behavior of Individual Investors' in George M Constantinides, Milton Harris and Rene M Stulz (eds), *Handbook of the Economics of Finance*, vol 2 (Elsevier 2013) <http://www.sciencedirect.com/science/article/pii/B9780444594068000226> accessed 1 March 2019. The data mentioned in both studies focuses on stock holding by retail investors. It seems however fitting to extrapolate from these conclusions and apply them to the bond market as it seems unlikely that retail investors failing to diversify on stocks would diversify on bonds. Indeed, on average sovereign bonds are less volatile, and traditionally perceived as less risky than corporate equity.

307 See e.g. *Abaclat and Others v. Argentine Republic* (n 17); *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17); *Mamatas et autres v. Greece* (n 18); *Alessandro Accorinti and others v. European Central Bank* (n 19); *Stefan Fahnenbrock et al C Hellenische Republic* [2015] Cour de Justice de l'Union Europeene C 226/13, C 245/13, C 247/13 et C 578/13.

308 Fisch and Gentile (n 73).

309 William F Sharpe, *Investments, William F. Sharpe, Gordon J. Alexander, Fourth Edition: Instructor's Manual* (Prentice Hall 1990); Andrei Shleifer and Robert W Vishny, 'The Limits of Arbitrage' (1997) 52 The Journal of Finance 35.

310 The legal value of the bonds differs from their facial value. The facial value of the bonds is simply the amount that the debtor has agreed to repay. The legal value of the bonds is the amount that a creditor could obtain though judicial means, and therefore could include an out of court settlement under the facial value, but also potentially the payment of late interests, punitive damages etc. On the idea that bonds trade at two values see *CIBC bank and Trust Company (Cayman) v Banco Central do Brasil, Banco Central do Brasil SA, and Citibank NA* United States District Court Southern District New-York 94 Civ. 4733 (LAP), 886 Database Fed Suppl 1105, cited by Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 304.

Under usual circumstances, arbitrage opportunities tend to be closed by market actors[311]. If a share of Apple Inc. is trading at $100 on the New-York Stock Exchange and $101 on the Chicago Stock Exchange, investors will flock to the NYSE, raising the demand on shares of Apple and sell in Chicago, bringing prices in line in both exchanges. However, the judicial value of the bonds rests entirely on the efficiency of the remedies designed to protect creditors. Hence, other market actors cannot by themselves, close the window for arbitrage.

The first major case involving such manoeuvres involved the Dart family and Brazil[312]. The Darts purchased Brazilian debt on the secondary market between 1991 and 1993, at a discount between 75% and 60%[313], and stored it in a Cayman based bank, specially created for that purpose: CIBC[314]. In 1993, Brazil negotiated a restructuring with major US banks leading to a swap between its outstanding loans and new bonds with a reduced face value[315], in the context of a Brady deal[316]. All creditors agreed to the restructuring, except the Dart who in the meantime had amassed Brazilian debt for a total face-value of $1.4 billion, making them Brazil's largest creditor[317]. The original debt instruments, however, required a majority of creditors to agree in order to trigger an acceleration clause[318]. Thus, aware of the Darts attempts and fearing a lawsuit, Brazil instructed Banco da Brazil to repurchase debt to ensure that the Dart would not own securities over the 49% threshold[319].

This lead CIBS to sue Brazil, Banco Central and Citibank (acting as an agent bank in the original instruments) in order to seek payment acceleration[320]. The Court denied summary judgments, and the parties later settled out of court with Brazil granting the Darts $25 millions in cash and $52.3 million in bonds[321].

More recently, NML and Elliott relied on the *pari passu*[322] clause against Argentina and Peru in order to attempt to coerce both sovereigns into settling out of court[323]. These judicial

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311 Shleifer and Vishny (n 309).
312 See Allegaert (n 44), 447.
313 ibid 447-448.
314 ibid; Power (n 44), 2747.
315 Power (n 44) 2747; Allegaert (n 44) 447.
316 Power (n 44) 2748.
317 ibid.
318 ibid.
319 ibid; Allegaert (n 44), 447.
320 *CIBC bank and Trust Company (Cayman) v. Banco Central do Brasil, Banco Central do Brasil S.A., and Citibank N.A.* (n 310).
321 Power (n 77); Allegaert (n 77).
322 The *pari passu* clause will be studied in more details in the next part of this thesis.
323 *NML Capital, LTD., et al. v The Republic of Argentina* (n 28); *Elliott Associates LP v Banco de la Nacion* [1999] United States Court of Appeal for the Second Circuit 98–9268, 98–9319, 194 Fed Report 3rd Ed 363; *Elliott Assocs, LP* [2000] Cour d'Appel de Bruxelles (8eme ch) 2000/QR/92.

means are particularly disruptive to the restructuring process. Reliance on the *pari passu* clause, notably, can disrupt entire restructuring processes[324]. Similarly, retail investor's use of investment arbitration threatens to disrupt restructuring processes by enabling creditors to challenge regulatory measures designed to facilitate restructurings[325].

The effect of these delays and inefficiencies are not purely financial. Restructuring processes have dire effects on the debtor's population[326]. Lengthening them unnecessarily prolong these sufferings. Because these inefficiencies were rooted in the efficient remedies granted to creditors under the creditor protection model, a change of model, a different way to regulate the sovereign debt market was necessary, leading to the advent of the anti-holdout model.

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[324] Kaplan (n 89); Gelpern, 'How Collective Action Is Changing Sovereign Debt Cover Story' (n 89); Fisch and Gentile (n 73); Christopher Wheeler and Amir Attaran, 'Declawing the Vulture Funds: Rehabilitation of a Comity Defense in Sovereign Debt Litigation' (Social Science Research Network 2003) SSRN Scholarly Paper ID 1575301 <http://papers.ssrn.com/abstract=1575301> accessed 6 November 2015; Krueger (n 76).

[325] Waibel, 'Opening Pandora's Box' (n 81); Julien Cazala, '- « Crise de La Dette Souveraine Grecque et Arbitrage En Matière d'investissement », Cahiers de l'arbitrage - Paris Journal of International Arbitration, 2015, N° 4, Pp. 722-729.' <https://www.academia.edu/32784883/_Crise_de_la_dette_souveraine_grecque_et_arbitrage_en_mati%C3%A8re_d_investissement_Cahiers_de_l_arbitrage_-_Paris_Journal_of_International_Arbitration_2015_n_4_pp._722-729> accessed 6 March 2019.

[326] Lumina, 'Report of the Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, Particularly Economic, Social and Cultural Rights (Mission to Argentina)' (n 6); Lumina, 'Report of the Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, Particularly Economic, Social and Cultural Rights (Mission to Greece)' (n 6).

3 The Creditor Protection Model

3.1 Introduction

In the previous chapter, this thesis has shown that sovereign debt can be understood as functioning via a mixture between a reputational model of cooperation between sovereigns and their creditors, and the provision, at the margins of credible commitment devices by borrowers.

A brief historical analysis of sovereign debt thus, logically reveals that some measure of creditor protection has, since the 4th century B.C., been the norm within the sovereign debt market. However, historically, these measures have insufficiently guaranteed creditor protection as they usually relied on a form of espousal by the creditor's national State.

This equilibrium began to change from the 1970s onwards. When developing sovereigns returned to capital markets, thanks to petro-dollar recycling, they did so in a completely different legal environment, as private creditors could sue sovereigns before domestic courts and, from the 1990s onwards, international courts. Litigation, however remained rare under the club-like structure provided by syndicated banking, and began when, following the Brady Plan, sovereign indebtedness became bonded, thus leading to creditor heterogeneity.

The norms applied to sovereign debt at the time, as will be shown in this chapter, can be understood as seeking to incentivise private creditors towards lending by providing them with efficient remedies against sovereigns. This thesis has dubbed this paradigmatic regulatory model the 'creditor protection model'. Its analysis is divided in three sections. The first section provides a general theory of the creditor protection model by highlighting, the necessary elements for the model to function. It illustrates them with a series of domestic law examples showing how these components have worked in practice. These examples have mostly been drawn from the practice of US courts since most sovereign debt transactions flow through New-York[327], but also because said practice has been the most controversial in recent years[328]. This brief survey of domestic court's and market actor's practice is not

[327] Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 4; Kupelyants (n 53) 6; Das, Papaioannou and Trebesch (n 4) 151–153; Michael Bradley and G Mitu Gulati, 'Collective Action Clauses for the Eurozone: An Empirical Analysis' (Social Science Research Network 2013) SSRN Scholarly Paper ID 1948534 <https://papers.ssrn.com/abstract=1948534> accessed 24 January 2020. Reference to the practice of other domestic courts and tribunals will however be made when relevant.
[328] See e.g. Gathii (n 161); Miller and Thomas, 'Sovereign Debt Restructuring' (n 73).

intended to be exhaustive but merely to highlight the fact that the creditor protection model is not purely an international law phenomenon, but has also been implemented at the domestic level[329].

The second objective of this chapter, treated in section 2, is to analyse how the creditor protection model has been implemented in International law. Section 2 *inter allia* focuses on the characterisation of sovereign bonds as investments for the purpose of the ICSID convention, on the characterisation of sovereign debt as an *acta de iure imperii,* and on the law of necessity as it applies to sovereign debt.

Finally, the last section of this chapter analyses the strengths and weaknesses of the creditor protection model. Its main takeaway is that creditor protection can provide an efficient way to incentivise creditors to lend to States, if economic incentives encourage creditors to cooperate when restructurings are necessary. Thus, in an environment, such as the post-Brady plan bond market when said incentives are lacking, the creditor protection model leads to collective action issues[330] as it provides holdouts with the means of disrupting debt restructurings, and incentivises them to do so.

3.2 A General Theory of the Creditor Protection Model

The purpose of the creditor protection model is to offer creditors efficient legal remedies to coerce the sovereign debtor towards fulfilling the obligations flowing from the sovereign debt relationship. It can therefore be understood as a judicial way of creating credible commitment for the sovereign debtor, as the efficient legal remedies granted to ensure that the debtor cannot renege upon its debt without facing legal consequences[331]. This reduces the legal and political risks tied to lending to sovereigns as it disincentivises them against repudiation[332].

[329] For a more exhaustive survey of domestic court's practice regarding sovereign debt see: Megliani, *Sovereign Debt* (n 50); Kupelyants (n 53).
[330] On collective action issues see Gelpern, 'How Collective Action Is Changing Sovereign Debt Cover Story' (n 89); Buchheit and Gulati, 'Sovereign Bonds and the Collective Will' (n 89); Dellas and Niepelt (n 297); Ghosal and Miller (n 158).
[331] On credible commitment theory see North (n 124); Vizcarra (n 229); Yang (n 191).
[332] On the role of contractual remedies in reducing the legal and political risks tied to sovereign lending see: Choi, Gulati and Posner (n 114); Eichengreen, Haussman and Panizza (n 114).

Thus, courts within the creditor protection model play the same role as Parliament did after the Glorious Revolution[333], or as the Gold Standard played prior to World War I[334], they effectively constrain States' options when it comes to debt. By doing so, in theory, the creditor protection model not only benefits creditors, whose position in the sovereign debt relationship is protected, but also the sovereign itself who benefits from lower interest rates and improved access to capital markets[335].

To effectively incentivise States towards repayment, the creditor protection model needs to fulfil three distinct conditions. First, creditors need to have access to courts, independent from the sovereign. Second, the obligations arising from the sovereign debt relationship need to be given effect. Finally, courts need to grant creditors remedies that will effectively coerce the debtor into repayment.

The combination of these three conditions creates a system in which creditors themselves can judicially enforce the obligations arising from the sovereign debt relationship, be ensured that their rights are neither waved away by courts or altered by the debtor, and that the remedies they obtain will coerce the debtor towards repayment, thus avoiding efficient breaches.

Before individually analysing each of these conditions, it should be noted that the purpose of this section and the next is to expose the internal logic of the creditor protection model, namely that judicial creditor protection incentivises lending and is therefore economically efficient. This internal logic, while intellectually sound[336] effectively leads to inefficiencies within the sovereign debt market, as will be analysed in section 3. However, if one wants to understand how these inefficiencies arose, one first needs to understand how, in theory, the creditor protection model can work.

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[333] North and Weingast (n 124); North (n 124); Beckett (n 188).
[334] Bordo (n 193).
[335] North and Weingast (n 124); North (n 124); Oosterlinck, Ureche-Rangau and Vaslin (n 192).
[336] The idea that efficient legal remedies are incentives to enter transaction is well rooted in the law and economics tradition. Posner notably advances the idea of 'efficient breach', stating that parties to a contract are incentivised towards compliance, unless the benefits from breach outweigh the costs engendered by the remedies granted to the other contracting party. See Richard A Posner, *Economic Analysis of Law* (2d ed, Little, Brown 1977) 56, cited in Klass (n 146) 363. See also John N Adams and Roger Brownsword, 'The Ideologies of Contract' (1987) 7 Legal Studies 205, 206–213; Ewan McKendrick, *Contract Law: Text, Cases, and Materials* (Eighth edition, Oxford University Press 2018) 9: highlighting the importance of 'sanctity of contract' type doctrines. For an application to sovereign debt see Choi, Gulati and Posner (n 114); Gathii (n 161).

3.2.1 Creditor Access to Courts Independent from the Sovereign

3.2.1.1 Creditor Access to Courts: Overview

Logically, the first step in ensuring that creditors benefit from efficient legal remedies against the sovereign debtor is to provide them with access to independent, competent *for a* for litigating sovereign debt.

Historically, the existence of such jurisdictions has been lacking. Domestically, access to courts against a foreign sovereign has been inexistent as States were shielded by their immunity of jurisdiction[337]. Internationally such access was conditional on the national state of the creditor agreeing to espouse its national's contractual claim. Since diplomatic protection adds a layer of political uncertainty to enforcement, and since litigating sovereign debt before the domestic courts of the debtor is tainted by fear of interference by debtor, access by creditors *themselves* to *independent* courts and tribunals is required under the creditor protection model.

Finally, access to courts is necessary for enabling creditors to obtain the legal remedies designed to coerce the sovereign were it to attempt not to fulfil its obligations. These remedies, as will be seen *infra* need to be judicial as it guarantees that the creditors themselves can wield them against a reluctant sovereign, further depoliticising enforcement[338]. The combination of these factors guarantees that the sovereign debtor can credibly commit to the obligations arising from the sovereign debt relationship.

In domestic law, two main examples of legal mechanism designed to ensure the competence of independent courts will be analysed in this section. First, the presence of forum selection clauses in sovereign debt contracts, second the creditor-friendly interpretation of the Act of State Doctrine, the comity defence and the champerty defence, by US courts.

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[337] On sovereign immunities and sovereign debt see: Weidemaier, 'Sovereign Immunity and Sovereign Debt' (n 82); Delaume (n 82).

[338] This difference renders judicial remedies more efficient than the more 'political' remedies which have been historically *en vogue* such as gunboat diplomacy, diplomatic settlement or the 'quasi-receivership' of debtor States. On these questions see Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 22–58. See also Weidenmier (n 175); Weidemaier, 'Contracting for State Intervention' (n 236); Ahmed, Alfaro and Maurer (n 95).

3.2.1.2 Creditor Access to Domestic Courts: Forum Selection Clauses

The sovereign bonds of developing States typically feature forum selection clauses. The elected jurisdiction is usually, either the second district of New-York, or London courts[339], as both jurisdictions are usually recognised for their expertise in financial matters[340].

Forum selection clauses pursue numerous separate objectives in transnational contract law. They foster certainty as they enable contracting parties to know *ex ante* which jurisdiction will be competent over disputes, they enable parties to choose the jurisdiction they see fit, either in terms of expertise or of closeness to the contract's place of performance, etc[341]. In addition to these functions, forum selection clauses, in sovereign debt contracts, also allow creditors to ensure that sovereigns cannot either legislate in order to prevent disputes from being brought on the basis of sovereign debt contracts[342], or that any other undue influence by the sovereign on the outcome of a dispute linked to the geographic location of the elected *for* is impossible.

Forum selection clauses lower the political risks tied to lending to a sovereign, as the latter cannot interfere in the dispute settlement process, and therefore incentivises lending[343]. However, the mere election of an independent domestic court is not sufficient to guarantee that creditors will, in practice, have access to said court. In order to guarantee that litigation actually occurs, further procedural obstacles for litigation against sovereigns need to be lifted[344].

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[339] Megliani, *Sovereign Debt* (n 50) 233; Das, Papaioannou and Trebesch (n 4); Kupelyants (n 53) 6.
[340] On choice-of-law clauses in sovereign bonds see in general: Das, Papaioannou and Trebesch (n 4); George Weisz, Nancy Schwarzkopf and Mimi Panitch, 'Selected Issues in Sovereign Debt Litigation' (1991) 12 University of Pennsylvania Journal of International Business 1; Horatia Muir Watt, 'L'immunité Souveraine et Les Fonds "Vautours"' [2012] Revue Critique de Droit International Prive 789.
[341] David H Taylor, 'The Forum Selection Clause: A Tale of Two Concepts' (1993) 66 Temple Law Review 785.
[342] For example by enacting legislation preventing their own domestic courts from litigating on their own bonds.
[343] Choi, Gulati and Posner (n 114).
[344] A potential obstacle to the effectivity of *forum selection* clauses could have been the *forum non conveniens* doctrine. However, on average, both US and English courts tend to respect contractual parties' decisions to elect them for dispute resolution. See *The Bremen v Zapata Off-Shore Co* [1972] US Supreme Court 407 U.S. 1 (1972); Taylor (n 341)., for US practice. For the UK see *Spiliada Maritime v Cansulex* [1987] AC 460 (House of Lords); Kupelyants (n 53) 73–75.

3.4.2.3 Creditor Access to Domestic Courts: the Act of State Doctrine, Comity and Champerty

In addition to sovereigns' immunity from jurisdiction, analysed in section 2, a series of potential procedural obstacles to a creditor's ability to enforce sovereign debt contracts before domestic common law courts can be mentioned: the Act of State doctrine, the comity defence and the champerty defence.

The common ground between these three norms is that they all prevent domestic courts from litigating a dispute over which they would normally be competent. In the case of the Act of State doctrine and the comity defence, incompetence stems from the sovereign nature of the debtor. For champerty it is the potentially speculative nature of litigation which can provide an obstacle against the enforcement of the contractual rights of creditors.

The Act of State doctrine prevents a US court, competent over a case, from hearing it if the case concerns the validity of the act of a sovereign on its own territory[345]. The act of State doctrine has mostly been developed by US and UK courts, and is usually absent from civil law regimes[346]. As early as the 1980s, it was recognised in the *Allied Bank*[347] case that the territorial limitation of the doctrine prevented it from applying in sovereign debt cases, as long as payment, was due in the US[348]. With most sovereign bonds subjected to New-York and specifying payment within the US[349], it appears that the potential of the Act of State doctrine's to limit litigation against defaulting sovereigns is quasi nil[350].

A second potential procedural obstacle to litigations against sovereigns by their creditors before US and UK courts is the comity defence. Comity is a conflict of law norm[351] allowing

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[345] M Erin Kelly, 'The Act of State Doctrine and Allied Bank Note' (1986) 31 Villanova Law Review 291; Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 28; *Underhill v Hernandez* (1897) 168 US 250 (US Supreme Court). See also in English law: *Blad v Blamfield* (1674) 36 ER 992 (English Court of Chancery).

[346] Fausto de Quadros and John Henry Dingfelder Stone, 'The Act of State Doctrine', *Max Planck Encyclopedia of Public international law* (OUP 2013).

[347] *Allied Bank v. Banco Credito Agricola de Cartago (Rehearing)* (n 262). See also *Libra Bank v Banco Nacional de Costa Rica* [1981] New-York Southern District Court 81 civ 7624 (CBM). On the convoluted process leading to the adoption of the Allied Bank decision see Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 35–38.

[348] *Allied Bank v. Banco Credito Agricola de Cartago (Rehearing)* (n 262); Kelly (n 345); Kupelyants (n 53) 182–183; Marc Lewyn, 'Foreign Debt - Act of State Doctrine - Unilateral Deferral of Obligations by Debtor Nations Is Inconsistent with United States Law and Policy: Allied Bank International v. Banco Credito Agricola de Cartago' (2015) 15 Georgia Journal of International & Comparative Law 657.

[349] Das, Papaioannou and Trebesch (n 4); Megliani, *Sovereign Debt* (n 50) 233; Kupelyants (n 53) 6.

[350] For a recent English interpretation of the Act of State doctrine see *Belhaj and another (Respondents) v Straw and others* (2017) 3 UKSC (UK Supreme Court). Cited in Kupelyants (n 53) 182.

[351] Donald Earl III Childress, 'Comity as Conflict: Resituating International Comity as Conflict of Laws' (2010) 44 U.C. Davis Law Review 11. On comity see Adrian Briggs, *The Principle of Comity in Private international*

for the recognition of acts linked to a foreign State's sovereignty by a domestic court who would otherwise have jurisdiction over them[352]. Fundamentally, comity relies on a balance of interests between the State of the elected forum for dispute settlement and a foreign State[353].

The applicability of the comity defence to sovereign debt restructuring in the US was settled in the *Pravin Banker*[354] case. Pravin had acquired, from another bank, an assignment on $9 millions of Peruvian debt. In 1992, the *Banco Popular del Peru*, stopped making interest payments on said debt, thus triggering an event of default[355].

The bank was originally owned by the Peruvian State but was privatized in 1992, following an agreement between Peru and the IMF[356]. The court concluded that granting Peru an indefinite stay in the proceedings, on the basis of comity, would transform the United-States government policy of 'voluntary restructuring'[357] into a "*judicially-enforced bankruptcy proceedings*"[358]. This justified, in the eyes of the court, refusing to apply the defence to Peru. Here again, the attachment of American jurisdictions to the enforceability of sovereign debt contracts, as well as its link to the efficiency of the sovereign debt market, is made clear[359].

A final defence raised by sovereign debtors against the competence of domestic courts has been the champerty defence. The champerty doctrine prohibits the acquisition of a debt-title with the sole purpose of suing the debtor[360].

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law (Martinus Nijhoff 2012) <http://referenceworks.brillonline.com/entries/the-hague-academy-collected-courses/*ej.9789004227286.065_182> accessed 27 January 2020; Thomas Schultz and Jason Mitchenson, 'Rediscovering the Principle of Comity in English Private international law' (2018) 26 European Review of Private Law 311; Jörn Axel Kämmerer, 'Comity', *Max Planck Encyclopedia of Public international law* (Oxford University Press 2006).

352 Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 31; Kämmerer (n 351); *Hilton v Guyot* (1895) 159 U S Rep 113 (United States Supreme Court). Regarding English court's appraisal of comity see Kupelyants (n 53) 35. On average, English courts have been reluctant to renounce to their competence on the basis of the comity defence. See e.g. *Goldman Sachs International v Novo Banco* [2015] EWHC 2371 (Appeals Court).

353 *Hilton v. Guyot* (n 352); Childress (n 351).

354 *Pravin Banker Ltd v Banco Popular del Peru* [1997] United States Court of Appeal for the Second Circuit 96–7183. See also Kupelyants (n 53) 103. For a commentary on *Pravin Banker* see Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 80.

355 *Pravin Banker Ltd. v. Banco Popular del Peru* (n 354); Wheeler and Attaran (n 324).

356 Wheeler and Attaran (n 324).

357 This policy had been expressly mentioned in the Allied Bank II, *amicus curiae* opinion, submitted by the US government. See *Allied Bank v. Banco Credito Agricola de Cartago (Rehearing)* (n 262); Lewyn (n 348).

358 *Pravin Banker Ltd. v. Banco Popular del Peru* (n 354); Wheeler and Attaran (n 324).

359 Gathii (n 161).

360 Champerty is codified for New York in: Purchase of claims by corporations or collection agencies (New-York Judiciary Law); Ronald L Cohen and Robert M Schwartz, 'Champerty and Claims Trading' (2003) 11 American Bankruptcy Institute Law Review 197; Hays (n 278).

Champerty came into play during vulture fund litigation, with Peru raising it against *Elliott*[361]. The case opposed the hedge fund to Peru's national bank following Peru's restructuring. *Elliott*, had purchased heavily discounted Peruvian bonds and was attempting to obtain payment on their full value before US courts[362]. *Banco de la Nacion* sought to dismiss the case by relying on champerty[363], arguing that the fund's investing strategy was chmapertuous. It was decided by the Court of Appeal that *Elliott*'s purchase of Peruvian bonds could not be characterised as such since the intent of the fund was not solely to bring suit but rather to be paid in full[364]. Elliott tied, in its argument, the unavailability of the champerty defence and the functioning of the secondary debt market[365]. In *Elliott*'s opinion, a broad reading of the champerty provision in the New-York judiciary law, would make the operation of the secondary bond market impossible since it would create uncertainty regarding the enforceability of the bonds of most creditors[366]. To quote the funds' lawyers, the champerty defence "*makes Wall Street tremble*"[367].

The policy implication of a narrow interpretation of the champerty defence are laid out clearly. Ensuring the enforceability of sovereign debt contracts, even the heavily discounted bonds of a distressed sovereign, is deemed necessary for the efficient functioning of the sovereign debt market.

3.2.2 The Sanctity of Creditors' Rights[368]

3.2.2.1 The Sanctity of Creditors' Rights: Overview

In addition to declare themselves competent, courts and tribunals, under the creditor protection model, need to give effect to the obligations of the debtor regarding the sovereign debt relationship. This ensures that the rights of creditors will, in practice, be judicially

[361] Cohen and Schwartz (n 360); Hays (n 278). See *Infra*.
[362] *Elliott Assocs., L.P. v. Banco de la Nacion* (n 28).
[363] ibid.
[364] *Elliott Associates L.P. v. Banco de la Nacion* (n 263); see commentary in Cohen and Schwartz (n 302). A similar approach has been followed by English courts in *Camdex International Ltd v Bank of Zambia (No 2)* (1996) 1997 Wkly Law Rep 632 (Court of Appeal); Hagan (n 76); Charles Proctor, 'Vulture Funds and Sovereign Debt - The Zambian Experience' (2007) 2007 Journal of South African Law 629. English courts seem to have similarly opted for a narrow reading of the champerty defence, limiting its uses for sovereign debt cases. See Kupelyants (n 53) 193.
[365] *Elliott Associates L.P. v. Banco de la Nacion* (n 323).
[366] ibid.
[367] ibid.
[368] The term was originally coined by Gathii, as mentioned *supra*, Gathii (n 161).

protected. This second component of the creditor protection model requires the combination of three distinct elements.

1. There needs to be a legal obligation tied to the repayment of the sovereign's debt.
2. This obligation needs to lead to a recognition of the State's responsibility.
3. This obligation cannot be emptied of its substance by the State's conduct or its regulatory activity.

The first element, in practice, is the least problematic, as it is self-evident that creditors need to have actual rights against the debtor to obtain efficient remedies coercing the sovereign to repay. In domestic law, said rights, broadly speaking are the contractual rights enshrined in the debt instrument emitted by the sovereign[369].

The second element can be more problematic. Indeed, the mere finding of a breach by a court is not sufficient to lead to the obtention of remedies by creditors. This finding needs to be accompanied by an absence of valid legal defence by the debtor. The debates surrounding the necessity defence as it applies to economic circumstances illustrate these difficulties.

The last element requires courts to prevent the State from emptying its obligations of their substance. States may do so in two main ways, either by legislating to alter the conditions of repayment, or by behaving in such a way that the obligations flowing from the sovereign debt relationship become meaningless.

Two main development have occurred, in domestic law, to guarantee the sanctity of creditor's rights. First, contractual mechanisms protect sovereign debt contracts against regulatory intervention. Second, the rateable payment interpretation of the *pari passu* clause prevents States from behaving in such a way as to create *de facto* senior categories of debt.

3.2.2.2 Contractual guarantees against a debtor's regulatory intervention

Historically, the sovereign nature of the debtor has enabled it to unilaterally alter the conditions under which the debt had been subscribed[370]. Historically, currency devaluations

[369] Kupelyants underlines that in English and US law "It is a fundamental principle that the creditor may thus recover its contractual entitlement in full" Kupelyants (n 53) 171.
The rights held by creditors in international will be analysed *infra* in the next section.

[370] On the political risks tied to unilateral modifications of the sovereign debt contract see Choi, Gulati and Posner (n 114); Barry Eichengreen and Ricardo Hausmann, 'Exchange Rates and Financial Fragility' (National Bureau of Economic Research 1999) Working Paper 7418 <http://www.nber.org/papers/w7418>; Eichengreen, Haussman and Panizza (n 114).

have been one of the main ways through which sovereign have altered, without consent from heir creditors, the conditions of their loans in order to facilitate repayment[371].

Unilateral attempts by sovereign to regulate over their debt are not however a purely historical phenomenon. Argentina, during its restructuring, famously enacted laws via which it attempted to prevent itself from repaying holdout creditors[372]. More recently, following its sovereign debt crisis, Greece unilaterally altered its domestic bonds in order to retroactively fit them with a Collective Action Clause[373].

In order to limit the legal and political risks tied to lending to sovereigns, the creditor protection model needs to remove the obligations arising from the debt relationship from the regulatory sphere of influence of the debtor[374]. Several domestic law examples of mechanisms designed to prevent States from regulating themselves out of their indebtedness can be mentioned.

As far as choice-of-law is concerned, most bonds elect either New-York or English law[375]. For issuing States and their creditors, the election of these two legal orders makes sense as it prevents debtors from being able to legislate to modify the conditions of the contract[376].

Regarding payment, sovereign bonds are usually payable in dollars, and not the issuer's currency. Similarly, payment is cleared by a third party, either a clearing house for bonds issued in Europe (*i.e.* Euroclear or Clearstream) or an American investment bank acting as trustee[377].

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[371] See Bullock (n 213); Eichengreen and Hausmann (n 370); Flandreau and Sussman (n 114).
[372] Decreto 1735/2007 Establécense los alcances, términos y condiciones del proceso de reestructuración de la deuda del Estado Nacional instrumentada en los bonos cuyo pago fue objeto de diferimiento según lo dispuesto por el Artículo 59 de la Ley Nº 25.827, mediante una operación de canje nacional e internacional. Suplemento de Prospecto, aplicable a la oferta internacional. Procedimiento Operativo para la República Argentina. Valor nominal máximo de los bonos que serán emitidos, Bonos Internacionales de la República Argentina y Bonos de la República Argentina. Modelo de Convenio de Fideicomiso. On the Lock Law see Porzecanski (n 164); *NML Capital, LTD., et al. v The Republic of Argentina* (n 28). More broadly, for an overview of Argentina's convoluted restructuring process see Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 235–284.
[373] *Mamatas et autres v. Greece* (n 18); Boudreau (n 90); Iversen (n 164); Kupelyants (n 53) 142. On Collective Action Clauses, see *infra*.
[374] Choi, Gulati and Posner (n 91).
[375] Megliani, *Sovereign Debt* (n 56) 233; Das, Papaioannou and Trebesch (n 4), 41-43.
[376] A 1958 English case brought against Greece illustrates the efficiency of said choice-of-law clauses. In *National Bank of Greece and Athens v Metliss*, it was ruled that a Greek moratorium act could not affect bonds emitted under English law. *National Bank of Greece and Athens v Metliss* [1958] AC 509 (Court of Appeal); Kupelyants (n 53) 141–142.
[377] Lee C Buchheit, 'Trustees versus Fiscal Agents for Sovereign Bonds' (2018) 13 Capital Markets Law Journal 410.

Here again, the purpose of these clauses is to prevent the debtor from being able to unilaterally alter the conditions of payment or to act as a buffer against a devaluation of the debtor's currency during a financial crisis[378]. There are three main exceptions to the use of these clauses. First US treasuries are issued in dollars, under US law and elect US jurisdictions[379]. Similarly, UK gilts are issued in British pounds, under UK law and elect UK jurisdictions[380]. Finally, the bonds of members of the Eurozone usually elect their own domestic law and jurisdiction and are payable in Euros[381].

The fact that these States are able to issue bonds domestically can be explained by the "original sin hypothesis" put forward by Eichengreen *et al.*[382]. The hypothesis, originally developed to explain the presence of currency clauses, states that certain developing countries are not able to borrow, either domestically[383] or abroad[384], in their own currency due to the distrust of financial markets. Indeed, these States suffer from greater volatility and are therefore more prone to see the value of their currency depreciate. In addition, these governments often suffer from a high debt-to-revenue ratio[385] which incentivises them towards debasing their currencies[386].

Thus, poorer governments since they are usually cursed with lower fiscal revenues and higher levels of debts may be tempted to devaluate their own currency to fulfil their contractual obligations with greater ease. This creates an additional risk for creditors as, in addition to the default risk of the debtor, they would also be facing a greater exchange rate risk[387]. Thus, borrowing abroad and in a foreign currency effectively binds those States for the future and acts as a credible commitment device. The same applies to borrowing under foreign law, or repayment via a third party geographically distinct from the debtor. Those measures prevent regulatory interventions from sovereigns which are perceived as riskier by capital markets.

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378 Eichengreen and Hausmann (n 370).
379 Megliani, *Sovereign Debt* (n 50) 233.
380 ibid.
381 ibid. Although there are exceptions to this rule. Belgium notably floats debt abroad. Kupelyants (n 53) 113.
382 Eichengreen, Haussman and Panizza (n 114).
383 Eichengreen and Hausmann (n 370).
384 ibid; Eichengreen, Haussman and Panizza (n 114).
385 Governments whose fiscal revenues are weak compared to their debt.
386 Eichengreen, Haussman and Panizza (n 114); Robert Lucas and Nancy Stokey, 'Optimal Fiscal and Monetary Policy in an Economy without Capital' (1983) 12 Journal of Monetary Economics 55; Guillermo A Calvo and Pablo E Guidotti, 'On the Flexibility of Monetary Policy: The Case of the Optimal Inflation Tax' (1993) 60 The Review of Economic Studies 667.
387 Choi, Gulati and Posner (n 114).

3.2.2.3 The Rateable Payment Interpretation of the pari passu clause

The *pari passu* clause is a standard contractual clause present in both sovereign and corporate debt instruments[388]. Its role, in a corporate context, is to prevent a debtor from issuing other debt instruments ranking senior to those containing the clause[389]. A standard version of the clause reads as such:

> *"The Notes rank, and will rank, pari passu in right of payment with all other present and future unsecured and unsubordinated External Indebtedness of the Issuer."*[390]

The problem with this seemingly innocuous contract language is that in a sovereign debt context, given the absence of a bankruptcy mechanism, the meaning of "*rank in right of payment*"[391] is uncertain. As opposed to corporate bankruptcies, sovereign debt restructurings lack a liquidation phase in which rank of payment would have any meaning[392].

The clause and its ambiguities mainly attracted the attention of commentators since *Elliott* used it to disturb Peru's restructuring by seizing the funds destined to pay the creditors having accepted a restructuring offer[393]. *Elliott* had purchased Brady bonds emitted by Peru, for a total of $20.7 million and due in September 2000[394]. After obtaining from New-York Courts a decision granting it $55.6 million[395], the fund sought enforcement. Peru, however, had decided to satisfy in priority the creditors having agreed to a debt restructuring. *Elliott* argued, and the New-York district court agreed supported by an expert opinion by Lowenfeld, that doing so constituted a breach of the *pari passu* clause[396].

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388 Buchheit and Pam (n 14).
389 ibid.
390 ibid. Other drafting of the clause are mentioned by Rodrigo Olivares-Caminal, 'Understanding the Pari Passu Clause in Sovereign Debt Instruments: A Complex Quest' (2009) 43 international lawyer (ABA) 1217.
391 See e.g. Buchheit, 'The Pari Passu Clause Sub Specie Aeternitatis' (n 75).
392 Olivares-Caminal, 'Rank Pari Passu or Not to Rank Pari Passu' (n 9), 1222; Buchheit and Pam (n 43), 4.
393 *Elliott Assocs., L.P.* (n 323). For an analysis of the historical origins of the pari passu clause see Buchheit and Pam (n 75); Benjamin Chabot and Mitu Gulati, 'Santa Anna and His Black Eagle: The Origins of Pari Passu?' [2014] Capital Markets Law Journal <https://scholarship.law.duke.edu/faculty_scholarship/3237>; Weidemaier, Scott and Gulati (n 75). For a critique of the 'contract originalist' approach to the *pari passu* clause, and of the relevance of such historical research for contemporary interpretations of the clause see W Mark C Weidemaier, 'Indiana Jones, Contracts Originalist' (2014) 9 Capital Markets Law Journal 255. Finally, on the failure of bond drafters to adapt to the challenges raised by the clause see Gulati and Scott (n 75).
394 *Elliott Assocs., L.P. v. Banco de la Nacion* (n 22); Buchheit and Pam (n 9), 6-8; Bratton (n 42), 823-824.
395 *Elliott Assocs., L.P. v. Banco de la Nacion* (n 28); Bratton (n 74); Olivares-Caminal, 'Understanding the Pari Passu Clause in Sovereign Debt Instruments' (n 390) 1223–1224.
396 *Elliott Associates L.P. v. Banco de la Nacion* (n 323).

The court adopted a ‘rateable payment’, sometimes dubbed ‘plain English reading’, of the clause[397]. Under this reading, *pari passu* forces States to pay all their creditors *pro rata*, at the same time, rather than paying a group of creditors, then another[398]. This interpretation relies on the idea that in a sovereign default, order of payment and rank of payment are identical. Summarily put, paying a group of creditors first amounts to create a senior category of instruments which would violate the *pari passu* clause[399]. Rateable payment thus guarantees the effectivity of the payment obligation arising from the sovereign debt contract.

The policy implications of such an interpretation of the clause are made clear in Lowenfeld’s expert opinion:

> *“(…) A borrower from Tom, Dick, and Harry can't say 'I will pay Tom and Dick in full, and if there is anything left over I'll pay Harry.' If there is not enough money to go around, the borrower faced with a pari passu provision must pay all three of them on the same basis.”* [400]

If one subscribes to the idea, as Lowenfeld seems to, that in sovereign insolvencies order of payment is equivalent to seniority[401], this interpretation guarantees holdout creditors’ right of payment sagainst a State attempting to favour restructured debt. Indeed, following the previous postulate, paying the restructured debt first, leads to creating a quasi-senior category of instruments. Hence, if States lack sufficient funds to satisfy all creditors the holdout debt will not be repaid in full[402]. The clause, read as such further lowers the legal risks attached to sovereign lending, as it prevents sovereigns from altering payment order and thus acts as another credible commitment device.

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397 For an analysis of said interpretation see e.g.: Wright (n 14); Cohen (n 74); Zamour (n 74); Kupelyants (n 53) 244–245.

398 A possible use of the clause might have been to guarantee ranks of payments when sovereign bonds used to be secured on specific streams of assets. See Buchheit and Pam (n 91); For a narrow intepretation of the clause see: *Kensington International Ltd v Republic of the Congo [2003] EWHC 2331 (Comm)* (EWHC (Comm)); *Export-Import Bank of the Republic of China v Grenada* [2014] United States Court of Appeals, second Circuit 12–2619–CV; *Republic of Nicaragua v LNC Investment LLC* [2004] Cour d’Appel Bruxelles (9th ch) 2003/KR/334.

399 Philip Wood, ‘The Origins and Future of Non-Discrimination in Sovereign Bankruptcies: A Comment’ (2014) 9 Capital Markets Law Journal 293.

400 *Elliott Associates L.P. v. Banco de la Nacion* (n 46); Lee C Buchheit and Jeremiah S Pam, ‘The Hunt for Pari Passu Cover Story’ (2004) 23 International Financial Law Review 20.

401 Wood, ‘The Origins and Future of Non-Discrimination in Sovereign Bankruptcies’ (n 399).

402 ibid.

3.2.3 Efficient Remedies to guarantee repayment

3.2.3.1 Efficient Remedies: Overview

The final condition for the creditor protection model to function is the existence of legal remedies enabling creditors to effectively coerce the sovereign. Historically creditors not only had to face difficulties in finding competent jurisdictions, but until recently also lacked ways to enforce rulings in their favour[403].

Indeed, while domestic courts' decisions overwhelmingly tend to favour creditors, the debtor's immunity from execution limits their ability to ensure that they are respected. These difficulties to find attachable goods belonging to sovereigns reluctant to pay are easily illustrated by *NML*'s enforcement saga against Argentina[404]. *NML*, *Elliott*'s sister-fund had purchased, a series of bonds issued by the South American Republic, at a steep discount[405]. It also obtained from US courts a favourable court decision against Argentina, for more than $2 billions[406]. Armed with this order, *NML* engaged in an odyssey of enforcement attempts on at least three continents[407], leading even to a dispute ITLOS[408] and to a dispute involving the launch by SpaceX of Argentinean satellites[409], with little to show in terms of results. Throughout those attempts, and nearly systematically, *NML* ran into Argentina's immunity, preventing it from seizing any of the republic's assets.

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[403] On enforcement difficulties regarding sovereign debt contract see Gregory R Day, 'Market Failure, Pari Passu, and the Law and Economics Approach to the Sovereign Debt Crisis' (2013) 22 Tulane Journal of International and Comparative Law 225; Kupelyants (n 53) 277; Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 124.
[404] Ingenito and Hioureas (n 82).
[405] ibid; Jamison Joiner, 'Past Due: An Introduction to Sovereign Debt, the Ongoing Dispute between NML Capital and Argentina, and Possible Ramifications of the Dispute's Outcome Case Note' (2015) 21 Law and Business Review of the Americas 85.
[406] *NML capital v Republic of Argentina* [2010] United States Court of Appeal for the Second Circuit 09-2707-cv (L), 09-2708-(CON), 09-2867-(CON), 09-2710-(CON), 09-2711-(CON), 09-2712-(CON), 09-2713-(CON), 09-2714-(CON), 09-2715-(CON), 09-2716-(CON), 09-2717-(CON), 09-2810-(CON), 621 Fed Report 3rd Ser 230.
[407] 'NML Capital Limited (Appellant) v Republic of Argentina (Respondent) - The Supreme Court' <https://www.supremecourt.uk/cases/uksc-2010-0040.html> accessed 6 June 2015; *République d'Argentine c NML Capital LTD* [2012] Cour de Cassation (Belgium) C.11.0688.F, 2013 J Trib 290; *NML Capital Limited v Republic of Argentina* [2011] UK Supreme Court UKSC 2010/0040, 2011 UKSC 31; *The Republic v High Court (Commercial Division), Accra, ex p Attorney-General, NML Capital Ltd 1st Interested Party; Republic of Argentina, 2nd Interested Party* [2013] Ghana Supreme Court J5/10/2013; *Société NML Capital c République d'Argentine* [2013] Cour de Cassation (1ère ch civ) (France) 10-25.938; *Société NML Capital c République d'Argentine* [2013] Cour de Cassation (1ère ch civ) (France) 11-13.323; *Société NML Capital c République d'Argentine* [2013] Cour de Cassation (1ère ch civ) (France) 11-40.450; *NML Capital Ltd c République d'Argentine* [2014] Cour de Cassation (Belgium) C.13.0537.F.
[408] *The 'ARA Libertad' case (Argentine v. Ghana)* (n 20).
[409] 'Argentina Faces Creditor Lawsuit over U.S. Satellite Contract' *Reuters* (26 March 2014) <https://www.reuters.com/article/usa-court-argentina-idUSL1N0MM28U20140326> accessed 13 May 2019.

In order to really incentivise lending to sovereigns, the creditor protection model needs to put in place judicial remedies that enable creditors to effectively coerce the sovereign. Domestically, such a remedy has been found, again, in the the *pari passu* clause with courts imposing *pro rata* payment as a remedy[410].

3.2.3.2 *The pari passu clause and pro rata payment*

Pro rata payment as a remedy, prevents debtors from making any payment on the restructured bonds without paying the holdouts at a similar rate. This, effectively, forces the debtor to either pay holdout debts, or to artificially default on the restructured debt. Faced with such a possibility, States usually cave in and pay holdouts to avoid the consequences of default[411]. This remedy changes the dynamic between States and their holdout creditors. Not only are the latter able to obtain satisfactory judgments from domestic courts, but *via pro rata* payment, they also possess an efficient remedy with which they can ensure that judgments cannot be ignored by a debtor.

Pro rata payment as a remedy differs from rateable payment as an interpretation of the clause[412]. *Pro rata* payment is a judicial remedy, a measure imposed by a court or tribunal as a response to the breach of an obligation. Rateable payment is the obligation whose breach must be established by creditors in order to obtain the remedy.

Moreover, while *pro rata* payment is usually used as a remedy for breaches of the *pari passu* clause interpreted in a rateable payment fashion[413], the 2012 NML capital case shows that the clause's interpretation and its remedy do not always go hand in hand[414].

Pro rata paymen, has been heavily criticised in the legal scholarship on sovereign debt[415]. As will be seen in section 3, its use has been one of the main causes of inefficiency created by the creditor protection model. However, put in its intellectual and historical context, *pro rata* payment makes economic sense. Faced with a sovereign debtor whose assets are

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[410] Day (n 346), 224-225.
[411] For the consequences of a rateable interpretation of the clause see e.g. Buchheit and Pam (n 43), 8-9.
[412] On rateable payment as a remedy, see Zamour (n 74).
[413] See *Elliott Associates L.P. v. Banco de la Nacion* (n 323); *Elliott Assocs., L.P.* (n 323).
[414] Zamour (n 74); *NML Capital, LTD., et al. v The Republic of Argentina* (n 28). As will be underlined during the analysis of the anti-holdout model, the interpretation of the Court of Appeal in *NML* is less restrictive than the rateable payment interpretation as traditionally understood.
[415] It could be pointed out that *pro rata* payment still lacks teeth as a remedy as it has only been used to punish breaches of the *pari passu clause*. However, given the structure of the modern bond market, and if the rateable payment interpretation or the NML interpretation of the clause is adopted, any refusal by a State to repay holdouts will lead to a breach of the clause. Indeed, by doing so, the debtor favours the restructured debt over the holdout debt, breaching the *pari passu* clause.

difficult to attach, creditors effectively lack ways via which to effectively ensure that their rights will be respected. *Pro rata* payment shatters this equilibrium by enabling holdouts to hold the rest of the creditor-base hostage until they have been satisfied.

This capacity to effectively coerce the sovereign, however disruptive, acts as an incentive for private entities to lend to States. Absent such remedies there is effectively no way for creditors of 'rogue States' to ensure that the judgments they obtain against the debtor will have any effect. Hence, *pro rata* payment, *ex ante* reassures creditors by providing them with the means to constrain debtors to repay their debts.

3.3 The Creditor Protection Model in international law

3.3.1 Introduction

Creditor protection, as a policy, is not merely apparent at the domestic and contract law level. Developments in international law have similarly attempted to reduce the unique risks tied to sovereign lending.

The most obvious area where international law has developed in that direction is by providing creditors with multiple *fora* for dispute settlement. Notably, the law on sovereign immunities evolved towards the recognition of sovereign debt restructurings as *acta de iure gestionis*[416], thus ensuring that sovereign debt can be adjudicated before domestic courts. Similarly, the competence of Investment tribunals on sovereign bonds[417] provides creditors with access to independent international courts and enables them to mobilise the remedies arising from International Investment Law[418]. Finally, the European Court of Human Rights has, on several occasion, recognised that sovereign debt restructuring could potentially violate article 1 of the 1st protocol to the ECHR[419].

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[416] See notaby: *Republic of Argentina v. Weltover, Inc.* (n 24).

[417] *Abaclat and Others v. Argentine Republic* (n 17); *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17); *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17).

[418] On the potential role of ICSID tribunals in sovereign debt disputes see alexander Szodruch, 'State Insolvency – Consequences and Obligations under Investment Treaties', *The International Convention on the Settlement of Investment Disputes (ICSID) : Taking Stock after 40 Years. R. Hofmann, C. Tams (eds.)* (nomos 2007); Waibel, 'Opening Pandora's Box' (n 81); Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 209–251.

[419] *De Dreux-Brézé c France* [2001] European Court of Human Rights 57969/00; *Thivet v France* [2000] European Court of Human Rights 57071/00; *Malysh and others v Russia* [2010] European Court of Human Rights 30280/03; *Mamatas et autres v. Greece* (n 18).

However, while the competence of international courts for sovereign debt disputes is probably the most important development within the international law on sovereign debt, it is not the sole aspect of the creditor protection model which has been implemented at the international level.

The applicability of Investment Law and Human Rights law to the sovereign debt relationship, like *forum selection* clauses, helps guaranteeing that the sovereign cannot unilaterally alter the content of the obligations it owes creditors. In the same vein, the narrow interpretation of the necessity defence can be read as a way to guarantee the sanctity of creditor's rights even during difficult economic circumstances.

Regarding enforcement, the remedies granted by Investment Tribunals and Human Rights courts both have the potential to provide creditors with some additional means to coerce the debtor into repayment.

3.3.2 Creditor Access to Independent International Courts

The first condition for the functioning of the creditor protection model is to grant creditors access to independent courts. International law has provided such access at three different levels: first, via the characterisation of sovereign bonds as *acta de iure gestionnis*. Second, via the characterisation of sovereign bonds as investments by investment tribunals. Finally, via the recognition that sovereign debt restructurings could potentially amount to a violation of the right to property as enshrined in the ECHR.

3.3.2.1 Sovereign Defaults and Restructurings as acta de iure gestionnis

International law distinguishes between two types of immunities. Immunity from jurisdiction is a procedural norm preventing a domestic *forum* to perform its adjudicative function against a sovereign[420]. Immunities from execution, on the other hand prevents the application of measures of constraint upon sovereign defendants, or certain categories of

[420] James Crawford and Ian Brownlie, *Brownlie's Principles of Public international law* (8th ed, Oxford University Press 2012) 489; European Convention on State Immunity (Basel) 1972; *Jurisdictionnal Immunities of the State (Germany v Italy; Greece intervening)* (2012) 2012 C J Rep 99 (International Court of Justice); United Nations Convention on Jurisdictional Immunities of States and Their Property (New York) 2004.

goods belonging to them, by foreign courts[421]. Both norms are recognised in customary international law[422], and find sources in domestic law[423].

The justification for granting immunities to sovereigns harkens back to the fundamental principle that *par in parem non imperium habetur*[424]. It is deeply rooted within the notions of sovereignty and equality[425]. Up until the middle of the 20th century, International law, and most domestic courts, sanctioned an absolute reading of jurisdictional immunities. In the absence of a reliable international *forum* for enforcement, this left bondholders without judicial recourses in case of default or repudiation[426].

From the 1950s onwards, the law on State immunity would evolve towards a restrictive reading of jurisdictional immunities[427]. In the US and the UK, main *fora* elected in sovereign bonds, this evolution was materialised in respectively the Foreign Sovereign Immunity Act (FSIA)[428] and the Sovereign Immunity Act[429] (SIA). International law evolved similarly, and the restrictive theory of State immunity is now considered customary[430].

The restrictive theory still recognises immunity as the default position but introduces one exception for commercial acts undertaken by sovereigns. It distinguishes between *acta de iure imperii*, covered by the immunity, and *acta de iure gestionnis*¸ over which domestic courts can have jurisdiction[431]. The criteria used for the distinction are debated within

[421] Crawford and Brownlie (n 420) 502; European Convention on State Immunity (Basel); United Nations Convention on Jurisdictional Immunities of States and Their Property (New York); *Jurisdictionnal Immunities of the State (Germany v. Italy; Greece intervening)* (n 420).
[422] See *Jurisdictionnal Immunities of the State (Germany v. Italy; Greece intervening)* (n 420).
[423] E.g. 'State Immunity Act 1978' <http://www.legislation.gov.uk/ukpga/1978/33> accessed 6 June 2015; Foreign Sovereign Immunity Act 1976.
[424] Peter-Tobias Stoll, 'Sovereign Immunity', *Max Planck Encyclopedia of Public international law* (Oxford University Press 2011) <http://opil.ouplaw.com.ezproxy.lib.gla.ac.uk/view/10.1093/law:epil/9780199231690/law-9780199231690-e1106?rskey=7MlIA3&result=1&prd=EPIL>.
[425] ibid.
[426] Weidemaier, 'Sovereign Immunity and Sovereign Debt' (n 47), 69-71.
[427] Weidemaier, 'Contracting for State Intervention' (n 174), 340-342; Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 7.
[428] Foreign Sovereign Immunity Act.
[429] Sovereign Immunity Act 1978 1978; Kupelyants (n 53) 63.
[430] *Jurisdictionnal Immunities of the State (Germany v. Italy; Greece intervening)* (n 420).
[431] The distinction between both types of acts is be customary, it is followed in both the UN Convention on Jurisdictionnal Immunities and the European Convention on State Immunity. While both conventions have not entered into force, they are largely considered to reflect CIL. See United Nations Convention on Jurisdictional Immunities of States and Their Property (New York); European Convention on State Immunity (Basel); *Jurisdictionnal Immunities of the State (Germany v. Italy; Greece intervening)* (n 420); Crawford and Brownlie (n 420) 490.

international instruments on immunity[432]. Some focus solely on the nature of the State's act[433], while others focus not only on its nature but also on its purpose[434].

In the US, the characterisation of sovereign bonds under the law of immunities was settled by the Supreme Court in the 1992 *Weltover case*[435]. The *Weltover* case finds its source in the 1980s Argentina crisis and the emission in 1982 of US registered bonds by Argentina to refinance its debt. Said bonds, once at maturity were unilaterally restructured by Argentina due to a lack of sufficient dollar reserves[436], leading to litigation in the US[437].

One of the questions at stake was whether Argentina's restructuring of its 1982 bonds, undertaken by presidential decree, constituted a commercial act under the FSIA. The Supreme Court, underlining that the FSIA aims at codifying the restrictive theory of State immunities, decided that the nature of the acts, rather than their purpose, ought to be taken in consideration for this assesment[438]. The Court thus defined a commercial act as an act that both a private or a sovereign party could undertake in "trade, traffic and commerce"[439]. A sovereign activity, *a contrario*, is one that a private party does not have the legal ability to undertake. Thus, as both private entities and sovereigns can emit and restructure bonds[440], Argentina's restructuring constituted a commercial act over which US courts could have jurisdiction[441]. By focusing on the private nature of debt restructurings, the Supreme Court views sovereign debt as fundamentally contractual, hence enabling domestic litigation.

This focus on the contractual nature of State indebtedness similarly features in a recent case before the European Court of Justice. The case was referred to the ECJ by a German domestic court regarding the applicability of *Regulation (EC) No 1393/2007 on the service in the Member States of judicial and extrajudicial documents in civil or commercial*

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[432] *Jurisdictionnal Immunities of the State (Germany v. Italy; Greece intervening)* (n 420); Stoll (n 424); United Nations Convention on Jurisdictional Immunities of States and Their Property (New-York) 2005; European Convention on State Immunity (Basel).
[433] E.g. European Convention on State Immunity (Basel).
[434] E.g. United Nations Convention on Jurisdictional Immunities of States and Their Property (New-York).
[435] *Republic of Argentina v. Weltover, Inc.* (n 18), 609-610. For a broader commentary on Immunities under the FSIA see Kupelyants (n 53) 73–77.
[436] Avi Lew, 'Republic of Argentina v. Weltover, Inc.: Interpreting the Foreign Sovereign Immunity Act' (1994) 17 Fordham international law Journal 726; *Republic of Argentina v. Weltover, Inc.* (n 22). For a view of the Weltover decision within the broader US case-law on immunity see David E Gohlke, 'Clearing the Air or Muddying the Waters--Defining a Direct Effect in the United States under the Foreign Sovereign Immunities Act after Republic of Argentina v. Weltover Comment' (1995) 18 Houston Journal of international law 261.
[437] *Republic of Argentina v. Weltover, Inc.* (n 18) 609-610.
[438] ibid.
[439] ibid, 614.
[440] ibid, 616-615.
[441] ibid; Lew (n 436).

matters[442]. The applicability of said regulation depends on the characterisation of the subject matter of the dispute as a 'civil or commercial matter'. From such a characterisation depends not only the applicability of Regulation No 1393/2007 but also whether the acts of a sovereign would be covered by immunity[443].

The case concerned German bondholders bringing action before domestic German courts following the retroactive insertion of a Collective Action Clause in their bonds[444]. They claimed that such action constituted not only an unlawful interference within their property rights but also a breach of contract[445]. The ECJ ruled that, while the Greek legislative intervention constituted a legislative act, "*it is not obvious that the adoption of [the Greek Bondholder Act 4050/2012] led directly and immediately to changes to the financial conditions of the securities in question(…).*"[446]

It added:

> *"[T]he issue of bonds does not necessarily presuppose the exercise of powers falling outside the scope of the ordinary legal rules applicable to relationships between individuals, hence the rules of private law."* [447]

As a result, the court ruled that the action brought by the German bondholders against Greece ought to be characterised as a civil or commercial matter[448]. The ECJ's reasoning in *Fahnenbrock* echoes closely the *Weltover* decision. The focus is put on the contractual nature of the acts of the sovereign, not on its purpose or effects. Here, even though Greece had introduced the retrofit CAC through legislative means, the European Court focuses on the nature of the borrowing instrument underlying the debtor's obligations.

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[442] *Stefan Fahnenbrock et. al. C Hellenische Republic* (n 307).
[443] In EU law, the distinction between civil and commercial matter is aligned on the distinction between *acta de iure imperii and acta de iure gestionnis*. The characterisation also leads to the applicability of the European private international law regulations. See Regulation No 1215/2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (recast) 2012, article 1; Regulation No 593/2008 on the law applicable to contractual obligations (Rome I) 2008, article 1; *Eirini Lechouritou et al v Dimosio tis Omospondiakis Dimokratias tis Germanias* [2007] CJCE C-292/05.
[444] *Stefan Fahnenbrock et. al. C Hellenische Republic* (n 307) paras 11–23. On *Fahnenbrock* see also Hayk Kupelyants, 'The German Taxpayer and the Greek Sovereign Debt' *Lexis PSL* (2015); Sebastian Grund, 'The Legal Consequences of Sovereign Insolvency – a Review of Creditor Litigation in Germany Following the Greek Debt Restructuring' (2017) 24 Maastricht Journal of European and Comparative Law 399.
[445] *Stefan Fahnenbrock et. al. C Hellenische Republic* (n 247) paras 11-23.
[446] ibid, para 57.
[447] ibid, para 53.
[448] ibid., para 59

At the heart of the debate on the characterisation of sovereign debt restructuring as *acta de iure imperii* or *acta de iure gestionnis* is the ability of creditors to easily enforce the contractual obligations arising from sovereign bonds[449]. Insisting on the contractual nature of the bonds, as the European Court of Justice[450] and the Supreme Court[451] do leads logically to their enforceability before domestic courts. Said competence matters for three main reasons. First, domestic courts are the main *forum* for adjudicating the contractual obligations arising from sovereign debt[452].

Second, the competence of domestic courts on sovereign debt cases is well established within the jurisdictions usually elected in sovereign bonds, furthering legal certainty. *A contratio*, as will be exposed *infra* there are debates regarding the characterisation of bonds as investments[453]. This ease of access to domestic courts, and the *quasi*-certainty that they will be competent enables creditors to know *ex ante*, that a default or repudiation will be justiciable.

Finally, in terms of remedies, while both international and domestic courts can award damages, so far, only domestic courts have granted *pro rata* payment to holdouts as a remedy. The ability to obtain *pro rata* payment as a remedy empowers creditors, *pro rata* payment has proved a very efficient way of coercing the State towards repayment. Damages, on the other hand, have historically proven difficult to obtain from a State refusing to pay.

Domestic courts' relative cheapness, the certainty of their competence and the potential efficiency of their remedies, mean that the characterisation of bonds and restructurings as

[449] It should be noted that in a 2005 judgment, the Italian court of cassation considered that acts undertaken for the purpose of restructuring sovereign debt as *acta de iure imperii*. The case concerned Argentina's 2000 restructuring and had been brought before Italian courts by Italian bondholders. While the court agrees that the emission of bonds constitutes an *acta de iure gestionnis*, it ruled, considering the "*whole context of the transaction*" that Argentina's restructuring constituted an *acta de iure imperii* since it aimed at managing an economic crisis. See *Ordinanza* (n 25); Megliani, *Sovereign Debt* (n 51) 246; Fabio Bassan, *The Law of Sovereign Wealth Funds* (Edward Elgar Publishing 2011) 96. Such an interpretation of the law of immunities appears however to be marginal.

[449] *Stefan Fahnenbrock et. al. C Hellenische Republic* (n 307).

[450] *Stefan Fahnenbrock et. al. C Hellenische Republic* (n 307).

[451] *Republic of Argentina v. Weltover, Inc.* (n 24).

[452] Unless investment tribunals are competent for the dispute on the basis of a BIT featuring an umbrella clause. In this case, arguably, the investment tribunal could adjudicate a breach of contract by the sovereign. It should however be underlined that the effect of umbrella clauses is quite uncertain as their interpretation has been heavily debated. On the application of umbrella clauses to sovereign debt instruments see Szodruch (n 418) 151–153.

[453] See e.g. *Poštová banka, a.s. and Istrokapital SE v. Hellenic Republic (Award)* (n 17); Francesco Montanaro, 'Poštova Banka SA and Istrokapital SE v Hellenic RepublicSovereign Bonds and the Puzzling Definition of "Investment" in International Investment Law' (2015) 30 ICSID Review - Foreign Investment Law Journal 549; Ortolani (n 81).

acta de iure gestionnis is essential to enable sovereigns to credibly commit to their debt obligations[454].

3.3.2.2 The Competence of Investment Tribunals on Sovereign debt

As domestic court recognised their competence over sovereign debt restructurings, ICSID tribunals have opened a new avenue for creditor litigation: Investor State Dispute Settlement (ISDS).

Under the ICSID convention, the competence[455] of International Investment Tribunals, *ratione materiae*, is usually determined via a "double-barrelled" test[456]. Under said test, the competence of a tribunal has to be established under both the specific bilateral investment treaty invoked, and article 25 of the ICSID convention.

While the ICSID convention does not define the term investment, it is generally accepted in arbitral case-law that an investment is composed of four key elements[457]:

1. The contribution of an asset (regardless of its size)
2. For a certain duration
3. Creating a risk for the investor
4. And contributing to the development of the host State[458]

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[454] On the potential inefficiencies of ICSID arbitration to coerce debtors see Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 124; Szodruch (n 418).

[455] The criteria to determine the competence of investment tribunals are heavily debated. However, when it comes to sovereign debt, investment tribunals have, on average, applied the double-barrelled test, followed by the Salini criteria, hence their analysis here. The focus on the Salini test and the double barrel test should therefore not be understood as an affirmation that both doctrines are unchallenged in the case-law and the scholarship on investment. On the notion of investment and the competence of investment tribunals *ratione materiae* see Emmanuel Gaillard, 'Identify or Define? Reflections on the Evolution of the Concept of Investment in ICSID Practice', *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer. C. Binder, U. Kriebaum, A. Reinisch, S. Wittich (eds.)* (Oxford University Press 2009); Engela C Schlemmer, 'Investment, Investor, Nationality, and Shareholders' [2008] The Oxford Handbook of International Investment Law <http://www.oxfordhandbooks.com.ezproxy.lib.gla.ac.uk/view/10.1093/oxfordhb/9780199231386.001.0001/oxfordhb-9780199231386-e-2> accessed 27 August 2018; Brigitte Stern, 'The Contours of the Notion of Protected Investment' (2009) 24 ICSID Review - Foreign Investment Law Journal 534.

[456] *Salini Costruttori S.pA and Italstrade S.pA v Kingdom of Morocco (decision on jurisdiction)* [2002] ICSID ARB/00/4, 129 J Droit Int 196; David AR Williams, 'Jurisdiction and Admissibility' [2008] The Oxford Handbook of International Investment Law <http://www.oxfordhandbooks.com.ezproxy.lib.gla.ac.uk/view/10.1093/oxfordhb/9780199231386.001.0001/oxfordhb-9780199231386-e-22> accessed 27 August 2018; Schlemmer (n 455); Nadakavukaren Schefer (n 40) 75.

[457] *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco (decision on jurisdiction)* (n 456); Nadakavukaren Schefer (n 40) 75; Schlemmer (n 455); Williams (n 456).

[458] See *Salini Costruttori S.pA and Italstrade S.pA v Kingdom of Morocco, Decision on Jurisdiction* (ICSID); and discussions in Williams (n 423); Schlemmer (n 422).

Several cases have examined whether sovereign credit instruments fall within the scope of this definition. In *Fedax vs Venezuela*[459] an arbitral tribunal examined this question for promissory notes issued to recognise a deb from Venezuela to a private company[460]. These notes were negotiable on a secondary market[461], like sovereign bonds. This lead Venezuela to claim that they could not constitute an investment as the nexus between the issuer and the holder of the instrument was too diffuse. In particular, the Venezuelan government argued that the mere holder of a note did not contribute to the economic development of the issuer[462].

The arbitral tribunal concluded that the negotiable nature of the notes *per se* could not prevent their characterisation as an investment as the host State "*enjoyed a continuous credit*"[463] during their maturity. Hence, noteholders, through mere possession, could be deemed to contribute to the economic development of their debtor[464]. In addition, the tribunal underlined the fact that the existence of a dispute regarding the payment of a principal sum and interests evidenced the existence of an investment for creditors[465].

In *Abaclat v. Republic of Argentina*[466], an arbitral tribunal examined whether sovereign bonds issued by Argentina, and held by several Italian nationals, could be characterised as investments. It is worth noting that the *Abaclat* tribunal did not subscribe to the *Salini* test. Instead, it focused on the *raison-d'être* of Article 25 ICSID, *i.e.* to "*encourage private investment while giving the Parties the tools to further define what kind of investment they want to promote*"[467].

The *Abaclat* tribunal thus limited its examination of the definition of investment to the Italy-Argentina BIT, reasoning that it would be nonsensical to refuse investors the protection that

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[459] *Fedax NV v The Republic of Venezuela, Decision of the Tribunal on Objections to Jurisdiction* [1997] ICSID ARB/96/3; Ortolani (n 81).
[460] For a commentary on Fedax, see also C Chatterjee, 'Investment-Related Promissory Notes Are Investments under the ICSID Convention: Fedax N. V. v. The Republic of Venezuela' (2002) 3 The Journal of World Investment & Trade 147.
[461] *Fedax NV v The Republic of Venezuela, Decision of the Tribunal on Objections to Jurisdiction* (n 426) paras 18-19 Ortolani (n 51) 387.
[462] *Fedax NV v The Republic of Venezuela, Decision of the Tribunal on Objections to Jurisdiction* (n 426) para 19.
[463] Ibid para 40.
[464] Ibid para 40.
[465] ibid; Ortolani (n 51) 387.
[466] *Abaclat and Others v. Argentine Republic* (n 12), para 364.
[467] ibid; Ortolani (n 81).

both sovereigns intended to grant on the basis of the Salini criteria[468]. As said definition encompassed sovereign bonds, the tribunal recognised its competence over the dispute.

As opposed to *Abaclat*, the *Ambiente Ufficio*[469] decision applied the *Salini* test to determine the characterisation of Argentinian sovereign bonds[470]. The case also concerned Italian bondholders, acting against the Argentinian restructuring measures.

The *Ambiente* tribunal also reached the conclusion that the bonds should be characterised as investments. It reasoned that the bondholders had made a significant contribution, not as individuals, but considering the bond issue as a whole[471]. The tribunal also considered the maturity of the bonds to constitute a sufficient length of time, not examining the duration for which secondary market holders had held the bonds[472]. It similarly agreed that bondholders were facing a risk different from a mere commercial risk given the possibility of regulatory intervention by the debtor in case of restructuring[473]. The bonds, according to the tribunal, also provided their holders with regular returns, in the form of interest and principal payment. Finally, it was found that the funds raised from the bond issuance were ultimately made available to Argentina and thuscontributed to its development[474].

The reasoning of these arbitral tribunals is noteworthy in that the characterisation of investment, and the protection granted the ICSID convention, follows the bonds across holders on the secondary market. Even if a bondholder has purchased bonds a day before they reached maturity, for cents on a dollar, they would still be considered to have made a substantial contribution to the development of the issuing State for a lengthy period of time. In other words, the identity of the bondholders does not matter, bonds are by themselves investments independently from those who hold them at the time of litigation.

[468] Ortolani (n 81).
[469] *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17). In addition to *Abaclat* and *Ambiente*, a third case was brought against Argentina by Italian bondhoders, *Alemanni*, as the reasoning in *Alemanni* does not differ in any substantial fashion from *Ambiente*, this thesis will not focus on its findings. See *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17); Ortolani (n 81) 402.
[470] Ortolani (n 81) 388–389.
[471] ibid; Ortolani (n 51) 388.
[472] *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 12) para 483; Ortolani (n 51) 389.
[473] *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 12) para 484; Ortolani (n 51) 389.
[474] *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 12) paras 485-487; Ortolani (n 51) 489.

In order to lead to the jurisdiction of an arbitral tribunal, bonds also have to be covered by the definition of investment in the relevant BIT. In both *Abaclat* and *Ambiente*, said BIT was the Argentina-Italy treaty, defining investments as:

> *" (...), any kind of asset invested or reinvested by an individual or a legal entity of one Contracting Party in the territory of the other Party, in conformity with the laws and regulations of the latter."*[475]

The treaty also provides a non-exhaustive list of types of investment, including:

> *"(c): obligations, private or public titles or any other right to performances or services having economic value, including capitalized revenues''*[476]

And

> *"(f): any right of economic nature conferred under law or contract, as well as any license and concession granted in compliance with the applicable provisions applicable to the concerned economic activities, including the prospection, cultivation, extraction and exploitation of natural resources''*[477].

Both the *Abaclat* and *Ambiente* tribunals considered that article 1 of the Argentina-Italy BIT defined investment broadly and that the notion of obligation in lit. c) did not exclude sovereign bonds[478]. Similarly, both tribunals agreed that bonds could also fall under lit. f) as they enshrine contractual rights[479].While both *Abaclat* and *Ambiente* tribunals recognised their jurisdiction over the Argentinian sovereign bonds, the case did not move to the merit. In *Abaclat* Argentina preferred settling out of court[480], while *Ambiente* was discontinued for lack of funding[481].

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[475] Agreement between Italy and Argentine Republic for the Promotion and Protection of Investment (signed in Buenos Aires) 1990; *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17); *Abaclat and Others v. Argentine Republic* (n 17).
[476] Agreement between Italy and Argentine Republic for the Promotion and Protection of Investment (signed in Buenos Aires), article 1. Cited in Ortolani (n 81) 391.
[477] Agreement between Italy and Argentine Republic for the Promotion and Protection of Investment (signed in Buenos Aires), article 1. Cited in Ortolani (n 81) 391.
[478] *Abaclat and Others v. Argentine Republic* (n 12), para 354; *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 12), para 491; Ortolani (n 51) 391.
[479] *Abaclat and Others v. Argentine Republic* (n 12), para 354; *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 12), para 491; Ortolani (n 51) 391.
[480] Ortolani (n 51) 384.
[481] ibid.

Thus, while the competence of investment tribunals over sovereign debt is not automatic, the broad language used in BIT definitions of investment, and its generous interpretation in the case-law, means that future investment tribunals are likely to recognise their competence over sovereign debt disputes[482].

This should not however be taken as meaning that ISDS is a friar's balm for creditors. While, the majority of the case law on the competence of investment tribunals on sovereign debt has been in favour of creditors, the recent *Poštová* case[483], casts a doubt as to whether sovereign bonds can be characterised as investments. Moreover, for ISDS to be available, creditors need to be nationals of a State having signed a BIT with the debtor[484] and this BIT needs to not exclude sovereign debt[485], rendering ISDS less certain than domestic litigation.

Despite these uncertainties, access to investment tribunals can be a powerful tool for creditors fearing a debt repudiation. While the competence of domestic courts is limited to breaches of contract, investment tribunals can adjudicate disputes focusing on regulatory interventions by the debtor, regardless of any contractual breach. This is particularly useful when the debtor attempts to legislate upon its bond to modify their content, thus leading to a loss for creditors without any actual breach having occurred.

For example, the *Poštová* case previously mentioned focused on the already discussed retroactive introduction by Greece of a Collective Action Clause in its domestic bonds[486]. This clause lead to all Greek domestic bonds to be restructured, even those whose holders had not consented. Said holders saw the value of their bonds being altered and faced the possibility of a lower return on their bond without any breach of contract having occurred[487]. Absent international litigation, whether before international tribunals[488] or Human Rights Courts[489], this would have left creditors with no judicial recourse against the Hellenic Republic.

Against that background, and despite its inherent uncertainties, the competence of investment tribunals on sovereign debt cases can thus act as a way for the sovereign to

[482] For a more in-depth analysis of BIT drafting on sovereign debt, see chapter 4 and 5.
[483] *Poštová banka, a.s. and Istrokapital SE v. Hellenic Republic (Award)* (n 17).
[484] *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco, Decision on Jurisdiction* (n 458); Schlemmer (n 455).
[485] For a list of treaties explicitly excluding sovereign debt see *Annex I*.
[486] *Poštová banka, a.s. and Istrokapital SE v. Hellenic Republic (Award)* (n 17); Montanaro (n 453).
[487] As the Greek regulatory measure had actively altered the bonds, the contract between Greece and its creditors had technically not been breached.
[488] *Poštová banka, a.s. and Istrokapital SE v. Hellenic Republic (Award)* (n 17).
[489] *Mamatas et autres v. Greece* (n 18).

credibly commit to repayment by enabling creditors to hold the sovereign accountable, even when it relies on its regulatory powers.

3.3.2.3 The European Court of Human Rights and Sovereign Debt

In addition to arbitral tribunals and domestic commercial courts, creditors of sovereigns have also seized the European Court of Human Rights over matters related to sovereign debt[490]. The ECtHR case-law on sovereign debt has been, on average, less discussed by the legal scholarship than the case-law of US courts or Investment tribunals[491]. This is easily explained by a series of reasons. First, the ECtHR case-law on sovereign debt is fairly limited. The Strasbourg court merely ruled on sovereign debt a handful of times, first following the fall of the USSR and the 1990s Russian debt restructuring, including a settlement over the Tsarist debt repudiation[492], and more recently regarding the Greek restructuring[493].

As investment tribunals, Human Rights Courts enable creditors to litigate regulatory actions by the State which impact repayment but are not constitutive of a breach of contract. Again, this allows creditors to potentially obtain a guarantee against a regulatory debt repudiation. However, as opposed to investment tribunals, the competence, *ratione personae* of the ECtHR is not subject to the conclusion of a BIT between the debtor and the creditor's nationals, but merely requires that the creditor falls under the debtor's jurisdiction[494]. Moreover, as far as the case-law of the ECtHR is concerned there seems to be, at today's

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[490] *De Dreux-Brézé c. France* (n 419); *Thivet v. France* (n 419); *Malysh and others v Russia* (n 419); *Mamatas et autres v. Greece* (n 18).
[491] See nevertheless, Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 182–187.
[492] *Malysh and others v Russia* (n 419); *De Dreux-Brézé c. France* (n 419); *Thivet v. France* (n 419). It should be noted that the *Thivet* and De *Dreux-Brézé* cases were not brought directly against the debtor (or in this case its successor) but again France which had agreed to settle the tsarist debt question by treaty with the Russian Federation. Claimants alleged in particular that said treaty was a breach of their rights as protected by article 1 of the first protocol.
[493] *Mamatas et autres v. Greece* (n 18).
[494] It also requires, logically, the debtor to be a signatory to the ECHR. European Convention on Human Rights (Rome) 1950, article 1. In general, the notion of jurisdiction in article 1 is understood in a territorial fashion, meaning that an applicant present on a sovereign's territory will be considered to be in said sovereign's jurisdiction. However, the Court has expanded the notion of jurisdiction so as to encompass cases where applicants were under the control of a respondent State while not on its territory. See e.g. *Banković and others v Belgium and 16 Other contracting States* [2001] European Court of Human Rights 52207/99; *Loizidou v Turkey* European Court of Human Rights 15318/89; Angelika Nußberger, 'The Concept of "Jurisdiction" in the Jurisprudence of the European Court of Human Rights' (2012) 65 Current Legal Problems 241; Marko Milanovic, 'From Compromise to Principle: Clarifying the Concept of State Jurisdiction in Human Rights Treaties' (Social Science Research Network 2008) SSRN Scholarly Paper ID 1139174 <https://papers.ssrn.com/abstract=1139174> accessed 28 January 2020.

date, little doubt that the contractual rights arising from sovereign bonds are protected under article 1 of the first protocol[495].

From a creditor's perspective this means that the competence of Human Rights Courts on sovereign debt cases is more predictable than that of investment tribunals[496]. Finally, examining the competence of the European Court of Human Rights on sovereign debt cases could shed light on potential similar adjudication before other Human Rights Courts or the European Court of Justice[497].

So far, the ECtHR has mostly been seized on the basis of article 1 of the first protocol, protecting the peaceful enjoyment of possessions. Article 1 states:

> *"Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law. The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties."*[498]

For article 1 of the first protocol to apply, *ratione materiae*, sovereign debt contracts need to be characterised as *possessions*[499]. Possessions, in the court's case-law, are depend upon the existence of a substantial economic interest for the applicant[500]. Contractual rights satisfy this condition as "*a 'legitimate expectation' of obtaining an 'asset' may also enjoy the protection of Article 1 of Protocol No. 1*"[501].

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[495] Regarding the European Convention of Human Rights, the language used by article 1 of the first protocol does not guarantee against expropriation *sensu stricto*, but protects the "peaceful enjoyment of possessions". The meaning of this expression will be examined *infra* in this section.

[496] In all of the aforementioned four cases the court recognised its competence in sovereign bond cases. *De Dreux-Brézé c. France* (n 419); *Thivet v. France* (n 419); *Mamatas et autres v. Greece* (n 18); *Malysh and others v Russia* (n 419).

[497] A series of cases related to sovereign debt were brought before the ECJ. In addition to the aforementioned Fahnenbrock case, the court was also seized by Italian claimants following the decision to exempt the bonds held by the European Central Bank from the Greek restructuring process. However, as opposed to the cases which are the focus of this thesis, this specific case did not oppose creditors and the sovereign debt but rather bondholders and the ECB itself. Some of the conclusions drawn from the case by the ECJ will, however, be examined in next part. See *Alessandro Accorinti and others v. European Central Bank* (n 19).

[498] European Convetion on Human Rights (Rome).

[499] For a brief discussion of this case-law and its applicability to sovereign bonds see Belle (n 135).

[500] *Anheuser-Busch Inc v Portugal* [2007] European Court of Human Rights 73049/01, para 63; *Mamatas et autres v. Greece* (n 13), paras 18-20.

[501] *Anheuser-Busch Inc v Portugal* (n 465), para 65; *Mamatas et autres v. Greece* (n 13), paras 18-20.

Hence, sovereign bonds, can be characterised as possessions, if their enforceability is supported by a continuous domestic case-law, as is often the case given their contractual nature [502]. Meaning that, so far, the Strasbourg court has systematically declared its competence over sovereign debt cases.

3.3.2.4 The Competence of International Courts: Overview

Access to courts, in International law, is guaranteed at two levels. First, as the doctrine of sovereign immunities evolved, and as sovereign bonds were interpreted as *acta de iure gestionnis,* International law has enabled creditors to seize domestic courts. Their competence has enabled creditors to access a cheap and reliable dispute settlement forum over which the contractual aspects of sovereign debt could be litigated, and particularly efficient remedies obtained.

Second, international litigation on sovereign debt allows creditors to litigate regulatory measures implemented by the debtor to reduce its debt obligations. The competence of investment tribunals on sovereign debt is heavily debated, and access to an investment tribunal is somewhat uncertain for creditors. However, the *Fedax* and Argentine cases show that ISDS may potentially provide creditors with means to engage the debtor's responsibility beyond mere contract breaches before international jurisdictions. Similarly, the competence of the European Court of Human Rights provides creditors with means to see that their property rights over sovereign debt titles are not violated by debtors.

These multiple *fora* for dispute settlement provide creditors with access to jurisdictions, the first step in ensuring that they obtain the efficient remedies at the centre of the creditor protection model. As regularly pointed out throughout this thesis, this does not only benefit creditors, but also debtors as the credible commitment provided by the creditor protection model enables them to access capital markets under more favourable conditions.

The competence of multiple jurisdictions over sovereign bonds should not however be understood as void of negative consequences. As will be highlighted at the end of chapter 4, this multiplicity of courts and tribunals able to litigate sovereign debt matters creates a risk of fragmentation of the law on sovereign debt[503]. Moreover, litigation before international

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[502] *De Dreux-Brézé c. France* (n 419); *Thivet v. France* (n 419); *Malysh and others v Russia* (n 419); *Mamatas et autres v. Greece* (n 18).
[503] Klabbers (n 23) 146.

courts is potentially highly disruptive to the restructuring process, as will be seen at the end of this chapter.

These weaknesses, however, only manifest when the ability to litigate is abused by holdout creditors. In a world where all stakeholders are incentivised towards bringing the sovereign debtor back to debt sustainability, ensuring that rogue States can be brought before a broad array of jurisdiction enhances the efficiency of the sovereign debt market by incentivising creditors to lend to all sovereigns.

3.3.3 The Sanctity of Creditor Rights in international law

The second condition for functioning of the creditor protection model is the recognition by courts and tribunals of the responsibility of the debtor in case of non-payment. To recall, this recognition requires a combination of three elements: first the existence of obligations tied to repayment, second the recognition of the State's responsibility and third, the inability of the sovereign to empty its obligations from their substance.

As was exposed in the previous section, in domestic law, the recognition of these obligations has been straightforward as the contractual rights of creditors are well established. However, the obligation to repay sovereign debts as enshrined in sovereign bonds or syndicated loan is not an international obligation, but rather a domestic law obligation[504]. International law, however, can potentially provide creditors with a series of rights. First, creditors are protected against unlawful direct or indirect expropriation by the sovereign debtor. The prohibition of unlawful expropriation has been recognised customarily[505], but also in Investment Treaties[506] and Human Rights Treaties[507].

In addition to their rights to property creditors of States can benefit from further treaty-based protections in investment law. If their national State has entered into a BIT with the debtor, creditors usually have a right, to a fair and equitable treatment, national treatment and most-

[504] Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 63.
[505] See e.g *Case concerning the Factory at Chorzow (claim for indemnity) (merits)* (n 40); Reinisch, 'Expropriation' (n 40) 411; Nadakavukaren Schefer (n 40) 196. As underlined by Reinisch, the customary prohibition of expropriation also covers intangible rights. See *Rudloff Case* 9 RIAA 244 (US-Venezuelan Claims Commission).
[506] The US model BIT, for example states "Neither Party may expropriate or nationalize a covered investment either directly or indirectly (…)". 'US Model BIT'. Cited by Nadakavukaren Schefer (n 40) 204.
[507] European Convention on Human Rights (Rome) article 14.

favoured nation treatment[508]. Similarly, if the debtor is a signatory to the European Convention on Human Rights, creditors are also entitled protection against discrimination[509].

While the fact that creditors benefit from those international rights against sovereign debtors is opened to little debate, their exact content within the context of sovereign debt is uncertain. The central issue is that, as previously mentioned, no investment case pertaining to sovereign debt has reached the merit stage. Similarly, the case-law of the European Court of Human Rights on the subject matter has been rather limited.

This dearth of case-law should not however be interpreted as meaning that international law does not burden sovereign debtors with obligations towards their creditors. This section will thus briefly examine how the prohibition of expropriation is applicable to the contractual rights held by creditors of sovereigns, and how standards of treatment contained in BITs similarly apply to creditors. Finally, this section will also examine how the narrow interpretation of economic necessity by international courts signifies that the obligations of debtors cannot easily be circumvented by their reliance on difficult economic circumstances.

3.3.4.1 Expropriation and Sovereign Debt

It has usually been agreed by international courts and tribunals that intangible contractual rights fall within the scope of the prohibition of unlawful expropriation. First, contractual rights are usually explicitly mentioned as a protected category of investment within BITs[510]. Similarly, most of the investment case-law on sovereign debt tends to consider that sovereign bonds are a protected category of investment[511]. Moreover, contractual rights are similarly protected by the customary standard on expropriation[512].

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508 For an overview of the potential rights available to bondholders under BITs see Waibel, 'Opening Pandora's Box' (n 81).

509 European Convention on Human Rights (Rome), protocol 1, article 1.

510 Reinisch, 'Expropriation' (n 40) 410.

511 *Abaclat and Others v. Argentine Republic* (n 17); *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17); *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17); Nakajima (n 81); Ortolani (n 81).

512 On the applicability of the customary prohibition of unlawful expropriation to 'intangible rights' see *Rudloff Case* (n 505); *Case concerning the Factory at Chorzow (claim for indemnity) (merits)* (n 40); *Case concerning certain German interests in Polish Upper Silesia (merits)* (1926) Series A-No 7 Collect Judgm (Permanent Court of International Justice); *Oscar Chinn case (Britain v Belgium)* (1934) 63 PCIJ Ser AB (Permanent Court of International Justice); Reinisch, 'Expropriation' (n 40) 410. It should be noted that a minority of the case-law tends to refuse to link the prohibition of expropriation of contractual rights with the existence of a physical asset. On this question see Waibel, 'Opening Pandora's Box' (n 81) 743. Citing *Starrett Housing Corporation v Iran* (Iran-US Claims Tribunl); *Phelps Dodge International Corp v The Islamic Republic of Iran* (Iran-US Claims Tribunals). This line of decision seems however to be marginal. Similarly, mixed-claims commissions have sometimes refused to recognise that unsecured bonds could be expropriated. See *Compagnie Generale*

The key question, when analysing whether non-payment by a sovereign amounts to expropriation, lies in the distinction between breach of contract and expropriation. Broadly speaking, the case-law on expropriation seems to recognise that the criteria for this distinction lies in the way in which the sovereign acts. For its acts to be characterised as expropriatory, the debtor ought to have relied on its 'sovereign capacity' or its 'public powers'. As such, *"the mere non-performance of a contractual obligation is not to be equated with a taking of property, (...)"*[513].

As far as sovereign debt is concerned, this means that non-payment for economic reasons, or even *mala fide* refusal to pay, may not be tantamount to expropriation[514]. *A contrario*, a repudiation of a sovereign's debt via regulatory means would more likely be characterised as such.

It should be noted that the law on expropriation as it currently stands would protect creditors, not only against direct expropriation, such as a regulatory debt repudiation, but also against indirect expropriation. Indirect expropriation is usually defined as: measures which result in the effective loss of management, use or control, or a significant depreciation of the value, of the assets of a foreign investor'[515]. For example, Greece's recent insertion of a collective action clause within its bonds could be characterised as an indirect expropriation as it resulted in a loss of control of the creditor's rights over their bonds[516].

In the current state of the law, not all expropriatory acts are unlawful. Expropriation is allowed if it is carried out for a public purpose[517], following due process, is non-

des Eaux de Caracas [Belgian Waterworks] v Venezuela (1903) 9 RIAA 333 (Commission Belgium-Venezuela); *Boccardo v Venezuela (Italy v Venezuela)* (1903) 99 Ralston Law Proced 80. Cited in Waibel, 'Opening Pandora's Box' (n 81) 744.

[513] See e.g. *Waste Management, Inc v United Mexican States ('Number 2')* [2004] ICSID ARB(AF)/00/3, para 174; Reinisch, 'Expropriation' (n 379) 418.

[514] Waibel, 'Opening Pandora's Box' (n 81) 745.

[515] Reinisch, 'Expropriation' (n 40) 442.

[516] On this question see Boudreau (n 90); *Mamatas et autres v. Greece* (n 18).

[517] There seems to be a confusion in the case-law on expropriation between public purpose as a condition for the lawfulness of the expropriatory act and public purpose as the differentiating element between a mere breach of contract and an expropriation. Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 745–746. The *Olguin* tribunal notably seemed to consider that mere non-payment did not amount to expropriation as the host State non-performance of a contractual obligation was not accompanied by specific intent. *Eudoro Armando Olguín v Republic of Paraguay* [2001] ICSID ARB/98/5; Waibel, 'Opening Pandora's Box' (n 81) 746; CH Schreuer, 'The Concept of Expropriation under the ETC and Other Investment Protection Treaties' (2005) 2 Transnational Dispute Management (TDM) para 118 <https://www.transnational-dispute-management.com/article.asp?key=596> accessed 29 January 2020. See also, *SGS Société Générale de Surveillance SA v Republic of the Philippines, Decision of the Tribunal on Objections to Jurisdiction* [2004] ICSID ARB/02/6; *CMS Gas Transmission Company v The Republic of Argentina (Award)* [2005] ICSID Tribunal ARB/10/8.

discriminatory and is accompanied by a prompt, adequate and effective compensation[518]. Of these conditions, the most critical from a creditor protection standpoint, is the obtention of a compensation.

At today's date, ICSID case-law tends to consider that payment of an 'adequate' compensation[519] entails payment of the 'market-value' of the expropriated item[520]. Given that the market value of sovereign bonds fluctuates on the secondary market, and given that the bonds of a restructuring sovereigns are usually traded at a discount, it is unlikely that a debt holder would be entitled to the bonds' legal value[521].

Beyond investment and customary law, the property rights of creditors of States part to the ECHR are also protected by article 1 of the first protocol[522]. Article 1 of the first protocol does not prohibit all interference by sovereigns with the property rights of applicants. Rather, it limits said interferences to a set of conditions. First, any interference with the right of applicants must be lawful, *i.e.* based in domestic law and not arbitrary[523]. The interference must also serve a public purpose[524]. Finally, the interference must strike a fair balance between the rights of applicants and the public purpose pursued by the sovereign[525].

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[518] Nadakavukaren Schefer (n 39) 169; W Michael Reisman and Robert D Sloane, 'Indirect Expropriation and Its Valuation in the BIT Generation' (2003) 74 British Yearbook of international law 115, 134.

[519] Compensation in this context differs from compensation as a remedy arising from a breach of international law. While the compensation as a condition for the lawfulness of an expropriation is calculated at the time of the expropriation, compensation as a remedy for breach aims at restoring the injured party to its situation pre-breach of international law. See the discussions in *Amoco International Finance Corporation v The Government of the Islamic Republic of Iran, National Iranian Oil Company, National Petrochemical Company and Kharg Chemical Company* (US-Iran Claims tribunal); cited by Reisman and Sloane (n 483) 136.

[520] It should be noted that the valuation of what constitutes an 'adequate' compensation in international law is heavily debated. A full *exposé* of such debates is unfortunately impossible within the limited contents of this thesis. As such, while this thesis espouses for the sake of its argument that compensation requires payment on the market value of the expropriated item, it does not intend to argue that such a position is universally accepted by investment tribunals. For an overview of these debates see notably Reisman and Sloane (n 518).

[521] Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 301.

[522] *Sensu stricto*, article 1 of the first protocol does not protect property rights, but rather the 'peaceful' enjoyment of possessions. However, *mutatis mutandis*, the protection offered by the ECHR can be understood as following the same purpose as the protection of property in general international law and investment law.

[523] DJ Harris and others, *Harris, O'Boyle & Warbrick: Law of the European Convention on Human Rights* (Third edition, Oxford University Press 2014) 670; *Case of the former King of Greece and others v Greece* [2000] European Court of Human Rights 25701/94; *Jahn and Others v Germany* [2005] European Court of Human Rights 46720/99, 72203/01 and 72552/01; *Špaček, s.r.o v the Czech Republic* (European Court of Human Rights); *Carbonara and Ventura v Italy* (European Court of Human Rights); *Beyeler v Italy* [2000] European Court of Human Rights 33202/96.

[524] The public purpose condition has been interpreted extremely broadly by the Strasbourg court. In practice, only regulatory measures taken "without reasonable foundation" are likely to be found as lacking public purpose. Harris and others (n 488) 668; citing *Jahn and Others v. Germany* (n 488); *Pressos Compania Naviera SA and others v Belgium* [1995] European Court of Human Rights 17849/91.

[525] Harris and others (n 523) 668–672.

As already underlined, the case-law of the European Court of Human Rights does not provide greater clarifications when it comes to whether ordinary sovereign debt restructurings amount to expropriation. The *De-Dreux Brézé* and *Thivet* cases focused on tsarist bonds still held by the applicants in the 1990s[526]. The Court, in both cases, summarily dismissed the applicants' arguments by underlining that following such a length of time, a reasonable investor could not hope to be paid in full on the face value of the bonds[527]. The recent *Mamatas*[528] case fits within the anti-holdout model rather than the creditor protection model.

The only relevant interpretation of article 1 of the first protocol is therefore the one in *Malysh v Russia*[529]. The *Malysh* case finds its source in the economic reforms undertaken by the Gorbashev government and aiming to transition the Russian economy towards the free market. One of these reforms was the emission by the Russian government of "commodity bonds" exchangeable against consumer goods. These bonds were not legal tender *per se*, but had a set nominal value and were transferable. The claimants in *Malysh*, were holders of Urozhay-90 (Harvest 90) bonds, commodity bonds given to agricultural workers in exchange for grain. In 1995, the bonds were recognised by Russia as part of its internal debt in the Commodity Bonds Act. The act also promised repayment within 10 years. In 2000, the Russian federation undertook a vast restructuring process, which culminated in 2009 with the enactment of legislation on the buyout by Russia of its commodity bonds for a fraction of their value[530].

The applicants claimed that Russia's failure to pay, as wells as the legislation it enacted on the bonds ,constituted an infringement of the peaceful enjoyment of their possessions[531]. The Court underlined that:

> *"(the) rule of law underlying the Convention and the principle of lawfulness in Article 1 of Protocol No. 1 require States not only to respect and apply, in a foreseeable and consistent manner, the laws they have enacted, but also, as a corollary of this duty, to ensure the legal and practical conditions for their implementation. In the context of the present case, those principles required the Russian State to fulfil in good time, in an*

[526] *De Dreux-Brézé c. France* (n 419); *Thivet v. France* (n 419).
[527] *De Dreux-Brézé c. France* (n 419); *Thivet v. France* (n 419).
[528] *Mamatas et autres v. Greece* (n 18).
[529] *Malysh and others v Russia* (n 419).
[530] For an overview of the facts of the case see ibid 5–13.
[531] *Malysh and others v Russia* (n 419).

appropriate and consistent manner, the legislative promises it had made in respect of claims arising out of the Urozhay-90 bonds.'[532]

In the paragraph above, the court highlights that it is the passivity of the Russian government when it came to provide actual measures designed to enable repayment of the holders of commodity bonds that was problematic. This passivity regarding payment justifies in the eyes of the court the finding of a breach by the Russian Federation.

The peculiarity of the facts in the *Malysh* case[533] renders the finding of principles applicable to most sovereign debt restructurings difficult. Realistically, all that can be glanced from *Malysh* is that States cannot ignore, for long periods of time, their obligations to creditors. The protection granted by the court is thus fairly minimal as it did not feel the need to pronounce itself more broadly on the protection guaranteed by article 1 as applied to sovereign debt.

It should also be added, regarding the protection of property by the Strasbourg court, that while the proportionality of expropriatory measures entails payment of an adequate compensation to the property-holder, said compensation, as with ICSID tribunals is calculated on the basis of the market value of the expropriated asset[534].

In general, the protection of property rights serves a dual purpose within the creditor protection model. These guarantees against expropriation provide a direct right to creditors, enforceable before international courts *in lieu* of the contractual obligations against the sovereign. Thus, the protection of property can be used by creditors as a substitute to actions for breach of contract. Moreover, the protection of property protects sovereign debt contracts from a debtor's attempt to empty sovereign debt obligations of their substance, either by relying on regulations altering the content of sovereign debt contracts or, as in the *Malysh* case, via the debtor's behaviour.

[532] ibid 82.
[533] Mostly, the fact that Russia for more than 10 years did very little to negotiate with its domestic creditors, and claimed that the inclusion of the Harvest 90 bonds in its internal debt was a 'mistake'.
[534] See e.g. *James and others v the United Kingdom* (European Court of Human Rights); Waibel, 'Opening Pandora's Box' (n 81) 302.

3.3.4.2 Other International Obligations and Sovereign Debt

In addition to the protection of property rights, BITs also protect creditors from discrimination on the basis of their nationality[535]. In particular, National Treatment clauses could prevent a restructuring State from favouring domestic holders of bonds over foreign bondholders protected by a BIT[536]. Similarly, Most Favoured Nation clauses would prevent a restructuring State from discriminating against creditors of a specific nationality, in favour of another group of foreign creditors[537].

While, so far, no arbitral tribunal has examined whether restructuring States have breached the two aforementioned clauses, it can be argued that their insertion in BITs shield foreign creditors against attempts of sovereign to discriminate in order to facilitate repayment. Beyond protection against discrimination, BITs provide creditors with two other shields against reluctant debtors: fair and equitable treatment (FET) clauses and umbrella clauses.

FET clauses are boilerplate BIT dispositions[538] which have been described as 'catch-all provisions for investor protection'[539], whose interpretation is 'surrounded by considerable fog'[540]. Broadly speaking[541], breaches of the clause have been found when sovereigns'

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[535] It should be noted that discrimination, not only on the basis of nationality, but also on other grounds is similarly prohibited under the European Convention on Human Rights. European Convetion on Human Rights (Rome), article 14.

[536] Waibel, 'Opening Pandora's Box' (n 81) 740. Domestic holders of bonds should not be confused with holders of domestic bonds. Holders of domestic bonds might be both nationals of the restructuring States or foreign investors, thus, a State restructuring its domestic debt in a more favourable fashion than its external debt might not breach a domestic treatment clause. On the other hand, were a State to discriminate on the basis of nationality in favour of national holders of its bonds would likely be found to have breached a national treatment clause.

[537] As pointed out by Waibel, such a situation seems unlikely as in most cases a sovereign does not know in advance the identity and nationality of most of its creditors. Thus, if discrimination occurs it will most likely be between national holders of bonds and foreign holders, thus leading to a breach of a national treatment clause or on the basis of acceptance of the restructuration offer. ibid.

[538] Michael Waibel, 'Fair and Equitable Treatment As Boilerplate' (Social Science Research Network 2019) SSRN Scholarly Paper ID 3401770 <https://papers.ssrn.com/abstract=3401770> accessed 29 January 2020. It should be noted that beyond treaty protection a customary fair and equitable protection seems to be recognised as, notably, asserted in the *Neer* case. *L F H Neer and Pauline Neer (USA) v United Mexican States* (1926) IV Rep Int Arbitr Awards 60 (Mexico-USA General Claims Commission); On this question see Todd J Grierson-Weiler and Ian A Laird, 'Standards of Treatment' [2008] The Oxford Handbook of International Investment Law 265–272 <http://www.oxfordhandbooks.com/view/10.1093/oxfordhb/9780199231386.001.0001/oxfordhb-9780199231386-e-8> accessed 29 January 2020; Christoph Schreurer, 'Fair and Equitable Treatment in Arbitral Practice' (2005) 6 Journal of World Investment & Trade 357, 359–364.

[539] Nadakavukaren Schefer (n 39) 327; Rudolf Dolzer, 'Fair and Equitable Treatment: A Key Standard in Investment Treaties' (2005) 39 The international lawyer 87.

[540] Waibel, 'Opening Pandora's Box' (n 81) 748.

[541] Rudolf Dolzer, 'Fair and Equitable Treatment: Today's Contours' (2013) 12 Santa Clara Journal of international law 7; Schreurer (n 545); Waibel, 'Opening Pandora's Box' (n 80) 748.

regulatory activity have lacked transparency[542], when investors legitimate expectations have not been protected[543], when investors have been coerced by the host State[544], when due process has not been respected[545], and when sovereigns acted in bad faith[546].

For creditors, the main advantage of FET clauses is that their operation is independent of a finding of discrimination by the sovereign[547]. Moreover, the catch-all nature of the clause potentially provides debt holders with a variety of potential ways to protect themselves against debt repudiations. Notably, a sovereign reneging upon its debt might be found to act in bad faith. This could also be characterised as a breach of due process, or the debtor's actions could be read as a non-respect of investors legitimate expectations[548].

Beyond treaty breaches, debt holders may be able to rely on umbrella clauses. Umbrella clauses are clauses whose purpose is to, arguably, extend the scope of application, *ratione materiae* of BITs to other obligations States have assumed towards investors[549].

Umbrella clauses typically stipulate that the State should "*observe any obligation it may have entered to*"; "*constantly guarantee the observance of the commitments it has entered into*" or "*observe any obligation it has assumed*"[550].

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542 See e.g. *Emilio Agustín Maffezini v The Kingdom of Spain (award)* [2000] ICSID ARB/97/7; *Técnicas Medioambientales Tecmed, SA (Award)v The United Mexican States* [2003] ICSID arbitral tribunal No. ARB (AF)/00/2; Dolzer (n 539) 92.

543 See e.g. *Electrabel SA v The Republic of Hungary (award)* [2005] ICSID ARB/07/19; *LG&E Energy Corp, LG&E Capital Corp, and LG&E International, Inc .v Argentine Republic (Decision on liability)* [2006] ICSID Tribunal ARB/01/2; *Suez, Sociedad General de Aguas de Barcelona, SA.and Vivendi Universal, SA v Argentine Republic (Award)* [2010] ICSID ARB/03/19; *Saluka Investments BV v The Czech Republic* (UNCITRAL); Dolzer (n 541) 19.

544 See e.g. *Eureko BV v Republic of Poland (partial award)* (ICSID); *Saluka Investments B.V. v. The Czech Republic* (n 550); Ioana Tudor, *The Fair and Equitable Treatment Standard in the international law of Foreign Investment* (Oxford University Press 2008) 169.

545 Including the provision by the host State of a stable and predictable legal framework. See e.g. *Técnicas Medioambientales Tecmed, S.A. (Award) v. The United Mexican States* (n 547); *CMS Gas Transmission Company v. The Republic of Argentina (Award)* (n 522); Tudor (n 549) 171; *Siemens AG v The Argentine Republic (award)* [2007] ICSID ARB/02/8.

546 On the relationship between FET clauses and good faith see Martins Paparinskis, 'Good Faith and Fair and Equitable Treatment in International Investment Law' (Social Science Research Network 2014) SSRN Scholarly Paper ID 2512664 <https://papers.ssrn.com/abstract=2512664> accessed 25 September 2017. Commenting on *Técnicas Medioambientales Tecmed, S.A. (Award)v. The United Mexican States* (n 506); *TECO Guatemala Holdings, LLC v Republic of Guatemala* [2013] ICSID arbitral tribunal ARB/10/23; *Ioan Micula, Viorel Micula, SC European Food SA, SC Starmill SRL and SC Multipack SRL v Romania* [2013] ICSID arbitral tribunal ARB/05/20.

547 Waibel, 'Opening Pandora's Box' (n 81) 748.

548 That is if the debt repudiation is the result of the sovereign acting in a public capacity and not in a commercial capacity. Again, treaty dispositions do not, in general, shield investors from mere contract breach.

549 Irmgard Marboe and August Reinisch, 'Contracts between States and Foreign Private Law Persons', *Max Planck Encyclopedia of Public international law* (Oxford University Press 2011).

550 See the study of umbrella clause drafting in Katia Yannaca-Small, 'Interpretation of the Umbrella Clause in Investment Agreements' (2006) 3 , OECD Working Papers on International Investment.

While the effect of umbrella clauses has been heavily debated, it is generally agreed that they “elevate” contractual obligations owed by the host to the status of treaty obligations[551]. Thus, while generally the competence of an international investment tribunal is not triggered by a mere breach of contract, umbrella clauses bring those contractual obligations within the scope of application *ratione materiae* of BITs. This enables investors to seize international tribunals when their contractual rights have been breached[552].

Again, there has been little substantial case-law on the application of umbrella clauses to sovereign debt contracts[553]. Umbrella clauses have the potential to enable creditors to seize international investment tribunals not only for breaches of treaty obligations, but also for breaches of contract. In effect, such clauses could ‘internationalise’ the payment obligation enshrined in sovereign bonds, thus making it directly enforceable before investment tribunals. Umbrella clauses, thus participate in the recognition of the enforceability of payment obligations arising from sovereign debt contracts[554].

3.3.4.3 Circumstances Absolving the Debtor for Breaches of International Obligations: Economic Necessity

The recognition by courts and tribunals that States have obligations towards their creditors is not sufficient to guarantee that creditors obtain efficient remedies enticing them to partake in sovereign lending. In addition, courts must recognise the sovereign’s responsibility when these obligations are left unfulfilled. When it comes to sovereign debt, the main defence available to States is to claim that the breach of creditors’ rights arose as a result of economic necessity.

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[551] Marboe and Reinisch (n 513); Rudolf Dolzer and Margrete Stevens, *Bilateral Investment Treaties* (Brill 1995) 81–82; Christoph Schreuer, ‘Travelling the BIT Route: Of Waiting Periods, Umbrella Clauses and Forks in the Road’ (2004) 5 The Journal of World Investment & Trade vii; see e.g. *Fedax NV v The Republic of Venezuela* [1998] ICSID ARB/96/3; *SGS Société Générale de Surveillance S.A. v. Republic of the Philippines, Decision of the Tribunal on Objections to Jurisdiction* (n 482); *CMS Gas Transmission Company v. The Republic of Argentina (Award)* (n 482); *Enron Corporation and Ponderossa Assets LP v Argentine Republic (Award)* (ICSID Tribunal); *Sempra Energy International v The Argentine Republic (Award)* [2007] ICSID Tribunal ARB/02/16.

[552] Again, it should be noted that the effect of umbrella clauses has been the object of heavy debates both in the investment law scholarship and in the case-law. The position articulated *supra*, seems however to be the most commonly shared within the field. For other interpretations see e.g. *SGS Société Générale de Surveillance SA v Islamic Republic of Pakistan (decision on jurisdiction)* (ICSID); *Joy Mining Machinery Limited v Arab Republic of Egypt (award on jurisdiction)* [2004] ICSID ARB/03/11. See also in general Schreuer (n 515); Yannaca-Small (n 514).

[553] The Fedax case, notably, was brought against Venezuela on the basis of an umbrella clause, however the debates on the application of the clause were limited. *Fedax N.V. v. The Republic of Venezuela* (n 551).

[554] On the relationship between “commitment” and umbrella clauses see also Thomas W Walde, ‘The Umbrella Clause in Investment Arbitration: A Comment on Original Intentions and Recent Cases’ (2005) 6 Journal of World Investment & Trade 183.

Necessity, as a defence, is invoked to preclude the wrongfulness of an international act that might otherwise have led to the recognition a State's responsibility[555]. The purpose of the necessity defence is to allow States to act in what would normally be a breach of international law in order to protect themselves against grave and imminent perils[556].

The necessity defence is enshrined in article 25 of the ILC articles on State responsibility[557] reading:

"1. Necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act:

(a) is the only way for the State to safeguard an essential interest against a grave and imminent peril; and

(b) does not seriously impair an essential interest of the State or States towards which the obligation exists, or of the international community as a whole.

2. In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:

(a) the international obligation in question excludes the possibility of invoking necessity; or

(b) the State has contributed to the situation of necessity."[558]

Article 25, has been recognised by the ICJ as codifying customary international law[559]. It lists a series of conditions for the successful invocation of the necessity defence. Given the

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[555] international law Commission, 'Draft Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries' <http://legal.un.org/ilc/texts/instruments/english/commentaries/9_6_2001.pdf>; Attila Tanzi, 'Necessity, State Of', *Max Planck Encyclopedia of Public international law* (Oxford University Press 2013); August Reinisch, 'Necessity in Investment Arbitration' (2010) 41 Netherlands Yearbook of international law 137; Tarcisio Gazzini, Wouter G Werner and Ige F Dekker, 'Necessity Across international law: An Introduction' in IF Dekker and E Hey (eds), *Netherlands Yearbook of international law Volume 41, 2010: Necessity Across international law* (T M C Asser Press 2011) <https://doi.org/10.1007/978-90-6704-737-1_1> accessed 15 May 2019.

[556] international law Commission, 'Draft Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries' (n 562); Tanzi (n 562).

[557] international law Commission, 'Draft Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries' <http://legal.un.org/ilc/texts/instruments/english/commentaries/9_6_2001.pdf> 71.

[558] ibid 80.

[559] *Case concerning the Gabcikovo-Nagymaros Project (Hungary/Slovakia)* (1997) 1997 ICJ Rep 7 (International Court of Justice) para 49; *Legal Consequences of the Construction of a Wall in the Occupied Palestinian Territory (Advisory Opinion)* 2004 ICJ Rep 136 (International Court of Justice) para 140; Reinisch

exceptional nature of the defence, the article ought to be interpreted narrowly and the conditions are cumulative[560].

First, the act for which the State invokes the necessity defence must be the only way via which a State could protect itself against a grave and imminent peril. Therefore, the necessity defence will not be available to a State if other less convenient means of protecting its interests were available[561]. Necessity must be invoked to protect an essential interest of the State, the essential nature of the interest being decided on a case by case basis[562]. In addition, the peril against which the State is acting ought to be grave and imminent, meaning that the danger must be certain, and not of a long-term or hypothetical nature[563].

Second, as underlined by article 25, 1, b), the necessity defence will be refused to a State for breaches of peremptory norms of International law[564], or if reliance on necessity is precluded by treaty[565]. Finally, the invocation of the necessity defence will fail if the State invoking it has contributed to the situation of necessity[566].

Once successfully invoked, necessity shields a State from international responsibility as long as the situation from which necessity arose lasts. Once this situation has passed, compliance with the international obligation is, once again, mandatory. Furthermore, compensation is owed for any loss encountered by the party to which the obligation was due, as per article 27[567].

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and Binder (n 24) 6; Christina Binder, 'Stability and Change in Times of Fragmentation: The Limits of Pacta Sunt Servanda Revisited international law and Practice' (2012) 25 Leiden Journal of international law 909.

[560] *Case concerning the Gabcikovo-Nagymaros Project (Hungary/Slovakia)* (n 559) para 51; Tanzi (n 555); Reinisch, 'Necessity in Investment Arbitration' (n 555).

[561] international law Commission (n 4), article 25, commentary para. 15; Reinisch and Binder (n 6) 39.

[562] international law Commission (n 4), article 25, commentary para. 15; Attila Tanzi, 'Necessity, State of', *Max Planck Encyclopedia of Public international law* (Oxford University Press 2013).

[563] *Case concerning the Gabcikovo-Nagymaros Project (Hungary/Slovakia)* (n 523) para 54; Matthew Parish, 'On Necessity' (2010) 11 Journal of World Investment & Trade 169.

[564] international law Commission (n 4), article 26; Tanzi (n 519).

[565] Tanzi (n 555).

[566] *Case concerning the Gabcikovo-Nagymaros Project (Hungary/Slovakia)* (n 523) para 40, citing Yearbook of the international law Commission, 1980, Vol. II, Part 2, p. 34.

[567] international law Commission (n 4), article 27; Tanzi (n 8); Reinisch and Binder (n 6). This obligation to compensate must be distinguished from full reparation following the breach of an international obligation, since article 27 does not, for example, encompass lost profits. This obligation to compensate must be distinguished from full reparation following the breach of an international obligation, since article 27 does not, for example, encompass lost profits

Because of those narrow conditions, reliance on necessity in economic matters, while technically possible is often difficult, as evidenced by a series of early 20th century cases[568].

In the *French Company of Venezuelan Railroads* case[569] France acted in diplomatic protection of a French company against Venezuela. The latter had requisitioned equipment belonging to the Company during a civil war. Venezuela claimed that necessity absolved it from said contractual obligations and the arbitral tribunal agreed, underlying that "*[Venezuela's] first duty was to itself. Its own preservation was paramount.*"[570].

In the *Société Commerciale de Belgique* case[571], Greece argued that economic necessity shielded it against the responsibility arising from late payment of arbitral awards to a Belgian Company. Greece posited, *inter alia*, that paying the aforementioned awards would alter the "*normal functioning of its public service*"[572]. Interestingly, while the PCIJ declined to review the case of jurisdictional grounds, Belgium had not contested Greece's argument[573].

The applicability of the necessity defence in economic circumstances has been the object of an often-contradictory case-law before ICSID tribunals. The cases were brought, mainly, following the 2000s Argentine financial crisis, thus justifying their analysis here. They all

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568 A series of early cases has also concerned *force majeure* in an economic context. While *force majeure* and necessity have been used interchangeably by the early XXth century international case-law, the present section will only focus on the cases which concerned what would, today, fall under necessity. As opposed to necessity, force majeure refers to a material impossibility to fulfil international obligations due to elements external to the States' conduct. See, international law Commission, '"Second Report on State Responsibility by Mr. James Crawford, Special Rapporteur (Addendum) A/CN.4/498/Add.2"' <https://www.ilsa.org/jessup/jessup13/James%20Crawford's%20Second%20Report%20on%20State%20Responsibility.pdf>; Simon Hentrei and Ximena Soley, 'Force Majeure', *Max Planck Encyclopedia of Public international law* (Oxford University Press 2011); *Case Concerning the payment of various serbian loans issued in France (France v Serbia)* (n 196); *Russian Claim for Indemnities: Arrears of interest claimed by Russia in indemnities due individuals injured in the war or 1877-1878 (Russia v Turkey)* (1912) 11 Rep Int Arbitr Awards 421 (Permanent Court of Arbitration).

569 *French Company of Venezuelan Railroads Case (France v Venezuela)* (n 96); 'Addendum - Eighth Report on State Responsibility by Mr. Roberto Ago, Special Rapporteur - the Internationally Wrongful Act of the State, Source of International Responsibility (Part 1)', *Yearbook of the international law Commission*, vol II (1980) <<http://legal.un.org/ilc/documentation/english/a_cn4_318_add5-7.pdf>>; Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2).

570 *French Company of Venezuelan Railroads Case (France v Venezuela)* (n 96), p. 535. The tribunal also underlined that Venezuela had not intended to injure or harm the French company by taking action, justifying the application of the necessity defence.

571 *Société Commercial de Belgique (Belgium v Greece)* (1939) A/B 78 Perm Court Int Justice Judgm Orders Advis Opin 159 (Permanent Court of International Justice); cited in 'Addendum - Eighth Report on State Responsibility by Mr. Roberto Ago, Special Rapporteur - the Internationally Wrongful Act of the State, Source of International Responsibility (Part 1)' (n 534) para 28; Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2).

572 *Société Commercial de Belgique (Belgium v Greece)* (n 537); cited in'Addendum - Eighth Report on State Responsibility by Mr. Roberto Ago, Special Rapporteur - the Internationally Wrongful Act of the State, Source of International Responsibility (Part 1)' (n 534) para 28.

573 'Addendum - Eighth Report on State Responsibility by Mr. Roberto Ago, Special Rapporteur - the Internationally Wrongful Act of the State, Source of International Responsibility (Part 1)' (n 569).

stemmed from a similar factual background: the measures enacted by Argentina following the crisis, and in particular the suspension of the peso-dollar convertibility which was legally guaranteed at the time[574]. Given that ICSID tribunals have recognised their jurisdiction[575] over sovereign debt cases, understanding the ICSID case-law on necessity is a required step to understand how creditor protection is achieved in international law.

The interpretation of the necessity defence within international investment law is linked to a first issue: the articulation of the customary standard with *ad hoc* necessity clauses within BITs[576]. The debate within the case-law is centred on whether necessity clauses within treaties import within the dispute a standard of interpretation different from the customary necessity defence[577].

The necessity clause in the US-Argentina BIT, at stake in the cases analysed here, reads:

> *"This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the Protection of its own essential security interests."*[578]

The articulation between the two dispositions was settled in the *Sempra*[579] annulment decision. It was decided by the committee that priority should be given to the treaty over the customary standard as the first operates as a form of *lex specialis*. The customary standard, however, remained used by arbitral tribunals in order to interpret the necessity defence featured in article XI[580].

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574 Waibel, 'Two Worlds of Necessity in ICSID Arbitration' (n 27); Asif H Qureshi, 'A Necessity Paradigm of "Necessity" in International Economic Law' in IF Dekker and E Hey (eds), *Netherlands Yearbook of international law Volume 41, 2010: Necessity Across international law* (T M C Asser Press 2011) <https://doi.org/10.1007/978-90-6704-737-1_5> accessed 15 May 2019.

575 *Abaclat and Others v. Argentine Republic* (n 5); *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 5); Ortolani (n 139).

576 Waibel, 'Two Worlds of Necessity in ICSID Arbitration' (n 29); Reinisch, 'Necessity in Investment Arbitration' (n 555); *LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc .v. Argentine Republic (Decision on liability)* (n 543); *Enron Corporation and Ponderossa Assets L.P. v Argentine Republic (Award)* (n 551); *Sempra Energy International v. The Argentine Republic (Award)* (n 551).

577 Waibel, 'Two Worlds of Necessity in ICSID Arbitration' (n 29); Reinisch, 'Necessity in Investment Arbitration' (n 555).

578 Treaty between the United-States of America and the Argentine Republic concerning the Reciprocal Encouragement and Protection of Investment (Buenos Aires) 1991.

579 See *Sempra Energy International v. The Argentine Republic (Award)* (n 515) para 348.

580 ibid; Reinisch and Binder (n 30). A similar reasoning is applied in the *Suez* decision, also involving Argentina, with a similar factual background but on the basis of the France-Italy BIT. *Impregilo S.pA v Argentine Republic (Award)* [2011] ICSID ARB/07/17.

In *CMS*[581] the arbitral tribunal refused to grant Argentina the benefit of the necessity defence. Interpreting necessity under the light of the customary standard, it underlines that the actions undertaken by Argentina to stabilise its financial situation did not constitute "the only way" via which Argentina could avert the effects of the crisis[582]. This is despite the fact that the tribunal recognised that "*the situation was difficult enough to justify the government taking action to prevent a worsening of the situation and the danger of total economic collapse*"[583]. Similarly, the tribunal was not convinced that Argentina had not contributed to its own damage[584].

The reasoning justifying this narrow interpretation of the customary standard in *CMS* underlines the economic logic behind its narrow interpretation of the necessity defence. The tribunal notes:

> *"If strict and demanding conditions are not required or are loosely applied, any State could invoke necessity to elude its international obligations. This would certainly be contrary to the stability and predictability of the law"*[585].

Similarly, in *Enron*[586], the arbitral tribunal justifies interpreting article XI of the US-Argentina BIT narrowly by invoking the object and purpose of the treaty. It states that:

> *"[T]he object and purpose of the Treaty is, as a general proposition, to apply in situations of economic difficulty and hardship that require the protection of the international guaranteed rights of its beneficiaries. To this extent, any interpretation resulting in an escape route from the obligations defined cannot be easily reconciled with*

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[581] *CMS Gas Transmission Company v. The Republic of Argentina (Award)* (n 517).
[582] ibid para 33; See also *Suez, Sociedad General de Aguas de Barcelona, S.A.and Vivendi Universal, S.A. v. Argentine Republic (Award)* (n 507); *Total SA v The Argentine Republic (Decision on liability)* [2010] ICSID ARB/04/01; Waibel, 'Two Worlds of Necessity in ICSID Arbitration' (n 23) 645-646; Reinisch, 'Necessity in Investment Arbitration' (n 519) 200-201.
[583] *CMS Gas Transmission Company v. The Republic of Argentina (Award)* (n 482), para 322.
[584] ibid para 329; Waibel, 'Two Worlds of Necessity in ICSID Arbitration' (n 23) 642; Reinisch, 'Necessity in Investment Arbitration' (n 519) 203. See also *Suez, Sociedad General de Aguas de Barcelona, S.A.and Vivendi Universal, S.A. v. Argentine Republic (Award)* (n 543); *Impregilo S.p.A. v. Argentine Republic (Award)* (n 580); Binder (n 559); *El Paso Energy International Company v The Argentine Republic (Award)* [2011] ICSID ARB/03/15. It should be noted that the CMS tribunal has relied on Argentina's difficult economic circumstances at the time of the breach to lower the amount of compensation owed to CMS. For a critique of this decision see Waibel, 'Two Worlds of Necessity in ICSID Arbitration' (n 29) 644.
[585] *CMS Gas Transmission Company v. The Republic of Argentina (Award)* (n 482) para 317.
[586] *Enron Corporation and Ponderossa Assets L.P. v Argentine Republic (Award)* (n 551).

that object and purpose. Accordingly, a restrictive interpretation of any such alternative is mandatory."[587]

The arbitral tribunal in *Sempra*, concurs, also relying on the object and purpose of the BIT to justify interpreting the BIT standard of necessity in light of the customary standard.[588]

Both tribunals, in *Enron* and *Sempra* ruled that the economic crisis unfolding in Argentina did not reach a sufficient threshold to trigger the necessity defence under the customary standard, since the very existence of Argentina was not at stake because of the crisis[589]. In addition, they underlined, as in *CMS* , that the actions taken by Argentina did not constitute the only way to prevent the damage caused by the financial crisis and that Argentina had contributed to said damage.[590]

Overall, most arbitral tribunals[591] seemed reluctant, given the narrow conditions of the necessity defence, to recognise that Argentina's actions and circumstances could amount to a State of necessity. While these cases have not focused on sovereign debt *per se*, their interpretation matters highlights the difficulty of debtors to rely on necessity to avoid their payment obligations. The argument advanced by commentators is that necessity is an ill-

[587] ibid, para 331.
[588] *Sempra Energy International v. The Argentine Republic (Award)* (n 515), para 300; Bart M Szewczyk, 'Sempra Energy International v. Argentine Republic' (2011) 105 American Journal of international law 547.
[589] *Enron Corporation and Ponderossa Assets L.P. v Argentine Republic (Award)* (n 515), para 299; *Sempra Energy International v. The Argentine Republic (Award)* (n 515), para 338; See also *Total S.A. v. The Argentine Republic (Decision on liability)* (n 549).
[590] *CMS Gas Transmission Company v. The Republic of Argentina (Award)* (n 517); *Enron Corporation and Ponderossa Assets L.P. v Argentine Republic (Award)* (n 551); *Sempra Energy International v. The Argentine Republic (Award)* (n 551).
[591] Contra e.g. *Continental Casualty Company v The Argentine Republic* [2011] ICSID ARB/03/9. See *infra* Part III. LG&E fits somewhat uneasily within the creditor protection/anti-holdout dichotomy exposed here. On the one hand, the LG&E tribunal relies on the customary criteria to interpret the BIT necessity defence, indicating a desire for creditor protection. On the other hand, its interpretation of the criteria, *in casu*, is sufficiently broad that it concludes that Argentina's responsibility should be absolved. Notably, it interpreted the essential interest criteria as shielding sovereign interests broader than those related to security. It notes in that regard "*To conclude that such a severe economic crisis could not constitute an essential security interest is to diminish the havoc that the economy can wreak on the lives of an entire population and the ability of the Government to lead. When a State's economic foundation is under siege, the severity of the problem can equal that of any military invasion." LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc .v. Argentine Republic (Decision on liability)* (n 543) para 238. Overall, the tribunal in LG&E also opts for a particularly 'hands-off' approach when it comes to assessing Argentina's governments, in particular in its assessment of the 'only way' criteria. However, as with the French Company case, it can reasonably be argued that it is less the interpretation of the tribunal which led to Argentina's responsibility to be expunged and more the specific circumstances of the case, in particular the severity of the Argentinean crisis. Read as such, LG&E would be interpreted as fitting within the creditor protection model, despite the sovereign's responsibility not being recognised. For a broader comment on LG&E see Waibel, 'Two Worlds of Necessity in ICSID Arbitration' (n 29).

fitted defence for debtor States[592]. The high threshold[593] it requires makes its application to sovereign debt cases difficult, and the ICSID cases on necessity are a prime example of this phenomenon.

The narrow interpretation of the necessity defence strengthens the rights of creditors when sovereigns face dire financial situations, and enhances the predictability of their circumstances. As highlighted by the *CMS*[594] and *Enron* tribunals[595], the predictability of the rights granted to investors in BITs requires that these rights remain enforceable even in cases where the sovereign debtor is in difficult circumstances. As such, the logic of the *CMS* and *Enron* tribunals is similar to the original sin hypothesis mentioned *supra*[596]. As the purpose of creditor protection is to reduce the political risk linked to contracting with sovereigns, and as sovereigns facing economic hardship are more likely to violate creditor's righs, to be efficient the remedies granted to creditors must be efficient in such circumstances[597].

The problem with this logic is that limiting the ability of States to curb the rights of creditors when they are in difficult financial circumstance can sometimes prevent debtors from enacting measures that could shield their population from the damages caused by a financial crisis. In that context, such a narrow reading of the necessity defence, one that requires the very existence of the sovereign to be at stake to be triggered, could be counter-productive as it deters States from preventatively acting in order to limit the often dire consequences of a sovereign debt crisis.

3.3.4 Efficient Remedies in international law

The final condition for the creditor protection model to function is the obtention by creditors of efficient remedies designed to coerce States into repayment. As far as international law is concerned, two broad types of remedies are available to creditors. The first is the seizing of the debtor's assets by creditors, the second is the obtention of damages.

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[592] See in general Waibel, 'Two Worlds of Necessity in ICSID Arbitration' (n 29).
[593] For a brief exposé of Argentina's economic situation, contrasted with arbitral decisions and the "grave and imminent" nature of Argentina's peril see: Qureshi (n 574).
[594] *CMS Gas Transmission Company v. The Republic of Argentina (Award)* (n 517).
[595] ibid; *Enron Corporation and Ponderossa Assets L.P. v Argentine Republic (Award)* (n 551).
[596] Also known as the original sin theory. Eichengreen, Haussman and Panizza (n 114); Flandreau and Sussman (n 114).
[597] Qureshi (n 574); Andrea K Bjorklund, 'Emergency Exceptions: State of Necessity and Force Majeure' [2008] The Oxford Handbook of International Investment Law <https://www.oxfordhandbooks.com/view/10.1093/oxfordhb/9780199231386.001.0001/oxfordhb-9780199231386-e-12> accessed 15 May 2019.

3.3.4.1 Immunity from Execution and Sovereign Debt

As with immunities from jurisdiction, international law has evolved towards restricting sovereign immunities from execution. The current state of the law is that, while immunity remains the norm, assets owned by the sovereign and used for commercial purposes are not protected from attachment attempts[598]. The key element for the distinction between assets used for 'commercial purpose' and those use for 'governmental purpose other than commercial' lies in the nature of the asset on which execution is attempted[599].

Sovereigns' immunity of execution can be contractually waived, and are waived in sovereign bonds[600]. Said waiver ought to be express and cannot be inferred from a waiver of jurisdictional immunity[601].

The restrictive theory applied to execution fits within the creditor protection model, as it enables creditors to obtain the sums via which they can obtain payment by attaching the debtor's assets. In practice, finding assets on which judgments can be executed has proven a particularly complex task for creditors[602], as shown once again by *NML*.

In Belgium and France, notably, NML sought to attach the sums held by the Argentine embassy in several banks[603]. Argentina, in its bonds, had waived it immunity of execution. However, both Belgian and French courts ruled that accounts held by diplomatic missions,

598 Stoll (n 424).

599 *Jurisdictionnal Immunities of the State (Germany v. Italy; Greece intervening)* (n 384) para 118; Stoll (n 388); James Crawford, 'Execution of Judgments and Foreign Sovereign Immunity' (1981) 75 American Journal of international law 820; international law Commission, 'Comments and Suggestions by the Working Group on Jurisdictional Immunities of States and Their Property', *'Report of the international law Commission on the Work of its 51st Session.* (1999); Kupelyants (n 409) 287–288.

600 On immunity waivers Weidemaier, 'Sovereign Immunity and Sovereign Debt' (n 47); Delaume (n 52) 812; Kupelyants (n 33) 288–289. For a court interpretation see See e.g. *A Company v Republic of X* (1990) 2 Lloyd's Rep 520 (Queen's Bench Division (commercial court)).

601 Most modern immunity waivers tackle both immunity from jurisdiction and immunity from execution. The typical boilerplate immunity waiver in sovereign bonds is similar to the following:
"*To the extent that the Republic may in any jurisdiction claim or acquire for itself or its assets immunity (sovereign or otherwise) from suit, execution, attachment (whether in aid of execution, before judgment or otherwise) or other legal process (whether through service or notice or otherwise), the Republic irrevocably agrees for the benefit of the Holders of Notes not to claim, and irrevocably waives, such immunity, to the fullest extent permitted by the laws of such jurisdiction.*". Merrill Lynch Int'l, U.S. $22,000,000,000 The Lebanese Republic Global Medium-Term Note Program 104 (2009) quoted in Weidemaier (n 99) 87, at note 126.

602 Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 124; 154–155; Jeremy Ostrander, 'The Last Bastion of Sovereign Immunity: A Comparative Look at Immunity from Execution of Judgements Notes and Comments' (2004) 22 Berkeley Journal of international law 541.

603 *République d'Argentine c. NML Capital LTD* (n 407); *Société NML Capital c. République d'Argentine* (n 407); *Société NML Capital c. République d'Argentine* (n 407); *Société NML Capital c. République d'Argentine* (n 407); *NML Capital Ltd c. République d'Argentine* (n 407).

in virtue of the principle *ne impediatur legatio*, were protected by a special immunity which could only be waived expressly, and not by a general immunity waiver[604].

Beyond diplomatic accounts, creditors of sovereigns have also sought to obtain payment on the foreign exchange accounts of central banks[605]. The case-law on the immunity of central bank accounts is particularly complex given that, on the one hand, central banks act usually with a public purpose[606] while, on the other hand, the nature of the acts of central banks is usually private[607]. To further muddy the waters, the relationship between governments and central banks, including their degree of independence, varies heavily from State to State[608].

Broadly speaking, the degree of immunity accorded to central banks varies heavily. Some States grant central bank assets a broad protection. The UK notably, provides a near-absolute immunity to central bank assets[609]. The US similarly protects assets of a central bank "*held for its own account (...) or its parent government*"[610]. This immunity does not protect

[604] See *Société NML Capital c. République d'Argentine* (n 407); *Société NML Capital c. République d'Argentine* (n 407); *Société NML Capital c. République d'Argentine* (n 407); *NML Capital Ltd c. République d'Argentine* (n 407). On the special nature of accounts held by diplomatic legations and their impact on sovereign debt processes see e.g. Bonafè (n 82); Pierre D'Argent, 'Saisie de Comptes d'ambassade, Immunité d'exécution et Renonciation Contractuelle.' 2013/15 Journal des Tribunaux 290. NML sought to contest before the ECtHR the compatibility of jurisdictional immunities with article 6 of the Convention, but the claim was ultimately dismissed by the Strasbourg court. *NML capital LTD v France* European Court of Human Rights 23242/12.

[605] Paul L Lee, 'Central Banks and Sovereign Immunity' (2002) 41 Columbia Journal of Transnational Law 327, 327.

[606] Broadly speaking, implementing monetary policy, but also acting as guarantors of the stability of the financial system by providing lending in last resort.

[607] Notably, the purchase and holding of low-risk securities. Ernest T Patrikis, 'Foreign Central Bank Property: Immunity from Attachment in the United States Symposium: Default by Foreign Government Debtors' (1982) 1982 University of Illinois Law Review 265, 265.

[608] For an overview of the case law on central bank immunities see Lee (n 605); Thomas Baxter and David Gross, 'Special Immunities: Central Bank Immunity'', *Sovereign Debt Management. R. Lastra, L. Buchheit (eds)* (Oxford University Press 2014); Patrikis (n 607).

[609] Section 14(4) of the Sovereign Immunities Act States: "Property of a State's central bank or other monetary authority shall not be regarded for the purposes of subsection (4) of section 13 above as in use or intended for use for commercial purposes; and where any such bank or authority is a separate entity subsections (1) to (3) of that section shall apply to it as if references to a State were references to the bank or authority". However, the immunity of the central bank assets can be lifted via an explicit waiver. See also *AIG Capital Partners Inc v Republic of Kazakhstan* (2006) 1 WLR 1420 (England and Wales High Court (Commercial Court)); Kupelyants (n 53) 294; Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 55–57.

[610] *EM LTD, NML Capital, Ltd, Plaintiffs–Appellees, v BANCO CENTRAL DE LA REPÚBLICA ARGENTINA, Republic of Argentina, Defendants–Appellants* (2011) 652 F 3d 172 (US Court of Appeals Second Circuit); Ingrid Brunk Wuerth, 'Immunity from Execution of Central Bank Assets', *The Cambridge Handbook of Immunities and international law. T. Ruys, N. Angelet, L. Ferro* (Cambridge University Press 2019) 272. For an overview of the US case-law on central bank immunities see Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 46–54.

holdings of central banks used for commercial banking purposes[611]. This specific immunity of central bank assets can, like diplomatic immunities, be waived contractually[612].

In theory these limits to sovereigns' immunity of execution favours creditors, as it provides them with more potential attachable assets. In practice, however, the seizure of State's property has not proved a particularly efficient way of obtaining repayment for creditors. First, the discovery of such assets is both an uncertain and costly prospect. It is made especially more difficult by the fact that the sovereign against which enforcement is sought is both facing economic difficulties[613] and might be reluctant to have said assets seized[614]. Beyond these material difficulties, the byzantine case-law briefly on specific immunities adds another layer of uncertainty for creditors. In particular, the contradictions in the case-law on embassy and central bank accounts, two of the most common form foreign sovereign monetary holdings, makes it impossible for creditors to know, *ex ante*, if the costs tied to enforcing judgments abroad are worth undertaking.

3.3.4.2 Remedies arising from Investment and Human Rights Law

Beside the attachment of goods or funds belonging to sovereigns, international law provides creditors with one other main type of remedy: damages.

Damages[615], within the ICSID system (and generally in international law), are traditionally understood to be compensatory and not punitive[616]. This means that the purpose of damages is to restore the victim of a breach of an international obligation as close as possible to the situation said victim would have been in, were the breach not to have occurred. To quote the famous Chorzow factory dictum:

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611 Wuerth (n 610) 272.
612 See *EM LTD., NML Capital, Ltd., Plaintiffs–Appellees, v. BANCO CENTRAL DE LA REPÚBLICA ARGENTINA, Republic of Argentina, Defendants–Appellants.* (n 610).
613 And might therefore liquidate some of its foreign holdings.
614 And could therefore either seek to keep them hidden or to hold them in such a way as to make attachment more difficult.
615 Damages, within this section are understood as "the legal duty to pay for the detrimental consequences that the victim of an unlawful act has suffered". Compensation, on the other hand refers to sums of money awarded to claimants as "financial reparation for expropriatory or quasi-expropriatory conduct. Hence, damages are the remedy granted to claimants as a reparation for breaches of their rights, while compensation is a condition for the lawfulness of expropriation measure. On this question see Thomas W Wälde and Borzu Sabahi, 'Compensation, Damages, and Valuation' [2008] The Oxford Handbook of International Investment Law 1052 <http://www.oxfordhandbooks.com.ezproxy.lib.gla.ac.uk/view/10.1093/oxfordhb/9780199231386.001.0001/oxfordhb-9780199231386-e-26> accessed 25 March 2019.
616 *Case concerning the Factory at Chorzow (claim for indemnity) (merits)* (n 40); Wälde and Sabahi (n 615).

> *"The essential principle contained in the actual notion of an illegal act—a principle which seems to be established by international practice and in particular by the decisions of arbitral tribunals—is that reparation must, as far as possible, wipe out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that act had not been committed."*[617]

There are two issues when it comes to the award of compensatory damages to creditors. The first is the valuation of the damage to creditors arising from a sovereign's breach of a treaty obligation, the second is the enforcement of arbitral awards.

The purpose of damages in International Investment Law being the compensation of the economic loss suffered by the investor, a tribunal in a sovereign debt case will need to determine the value of the bondholder's investment. The way investments are valued by arbitral tribunals is usually by reference to their 'fair market value', understood as a '*reasonable price that would normally be paid by a willing buyer for the asset*'[618]. In the case of sovereign bonds, said value is easily found in the value at which the bonds *a quo* are publicly traded[619]. The total amount of damages will not however automatically be identical to the market value of the bonds. Indeed, damages seek to compensate for the *entirety* of the economic losses of the investor and therefore include interest for non-payment[620].

The fact that the value of a sovereign's bonds is anchored by its market value, will hardly satisfy creditors in most circumstances, as the bonds of a restructuring sovereign trade at a discount. Moreover, even if one ignores the issues surrounding the valuation of sovereign bonds, obtaining payment from a reluctant debtor following investment litigation might not be straightforward. On the one hand, holders of an arbitral award are in a comparatively better positions than creditors having sought redress before domestic courts. Indeed, article 53 and 54 of the ICSID Convention create a system where arbitral awards are quasi-

[617] *Case concerning the Factory at Chorzow (claim for indemnity) (merits)* (n 379) para 47.
[618] Sergey Ripinsky and Kevin Williams, *Damages in International Investment Law* (BIICL 2008) 182–84. For an application see e.g. *Starrett Housing Corporation v. Iran* (n 512); *Sempra Energy International v. The Argentine Republic (Award)* (n 551); *Enron Corporation and Ponderossa Assets L.P. v Argentine Republic (Award)* (n 551); *Southern Pacific Properties (Middle East) Limited v Arab Republic of Egypt* [1992] ICSID ARB/84/3.
[619] For example, the tribunal in *British Gas v. Argentina* evaluated BG's damage by reference to the drop in the company's share following Argentina's actions. *BG Group Plc v The Republic of Argentina (final award)* (UNCITRAL); Ripinsky and Williams (n 618) 216. See also *Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt* (n 618). *Contra Enron Corporation and Ponderossa Assets L.P. v Argentine Republic (Award)* (n 551). The argument in *Enron* was that in an illiquid market, the value of publicly traded shares inaccurately represents the value of the underlying assets. While this reasoning is coherent for shares it seems that it does not translate to sovereign bonds as the underlying asset is a debt with no other inherent value.
[620] Wälde and Sabahi (n 615) 1106.

automatically recognised by domestic courts[621]. This, logically, reduces the legal uncertainties linked to the enforcement. On the other hand, obtaining payment from a sovereign, still requires the discovery of attachable assets belonging to said sovereign. Given the current State of the law of immunities such discovery process is fraught with uncertainty, and is thus particularly unsatisfactory from a creditor protection perspective[622].

Remedies obtainable under the European Convention of Human Rights face a similar set of issues[623]. As with investment tribunals, the main form of remedy granted by the Strasbourg Court is the award of damages[624], or 'just satisfaction'[625] in the language of the Convention. These damages are, like those awarded by arbitral tribunals, essentially compensatory. When it comes to compensation for expropriation, the Court, like ICSID tribunals, bases the appropriateness of the compensation on the market value of the expropriated property[626].

3.3.4.3 The Efficiency of international law Remedies: Overview

The picture when it comes to the obtention by creditors of efficient remedies in international law is muddier than in other areas of the creditor protection model. On the one hand, changes in the law of immunities have theoretically increased the likelihood that creditors will find attachable assets with which they can repay themselves. On the other hand, in practice, finding such assets can often prove difficult for creditors, and contradictions within the international case-law on immunities renders this process unpredictable.

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[621] Article 54 states that "*Each Contracting State shall recognize an award rendered pursuant to this Convention as binding and enforce the pecuniary obligations imposed by that award within its territories as if it were a final judgment of a court in that State.*" Convention on the Settlement of Investment Disputes between States and Nationals of Other States (Washington) 1965, art 54. See also Alan S Alexandroff and Ian A Laird, 'Compliance and Enforcement' [2008] The Oxford Handbook of International Investment Law <http://www.oxfordhandbooks.com.ezproxy.lib.gla.ac.uk/view/10.1093/oxfordhb/9780199231386.001.0001/oxfordhb-9780199231386-e-29> accessed 25 March 2019.

[622] Article 55 of the ICSID convention makes clear that the recognition of arbitral award does not entail any modifications within the law of immunities. Convention on the Settlement of Investment Disputes between States and Nationals of Other States (Washington).

[623] It should be noted that the primary duty to provide remedies under the system created by the European Convention on Human Rights lies within the domestic court system of the member States, with the Court playing a subsidiary role.

[624] The Court has, rarely, opted for a form of restitution in kind, but only in cases involving violations of article 6 of the Convention.

[625] European Convention on Human Rights (Rome), article 41. On just satisfaction see e.g. Octavian Ichim, *Just Satisfaction under the European Convention on Human Rights* (Cambridge University Press 2015); Linos-Alexander Sicilianos, 'The Role of the European Court of Human Rights in the Execution of Its Own Judgments: Reflections on Article 46 ECHR', *Judgments of the European Court of Human Rights - Effects and Implementation* (Nomos Verlagsgesellschaft mbH & Co KG 2014).

[626] See e.g. the reasoning of the Court in *Mamatas et autres v. Greece* (n 34), examined *infra*.

Moreover, international courts and tribunals' reliance on damages as a remedy, means that creditors can hardly find more efficient ways to coerce States.

This lack of creditor protection at the international level, should however be tempered by two caveats. First, a dearth of effective enforcement mechanisms is less a symptom of the international law on sovereign debt *per se*, and more a sickness of the international legal regime in general. Second, despite this lack of effective enforcement, it should be noted that, on average, decisions of international courts are respected by the losing party[627]. This potentially indicates that while the remedies provided by international law might not be *per se* efficient, the potential fallout from a lost international case may be enough to coerce debtors into repayment.

3.4 The Strengths and Weaknesses of the Creditor Protection Model

3.4.1 The Strengths of the Creditor Protection Model

3.4.1.1 The Law on Sovereign Debt as a Credible Commitment Device

The main strength of the creditor protection model is that it enables sovereign debtors to credibly bind themselves to their sovereign debt obligations. It does so by subjecting sovereigns to the jurisdiction of independent courts and tribunals which protect creditor's rights and provide them with relatively efficient remedies.

Credible commitment devices lower the legal and political risks tied to sovereign lending for creditors[628]; thus, at the margin, reducing the costs of borrowing for the sovereign[629]. This new form of credible commitment differs from previous historical trends for two reasons. First, as opposed to domestic constitutional institutions[630], judicial enforcement of sovereign debt is fully independent from the sovereign and functions for domestic as well as external debt. Second, as opposed to the previous international methods of enforcement[631]

[627] See Guzman (n 110) 7–8.
[628] North and Weingast (n 124); ibid; Choi, Gulati and Posner (n 114).
[629] Choi, Gulati and Posner (n 114).
[630] North and Weingast (n 28); North (n 87); Stasavage (n 126); Oosterlinck, Ureche-Rangau and Vaslin (n 128).
[631] Supersanctions, gunboat diplomacy and diplomatic protection. Mitchener and Weidenmier (n 91); Weidenmier (n 175); Weidemaier, 'Contracting for State Intervention' (n 236).

domestic court litigation, ICSID arbitration and ECtHR litigation are independent from the political motivations of a sovereign espousing creditors' claims, thus fostering certainty.

Moreover, changes in the law of immunities, the automatic recognition of arbitral decisions under ICSID and *pro rata* payment as a remedy for breaches of the *pari passu* clause, have increased the likelihood that creditors will be able to effectively coerce the sovereign into respecting its sovereign debt obligations. This can be one either by obtaining payment via the attachment of the debtor's assets or by forcing the debtor into settling out of court.

The credible commitment aspects of the creditor protection model are further reinforced by the fact that sovereign debt is contractually removed from the debtor's sphere of regulatory influence. This occurs contractually via choice-of-law and currency clauses, and by internationally the fact that treaty obligations and custom protect creditors against regulatory intervention by the debtor.

Finally, the narrow interpretation of the necessity defence, and the rateable payment interpretation of the *pari passu* clause prevent debtors from emptying their sovereign debt obligations of their substance, thus further ensuring that the rights of creditors will be upheld.

These credible commitment devices foster certainty when it comes to sovereign debt, theoretically lowering borrowing prices for sovereigns. These better borrowing conditions, in turn, lower the negative impacts of sovereign indebtedness on the debtor's population.

3.4.1.2 Creditor Protection and the Rule of Law

From a deontological standpoint, a second strength of the creditor protection model is that the systematic protection of creditor's rights aids in preventing sovereigns from repudiating their debts, thus strengthening the rule of law at a global level.

While debt repudiations have been rare[632], the ability of States to ignore, without facing real punishment, the contractual obligations of private entities has often been the norm. This ability is problematic from an accountability and a rule-of-law standpoint. Given the importance of these two values in contemporary transnational law[633], ensuring that States

[632] See e.g. Meyer, Reinhart and Trebesch (n 168).
[633] See e.g. 'Charter of the United Nations (San Francisco)', article 1. Ian Brownlie, *The Rule of Law in International Affairs: international law at the Fiftieth Anniversary of the United Nations* (Martinus Nijhoff Publishers 1998).

are judicially held to their contractual commitments is both economically sound, and a politically and philosophically coherent policy standpoint in most modern democracies.

The fact that creditor protection mechanisms fit within a broader narrative of transnational law as a tool for furthering the rule of law[634] helps to explain why courts and tribunals have subscribed to creditor protection as a policy. Beyond the functioning of the sovereign debt market, creditor protection enables courts to ensure that, even for sovereigns, *contracta sunt* indeed *servanda*.

Finally, and controversially, attachment to the rule of law can legitimate the behaviour of holdouts, painting them less as ‘vultures’ profiting from a sovereign’s distress but as guardians of the good functioning of the sovereign debt market[635].

3.4.1.3 Creditor Protection as an Incentive towards Good Governance

As will be exposed *infra*, the main weakness of the creditor protection model is that it makes necessary debt restructurings more difficult for all parties involved. While, in general, this is a source of inefficiency, it can be argued that, difficult debt restructurings incentivise debtors towards good governance.

This argument purports that, if debt restructurings are easy for sovereigns, there is a risk of moral hazard, as governments could over-borrow or over-spend and restructure with ease when debts become unsustainable[636]. If one subscribes to this model of state behaviour, increasing the costs of debt restructurings will deter sovereigns from irresponsible economic behaviour and therefore ultimately reduce the likelihood of sovereign debt crises. This, again, benefits both creditors and the sovereign’s population.

[634] See e.g. ‘Charter of the United Nations (San Francisco)’, article 1. Ian Brownlie, *The Rule of Law in International Affairs: international law at the Fiftieth Anniversary of the United Nations* (Martinus Nijhoff Publishers 1998).

[635] See in this sense Fisch and Gentile (n 73); Cohen (n 74).

[636] In that sense see Fisch and Gentile (n 73); Cohen (n 74); Choi, Gulati and Posner (n 114); Choi and Posner (n 91).

3.4.1.4 Creditor Protection as a way to promote legal certainty

Creditor protection improves legal certainty at several levels. First, by removing sovereign bonds from the debtor's regulatory reach, they ensure that the legal framework supporting said bonds will not be altered in times of crisis[637].

Second, at the individual level, the relationship between sovereigns and their creditors is more predictable within the creditor protection model. Because the rights of creditors under this first model are systematically enforced by courts, and because jurisdictions systematically recognised their competence, there are little doubts on the interpretation of most norms.

Moreover, while there are doubts regarding the normativity of certain of the norms underlying the anti-holdout model, the norms forming the creditor protection model are, on average, broadly considered to be normative and their interpretation is generally agreed upon.

3.4.2 The Weaknesses of the Creditor Protection Model

3.4.2.1 Collective Action Issues during Bond Restructuring

The main weakness of the creditor protection model is that judicially empowering bondholders leads to inefficiencies during debt restructurings.

Fundamentally, bonded sovereign debt restructurings face collective action problems in that the interests of each individual creditor are at odds with the interest of the creditor-base as a collective[638]. To put it simply, while each creditor can maximise its utility by refusing a haircut on its debt instrument, if all creditors do so, the debtor ultimately defaults thus leading to greater losses for all parties involved[639].

Moreover, during a restructuring, any holdout increases the haircut necessary for a debtor to return to debt sustainability, thus increasing the costs of restructurings for the other stakeholders.

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[637] See, in general, Choi, Gulati and Posner (n 114).

[638] Gelpern, 'How Collective Action Is Changing Sovereign Debt Cover Story' (n 302); Dellas and Niepelt (n 297).

[639] Gelpern, 'How Collective Action Is Changing Sovereign Debt Cover Story' (n 302); Dellas and Niepelt (n 297).

As pointed out *supra*, this had not been an issue during the syndicated era of sovereign lending. First, lenders were incentivised towards helping sovereigns to reduce unsustainable debt burdens, as this would lead to future benefits. Second, the rules of syndication ensured that once a qualified majority of banks agreed to a restructuring deal, all banks would be bound by the agreement. Post-Brady plan, with bonds becoming the main instrument for sovereign indebtedness, this equilibrium was shattered. Contractually, any creditor could hold out and some actors had no incentives to ensure that the sovereign could return to debt sustainability.

This led to two inter-related problems:

First, holdouts have been able to disrupt restructuring processes by relying on the efficient remedies granted to creditors. This has led to more uncertainty during restructuring processes[640], and overall increased costs for the sovereign and the rest of its creditor base.

Second, efficient legal remedies, as they increase the likelihood of full repayment on sovereign bonds, economically incentivise holding out. The most notable example of this relationship is vulture fund litigation, efficient judicial remedies are essential to the arbitrage strategy of vulture funds. These remedies thus encourage these funds to purchase distressed debt and holdout during restructuring.

The combination of those two issues has meant that under the creditor protection model, more creditors are encouraged to holdout and that when they do so the costs to the sovereign and the rest of the creditor-base are greater.

3.4.2.2 Limits to Regulatory Tools Available to Sovereigns for Managing Debt Crises

A second issue regarding the creditor protection model is that shielding sovereign debt from the regulatory reach of the debtor inherently limits the variety of tools available to the latter to manage debt crises.

Fundamentally, choice-of-law clauses, currency clauses, and a narrow reading of the necessity defence, prevent sovereign debtors from using their legislative or regulatory powers to facilitate their restructuring processes. In particular, borrowing in a foreign

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[640] In particular when litigation was directed at regulatory measures taken to facilitate the debt workout or has relied on the *pari passu* clause.

currency prevents the debtor from being able to devalue its money in order to meet payment obligations. This effect is compounded when the sovereign's own currency, due to fears linked to its financial situation, loses value, forcing the borrower to purchase increasingly expensive foreign monies to face payment obligations[641].

Similarly, choice-of-law clauses prevent debtors from deploying legislative strategies to facilitate debt restructurings. As recently shown by Greece with its retroactive introduction of a CAC, such a solution not only speeds up a restructuring process but might also be desired by a vast majority of the sovereign's creditors[642].

Finally, in international law, the narrow reading of the necessity defence prevents sovereigns from breaching their investment treaty obligations in the face of mounting economic pressure. Again, such a narrow reading, while it *ex ante* reassures creditors, limits the variety of strategies available to a sovereign when dealing with a sovereign debt crisis.

This weakness of the creditor protection model should essentially be read as a trade-off. A State can borrow in its own currency and under its own laws, but if it is perceived as risky by market actors, it will do so at a potentially prohibitive premium. The irony of this trade-off is that, as a rule, the States able to borrow using contractual instruments that they can regulatorily alter are those who are the least likely to need such intervention. *A contrario*, the States most likely to need all the available tools for managing a sovereign debt crisis often need to recourse to foreign-law and foreign-currency borrowing to fund themselves.

3.4.2.3 Inefficient Restructurings, the Human Rights Costs of Debt Crises and Backlash against Global Liberal Institutions

Inefficient debt restructurings, such as those caused by holdout litigation, are not only problematic from an economic standpoint but also have political and social ramifications.

First, sovereign debt restructurings have well-documented negative effects on sovereign's ability to fulfil their duties pertaining to their population's social and political rights[643]. Thus,

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[641] Flandreau and Sussman (n 114).
[642] See Iversen (n 164).
[643] Lumina, 'Report of the Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, Particularly Economic, Social and Cultural Rights (Mission to Argentina)' (n 6); Lumina, 'Report of the Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, Particularly Economic, Social and Cultural Rights (Mission to Greece)' (n 6); *Sovereign Debt and Human Rights* (n 70).

ensuring that sovereigns return to debt sustainability as smoothly as possible is not only economically efficient, but also limits the negative consequences of a debt crisis on a sovereign's population.

As such, when the creditor protection model, combined with bonded sovereign debt, encouraged holdouts and lengthened restructuring processes, the population of usually economically fragile States pays the price of inefficiency. This, understandably, fuelled anti-capitalist or anti-debt movements, both within the global civil society, and resulted in the election by debtors of far-left or far-right parties, as exemplified by Greece's election of Syriza, and the rise of the Golden Dawn party during its financial crisis[644].

Within this specific context, vulture fund litigation has fuelled anti-liberal rhetoric, both by debtor States governments and the broader public. The use of courts for arbitrage by those specialised hedge funds, as well as the fact that their profits emerged from speculations over a sovereign in economic distress has regularly sparked outrage. In particular, *Elliott* and *NML*'s reliance on domestic courts during the sister-funds decade-long sparring with Argentina enflamed the rhetoric of the Kirchner governments, leading it to characterise all holdouts as vultures and to vow not to accept any unfavourable decision from a US court[645]. Such a refusal to comply with a competent court's decision, cannot help but threaten the rule of law at the international level.

Against that background. holdout litigation was cast as the prototypical example of a global financial system gone mad and designed to serve the interest of the few over those of the many. The fact that vulture funds were the financial tools of billionaires hardly escaped the attention of the international press and helped fuel the backlash[646].

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[644] See e.g. Sofia Vasilopoulou and Daphne Halikiopoulou, 'The Rise of the Golden Dawn in the Context of the Greek Crisis' in Sofia Vasilopoulou and Daphne Halikiopoulou (eds), *The Golden Dawn's 'Nationalist Solution': Explaining the Rise of the Far Right in Greece* (Palgrave Macmillan US 2015) <https://doi.org/10.1057/9781137535917_2> accessed 27 March 2019. For an "insider" take on the question see Varoufakis (n 96).

[645] *NML Capital, LTD., et al. v The Republic of Argentina* (n 28); Porzecanski (n 164).

[646] See e.g. Renae Merle, 'How One Hedge Fund Made $2 Billion from Argentina's Economic Collapse' *The Washington Post* (29 March 2016) <https://www.washingtonpost.com/news/business/wp/2016/03/29/how-one-hedge-fund-made-2-billion-from-argentinas-economic-collapse/>; Greg Palast, 'How Barack Obama Could End the Argentina Debt Crisis' *The Guardian* (7 August 2014) <https://www.theguardian.com/business/economics-blog/2014/aug/07/argentina-debt-crisis-barack-obama-paul-singer-vulture-funds> accessed 19 February 2020.

4. The Anti-holdout model

4.1 Introduction

The previous chapter highlighted the functioning of the creditor protection model and the role it played in the development of the collective action issues which plagued sovereign debt restructurings in the 1990s and 2000s. In the face of these issues, a realignment of the regulatory framework on sovereign debt was needed. The sum of the changes which occurred as a result can be understood as the anti-holdout model.

At the heart of the anti-holdout model is the idea that, to be efficient, the law on sovereign debt ought to enable States to restructure unsustainable debts. As previously exposed, prompt and efficient sovereign debt restructurings are wealth-maximising since they enable a faster return of the sovereign to capital markets. More importantly, efficient debt restructurings limit the negative aspects of a sovereign debt crisis on the debtor's finances, and therefore on its ability to fulfil the needs of its population[647].

This chapter 4 will first focus on the key components of the anti-holdout model, relying on domestic law examples to illustrate their functioning. Then, it will focus on their implementation in international law. The last section will be centred on the advantages and disadvantages of the anti-holdout model.

4.2 A General Theory of the Anti-holdout model

If the creditor protection model can be understood as a judicial way of creating credible commitment, the anti-holdout model is better summarised as a regulatory method to

[647] On the impact of debt restructurings and high debt burdens on a sovereign's population see Lumina, *Sovereign Debt and Human Rights* (n 6); Lumina, 'Report of the Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, Particularly Economic, Social and Cultural Rights (Mission to Argentina)' (n 6); Lumina, 'Report of the Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, Particularly Economic, Social and Cultural Rights (Mission to Greece)' (n 6). See also Olivier De Schutter, *Sovereign Debt and the Right to Food* (Oxford University Press 2018) <http://www.oxfordscholarship.com/view/10.1093/oso/9780198810445.001.0001/oso-9780198810445-chapter-11> accessed 7 February 2020; Tim Jones, *Sovereign Debt and the Right to Health* (Oxford University Press 2018) <http://www.oxfordscholarship.com/view/10.1093/oso/9780198810445.001.0001/oso-9780198810445-chapter-12> accessed 7 February 2020; Gail Hurley, *Sovereign Debt and the Right to Development* (Oxford University Press 2018) <http://www.oxfordscholarship.com/view/10.1093/oso/9780198810445.001.0001/oso-9780198810445-chapter-14> accessed 7 February 2020.

incentivise creditors towards accepting reasonable debt restructuring offers[648]. The anti-holdout model has three essential components: majority decision making [649] during restructurings, a limitation of the remedies available to creditors, and the re-allocation of funds to facilitate the debtor's return to debt sustainability.

Overall, the anti-holdout model has two main effects on the creditor-debtor relationship. First, the costs of restructurings are shared by the entirety of the creditor base, and not just by the creditors having agreed to a restructuring offer. Second, as contesting restructuring processes is increasingly more difficult, debt restructurings are more certain, faster, and thus less costly[650].

In addition, the fact that restructurings have to be majoritarily agreed both fosters negotiations between creditors and debtors[651] and strengthens the virtuous path-dependency between debtors and their larger creditors. The latter, being the largest bondholders, they effectively own the controlling share of a restructuring sovereign's bonds and benefit from its return to debt sustainability.

These effects do not mean that the anti-holdout model is a panacea for sovereign debt. As will be shown in the last section of this third chapter, the anti-holdout model provides little incentives for States to restructure their debts as early as they should. Moreover, its effects disproportionately affect small bondholders, and its implementation gives rise to risks of further fragmentation in the law on sovereign debt.

Before delving into a more in depth analysis of the components of the anti-holdout model, the change in the actors responsible for law-making between both models ought to be

[648] A key question regarding the restructuring model is the definition of what constitutes a "reasonable" restructuring offer. Economically, a reasonable restructuring offer could be understood as a restructuring offer which provides sovereign with sufficient relief to return to debt sustainability while limiting as much as possible adverse effects on creditors. The problem with such an understanding of a reasonable debt restructuring is that it is often difficult to know *ex ante*, if a suggested haircut will be too small or too large. For the purpose of the restructuring model, this thesis understands a reasonable restructuring offer as one that is acceptable by a majority of a sovereign's creditors.

[649] As opposed to restructurings on an 'each-creditor for itself' basis, as was the case under the creditor protection model.

[650] See e.g. Cephas Lumina, *Curbing 'Vulture Fund' Litigation* (Oxford University Press 2018) 504–505 <http://www.oxfordscholarship.com/view/10.1093/oso/9780198810445.001.0001/oso-9780198810445-chapter-27> accessed 7 February 2020; William W Bratton and G Mitu Gulati, 'Sovereign Debt Restructuring and the Best Interest of Creditors' (Social Science Research Network 2010) SSRN Scholarly Paper ID 387880 <http://papers.ssrn.com/abstract=387880> accessed 6 November 2015; John Coffee and William Klein, 'Bondholder Coercion: The Problem of Constrained Choice in Debt Tender Offers and Recapitalizations' (1991) 58 U. Chi. L. Rev. 1207.

[651] As finding a solution agreeable to a majority of creditors requires negotiating with the latter. See Matthias Goldmann, 'Putting Your Faith in Good Faith: A Principled Strategy for Smoother Sovereign Debt Workouts' (2016) 41 Yale Journal of international law 117.

mentioned. Essentially, the creditor protection model had been implemented in a relatively de-centralised manner, either by private parties, via contract drafting, or by courts and tribunals[652].

Within the anti-holdout model, the drivers of legal innovation are overwhelmingly governments, international organisations such as UNCTAD[653] and the UNGA[654], or other public agencies such as the IMF[655] or ESM[656]. The inefficiencies examined *supra* can be read as a failure by market actors and judges to adapt sovereign debt regulation to the post-Brady bond market. This, logically, warranted top-down involvement in sovereign debt regulation.

The reasons behind this market failure are currently uncertain. Interviews with the lawyers drafting sovereign debt contract have yielded several possible explanations for the lack of change in sovereign debt's contractual design: inertia, risk aversion, or simply high transaction costs[657].

Explaining why judges failed to adapt to the modern bond market when deciding on sovereign debt is more difficult. Moreover, the absence of qualitative research on the topic renders any such exercise purely speculative. It might be that judges, when deciding on sovereign debt restructurings, chose to make their decisions fit within the broader regulatory paradigm on sovereign debt. Thus, when the regulation on sovereign debt was tilted towards creditor protection, judges decided in a creditor protection fashion. When it is geared towards restructuring, they favour easier restructurings. While such a reading of events favours a vision of the judge as the impartial 'mouth of the law' rather than an actual law-maker, it has a fairly tautological quality in a legal environment where judicial law-making plays a central role. Alternatively, one could read this failure of judicial adaptation as fitting within the narrative that the law is reactive to social changes. Under that reading, when the 'real life' conditions of sovereign lending were altered, there was a lag during which the regulatory

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[652] While changes in the law of immunities were undoubtedly the result of government intervention, the application of said law of immunities to sovereign debt was the result of judicial interpretation. Similarly, the characterisation of sovereign bonds as investments was a product of judicial interpretation, so was the rateable interpretation payment of the *pari passu* clause, etc. For an overview of the public sector involvement in Greece's restructuring see notably Philip R Wood, 'How the Greek Debt Reorganisation of 2012 Changed the Rules of Sovereign Insolvency' (2013) 14 Business Law International 3.
[653] United Nations Conference on Trade and Development (n 21).
[654] United Nations General Assembly, 'Resolution 69/319: Basic Principles on Sovereign Debt Restructuring Processes' (n 22).
[655] International Monetary Fund (n 13).
[656] Treaty Establishing the European Stability Mechanism (Brussels) 2012.
[657] On this question see Gulati and Scott (n 75); Weidemaier, Scott and Gulati (n 75).

paradigm remained unchanged. The anti-holdout model can thus be read as the law 'catching up' with the real world.

Regardless of its causes however, it is undeniable that this failure to adapt to the new bond market by the lawmakers for sovereign debt had to be remedied and that the logical entities for doing so were the aforementioned public entities.

4.2.1 Majority Decision-Making during Restructuring

4.2.1.1 Majority Decision Making: Overview

The first component of the anti-holdout model is majoritarian debt restructurings. Acceptance of the restructuring proposal under the anti-holdout model is not decided by each creditor for themselves, but by a majority or qualified majority of creditors, binding the minority to their decisions[658].

Majoritarian debt restructurings provide several advantages. First, because a minority of bondholders is bound by the decision of the majority, the possibilities for holdout litigation are limited[659]. This, logically, fosters certainty as the results of the restructuring negotiation cannot be challenged.

Second, majoritarian restructurings incentivise sovereigns and their creditors towards negotiated solutions to sovereign debt crises[660]. If support by a qualified majority of creditors is required for a debt restructuring to go forward, States have to negotiate with their creditors in order to garner sufficient support for their restructuring offer to be accepted[661]. Moreover, these negotiations also strengthen the legitimacy of the restructuring process[662]. Indeed, under the previous system for debt restructurings States have on occasion contented

658 Majoritarian debt restructuring was already one of they components of the SDRM system pushed forward by the IMF see Krueger (n 76).
659 This, inherently, is the logic behind the insertion of collective action clauses.
660 See Goldmann, 'Putting Your Faith in Good Faith: A Principled Strategy for Smoother Sovereign Debt Workouts' (n 651).
661 ibid 131.
662 Such legitimacy would stem from the participatory nature of the negotiation process as well as its perceived democracy. On issues of legitimacy within the current "non-system" of sovereign debt workouts see Odette Lienau, 'The Challenge of Legitimacy in Sovereign Debt Restructuring' (2016) 57 Harvard international law Journal 151. See also Terence Halliday, 'Legitimacy, Technology, and Leverage: The Building Blocks of Insolvency Architecture in the Decade Past and the Decade Ahead' (2007) 32 Brooklyn Journal of international law <https://brooklynworks.brooklaw.edu/bjil/vol32/iss3/13>.

themselves with providing their creditors with ‘take it or leave it’ offers, threatening not to pay any creditors who refused to take the haircut on their bonds[663].

It should be noted that the majority here is not understood as being calculated on a *per virem* basis, but on a bond-by-bond basis. The fact that, under the anti-holdout model, majorities are estimated on such a basis further enhances the likelihood of prompt and efficient restructurings. Essentially, in any given restructuring scenario it is likely that the bulk of a sovereign’s bonded debt is held by large financial institutions[664] with vulture fund and individual holdings being comparatively marginal. As was pointed out during this thesis’ analysis of the syndicated loan market, large financial institutions benefit from a fast return of the sovereign to debt sustainability as said return provides them with future benefits.

When those large creditors are banking institutions, regulatory capital adequacy requirements enable them to withstand the costs engendered by a haircut on their sovereign debt holdings[665], ensuring that said institutions will not be threatened by sovereign failure. This further ensures that they will agree to reasonable restructuring offers. Moreover, larger creditors can purchase credit default swaps (CDS) on their sovereign bonds[666]. Sovereign CDS enable their buyer to obtain payment from the seller to off-set the default risks attached to the bonds of a sovereign. In practice this means that institutional investors[667] have

[663] See e.g. Argentina’s first offers to its creditors during its 2000s crisis discussed in Miller and Thomas, ‘Sovereign Debt Restructuring’ (n 73) 1492.
[664] IMF, ‘Sovereign Investor Base Dataset for Emerging Markets’ (n 3).
[665] Within the EU, capital adequacy requirements are implemented via directive. See ‘Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on Access to the Activity of Credit Institutions and the Prudential Supervision of Credit Institutions and Investment Firms, Amending Directive 2002/87/EC and Repealing Directives 2006/48/EC and 2006/49/EC Text with EEA Relevance’ <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32013L0036>; Katarzyna Sum, ‘Basel III: Assessment of the Guidelines for Regulatory Reform’ in Katarzyna Sum (ed), *Post-Crisis Banking Regulation in the European Union: Opportunities and Threats* (Springer International Publishing 2016) <https://doi.org/10.1007/978-3-319-41378-5_2> accessed 26 September 2019; Mark Petersen and Janine Mukuddem-Peterson, *Basel III Liquidity Regulation and Its Implications*.
[666] Credit default swaps are financial derivatives in which a “*seller of protection (…) agrees to pay the buyer of protection (…) an amount if during an agreed period a prescribed credit event occurs (…) in relation to an greed reference obligation of a reference entity.”* Wood, *Law and Practice of International Finance* (n 253) 433. To put it simply a credit derivative is a financial instrument whose function is to provide it buyer a quasi-insurance or guarantee if during an agreed period of time the obligations of an agreed issuer are subject to a downgrade in credit-worthiness, an event of default and/or a restructuring. There are differences between a CDS and an insurance or a guarantee. Notably, as opposed to guarantees, CDSs apply to events beyond mere non payment. As opposed to both guarantees and insurance contract, the holder of a CDS need not be the holder of the reference transaction and there is no automatic subrogation of the protection seller to the protection buyer once the transaction has been settled. ibid 434.
[667] The Over the Counter (OTC) credit derivatives market is largely regulated under ISDA master agreement. The ISDA master agreement is a standard agreement covering derivatives trading (except repos and stocklending), as well as the netting and the set-off linked to derivatives transactions. Participation to transactions under the ISDA Master Agreement are typically limited to entities demonstrating that they possess the financial ability to withstand the losses that derivative trading can lead to. Ths fundamentally excludes most retail investors from the OTC derivatives market. On the ISDA master agreement see Wood, *Law and Practice of International Finance* (n 253) 440–442.

financial tools available to off-set the costs of debt restructurings, thus further incentivising them to collaborate with the debtor[668].

4.2.2.2 Majority Decision Making in Sovereign Debt Contracts: Collective Action Clauses

Collective action clauses (or CACs) are contractual clauses allowing for modifying payment terms (either the amount or the maturity of the bond) across several bond issuances via a vote by bondholders, usually requiring a qualifying majority[669]. The scope of CACs varies, ranging from encompassing a single bond issue, aggregating several of them[670], or binding the entirety of the bondholders of a sovereign[671]. Their introduction in sovereign bonds predates the model shift to restructuring protection, with the first clauses of this type in US bonds being introduced as early as 1997 in Kazakh bonds[672].

However, following vulture fund litigation CACs became widespread, with the US treasury[673], the IMF[674] and the European Stability Mechanism[675] pushing for their insertion in all bonds[676]. Moreover, CACs have been a central element of the Greek restructuring

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668 Following the Greek financial crisis notably, purchase of sovereign CDS on southern European debtors has dramatically risen, seemingly indicating a desire by financial institutions to hedge their positions on bonds emitted by those sovereigns. See IMF, 'Global Financial Stability Report, Chapter 2: A New Look at the Role of Sovereign Credit Default Swaps' <https://www.imf.org/~/media/Websites/IMF/imported-flagship-issues/external/pubs/ft/GFSR/2013/01/pdf/_c2pdf.ashx+&cd=4&hl=fr&ct=clnk&gl=uk>.

669 Bratton and Gulati (n 650); Buchheit, 'Restructuring a Nation's Debt Capital Markets' (n 79).

670 Gelpern, 'How Collective Action Is Changing Sovereign Debt Cover Story' (n 302); Liu and others (n 90); Leland Goss, 'Sovereign Debt Restructuring Made Easy Special Focus: Debt Capital Markets in Association with the ICMA' (2013) 32 International Financial Law Review 62. Technically, collective action clauses can be divided in four main types: majority action clauses, which enable a majority of bondholder to alter contractual dispositions, collective representation clause, which establish a representative forum for debtor-creditor cooperation, sharing clauses share proceeds obtained from the debtor amongst creditors and acceleration clauses requiring a minimum creditor support for payment acceleration in case of default. Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 111. When this thesis refers to CACs it only focuses on majority action clauses since they have been the most discussed type of clause, both in the legal scholarship on sovereign debt and in the public sector. Moreover, it seems that market practice similarly has opted for this type of CAC. ibid 111–112. For an early scholarly writing in favour of using CACs see John Taylor, 'Sovereign Debt Restructuring: A US Perspective. Speech at the Conference "Sovereign Debt Workouts: Hopes and Hazards". Institute for International Economics' <https://www.piie.com/commentary/speeches-papers/sovereign-debt-restructuring-us-perspective>.

671 Anna Gelpern, Ben Heller and Brat Setser, 'Count the Limbs. Designing Robust Aggregation Clauses in Sovereign Bonds', *Too Little Too Late: The Quest to Resolve Sovereign Debt Crises* (Columbia University Press 2016).

672 Megliani, *Sovereign Debt* (n 50) 59. Prior to this push, CACs had been a usual feature of English law bonds. Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 111.

673 Mark Sobel, 'Strengthening Collective Action Clauses: Catalysing Change—the Back Story' (2016) 11 Capital Markets Law Journal 3.

674 International Monetary Fund, 'Strengthening the Contractual Framework to Address Collective Action Problems in Sovereign Debt Restructuring' [2014] IMF Policy Paper <https://www.imf.org/external/np/pp/eng/2014/090214.pdf>.

675 Treaty Establishing the European Stability Mechanism (Brussels).

676 Prior to this push, CACs had been a usual feature of English law bonds. Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 111.

process, with large creditors requiring their introduction in Greek domestic bonds before accepting any restructuring offer from the Hellenic State[677].

The ICMA has issued a standardised version of the CAC[678], allowing for three different voting techniques. The standard clause provides norms regarding the convening and conduct of a meeting of bondholders in order to allow a vote. It also gives guidance regarding the production of written resolutions by bondholders for the same purpose. Under the standard drafting, a restructuring of a single bond issue can be achieved by a "*a Single Series Extraordinary Resolution or a Single Series Written Resolution*"[679] of the bondholders.

The ICMA standard clause defines a Single Series Extraordinary Resolution as:

> *"a resolution passed at a meeting of Noteholders duly convened and held in accordance with the procedures prescribed by the Issuer and the [Fiscal Agent/Trustee/other bondholder representative] pursuant to paragraph (a) (Convening Meetings of Noteholders; Conduct of Meetings of Noteholders; Written Resolutions) by a majority of:*
>
> A. *in the case of a Reserved Matter[680], at least 75 per cent. of the aggregate principal amount of the outstanding Notes; or*
>
> B. *in the case of a matter other than a Reserved Matter, more than 50 per cent. of the aggregate principal amount of the outstanding Notes."[681]*

It defines a Single Series Written Resolution as *"a resolution in writing signed or confirmed in writing by or on behalf of the holders of:*

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677 *Mamatas et autres v. Greece* (n 18); Boudreau (n 90); Buchheit, 'Restructuring a Nation's Debt Capital Markets' (n 79).

678 International Capital Market Association, 'Standard Aggregated Collective Action Clauses ("CACS") for the Terms and Condictions of Sovereign Notes' <https://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/Primary-Markets/primary-market-topics/collective-action-clauses/>. The ICMA is a self-regulatory organisation tasked with providing financial actors, (especially European ones) with standardised contractual provisions in order to improve the overall efficiency of financial market. Ramanna Vishwanath and Chandrasekhar Krishnamurti, *Investment Management: A Modern Guide to Security Analysis and Stock Selection* (Springer Science & Business Media 2009) 43.

679 International Capital Market Association (n 678).

680 Reserved matter is understood *inter* alia¸ as any changes to the payment conditions of the bond (payment, interest rates, principal, maturity, currency), a change on the condition of the vote by bondholders, a change of governing law or competent jurisdiction regarding the bonds, a debt swap or debt conversion, a change to the definition of Reserved Matter, or the issuance of securities or guarantees by the debtor.

681 International Capital Market Association (n 678).

A. *in the case of a Reserved Matter, at least 75 per cent. of the aggregate principal amount of the outstanding Notes; or*

B. *in the case of a matter other than a Reserved Matter more than 50 per cent. of the aggregate principal amount of the outstanding Notes.*

Any Single Series Written Resolution may be contained in one document or several documents in the same form, each signed or confirmed in writing by or on behalf of one or more Noteholders."[682].

Thus, payment conditions on a single bond issue can be modified either by obtaining a written agreement by 75% of the bondholders[683] or by convening a meeting of the bondholders during which a vote is issued.

For a restructuring across several issues, the ICMA model clause offers two voting models: Single-limb voting and double-limb voting. Under the first option, modifications to a Reserved Matter across several bond issues requires either obtaining a two-thirds majority of votes across all bonds, organising separate meetings of bondholders for each bond issue or, obtaining a written agreement from 75% of the bondholders[684].

Finally, several bond issues can be restructured, under the standardised ICMA CAC via a Multiple Series Two Limb Extraordinary Resolution. A Multiple Series Two Limb Extraordinary Resolution means:

"a resolution considered at separate meetings of the holders of each affected series of Debt Securities Capable of Aggregation (…) which is passed by a majority of:

A. *at least 662 /3 per cent. of the aggregate principal amount of the outstanding debt securities of affected series of Debt Securities Capable of Aggregation (taken in aggregate); and*

[682] ibid.
[683] Under the clause, the votes are computed by bond and not by bondhoder. In other words, the rule for CAC sis one bond = one vote, and not one man = one vote. It should however be noted that certain bonds can be excluded from the count if they are held by the debtor or an entity controlled by the debtor, in order to avoid conflict of interest.
[684] International Capital Market Association (n 678).

> B. *more than 50 per cent. of the aggregate principal amount of the outstanding debt securities in each affected series of Debt Securities Capable of Aggregation (taken individually).*"[685]

Several bond issues can similarly via a "Multiple Series Two Limb Written Resolution"[686]. Under the two limbs voting system a double majority of bondholders need to be reached: a two thirds majority within each bond issue as well as a simple majority across all issues[687].

CACs are one of the central features of the contemporary regulatory model on sovereign debt[688]. Their insertion in the vast majority of sovereign bonds effectively implements majoritarian debt restructuring at the contractual level. Under the contractual regime inaugurated by CACs, the only way for a bondholder to refuse a modification to their bonds is to acquire a controlling share in bond issues covered by a same collective action clause, a task which, while not impossible, can be extremely costly given the sums involved[689].

4.2.2 Limiting the Remedies Available to Creditors

4.2.2.1 Limiting the Remedies Available to Creditors: Overview

The second component of the creditor protection model is a limitation of the remedies available to creditors. This limitation has taken three different forms, in direct contrast to the components of the creditor protection model:

First, access to courts and tribunals for creditors has been curbed. This limits the likelihood of creditors obtaining efficient remedies and limits the uncertainties tied to enforcement attempts against restructuring sovereigns. Second, exceptions to State's obligations regarding sovereign debt have been carved. This, not only limits creditors' ability to obtain payment, but also enables sovereign debtors to deploy regulatory tools to facilitate their debt

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[685] ibid.

[686] It means the aggregation of votes for *"each resolution in writing (with a separate resolution in writing or multiple separate resolutions in writing distributed to the holders of each affected series (…) which, when taken together, has been signed or confirmed in writing by or on behalf of the holders of: (A) at least 662 /3 per cent. of the aggregate principal amount of the outstanding debt securities of all the affected series of Debt Securities Capable of Aggregation (taken in aggregate); and (B) more than 50 per cent. of the aggregate principal amount of the outstanding debt securities in each affected series of Debt Securities Capable of Aggregation (taken individually)*. ibid.

[687] Gelpern, Heller and Setser (n 11).

[688] On the importance of CACs see Weidemaier and Gulati (n 11); Stolper and Dougherty (n 11).

[689] This issue is further compounded when several bond issues are covered by a same CAC.

restructurings. Finally, the efficiency of the remedies granted to creditors has been limited. This similarly reduces the disruptive effects of successful enforcement attempts by creditors.

In addition to those effects, the limitation of remedies available acts as an incentive against holding out on reasonable restructuring offer. With the obtention of efficient remedies for creditors less likely, reliance on courts and tribunals as a way for economic actors to obtain payment, is rendered increasingly uncertain. The same applies to the likely pay-off for litigation since the means available to coerce a State towards repaying have been curbed[690]. To use an imperfect analogy, if one understands that holdout litigation is a gamble by creditors to obtain full payment, the limitation of available remedies lowers the odds of winning without lowering the downsides. The equilibrium in this situation is that creditors are incentivised against holding out and relying on litigation. These incentives, as will be seen, are more efficient against vulture funds since their investing strategy is expressly based on the likelihood of obtaining a favourable outcome through judicial means.

CACs play a central role in limiting creditor's access to courts. As previously explained, as the activation of collective action clauses change the content of the contractual obligations owed by the sovereign, any action for breach based on the original contractual conditions is impossible. However, CACs, while undeniably effective in limiting holdout litigation are not a universal solution. First, it is theoretically possible for a creditor to obtain a controlling share of bonds covered by a same CAC, thus enabling them to retain their ability to sue[691]. Moreover, prior to a CACs' activation, or if a vote fails, creditors retain the ability to litigate against the debtor. Finally, while the share of bonds featuring CACs is rising there remains series lacking the now standard clause, thus litigation on these bonds remains possible[692].

Therefore, a series of other domestic legislation, contractual innovations and interpretations have been put forward to limit the availability of judicial remedies to creditors of distressed sovereigns. The following sections will focus on three of these: the rank of payment drafting,

[690] The limitation of remedies available to creditors means that the average likely amount of money potentially obtainable via litigation is smaller.
[691] Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 111.
[692] For a broader overview of the limits on the current contractual model for sovereign debt restructuring see notably Richard Gitlin and Brent House, 'Contractual and Voluntary Approaches to Sovereign Debt Restructuring - There Is Still More to Do', *Too Little, Too Late. The Quest to Resolve Sovereign Debt Crises. M. Guzman, J. Ocampo, J. Stiglitz (eds)* (Columbia University Press 2016); James A Haley, 'Sovereign Debt Restucturing. A Coasean Perpsective', *Too Little, Too Late. The Quest to Resolve Sovereign Debt Crises. M. Guzman, J. Ocampo, J. Stiglitz (eds)* (Columbia University Press 2016).

and interpretation, of the *pari passu* clause, the Belgian Anti-Vulture Fund Act and dispositions limiting the ability of creditors to attach a sovereign's assets.

4.2.2.2 <u>*Alternative Readings of the pari passu clause*</u>

The rank of payment interpretation of the *pari passu* clause reads the clause as requiring creditors to not create any other debt instrument ranking *senior* to those containing the clause[693]. In practice, it prevents the creation by the State of secured debt[694], or the emission of other types of *senior* debt by a sovereign[695].

The US New-York Southern District Court in the *import-export bank of China v. Grenada*[696] case features such a reading of the clause. The case concerned four loan agreements between the *ex-imp. Bank* and the Republic of Grenada for a total over $20 million[697]. Grenada had issued a memorandum stating that it would not pay any non-restructured debt and made substantial payments on its external debt, but not on the four loans in question[698]. The District Court ruled that given the fact that Grenada had not taken any legislative actions to ensure the subordination of the loan agreements, the *pari passu* clause was not breached[699]. There were differences between the *Ex-Imp* case and the *Elliot* and *NML* decisions. First, the wording of the *pari passu* clause in Grenada's credit instruments was more restrictive than the one in the *NML* case[700]. Second, as opposed to Argentina, Grenada had not legislated regarding payment to holdouts[701].

From a strict legalistic perspective, the difference in the behaviour of Argentina and Grenada does not seem to be a decisive factor for justifying such a decision. The Argentinean bonds

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693 Zamour (n 74).

694 The emission of secured debt is now a rarity within the sovereign debt market. However, it used to be common in the early XXth century for States to guarantee bonds by attaching specific revenue streams to their repayments. Lee Buchheit, following archival research on the *pari passu* clause mentions in particular a Greek bond secured against the payments of a specific tobacco tax. Such practice fell into disuse as, in the era of absolute jurisdictional immunities, attaching the assets used by the State to secure the debt was impossible. Buchheit and Pam (n 14).

695 On the distinction between rateable payment and rank of payment interpretations of the clause see Rodrigo Olivares-Caminal, 'Rank Pari Passu or Not to Rank Pari Passu: That Is the Question in Sovereign Bonds after the Latest Episode of the Argentine Saga' (2009) 15 Law and Business Review of the Americas 745; Zamour (n 74).

696 *Export-Import Bank of the Republic of China v. Grenada* (n 28). For a broader commentary on the significance of the *Ex-Imp* case see Joseph Cotterill, 'Sovereign Pari Passu and the Litigators of the Lost Cause' (2014) 9 Capital Markets Law Journal 18.

697 *Export-Import Bank of the Republic of China v. Grenada* (n 22) para 1-2.

698 Ibid.

699 Ibid para 6.

700 *NML Capital, LTD., et al. v The Republic of Argentina* (n 22), pp 6-8.

701 ibid; *Export-Import Bank of the Republic of China v. Grenada* (n 22) para 1-2.

at cause in *NML* were issued under US law[702]. Thus, law-making by Argentina could not have had an impact upon the ranking of the bonds, or the obligation of Argentina regarding its bondholders. There is therefore little difference between enacting a "Lock Law"[703] and issuing a memorandum having the same effect. Rather than factual differences being the determining factor for the disparity between the *NML* and *Em-Imp* decisions, it seems should thus be read as adopting a more restrictive reading of the clause.

In addition to this alternative judicial interpretation, international institutions advocated for an improved drafting of the clause, limiting its disruptive effects[704]. Thus, the ICMA standard *pari passu* clause now reads:

> *"The Notes are the direct, unconditional and unsecured obligations of the Issuer and rank and will rank pari passu, without preference among themselves, with all other unsecured External Indebtedness of the Issuer, from time to time outstanding, provided, however, that the Issuer shall have no obligation to effect equal or rateable payment(s) at any time with respect to any such other External Indebtedness and, in particular, shall have no obligation to pay other External Indebtedness at the same time or as a condition of paying sums due on the Notes and vice versa"*[705].

Similarly, the IMF's Executive Board endorsed in 2014 the inclusion of a similar "enhanced *pari passu* provision" within sovereign bonds[706].

Given the adverse effects that the rank of payment interpretation of the clause had on restructuring processes, and given its potential efficiency in coercing most sovereigns towards repayment, it is undeniable that this narrowing of the clause should be read as a

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702 *NML Capital, LTD., et al. v The Republic of Argentina* (n 22) pp 6-8.
703 See e.g. Ley 26017 -Deuda Publica, Bonos - Disposiciones adicionales 2005 (Boletín Oficial) 1, 26; Decreto 1735/2007 Establécense los alcances, términos y condiciones del proceso de reestructuración de la deuda del Estado Nacional instrumentada en los bonos cuyo pago fue objeto de diferimiento según lo dispuesto por el Artículo 59 de la Ley Nº 25.827, mediante una operación de canje nacional e internacional. Suplemento de Prospecto, aplicable a la oferta internacional. Procedimiento Operativo para la República Argentina. Valor nominal máximo de los bonos que serán emitidos, Bonos Internacionales de la República Argentina y Bonos de la República Argentina. Modelo de Convenio de Fideicomiso. (n 372). There is however a difference between the *Ex-Imp* memorandum and the Lock Law. Grenada, in its memorandum promised to pay the restructured debt first, and then, if possible, the holdout, in a fashion similar to Peru's in the *Elliott* case, while Argentina in the Lock Law plainly refused payment to holdouts. *Export-Import Bank of the Republic of China v. Grenada* (n 28); *Elliott Assocs., L.P. v. Banco de la Nacion* (n 28); *NML Capital, LTD., et al. v The Republic of Argentina* (n 28).
704 It appears that in English law, a similar rank of payment interpretation of the clause has been adopted. See Lachlan Burn, 'Pari Passu Clauses: English Law after NML v Argentina' (2014) 9 Capital Markets Law Journal 2; Kupelyants (n 53) 299.
705 International Capital Markets Association (n 12).
706 International Monetary Fund (n 13).

limitation of creditors' remedies. In the contemporary sovereign debt market, the likelihood that a State will create *senior* categories of debt by assigning securities or ear-marking revenue flows for a specific bond are slim[707]. Therefore, the rank of payment version of the clause renders it pointless in the current setting.

An alternate, but equally restrictive position on the clause has been pushed forward by the Brussels' Court of appeal in *Republic of Nicaragua vs. LNC Investment LLC and Euroclear Bank SA*[708]. The Case opposed *LNC* and the Republic of Nicaragua, the former pursuing execution of a judgment granted in 1999 by a US court providing compensation for a former Nicaraguan default[709]. While the lower Belgian court followed the *Elliott* interpretation, the Brussels court of appeal reversed its previous jurisprudence. In its second foray within the debate on *pari passu*, the court refused to allow *LNC*, to prevent *Euroclear* from transferring payment on restructured Nicaraguan bonds, in stark contract to its previous *Elliott* decision[710]. It held that an injunction against the clearing house could not be granted since Euroclear was not complicit in the payment of interest in violation of the *pari passu* clause[711]. In other words, according to the court, a mere breach of the clause by Peru is not sufficient for determining whether Euroclear can be coerced into stopping payment from flowing, rather, what matters is Euroclear's behaviour *in concreto*[712].

As with the rank of payment interpretation of the clause, such a reading, anchoring itself on the notion of privity of contract and third-party complicity, effectively limits the ability of creditors to disrupt sovereign debt restructurings by relying on the clause.

Finally, a fourth potential interpretation of the clause was advanced in the 2012 *NML* decision[713]. As exposed in the first part of this thesis, the remedy granted to *NML* by the district court and the court of Appeal for the violation of the *pari passu* clause fits within the creditor protection model. It seems however that the court, in its interpretation of the clause itself echoes the concerns behind the anti-holdout model. To recall, the roots of the case lie in the Argentinean restructuring of the early 2000's and the adoption by Argentina of the 2005 Lock Law[714]. Argentina pleaded that the *pari passu* clause as integrated in its bonds

[707] See notably the analysis in Buchheit and Pam (n 14).
[708] *Republic of Nicaragua v LNC Investment LLC* (n 398).
[709] ibid.
[710] *Elliott Assocs., L.P.* (n 323).
[711] *Republic of Nicaragua v LNC Investment LLC* (n 398).
[712] ibid.
[713] *NML Capital, LTD., et al. v The Republic of Argentina* (n 28).
[714] ibid pp 6-8.

only applied to cases of *de lege* subordination[715], while NML capital argued that it also encompassed de facto subordination, such as the one created by the Lock Law[716].

The Court of Appeal decided that:

> *"the combination of Argentina's executive declarations and legislative enactments have ensured that plaintiffs' beneficial interests do not remain direct, unconditional, unsecured and unsubordinated obligations of the Republic and that any claims that may arise from the Republic's restructured debt do have priority in Argentinian courts over claims arising out of the Republic's unstructured debt."*[717].

Thus under the *NML* reading, the clause has been breached not because Argentina failed to provide the fund with rateable payment. Rather, Argentina's behaviour *in litis* and out of courts made clear that it intended to subordin*ate NML's* debt, triggering the clause. Strikingly, this standard of behaviour is less constraining upon the debtor as the rateable interpretation of the clause laid out in *Elliott*[718].

In addition to this narrower interpretation of the clause, the Court of Appeal in *NML* also takes in consideration the effects of its ruling on the sovereign debt market. The Court of Appeal underlines, regarding the potential effects of the remedy granted to *NML* for the violation of the clause:

> *"99% of the aggregate value of New York-law bonds issued since January 2005, including [the Exchange Bonds]. Only 5 of 211 issuances under New York law during that period did not include collective action clauses, and all of those issuances came from a single nation, Jamaica. Moreover, none of the bonds issued by Greece, Portugal or Spain – nations identified by Argentina as the next in line for restructuring – are governed by New York Law."*[719]

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[715] *NML Capital, LTD., et al. v The Republic of Argentina* (n 22), p. 16.
[716]ibid..
[717] ibid p 20.
[718] ibid; *Elliott Assocs., L.P. v. Banco de la Nacion* (n 22). On this question see Zamour (n 42).
[719] *NML Capital, LTD., et al. v The Republic of Argentina* (n 22) p 8.

The Court of Appeal, in other words, justifies its decision to grant *NML* extraordinary remedies by arguing that given the current state of bond drafting, protecting creditors in such a way does not lead to collective action issues[720].

It is useful to read *NML* as a transitional case between both models. The Court of Appeal for, as per the anti-holdout model, that granting creditors exorbitant remedies in the modern bond market is inefficient. However, given what the court sees as the extraordinary circumstances of the case, and given that bond drafting had evolved since *Elliott*, the Court decided to protect *NML* against Argentina's behaviour by requiring rateable payment.

Despite the concerns expressed in NML, it seems undeniable that the general trend regarding the *pari passu* clause is towards a limitation of creditors' remedies designed to limit their detrimental effects on restructuring processes.

4.2.2.3 The Belgian Anti-Vulture Fund Act

The second piece of domestic law limiting the remedies available to creditors examined in this thesis is the Belgian "Anti-Vulture Fund Act"[721]. The Belgian act, *ratione materiae,* has a limited scope, it applies solely to vulture funds, defined in the act as creditors active on the secondary market, and seeking to obtain an illegitimate gain through the purchase of sovereign credit instruments[722].

The characterisation of as an illegitimate gain for the purpose of the act requires a two-tiered test. First, the difference between the price of the credit instrument held by the debtor and its nominative value, or the amount the creditor seeks to obtain, must be 'manifestly disproportionate'[723]. Second, in addition, the transaction must fulfil at least two of the conditions enumerated in the act[724].

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[720] Zamour (n 74).
[721] Loi du 12 juillet 2015 relative à la lutte contre les activités des fonds vautours. For a broader analysis of the act see Lucas Wozny, 'National Anti-Vulture Funds Legislation: Belgium's Turn Survey: The New Activists and Corporate Governance: Notes' (2017) 2017 Columbia Business Law Review 697; Alexandre Belle, 'La Loi Belge Anti-Fonds Vautours Au Sein Du Droit International Sur La Dette Souveraine : Le Droit National Comme Outil de Signalement et de Gestion de Risques de Défaut' (2019) 2018 Revue Belge de Droit International / Belgian Review of international law 152.
[722] Loi du 12 juillet 2015 relative à la lutte contre les activités des fonds vautours.
[723] ibid.
[724] (1)The debtor must be defaulting or clause to default at the time of the purchase of the debt titles. (2) The creditor is incorporated in a tax haven. (3) The creditor has systematically used legal proceedings against the sovereign debtor in order to obtain payment on its debt titles. (4) The debtor is undergoing a restructuring process and the creditor has refused to take part in said process. (5) The creditor has abused of the debtor's weakness to negotiate a disproportionate settlement agreement. (6) Payment of the sums asked by the creditor

If a creditor is characterised as a vulture fund for the purpose of the act, then the amount obtainable either in payment, or in execution, before Belgian tribunals is capped at the market value of its credit titles at the moment of their purchase[725].

The Belgian anti-vulture act is unique as it is, at today's, date the sole piece of legislation seeking to prevent vulture funds from benefitting of secondary market purchases. Its functioning is inspired by the abuse of rights doctrine and the "*lésion qualifiée*"[726] theory – the acceptance that a disproportion between two obligations can lead to the rescission of a contract[727]. The first of these legal constructions features heavily within the international law elements of the restructuring protection model, as exposed *infra*.

From a comparative law perspective, the act uses notion close to the common law champerty defence, analysed in chapter 3[728]. The purpose of the Belgian act is, as the champerty defence, to prevent creditors to use civil courts as a way to profit from speculation[729]. The Belgian act, according to the *travaux préparatoires* pursues a double objective by focusing on vulture funds. The first is to prevent the acquisition of "immoral gains" using Belgian courts and tribunals[730]. The second, more relevant purpose, is to strike against the disruption caused by vulture funds within the sovereign debt market[731].

The Belgian Anti-Vulture Fund Act, fundamentally, is designed as an incentive against vulture fund litigation[732]. It caps the amount that can be obtained through Belgian courts and

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would have an unfavourable impact on the public finances of the State debtor and is susceptible to compromise the socio-economic development of its population. ibid; Wozny (n 721); Belle (n 721).

725 Loi du 12 juillet 2015 relative à la lutte contre les activités des fonds vautours.

726 ibid; 'Proposition de Loi Relative à La Lutte Contre Les Activités Des Fonds Vautours, Doc. Parl., Ch. Repr., 19 Juin 2015, N°54-1057/003' <http://www.lachambre.be/kvvcr/showpage.cfm?section=/flwb&language=fr&cfm=/site/wwwcfm/flwb/flwbn.cfm?lang=F&legislat=54&dossierID=1057>.

727 The *lésion qualifiée* theory does not stem directly from the civil code but is a judicial innovation. In Belgian law see *Cour de Cassation (Belgique) arret du 10 Septembre 1971* (1972) 1 Pasicrisie 28. For an overview of the theory's role in contract law see notably Catherine Goux, 'L'erreur, le dol et la lésion qualifiée: analyse et comparaisons' <https://researchportal.unamur.be/en/publications/lerreur-le-dol-et-la-l%C3%A9sion-qualifi%C3%A9e-analyse-et-comparaisons> accessed 20 February 2020.

728 RD Cox, 'Champerty as We Know It' (1982) 13 Memphis State University Law Review 139.

729 ibid; 'Proposition de Loi Relative à La Lutte Contre Les Activités Des Fonds Vautours, Doc. Parl., Ch. Repr., 19 Juin 2015, N°54-1057/003' (n 726).

730 'Proposition de Loi Relative à La Lutte Contre Les Activités Des Fonds Vautours, Doc. Parl., Ch. Repr., 19 Juin 2015, N°54-1057/003' (n 726).

731 It should be noted here that vulture funds used the Belgian courts and tribunals on multiple occasion. First by seeking to attach payment flowing through Euroclear, seated in Bruxelles by using the *pari passu* clause, as exposed *supra*; second by seeking unsuccessfully to enforce court decision on the accounts of the Argentinean embassy in Bruxelles. *Elliott Assocs., L.P.* (n 323); *Republic of Nicaragua v LNC Investment LLC* (n 398); *République d'Argentine c. NML Capital LTD* (n 407); 'Proposition de Loi Relative à La Lutte Contre Les Activités Des Fonds Vautours, Doc. Parl., Ch. Repr., 19 Juin 2015, N°54-1057/003' (n 726).

732 In that context, the anti-vulture fund act only seeks to disincentivise one specific category of holdouts, vulture funds. Because the amount used by the act is the price of the bonds paid by the bondholder, it is unlikely

tribunals to the market value of the bonds[733]. As vulture funds act as arbitrageurs, profiting from the difference between the market value of the bonds and their legal value[734], the act shuts down their profit window, making it impossible for a vulture funds to raise profits by relying Belgian courts and tribunals.

4.2.2.4 Legislation reinforcing Sovereign Immunities

A final way via which domestic lawmakers have limited the remedies available to creditors has been to further reduce the potential pool of attachable assets a litigating creditor could seize. In 2010, the United Kingdom enacted the Debt Relief (Developing Countries) Act[735]. The aim of the act is to prevent enforcement on the funds directed to aid for the development of Heavily Indebted Poor Countries. Belgium had enacted similar legislation in 2008[736].

Similarly, France enacted an anti-vulture fund legislation pursuing the same objective, although with a wider scope of application than the Belgian and UK act. The 2016 French act on "*transparency, fight against corruption and modernisation of economic life*"[737] focuses in its article 60 on vulture fund litigation.

The French act prevents the attachment of sovereign assets, regardless of their nature, by a State's creditor if three conditions are fulfilled:

1. The sovereign debtor features on the list of beneficiaries for aid to development drawn by the OECD.
2. The creditor obtained its debt title when the debtor was either in default or had emitted a restructuring proposal.

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that retails investors, would fall under its scope of application, unless they have purchased their bonds at a steep discount on the secondary market.

[733] In practice however, the effects of the act being limited to lawsuits brought to Belgium, its broader effects on the sovereign debt market are bound to be limited. On the potential effects of the act and its role within the current legal landscape on sovereign debt see Belle (n 721).

[734] On the two values of sovereign bonds see *CIBC bank and Trust Company (Cayman) v. Banco Central do Brasil, Banco Central do Brasil S.A., and Citibank N.A.* (n 190); Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 1) 304. On vulture funds as arbitrageurs see Belle (n 548). On vulture funds trading strategy in general see Jonathan I Blackman and Rahul Mukhi, 'Evolution of Modern Sovereign Debt Litigation: Vultures, Alter Egos, and Other Legal Fauna, The' (2010) 73 Law and Contemporary Problems 47; Fisch and Gentile (n 73).

[735] Debt Relief (Developping Countries) Act 2010.

[736] Loi visant à empêcher la saisie ou la cession des fonds publics destinés à la coopération internationale, notamment par la technique des fonds vautours, article 60.

[737] Ibid

3. The debtor's default or restructuring has occurred less than 48 months prior to a creditor's attempt to attach the sovereign's assets[738].

The main difference between the French act and the UK and Belgian act is that in France's case, the entirety of a sovereign's assets is shielded from attachment. In the other acts, only the funds directed towards aid for development are protected. However, the French act requires a default or restructuring proposal to have occurred when the others do not.

Apart from these differences, the three acts pursue the same objective: preventing the assets of particularly vulnerable debtors to be attached by creditors. By preventing attachment of sovereign's assets, domestic lawmakers can disincentivise holding out. As exposed in chapter 3, one of the main reasons why holdout creditors had to rely on the *pari passu* clause to obtain payment on their bonds lied in the difficulty to find attachable assets belonging to a sovereign. Limiting said overall pool of asset, should further discourage creditors from refusing to participate in a restructuring process.

In addition, focusing on States relying on aid for development and granting them specific protection makes sense as these State need access to these funds to return to financial stability. Hence, shielding the funds of economically distressed States from attachment helps in ensuring that said States will be able to meet their contractual obligations to most creditors and therefore be able to return to capital markets. Moreover, the protection of the assets of particularly vulnerable debtors protects their population as it is most likely to suffer during the restructuring process.

This protection of particularly vulnerable debtors has parallels in international law, in particular the move apparent in the decision of the Eritrea-Ethiopia decisions towards limiting war reparations if they prevent a State from fulfilling its obligations under International Human Rights[739]. The logic here appears similar in that special protection is granted to economically vulnerable States and their population to guarantee that the

[738] LOI n° 2016-1691 du 9 décembre 2016 relative à la transparence, à la lutte contre la corruption et à la modernisation de la vie économique.
[739] *Final Award, Ethiopia's Damage Claim* (2009) XXVI Rep Int Arbitr Awards 631 (Eritrea-Ethiopia Claims Commission); d'Argent (n 60); Pierre D'Argent, 'La Commission des réclamations Erythrée/Ethiopie : suite et fin' (2009) 55 Annuaire Français de Droit International 279; Michael J Matheson, 'Damage Awards of the Eritrea-Ethiopia Claims Commission, The' (2010) 9 Law & Practice of International Courts and Tribunals 1.

sovereign's responsibility does not prevent it from protecting the human rights of its population[740].

Finally, in addition to preventing creditors from attaching funds linked to aid for development, Belgium, in reaction to the *Elliott* case has also legislated to prevent creditors from blocking payments flowing through Euroclear[741]. While Euroclear is not sovereign, and therefore the modifications of the 1999 Euroclear act cannot be read as a strengthening of sovereign immunities *sensu stricto*, the purpose of shielding payment flowing through the clearing house is similar to the one of the dispositions mentioned above.

4.2.3 The Provision of Funds to facilitate the Debtor's Return to Debt Sustainability

4.2.3.1 The Provision of Funds to the Debtor: Overview

So far, the legal dispositions analysed in this section focused on deterring holdout enforcement, either by a curbing of creditor's ability to disrupt the restructuring process or by focusing on the process via which States and their creditors can reach an agreement. The last key component of the anti-holdout model is the development of legal tools enabling the State to obtain the liquidities necessary to ensure its return to debt sustainability.

Ensuring that the sovereign can return to debt sustainability as swiftly as possible during times of crisis makes sense as doing so encourages creditors to accept a restructuring proposal given that it reduces the likelihood of the sovereign ultimately defaulting. Moreover, again, it limits the impact of restructurings and defaults on the debtor's population. Most of the domestic law measures designed to facilitate the obtention of haircuts have already been examined within this chapter and thus, will only be briefly mentioned only so far as they enable the State to obtain additional liquidities. The international law aspects of this component, as with other components is analysed in the following section.

[740] Similar principles seem to have been followed regarding the German World War I and World War II debt, as well as for Congo's debt. For an overview of the question see Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 148–153.
[741] Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 94; 'Loi Du 28 Avril 1999 Visant à Transposer La Directive 98/26/CE Du 19 Mai 1998 Concernant Le Caractère Définitif Du Règlement Dans Les Systèmes de Paiement et de Règlement Des Opérations Sur Titres.'

4.2.3.2 The role of Domestic Law in re-allocating Funds to the Debtor

As previously exposed, the main purpose of Collective Action Clauses is to prevent holdouts by binding large swaths of a State's creditors to a same restructuring plan via a vote. In that regard, CACs not only implement majoritarian decision making during sovereign debt restructurings, but also facilitates the obtention of a haircut by the sovereign. Logically, if holders of bonds issued with a Collective Action Clause cannot holdout, States benefit of the haircut on their sovereign bonds when, without the clause they would have to pay this particular class of creditors in full. As such, this enables sovereigns to free up more liquidities during a restructuring process without requiring larger cutbacks on repayment for all creditors, thus avoiding future market punishment or a refusal by a majority of creditors.

In other words, CACs let sovereigns reduce payment to creditors who otherwise would have been paid in full without needing to further negotiate, or further reduce repayment to creditors who have already accepted a restructuring offer. As CACs, the aforementioned reinforcement of immunities for particularly vulnerable sovereigns further protect their access to liquidities as it prevents foreign creditors to seize funds that the debtor could use in order to bring itself back to debt sustainability.

4.3 The Anti-holdout model in international law

4.3.1 Introduction

In the absence of a multilateral system dealing with sovereign debt restructuring, understanding how international law has moved towards the anti holdout model requires focusing on a broad array of sources. In treaty law, there appears to be a movement towards the exclusion of sovereign debt from the scope of application *ratione materiae* of BITs.

International soft law, namely the UNCTAD principles on sovereign lending and borrowing [742] and the UNGA resolution on basic principles for sovereign debt restructuring[743] have pushed forward for the application of the general principle of good faith, and the abuse of rights doctrine to sovereign debt disputes. Said principles seem to have been

[742] United Nations Conference on Trade and Development (n 21).
[743] United Nations General Assembly, 'Resolution 69/319: Basic Principles on Sovereign Debt Restructuring Processes' (n 22).

applied in the case law of the ECtHR[744] and the ECJ[745]. Lastly, the international norms regarding the bail-out of States facing sovereign debt crises have been broadened following the Greek crisis.

As previously, this thesis will treat each component of the anti-holdout model separately. In particular, it argues that the use of good faith and the abuse of rights doctrine bring majoritarian decision making before international courts. Similarly, the explicit exclusion of sovereign debt from BITs and other IIAs, the *Poštová* decision, and a broader reading of the necessity defence limit the remedies available to creditors. Finally, changes in the international law on bailouts has served as a way to further increase the access of heavily indebted sovereigns to the liquidities they need to fulfil their immediate payment obligations.

4.3.2 Good Faith and the Abuse of Rights Doctrine as Implementing Majoritarian Decision-Making at the International Level

The use of good faith and the abuse of rights doctrine in international litigation on sovereign debt has been pushed forward by the UNCTAD's principles on sovereign debt restructuring[746] and the recent UN General Assembly resolution on sovereign debt[747]. In order to understand their potential for sovereign debt litigation, one must first determine the normativity of those principles, either as part of the soft law instruments which enshrine them or in general international law.

4.3.2.1 The Normativity of the UNCTAD Principles and the UNGA Resolution

In 2012, UNCTAD adopted the principles on promoting responsible sovereign lending and borrowing[748]. Their drafting began in 2009, in the wake of the financial crisis in order to facilitate coordination between creditors and debtor-States by establishing a set of common principles and practices related to sovereign debt[749]. The idea was to rely on a common

[744] *Mamatas et autres v. Greece* (n 18).
[745] *Alessandro Accorinti and others v. European Central Bank* (n 19).
[746] United Nations Conference on Trade and Development (n 16) 3–5.
[747] United Nations General Assembly, 'Resolution 69/319: Basic Principles on Sovereign Debt Restructuring Processes' (n 22); Goldmann, 'Putting Your Faith in Good Faith: A Principled Strategy for Smoother Sovereign Debt Workouts' (n 651).
[748] United Nations Conference on Trade and Development (n 16) 3-5.
[749] ibid; Carlos Espósito, Yuefen Li and Juan Pablo Bohoslavsky, 'Introduction' in Carlos Espósito, Yuefen Li and Juan Pablo Bohoslavsky (eds), *Sovereign Financing and international law* (Oxford University Press 2013) <http://www.oxfordscholarship.com/view/10.1093/acprof:oso/9780199674374.001.0001/acprof-9780199674374-chapter-1> accessed 3 October 2016, 3.

international soft law instrument to fill the international legal void, and smooth out the discrepancies in the domestic law approaches, regarding sovereign indebtedness[750].

The principles were drafted by an expert group involving leading authorities in law and economics, private investors, and NGOs. It also involved the Bretton Woods institutions as well as representatives from the Paris Club as observers[751].

UNCTAD identifies seven principles governing the behaviour of lenders:

- Agency (the recognition that the debtor-State is responsible for their population's interest);
- Informed decisions (the responsibility to provide information to the debtor);
- Due authorization;
- Responsible credit decision;
- Project financing;
- International cooperation (duty to comply with UN sanctions)
- Debt restructurings (duty to restructure in good faith if the debtor is manifestly unable to service its debts)[752].

For borrowers the principles are:

- Agency;
- Binding Agreements (the fact that a sovereign debt contract is a binding agreement);
- Transparency;
- Disclosure and Publication;
- Project Financing;
- Adequate management and monitoring
- Avoiding incidences of over borrowing
- Restructuring (if a restructuring is unavoidable, it should be effectuated in a prompt efficient and fair manner)[753].

Similarly, the UN General Assembly adopted a series of 9 basic principles:

Notably, principle 1 states:

> *"A Sovereign State has the right, in the exercise of its discretion, to design its macroeconomic policy, including restructuring its sovereign debt, which should not be*

[750] United Nations Conference on Trade and Development (n 16) 3-5.
[751] United Nations Conference on Trade and Development (n 16) 3-4.
[752] ibid.
[753] ibid.

frustrated or impeded by any abusive measures. Restructuring should be done as the last resort and preserving at the outset creditors' rights."[754]

Principle 2 adds:

"Good faith by both the sovereign debtor and all its creditors would entail their engagement in constructive sovereign debt restructuring workout negotiations and other stages of the process with the aim of a prompt and durable re-establishment of debt sustainability and debt servicing, as well as achieving the support of a critical mass of creditors through a constructive dialogue regarding the restructuring terms"[755]

The resolution, in its principles 3 and 4 also establishes a duty of transparency and impartiality for all actors involved. It imposes a duty of equitable treatment on the State debtor, underlining that:

"Creditors have the right to receive the same proportionate treatment in accordance with their credit and its characteristics. No creditors or creditor groups should be excluded ex ante from the sovereign debt restructuring process."[756]

Principle 7 underlines the importance of legitimacy and the respect of the rule of law during restructuring processes. The resolution also reaffirms the right of States to their sovereign immunities in its principle 6.

Principle 8 establishes a principle of sustainability of sovereign debt restructurings, meaning that:

"sovereign debt restructuring workouts [should be] completed in a timely and efficient manner and lead to a stable debt situation in the debtor State, preserving at the outset creditors' rights while promoting sustained and inclusive economic growth and sustainable development, minimizing economic and social costs, warranting the stability of the international financial system and respecting human rights."[757]

[754] United Nations General Assembly (n 17) principle 1.
[755] ibid principle 2.
[756] ibid principle 5.
[757] ibid principle 8.

Finally, the resolution underlines the majoritarian nature of sovereign debt restructurings, underlining that:

> *"sovereign debt restructuring agreements that are approved by a qualified majority of the creditors of a State are not to be affected, jeopardized or otherwise impeded by other States or a non-representative minority of creditors, who must respect the decisions adopted by the majority of the creditors. States should be encouraged to include collective action clauses in their sovereign debt to be issued"*[758].

The Resolution was adopted by 136 votes to 6, and 41 abstentions[759]. On average, creditor States either voted against (notably the United Kingdom and the United States), or abstained[760].

As their mere adoption by UNCTAD and the UNGA does not automatically lead to their normativity, there are two possible sources for their mandatory nature. First, the resolution and the basic principles could codify norms that are already normative[761]. Second, the adoption of these texts by both international organisations could create new customary international law[762].

The argument that the UNGA resolution and the UNCTAD principles can create new customary norms is problematic for two reasons[763]. Custom, to arise, as per the ICJ case-law needs a combination of two elements: State practice and *opinio iuris cive necessitatis*[764]. The

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[758] ibid principle 9.
[759] 'General Assembly Sixty-Ninth Session (Official Records) 102nd Plenary Meeting' <http://www.un.org/en/ga/search/view_doc.asp?symbol=A/69/PV.102> 9.
[760] ibid.
[761] On this question see Goldmann (n 617) 119-120. See also generally Matthias Goldmann, 'On the Comparative Foundations of Principles in international law' in Carlos Espósito, Yuefen Li and Juan Pablo Bohoslavsky (eds), *Sovereign Financing and international law* (Oxford University Press 2013) <http://www.oxfordscholarship.com/view/10.1093/acprof:oso/9780199674374.001.0001/acprof-9780199674374-chapter-6> accessed 6 October 2016; Howse (n 29).
[762] Howse (n 31).
[763] The arguments *infra* focus purely on the normative impact of the UNCTAD principles and the UNGA resolution. Beyond those two soft law instruments it is undeniable that, in general, international *soft law*, and in particular UNGA resolutions can create new customary international law. See e.g. Marko Divac Öberg, 'The Legal Effects of Resolutions of the UN Security Council and General Assembly in the Jurisprudence of the ICJ' (2005) 16 European Journal of international law 879; Stephen M Schwebel, 'The Effect of Resolutions of the U.N. General Assembly on Customary international law' (1979) 73 Proceedings of the ASIL Annual Meeting 301; *Legal Consequences for States of the Continued Presence of South Africa in Namibia (South West Africa) notwithstanding Security Council Resolution 276 (1970), Advisory opinion* [1971] ICJ Rep 16 (International Court of Justice). However, this thesis argue that these two specific instances of *soft law* have not done so.
[764] *North Sea Continental Shelf Cases, Federal Republic of Germany v. Denmark, Federal Republic of Germany v. Netherlands* (n 377) para 77; Crawford and Brownlie (n 384) 23; Jan Klabbers, *international law* (2nd Edition edition, Cambridge University Press 2013) 28–32.

International Court of Justice, notably in its *Nicaragua*[765] and its *Nuclear Weapons*[766] decisions, seems to consider that votes in favour of a general assembly resolution can, in certain circumstances, constitute the evidence of an *opinio iuris*[767]. In order for it to be the case, one must either show that the votes in favour of the resolution were cast by States believing in the normative content of the resolution, or that the resolution is framed in a normative manner[768], this, arguably could be the case here.

However, even if one agrees that the two *soft law* instruments prove a favourable *opinio iuris*, identifying a general and constant State practice on sovereign lending and borrowing is more problematic. The vast majority of creditors since the 1970s have been private entities whose practice cannot create new customary norms[769]. Moreover, when sovereigns have been involved in restructuring a debtor's sovereign debt, the solutions deployed have been varied, usually implemented on an *ad hoc* basis, and generally driven more by the "*desire to develop pragmatic solutions for concrete problems"*[770] rather than the creation of general norms[771].

However, certain dispositions of both texts can be deemed to codify already existing norms of international law, in particular those referring to good faith[772].

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[765] *Case concerning Military and Paramilitary Activities against Nicaragua (Nicaragua v United-States) (merits)* (1986) 1986 ICJ Rep 14 (ICJ) 100-101, 106-108, cited notably by Alain Pellet, 'La Formation Du Droit International Dans Le Cadre Des Nations Unies' (1995) 6 European Journal of international law 401, 416.
[766] *Legality of the Threat or Use of Nuclear Weapons (advisory opinion)* (1996) 1996 ICJ Rep 226 (ICJ) para 71.
[767] Pellet (n 773); Blaine Sloan, 'General Assembly Resolutions Revisited (Forty Years Later)' (1988) 58 British Yearbook of international law 39.
[768] Pellet (n 734) 406; Sloan (n 736); Waibel, 'Out of Thin Air?' (n 25) 90.
[769] Waibel, 'Out of Thin Air?' (n 25) 90.
[770] ibid 91.
[771] Ibid.
[772] In this sense see Antonis Bredimas, Anastasios Gourgourinis and Georges Pavlidis, *The Legal Contours of Sovereign Debt Restructuring under the UNCTAD Principles: Antagonism and Convergence between Standards of Domestic Insolvency Law and International Investment Protection Law* (Oxford University Press 2013) <http://www.oxfordscholarship.com/view/10.1093/acprof:oso/9780199674374.001.0001/acprof-9780199674374-chapter-7> accessed 20 February 2020; United Nations Conference on Trade and Development (n 16), preamble.

4.3.2.2 Good Faith and the Abuse of Rights Doctrine in General international law

Good faith is usually understood as a general principle of international law, as defined by article 38 of the ICJ statute[773]. The abuse of rights doctrine seems to be generally understood as a subset of the obligation to act in good faith[774].

As defined by Oppenheim, general principles of international law refer to "*the general principles of municipal jurisprudence, insofar as they are applicable to relations of States*"[775]. This echoes the idea, expressed in article 38, that the legal principles of law recognized by the "*civilized nations*" are *per se* sources of international law[776]. Thus understood, general principles, as featured in article 38 are legal norms shared by most domestic legal orders, and applicable to the management of international relations[777].

Good faith, and the abuse of rights doctrine are well recognised within domestic law, whether civil or common. Good faith, features in articles 1134 of the French Civil Code[778], 242 of the German Civil Code[779], article 5 (3) of the Swiss Constitution[780] or article 1-201 of the US UCC[781]. While English common law does not seem to require a general duty of good faith, it recognises separate distinct obligations which are usually classified under the good faith umbrella-term in other legal regimes[782]. Thus, the recognition of good faith as a general principle of international law is hardly surprising.

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[773] Statute of the International Court of Justice 1945; Steven Reinhold, 'Good Faith in international law' (2013) 2 UCL Journal of Law and Jurisprudence 40; Markus Kotzur, 'Good Faith (Bona Fide)', *Max Planck Encyclopedia of Public international law* (2009) <http://opil.ouplaw.com/view/10.1093/law:epil/9780199231690/law-9780199231690-e1412?rskey=fhLubm&result=1&prd=EPIL>; Malcolm N Shaw, *international law* (8 edition, Cambridge University Press 2017) 77.

[774] The relationship between the two principles is heavily debated in the international legal scholarship. While most authors argue that the abuse of rights doctrine is a sub-category or a corollary of the good faith principle containing different obligations than good faith in general some authors have argued that the two notions are for all intents and purposes equivalent. Goldmann, 'Putting Your Faith in Good Faith: A Principled Strategy for Smoother Sovereign Debt Workouts' (n 617); Robert Kolb, 'Principles as Sources of international law (With Special Reference to Good Faith)' (2006) 53 Netherlands international law Review 1, 463; *Fisheries Case (United-Kingdom v Norway)* (1951) 1951 ICJ Rep 116 (ICJ) 141-142.

[775] L Oppenheim, RY Jennings and Arthur Watts, *Oppenheim's international law. Vol.1: Peace* (9th ed, Longman 1992) para 12; cited in Crawford and Brownlie (n 384) 35.

[776] Statute of the International Court of Justice, article 38; Crawford and Brownlie (n 384) 35.

[777] Ibid; Kolb (n 744) 3-4.

[778] Code Civil (France) version consolidée au 1 mars 2019, article 1134.

[779] Bürgerliches Gesetzbuch s 242.

[780] Federal Constitution of the Swiss Confederation of 18 April 1999 s 5.

[781] Uniform Commercial Code ss 1–201; Reinhold (n 743) 42-44; See also Bernardo Cremades, 'Good Faith in International Arbitration' (2012) 27 American University international law Review <https://digitalcommons.wcl.american.edu/auilr/vol27/iss4/4>.

[782] Notably the principle of promissory estoppel. It should however be noted that Lord Mansfield noted in a 1766 case that good faith is “"the governing principle... applicable to all contracts and dealings”. Carter v Boehm [1766] 97 ER (KB) 1162 ; Reinhold (n 743) 43.

While originally a civil law praetorian innovation, the abuse of rights doctrine finds equivalent within common law systems[783]. The abuse of rights principle's normativity, in that context has been generally been understood as deriving from the normativity of good faith. It can also be argued that it stems from its existence in civil law and the law of socialist States, as well as of these similar common law principles[784].

In international law, both good faith and the abuse of rights doctrine feature in the case-law of the ICJ[785] and the PCIJ[786], and numerous other International Courts and Tribunals[787]. While the normativity of good faith and the abuse of rights doctrine in international law seems well established, the exact content of these dispositions appears less defined.

Regarding good faith the content of the norm varies in international law. Good faith, notably, plays a central role regarding negotiations to solve disputes amicably[788]. It plays a key role in the VCLT, in particular regarding the applicability of treaty provisions post-signature but prior to their entry into force[789]. Good faith is also generally understood as a key principle of treaty interpretation[790].

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[783] For a discussion of common law application see in general Michael Byers, 'Abuse of Rights: An Old Principle, a New Age' (2002) 47 McGill Law Journal 489; Anna di Robilant, 'Abuse of Rights: The Continental Drug and the Common Law' (Social Science Research Network 2014) SSRN Scholarly Paper ID 2457018 <https://papers.ssrn.com/abstract=2457018> accessed 20 October 2016; Alexandre Kiss, 'Abuse of Rights', *Max Planck Encyclopedia of Public international law* (Oxford University Press 2006) <http://opil.ouplaw.com/view/10.1093/law:epil/9780199231690/law-9780199231690-e1371>; BO Iluyomade, 'Scope and Content of a Complaint of Abuse of Right in international law' (1975) 16 Harvard international law Journal 47.

[784] Kiss (n 791); Byers (n 791); Pierre-Emmanuel Moyse, 'L'Abus de Droit: L'Antenorme - Partie 1' (2011) 57 McGill Law Journal 859; Nikolaos Politis, 'Le Problème Des Limitations de La Souveraineté et La Théorie de l'abus Des Droits Dans Les Rapports Internationaux', *Recueil des cours, Collected Courses (Académie de Droit International de la Haye/Hague Academy of international law)*, vol 6 (Brill | Nijhoff 1925); Iluyomade (n 791).

[785] See e.g. *Nuclear Tests Case (New Zealand v France)* [1974] ICJ Rep 457 (International Court of Justice) para 49; *Pulp Mills on the River Uruguay (Argentina v Uruguay)* (2010) 2010 ICJ Rep 14 (ICJ) para 145; *Case concerning the Rights of Nationals of the United States of America in Morocco (France v United States of America)* [1952] ICJ Reprorts 1952 176 (ICJ) p 212; cited notably in Reinhold (n 743); Iluyomade (n 753).

[786] *Case concerning the Factory at Chorzow (claim for indemnity) (merits)* (n 379) p 15.

[787] See *inter allia Trail smelter case (United States, Canada)* (1941) III Rep Int Arbitr Awards 1905; *United States - Import Prohibition of Certain Shrimp and Shrimp Products, India and ors v United States* [2001] WTO Appelate Body WT/DS58/AB/RW.

[788] Reinhold (n 773) 56.

[789] 'Vienna Convention on the Law of Treaties (with Annex) (Vienna)' s 38 <https://treaties.un.org/doc/publication/unts/volume%201155/volume-1155-i-18232-english.pdf>, article 26; See also *Case concerning certain German interests in Polish Upper Silesia (merits)* (n 477) para 123; for a similar take in EU law see *Opel Austria GmbH v Council of the European Union* [1997] CJEU T-115-94, para 89.

[790] 'Vienna Convention on the Law of Treaties (with Annex) (Vienna)' (n 759) s 31, article 31. On this question see Eric De Brabandere and Isabelle Van Damme, *Good Faith in Treaty Interpretation* (Oxford University Press 2015) <http://www.oxfordscholarship.com/view/10.1093/acprof:oso/9780198739791.001.0001/acprof-9780198739791-chapter-3> accessed 7 March 2019.

Generally, the ICJ seems to read good faith not as having a content of its own, but rather as a qualifier for the content and the exercise of other legal rights and obligations. Therefore, the rights derived from good faith and the abuse of rights doctrine are generally characterised as ‘interstitial’[791].

In international investment law, good faith has mostly been employed by arbitral tribunals in the context of litigation including FET clauses. It has, *inter alia*, been used as a way to protect investor’s legitimate expectations[792]. Alternatively, it has been used by States as a mean to dismiss claims brought by investors acting in *mala fide*[793].

Traditionally, the abuse of rights doctrine has been read as containing three different obligations:

- The prohibition, for a State, to exercise its rights in such a way as to hinder another State from enjoying its own rights[794].
- The prohibition for a State to exercise its rights for an end which they were not intended for[795]
- The prohibition of the arbitrary exercise of a right, causing injury to another party[796]

A common ground between good faith and the abuse of rights doctrine is that they seek to create a limit to the way in which usually recognised international rights can be exercised by their holders[797]. They are, in other words, a limit to an individualistic use of rights, placed in

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[791] *Case concerning Border and Transborder Armed Actions (Nicaragua v Honduras) (Jurisdiction and Admissibility)* (1988) 1998 ICJ Rep 69 (ICJ) para 60; *Nuclear Tests Case (New Zealand v. France)* (n 755) para 49; Sanja Dajic, ‘Mapping the Good Faith Principle in International Investment Arbitration" Assessment of Its Substantive and Procedural Value’ (2012) 46 Zbornik Radova 207. See also Vaughan Lowe, *The Politics of Law-Making: Are the Method and Character of Norm Creation Changing?* (Oxford University Press 2001) <http://www.oxfordscholarship.com/view/10.1093/acprof:oso/9780199244027.001.0001/acprof-9780199244027-chapter-11> accessed 6 March 2019; Andreas R Ziegler and Jorun Baumgartner, ‘Good Faith as a General Principle of (International) Law’ in Andrew D Mitchell, M Sornarajah and Tania Voon (eds), *Good Faith and International Economic Law* (Oxford University Press 2015) <http://www.oxfordscholarship.com/view/10.1093/acprof:oso/9780198739791.001.0001/acprof-9780198739791-chapter-2> accessed 1 September 2016, 15.

[792] *Saluka Investments B.V. v. The Czech Republic* (n 507) para 231 et s.; *Técnicas Medioambientales Tecmed, S.A. (Award)v. The United Mexican States* (n 506) para 70 et s. See discussions in Paparinskis (n 510); Dajic (n 761).

[793] See e.g. *Robert Azinian, Kenneth Davitian, & Ellen Baca v The United Mexican States* [1999] NAFTA ARB (AF)/97/2; Dajic (n 761) 228. On this question see also Stephan W Schill and Heather L Bray, *Good Faith Limitations on Protected Investments and Corporate Structuring* (Oxford University Press 2015) <http://www.oxfordscholarship.com/view/10.1093/acprof:oso/9780198739791.001.0001/acprof-9780198739791-chapter-5> accessed 7 March 2019.

[794] Reinhold (n 743) 49.

[795] ibid.

[796] Ibid

[797] Ziegler and Baumgartner (n 761) 11-12; Hersch Lauterpacht, *The Function of Law in the International Community* (The Clarendon press 1933) 286.

the interest of a collectivity[798]. Understood as such, good faith and the abuse of right doctrine requires courts and tribunals to balance the interests of the party exercising its own rights with the damage caused to others by the exercise of said right[799]. To quote the famous *US-Shrimp* Case:

> "*One application of* [good faith], *the application widely known as the doctrine of abus de droit, prohibits the abusive exercise of a state's rights and enjoins that whenever the assertion of a right 'impinges on the field covered by [a] treaty obligation, it must be exercised bona fide, that is to say, reasonably'*."[800]

The Appellate Body, in that case, used the concept of reasonableness to create a limit on the exercise of rights by sovereigns when those rights "*impinge on the field covered by a treaty obligation*"[801]. In other words, if by exercising its rights, a State threatens the rights of others one must determine if the State has exercised its right in a reasonable fashion[802].

As previously mentioned, the idea that the exercise by State of their discretionary rights is limited by general principles of International law is heavily debated in the international legal scholarship.

Notably, the idea that a limit could be put on the exercise of rights by sovereigns seems to run against the *Lotus* principle[803]. Indeed, if International law enables States to do anything it does not prohibit[804], the international liability of a State should not logically be invoked when States exercise rights they hold[805]. Similarly, good faith and the abuse of rights, especially linked with the concept of reasonableness and the idea that there is a "*fonction*

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798 Duncan Kennedy and Marie-Claire Belleau, 'François Gény Aux États-Unis', *François Gény: mythes et réalités 1899-1999, Centenaire de Méthode d'interprétation et sources en droit privé positif - essai critique C. Thomasset, J. Vanderlinden, P. Jestaz (eds)* (Les éditions Yvon Blais 2000); di Robilant (n 783).

799 See Kennedy and Belleau (n 798); di Robilant (n 783).

800 *United States - Import Prohibition of Certain Shrimp and Shrimp Products, India and ors v United States* (n 787).

801 ibid para 158.

802 For an overview of the use of good faith within the WTO framework see Helge Elisabeth Zeitler, '"Good Faith" in the WTO Jurisprudence – Necessary Balancing Element or an Open Door to Judicial Activism?' (2005) 8 Journal of International Economic Law 721. Beyond US-Shrimp, good faith is also used in the WTO Dispute Settlement System as requiring parties to use dispute settlement in good faith. Peter Van Den Bossche, *The Law and Policy of the World Trade Organization* (Cambridge University Press - MUA) 267–268 <https://www.dawsonera.com/abstract/9780511670671> accessed 20 January 2015. See e.g. *US-FSC* (WTO Appelate Body report); *Argentina - Poultry Anti Dumping Duties (2003)* (WTO Appelate body).

803 *The Case of the SS Lotus* (1927) Series A-n10 Publ Perm Court Int Justice 3 (PCIJ).

804 ibid; Armin von Bogdandy and Markus Rau, 'The Lotus', *Max Planck Encyclopedia of Public international law* (OUP 2006); Reinhold (n 781).

805 Robert Kolb, 'La Règle Résiduelle de Liberté En Droit International Public ("Tout Ce Qui n'est Pas Interdit Est Permis") : Aspects Théoriques' (2001) 34 Revue Belge de Droit International / Belgian Review of international law 100; Reinhold (n 743) 57-58.

sociale des droits"[806], seem closely linked to natural law or at least a view of international law as a systematically coherent legal order[807].

While these criticisms of good faith and the abuse of rights doctrine are sound from a theoretical point of view, it seems that, in practice, the normativity of both norms is well established. Their use by well-established international adjudicative bodies appears to constitute a sufficient indication that international courts and tribunals might rely on both principles when adjudicating disputes on sovereign debt, regardless of the theorical objections against these norms.

4.3.2.3 Applying Good Faith and the Abuse of Rights Doctrine to Sovereign Debt

While the content of the obligations flowing from the general principle of good faith is debated in international law, the legal scholarship on sovereign debt, and the soft law instrument mentioned above, have highlighted several potential applications of the principles to debt restructurings.

If we focus on mentions of good faith in the UNCTAD principles and the UNGA resolution, the principles requires creditors to: "*behave in good faith and with cooperative spirit to reach a consensual rearrangement of those obligations"*[808] when a State is manifestly unable to service its debts.

Principle 7 adds that in that case, "*Creditors should seek a speedy and orderly resolution to the problem*"[809]. Similarly, the UNGA resolution encourages creditors and debtors to behave in good faith as it would entail the prompt and efficient resolution of sovereign debt crises[810]. The resolution also notes in its first principle that sovereign debt restructuring process should not be impended by any *abusive* measures by creditors[811].

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[806] This particular conception of the abuse of rights doctrine traces back to Louis Josserand, *De l'esprit Des Droits et de Leur Relativité: Théorie Dite de l'abus Des Droits* (Dalloz 1927).
[807] di Robilant (n 753) 713.
[808] United Nations Conference on Trade and Development (n 16) principle 7.
[809] ibid.
[810] United Nations General Assembly (n 17), principle 2.
[811] ibid.

One can divide the good faith principle, as understood in these two soft law instruments in three separate obligations:

First, good faith could provide the source for an obligation on the part of both debtors and creditors to restructure sovereign debt when a State's indebtedness becomes unsustainable. Principle 7 of the UNCTAD principles clearly expresses a duty to restructure in good faith when the sovereign debtor is manifestly unable to fulfil its contractual obligations[812]. The UNGA resolution hints at a similar understanding of the notion, but applies it to both parties of the sovereign debt transaction[813].

Second, good faith could form the basis of an obligation for both States and their creditors to negotiate during restructuring processes[814]. Again here, the idea expressed by UNCTAD that creditors should seek a speedy solution to sovereign debt crises hints at an obligation negotiate with the debtor in order to reach restructuring agreements[815]. Similarly, the reciprocal nature of the good faith obligation featured in the UNGA resolution implies that both States and their creditors should seek solutions to sovereign debt crises[816], thus implying a need for negotiation to reach such agreements[817].

Finally, good faith and the abuse of rights doctrine could provide a prohibition for creditors to disrupt sovereign debt restructuring processes[818]. Notably the UNGA resolution underlines that creditors cannot disrupt restructuring processes through abusive measures[819].

Applied to sovereign debt, good faith and the abuse of rights doctrine have several advantages. First, as general principles, they are already normative. This allows them to be applied in sovereign debt cases without requiring international law-making which would be opposed by creditor States[820]. Said opposition, famously, prevented the adoption of an IMF plan to create a Sovereign Debt Restructuring Mechanism rooted in international law[821].

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812 United Nations Conference on Trade and Development (n 16) principle 7.
813 United Nations General Assembly (n 17) principle 2.
814 Goldmann, 'Good Faith and Transparency in Sovereign Debt Workouts (Paper Prepared for the Second Session of the UNCTAD Working Group on a Debt Workout Mechanism)' (n 54) 10.
815 United Nations Conference on Trade and Development (n 16) principle 7.
816 United Nations General Assembly (n 17) principle 2.
817 In this sense see Goldmann, 'Putting Your Faith in Good Faith: A Principled Strategy for Smoother Sovereign Debt Workouts' (n 617) 130-131.
818 Goldmann, 'Good Faith and Transparency in Sovereign Debt Workouts (Paper Prepared for the Second Session of the UNCTAD Working Group on a Debt Workout Mechanism)' (n 54) 12.
819 United Nations General Assembly (n 17) principle 1.
820 Goldmann, 'Putting Your Faith in Good Faith: A Principled Strategy for Smoother Sovereign Debt Workouts' (n 617) 140.
821 For an overview of the criticisms of the IMF SDRM proposal see Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 160–167.

Therefore, by relying on general principles whose normativity is already broadly accepted, UNCTAD and the General Assembly can ensure that at least part of the content of their soft law instruments could find application *de lege lata*.

Second, as general principles, good faith and the abuse of rights doctrine find their source in domestic law. Far from merely cementing the normativity of good faith at the international level, the recognition of similar principles by domestic jurisdictions plays a key role in the application of obligations arising from good faith to sovereign debt litigation[822]. As already noted, the bulk of litigation, when it comes to sovereign debt, occurs at the domestic level. As good faith transcends the boundaries of international law it can potentially be applied before domestic jurisdictions[823]. As such, good faith obligations and the abuse of rights doctrine have the potential to be used by international courts and tribunals as well as domestic courts as a way to limit the remedies available to creditors. However, the effect of good faith is not merely to limit the remedies available to creditors. It encourages both parties in the debt transaction to negotiate sovereign debt restructurings. As such good faith strengthens, *de iure*, collective decision making.

[822] Goldmann, 'Putting Your Faith in Good Faith: A Principled Strategy for Smoother Sovereign Debt Workouts' (n 617) 140.

[823] This use of general principles as a way to bridge the gap between international and domestic law when it comes to sovereign debt litigation is a central element of the "*incremental approach*" to sovereign debt restructuring described by Bohoslavky and Goldmann. The incremental approach to sovereign debt restructuring is centred on the idea that debt sustainability is a "principle of public international law", understood by the authors as an axiomatic principle, that should guide the interpretation of other international norms. The argument of the authors relies on the idea that legal developments regarding sovereign debt since the 1950s, have led to the recognition by international actors that debt sustainability, as a principle, is recognised as a goal by a broad range of International Organisations. The authors base their arguments, *inter alia*, on the practice of International Organisations such as the Paris Club and the IMF during the second half of the 20th century, and more recently on the recognition of debt sustainability in the UNCTAD principles and the UNGA resolutions. Bohoslavsky and Goldmann (n 80).While this thesis agrees with the idea that, in facts, international practice has evolved towards the protection of debt sustainability, the claim that these actions have led to the elevation of debt sustainability as a key principle of international law, systematizing the international regulation of sovereign debt seems contestable. In particular, the use by the authors of Paris club practice to evidence the fact that debt sustainability would have reached such a status seems questionable for two reasons. First, Paris club negotiations only concern bilateral debts, therefore excluding most of the current source of sovereign indebtedness. Second, Paris club negotiations are conducted on a case-by-case basis, which seems to indicate that the sovereign taking part to said negotiations do so without the intent of developing new international legal norms. In addition, the reticence of creditor States towards the adoption of the UNCTAD principles and the UNGA resolution casts a doubt on whether or not one can characterise debts sustainability as an axiomatic principle of law. James A Haley, 'Sovereign Debt Restructuring: Good Faith or Self-Interest?' <https://www.cigionline.org/publications/sovereign-debt-restructuring-good-faith-or-self-interest> accessed 7 March 2019; Daphne Josselin, 'Regime Interplay in Public-Private Governance: Taking Stock of the Relationship between the Paris Club and Private Creditors between 1982 and 2005' (2009) 15 Global Governance 521; Vourc'h (n 57).

In addition to this pre-established normativity, good-faith-like reasoning has been used in two recent cases by the ECtHR and the ECJ to introduce majoritarian decision making in the international law on sovereign debt.

4.3.2.4 Quasi-Good Faith Obligations in the International Case-Law on Sovereign Debt

In the already mentioned *Mamatas* case[824], the European Court of Human Rights had to rule on the legality of the retroactive insertion by Greece of a collective action clause in Greek domestic bonds, during its 2012 restructuring process[825]. The applicants, a large number of individual holders of Greek nationals, holders of domestic bonds emitted by the Hellenic Republic alleged that said retroactive introductions breached, *inter* alia, article 1 of the 1st protocol to the ECHR[826].

Several issues ought to be highlighted regarding the background of the case. First, the retrofit CAC had been presented as a key feature of the Greek restructuring process and was expressly required by Greece's largest creditors[827]. Second, the applicants, because they were small holders, had not been invited to the negotiations regarding the Greek restructuring process[828]. Lastly, the Hellenic Republic's government had promised small investors that their bonds would not be affected by the restructuring process[829]. However, following the retroactive introduction of the CAC, the applicants faced a haircut on their bonds, despite refusing Greece's restructuring offer[830], as the restructuring plan had been approved by 91% of its creditors[831].

The proportionality test applied by the ECHR in *Mamatas* recalls the logic of the good faith principle or the abuse of rights doctrine[832]. The courts' reasoning is centred on three main axis.

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824 *Mamatas et autres v. Greece* (n 18).
825 Iversen (n 164).
826 *Mamatas et autres v. Greece* (n 13) para 8–25.
827 *Mamatas et autres v. Greece* (n 13) para 116; On the Greek restructuring process, and in particular the introduction of the retrofit CAC see Boudreau (n 49); Lee C Buchheit and G Mitu Gulati, 'How to Restructure Greek Debt' (Social Science Research Network 2010) SSRN Scholarly Paper ID 1603304 <http://papers.ssrn.com/abstract=1603304> accessed 19 August 2016.
828 *Mamatas et autres v. Greece* (n 13) para 12.
829 ibid.
830 The refusal of the applicants to participate in the restructuring process is meaningless once the CAC had been inserted in their bonds and once the required majorities had been reached.
831 *Mamatas et autres v. Greece* (n 13) para 20.
832 It should be noted that the Court, in its analysis of the Mamatas case does not apply the abuse of rights disposition featured in article 13 of the European Convention of Human Rights.

First, the Court focuses on the market value of the bonds at the time of the Greek restructuring. As said value was low, compared to the facial value of the bonds, the Court concludes that it seemed likely, at the time, that Greece would not be able to fulfil its contractual obligations[833]. In other words, the low value of the bonds is used by the court as an indication that the transaction in which the applicants were involved entailed a significant risk.

Second, the Court underlined that, while CACs did not feature in Greek domestic bonds, at the time of the restructuring, they were standard most international bond issues, and had been made mandatory by the for all Eurozone external debts[834]. Similarly, the Court noted that the retrofit CACs had been asked by Greece's largest creditors for the restructuring to proceed[835].

The Court then highlighted the risk inherent to all financial transactions, in particular those on sovereign debt. Then, drawing from the *Accorinti*[836] case exposed *infra*, it underlined that the applicants, in *Mamatas*[837], cannot have be characterised as "*prudent and circumspect*"[838] investors. Thus, they could not prevail themselves from having "*legitimate expectations*"[839] to be repaid.

Indeed, according to the Strasbourg Court, Greek bondholders, at the time of the restructuring knew, or ought to have known, of Greece's difficult financial position[840]. Thus, a prudent and circumspect investor should have, given Greece's circumstances, liquidated its position on Greek bonds. Failure to do so preventing them from having "*legitimate expectations*" to be repaid in full given Greece's financial health[841]. As such, the haircut caused by the retroactive introduction of a CAC in Greek bonds was deemed proportionate[842].

Several elements of the Court's reasoning in *Mamatas* need to be highlighted. First, the Court ties the proportionality of Greece's actions during its restructuring process to the legitimate expectations of creditors of obtaining repayment.

833 *Mamatas et autres v. Greece* (n 13) para 112.
834 ibid; Treaty Establishing the European Stability Mechanism (Brussels) article 12.
835 *Mamatas et autres v. Greece* (n 13) para 116.
836 *Alessandro Accorinti and others v. European Central Bank* (n 19).
837 *Mamatas et autres v. Greece* (n 13) 118.
838 ibid.
839 ibid; *Alessandro Accorinti and others v. European Central Bank* (n 14) para 76.
840 *Mamatas et autres v. Greece* (n 13) para 117-118.
841 ibid.
842 ibid.

Second, whether creditor's expectations are legitimate is dependent on three factors. First, the market value of the bonds, used as an indicator of the riskiness of the transaction. Second, the behaviour of the majority of creditors, *i.e.* whether most creditors accepted the restructuring offer or the retroactive insertion of the CAC. As with CACs, the majority here seems to be counted on a bond-by-bond basis. Third, the behaviour of the applicants *in concreto*, *i.e.* whether they liquidated their position when the situation appeared risky.

A similar line of reasoning features in *Accorinti v ECB*. The *Accorinti* case was introduced by small holders of Greek debt, however those were contesting the exclusion of the European Central Bank from the Greek restructuring process[843], and not the restructuring *per se*. The applicants argued that the exclusion of Greek bonds held by ECB from the restructuring process breached the EU law principle of legal certainty. They also contended that the exclusion of the bank breached the international law principle stating that creditors of a sovereign should be treated equally[844].

The applicants, *inter alia*, pleaded that their legitimate expectations had been breached by central bank as it concluded a separate exchange agreement with Greece, refused to participate in the Greek restructuring process, made Greek bonds eligible as collateral via a buy-back scheme only opened to other central banks[845]. These facts, according to the claimants, lead to a on their bonds since the private sector had to shoulder on its own to costs of the Greek restructuring[846].

The applicants underlines that their legitimate expectations been breached since ECB, through its president, had reassured holders of Greek bonds that the Bank would be part of a voluntary exchange. ECB had also allegedly promised that the Hellenic Republic would not default, that any restructuring of the Greek debt would be voluntary, that no reduction of the nominal value of the bonds could be imposed, and that if restructuring should occur, the Greek bonds would not be accepted as collateral by ECB[847]. The applicants claimed that, having relied on those assertions from Frankfurt, they incurred a loss on their holdings[848].

[843] *Alessandro Accorinti and others v. European Central Bank* (n 19).
[844] ibid paras 5-48.
[845] ibid.
[846] ibid.
[847] ibid.
[848] ibid.

According to the ECJ case-law, three conditions must be fulfilled for legitimate expectation against an EU authority to exist:

1) *"precise, unconditional and consistent assurances originating from authorised and reliable sources must have been given to the person concerned by the EU authorities"*[849]
2) *"those assurances must be such as to give rise to a legitimate expectation on the part of the person to whom they are addressed"*[850]
3) *"the assurances given must be consistent with the applicable rules"*[851]

Applying these principles to the *Accorinti* case, the court noted that:

> *"[W]here a prudent and circumspect economic operator is able to foresee the adoption of an EU measure likely to affect his interests, he cannot rely on that principle if the measure is adopted. Nor can economic operators have a legitimate expectation that an existing situation which is capable of being altered by the EU institutions in the exercise of their discretion will be maintained, especially in an area such as monetary policy, the subject-matter of which is constantly being adjusted according to variations in the economic situation"*[852].

Moreover, the Court added *obiter dicta*, that the purchase of sovereign debt is, *per se*, entailing a risk of loss on one's investment since it is subject to the "*hazardous movements*"[853] of capital markets. Regarding Greek bonds in particular, the Court pointed that, "*[i]n the light of the economic situation of the Hellenic Republic and the uncertainties concerning it at the time, the investors concerned cannot claim to have acted as prudent and circumspect economic operators*"[854]. This is especially the case given that some applicants purchased some of their securities when the Greek crisis was at its peak[855].

Given these facts, holders of Greek bonds "*were supposed to be aware of the highly unstable economic situation that determined the fluctuation of the value of the Greek bonds which*

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[849] ibid para 73.
[850] ibid, para 75.
[851] ibid.
[852] ibid para 82. The ECJ similarly highlighted that ECB's declarations could not have led to legitimate expectations since, *inter alia*, ECB is not responsible for decisions by a Member State to restructure its public debt. ibid.
[853] ibid.
[854] ibid.
[855] ibid.

they had acquired and also the appreciable risk of at least a selective default by the Hellenic Republic".

Building from these reasons the ECJ thus ruled:

> *"[A] prudent and circumspect economic operator […] could not have ruled out the risk of a restructuring of the Greek public debt, given the differing views prevailing in that regard within the euro area Member States and the other bodies involved"*[856].

The common thread between the *Mamatas* and *Accorinti* decisions is that both European Courts use the notion of legitimate expectations to limit the rights of creditors during restructuring processes. They hold that prudent and circumspect creditors should either liquidate their holdings of sovereign bonds if a restructuring is imminent, or accept the idea that they will suffer a loss.

This reasoning echoes the general principle of good faith, in particular its application as a reasonableness test. The key question raised by both these decisions lies in the determination of what constitutes a "*prudent and circumspect investor*"[857]. The criteria advanced by both jurisdictions rely on two distinct elements: first, the market value of the bonds they hold, second, the acceptance by a majority of actors of the measures implemented during the restructuring.

Regarding the first criteria, the logic of both courts is to use the market value of the bonds of a State as a proxy for default risk[858]. Quite logically, as implied by the European courts, if a State's default appears to be imminent, creditors not willing to assume the risk linked to said default sell, causing the market value of the bonds to plummet. Taking into account the price of the bond in the reasonableness test itself[859], introduces majority decision-making within appraisal by the courts of the necessity of restructuring process. The price of sovereign bonds plummeting is literally an indication of investors "voting with their feet" on the ability of a sovereign to repay its debt.

Similarly, the fact that both courts consider the acceptance by investors of the restructuring measures is a second way of introducing collective decision-making elements in their

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[856] ibid.
[857] *Mamatas et autres v. Greece* (n 18); *Alessandro Accorinti and others v. European Central Bank* (n 19).
[858] *Mamatas et autres v. Greece* (n 18); *Alessandro Accorinti and others v. European Central Bank* (n 19).
[859] And not to compute compensation, whether when assessing the lawfulness of an expropriation or at the *quantum* stage.

reasoning[860]. It enables them to ensure that most creditors are in favour of the restructuring measures pursued by the State.

4.3.3 Limiting Creditors' Remedies in international law

In addition to the potential use of good faith and the abuse of rights doctrine, international law has moved towards limiting the remedies available to creditors in two main areas. First, there is a trend in International Investment Law towards the exclusion of sovereign bonds from ISDS instruments. Second, there has been a push for a broader reading of the necessity defence, both in International Soft Law and in the case-law on economic necessity.

4.3.3.1 The Exclusion of Sovereign Debt from ISDS

As exposed in the third chapter of this thesis, the characterisation of sovereign debt as an investment for the purpose of International Investment law[861] is one of the key components in implementing the creditor protection model.

In response to said characterisation three movements within treaty drafting have occurred. First, the EU integrated trade-and-investment treaty drafting practice features specific dispositions on sovereign debt[862]. Second, there is an increase in the number of BITs explicitly excluding sovereign debt instruments from their scope of application *ratione materiae*. Finally, a recent arbitral decision declined to characterise sovereign bonds as investments under the meaning of article 25 of the ICSID convention[863].

Regarding EU treaty drafting, CETA has included specific provisions on sovereign debt. Annex 8-B article 2 reads:

> *"No claim that a restructuring of debt of a Party breaches an obligation under Sections C and D may be submitted, or if already submitted continue, under Section F if the restructuring is a negotiated restructuring at the time of submission, or becomes a*

[860] *Mamatas et autres v. Greece* (n 18); *Alessandro Accorinti and others v. European Central Bank* (n 19).
[861] *Abaclat and Others v. Argentine Republic* (n 17); *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17); *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17).
[862] 'Comprehensive Economic and Trade Agreement between Canada, of the One Part, and the European Union and Its Member States, of the Other Part, 14 September 2016 (Brussels)' article 12.
[863] *Poštová banka, a.s. and Istrokapital SE v. Hellenic Republic (Award)* (n 17).

negotiated restructuring after such submission, except for a claim that the restructuring violates Article 8.6 or 8.7."[864]

Article 3 adds:

"Notwithstanding Article 8.22.1(b) and subject to paragraph 2, an investor of a Party may not submit a claim under Section F that a restructuring of debt of a Party breaches an obligation under Sections C and D (other than Article 8.6 or 8.7)7 unless 270 days have elapsed from the date of submission by the claimant of the written request for consultations pursuant to Article 8.19."[865]

In other words, CETA excludes any claims on sovereign debt once a negotiated restructuring has been agreed upon[866]. This exclusion should apply to either a restructuring via collective action clauses or a traditional debt swaps where a critical mass of creditors has been reached. In addition, CETA also instigates a 270 days freeze on litigation after a potential litigant places a request for consultation in the context of CETA dispute settlement[867].

Such a mechanism, while currently unique in international law has been advocated by the IMF[868] as a way to solve the collective action issues arising during sovereign debt restructurings. The stay on proceedings introduced in CETA serves two purposes. The first is to shield restructuring processes from holdout enforcement via the CETA dispute resolution mechanism. The second is to strengthen collective decision making by providing States and their creditors with a window to negotiate without risks of interruption by

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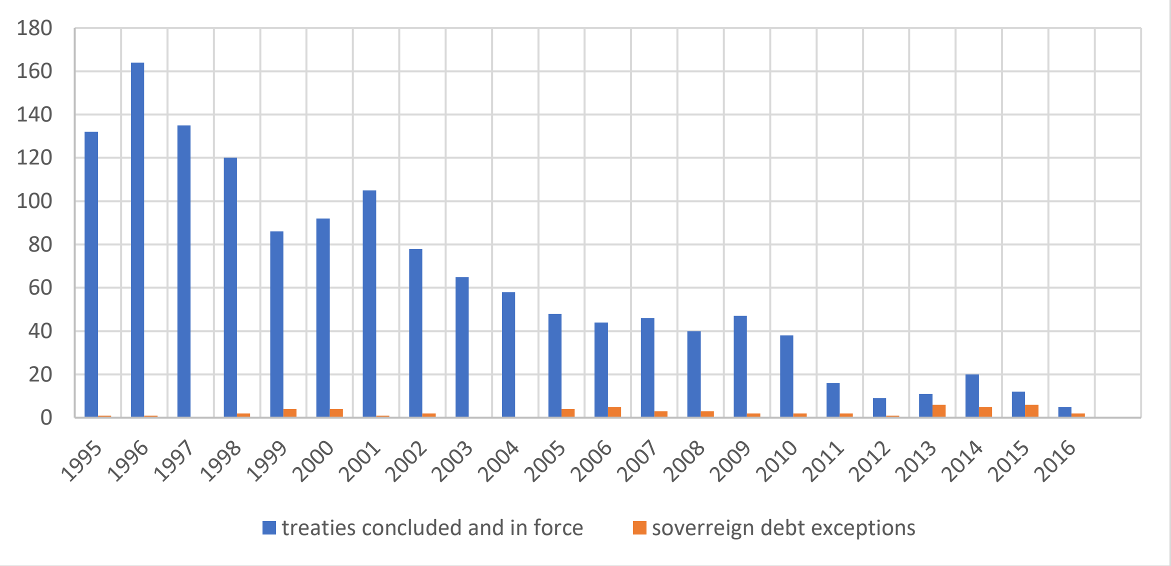
[864] 'Comprehensive Economic and Trade Agreement between Canada, of the One Part, and the European Union and Its Member States, of the Other Part, 14 September 2016 (Brussels)' (n 862). It should be noted that NAFTA explicitly excludes sovereign debt from its definition of investment. On this question see notably Kevin P Gallagher, 'The New Vulture Culture: Sovereign Debt Restructuring and International Investment Rules', *The Clash of Globalizations: Essays on the Political Economy of Trade and Development Policy. K. Gallagher (eds.)* (Anthem Press 2013); Kevin P Gallagher, 'Financial Crises and International Investment Agreements: The Case of Sovereign Debt Restructuring' (2012) 3 Global Policy 362.
[865] 'Comprehensive Economic and Trade Agreement between Canada, of the One Part, and the European Union and Its Member States, of the Other Part, 14 September 2016 (Brussels)' (n 862).
[866] The Treaty defines negotiated restructuring as "*restructuring or rescheduling of debt of a Party that has been effected through (a) a modification or amendment of debt instruments, as provided for under their terms, including their governing law, or (b) a debt exchange or other similar process in which the holders of no less than 75 per cent of the aggregate principal amount of the outstanding debt subject to restructuring have consented to such debt exchange or other process*". Ibid. However, litigation over negotiated restructurings is still available for breach of the most-favoured-nation or the national treatment clause. Ibid. It should also be noted that the US has followed a similar approach in a number of its BITs see: Kevin P Gallagher, 'Financial Crises and International Investment Agreements: The Case of Sovereign Debt Restructuring' (2012) 3 Global Policy 362.
[867] 'Comprehensive Economic and Trade Agreement between Canada, of the One Part, and the European Union and Its Member States, of the Other Part, 14 September 2016 (Brussels)' (n 831) annex 8-b.
[868] Krueger (n 41) 11.

holdouts. Against that background, the stay on proceedings implemented in CETA implements both the first and second component of the anti-holdout model.

In a similar fashion, it seems that newly concluded BITs have an increased tendency to exclude sovereign debt restructuring from their scope of application. Overall, a total of approximately 56 treaties currently in force explicitly exclude sovereign debt. While the overall share of treaties doing so is small, the 'sovereign debt exception' seems to have become more common in the recent year has shown in the graph hereunder[869].



This increase in the exclusion of sovereign debt from newly concluded treaties is both the result of an increase in the total number of sovereign debt exceptions since 2011, and a decrease in the overall number of treaties concluded. In other words, while less and less BITs are concluded, an increasingly large number of them explicitly excludes sovereign bond from their scope of application.

As with the CETA exception, the exclusion of sovereign debt from BITs can be analysed as a way to shield restructuring processes from holdout enforcement via investment tribunals. Explicitly excluding sovereign debt from BITs ensures that even if sovereign bonds are characterised as investments under the meaning of article 25 of the ICSID convention, an

[869] The data for this chart is sourced from the Investment Policy Hub by UNCTAD, the treaties considered are all treaties still in force. The treaties included are both bilateral investment treaties *sensu stricto* and the other treaties including investment provision. Finally, some treaties while not excluding sovereign debt in the definition of investment include sovereign debt in a list of areas for reservations, they have been included in this list. Notably this seems to be the practice of the government of Canada. For a list of the treaties included, see *annex I*.

arbitral tribunal could not have the competence, *ratione materiae*, to rule on sovereign debt restructuring processes.

Regarding article 25 of the ICSID convention the *Poştovâ* tribunal ruled *obiter dictum* that sovereign bonds cannot be characterised as investments as defined by the Convention[870]. The case involved two claimants, a Slovak bank, *Poştovâ banka* and one of the banks shareholders, a European Public Limited Liability Company consolidated under Cypriot law named *Istrokapital*. Both argued that some of the measures implemented during the Greek restructuring were violating the Greece-Slovakia and the Greece-Cyprus BITs[871].

On the characterisation of bonds as investments[872], the arbitral tribunal noted that the mere holding of sovereign bonds, remote from another economic venture, does not qualify as a contribution to the host's State development[873]. The idea advanced by the tribunal is that the funds raised by the bonds only provide for the budgetary needs of the debtor and do not lead to "*economically productive activities*"[874]. The arbitral tribunal also stated that the risk created by the holding of sovereign bonds does not constitute an investment or operational risk[875], but rather should be understood as a mere commercial risk. This line of reasoning held even when the sovereign retroactively legislated to incorporate collective action clauses in the bonds[876].

So far, the *Poštová* decision appears to be an outlier within the ICSID case-law on sovereign debt[877]. Nevertheless, the decision to exclude sovereign bonds from ICSID's competence, *ratione materiae*, would, if it were to be picked up in subsequent arbitral practice, lead to a stark limitation of the international remedies available to creditors.

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[870] *Poštová banka, a.s. and Istrokapital SE v. Hellenic Republic (Award)* (n 17).

[871] For a comment on the *Poştovâ* decision and its place within the current investment case-law on sovereign debt see Kei Nakajima, 'Parallel Universes of Investment Protection? A Divergent Finding on the Definition of Investment in the Icsid Arbitration on Greek Sovereign Debts' (2016) 15 The Law & Practice of International Courts and Tribunals 472; Dimitrios V Skiadas, 'Portfolio Investments in an EU Country under Crisis: Lessons from the ICSID Decision on the Case "Poštová Banka, a.s. and Istrokapital SE vs. The Hellenic Republic" - the Greek PSI Case' (2016) 3 International Journal of Diplomacy and Economy 167.

[872] The Poştovâ tribunal also ruled that the Greek bonds were not covered by the definition of investment in the Greek-Slovakian BIT, as opposed to the Argentinian bonds in the Italy-Argentina treaty. Similalry the tribunal ruled that the holding of shares in one of Greece's creditors did not give rise to ICSID competence.

[873] *Poštová banka, a.s. and Istrokapital SE v. Hellenic Republic (Award)* (n 12) 360-371; Cazala (n 265).

[874] *Poštová banka, a.s. and Istrokapital SE v. Hellenic Republic (Award)* (n 12) para 363; Cazala (n 265).

[875] *Poštová banka, a.s. and Istrokapital SE v. Hellenic Republic (Award)* (n 12) para 363.

[876] Boudreau (n 49); *Poštová banka, a.s. and Istrokapital SE v. Hellenic Republic (Award)* (n 12) para 368-369.

[877] Nakajima (n 871) 489. Noting, moreover, that the Postova tribunal does not engage in its decision with the rulings of its predecessor on sovereign debt and article 25 of the ICSID convention.

At today's date, the *Poštová* decision, combined with a growing body of IIAs explicitly excluding sovereign debt renders the obtention of such remedies more uncertain for creditors. By itself, and given the costs linked to investment arbitration, this increased uncertainty should incentivise creditors against litigating sovereign debt at the international level.

4.3.3.2 A Broader Interpretation of the Necessity Defence

Another development in the international law on sovereign debt pushed forward by UNCTAD and the UN General Assembly, as well as legal scholars on sovereign debt, focuses on necessity as a circumstance excluding State responsibility[878].

The issue regarding necessity as a defence for State restructuring their debt is that the traditional reading of the norm is too restrictive to allow its effective use in an economic context[879]. Notably, in order to be able to invoke necessity, States have to demonstrate that they are acting to protect one of their essential interest against a grave and imminent peril; that breaching their international obligations is the only way to do so; that they have not contributed to the situation leading to the breach of international law; the obligation breached is not one of *ius cogens*[880].

Thus, it would extremely difficult for a debtor State to prove that it has not contributed to the situation leading to the invocation of the necessity defence and that it doesn't have another solution than breaching international law to solve its debt crisis[881]. Finally, some authors underline that were a State of necessity to be employed to cover restructuring measures, the obligation of the debtor would only be suspended for the duration of the imminent peril. Thus, the debtor would still be bound to procure compensation to the victims

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[878] United Nations General Assembly, 'Resolution 69/319: Basic Principles on Sovereign Debt Restructuring Processes' (n 21); UNCTAD, 'Guidelines on Responsible Sovereign Lending and Borrowing (Draft Version)' <http://www.unctad.info/upload/Debt%20Portal/RSLB%20Guidelines/RSLB%20Guidelines%2025%20Aug%202014.pdf>; Reinisch and Binder (n 28); 'Argentinean State Bonds - Defense of Necessity in Relationship between State and Private Debtors' (2007) 101 American Journal of international law 857.

[879] 'Argentinean State Bonds - Defense of Necessity in Relationship between State and Private Debtors' (n 878); Reinisch and Binder (n 30); Waibel, 'Two Worlds of Necessity in ICSID Arbitration' (n 29).

[880] international law Commission, 'Draft Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries' (n 519) 80; *Case concerning the Gabcikovo-Nagymaros Project (Hungary/Slovakia)* (n 523) para 49; *Legal Consequences of the Construction of a Wall in the Occupied Palestinian Territory (Advisory Opinion)* (n 523) para 140. For a more detailed expose of these conditions see *supra*.

[881] See e.g. the very restrictive interpretation of the necessity defence applied in *Enron Corporation and Ponderossa Assets L.P. v Argentine Republic (Award)* (n 551); *LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc .v. Argentine Republic (Decision on liability)* (n 543); Waibel, 'Two Worlds of Necessity in ICSID Arbitration' (n 29); *CMS Gas Transmission Company v. The Republic of Argentina (Award)* (n 517).

of the breach[882], again this is of little help for a debtor seeking to reduce its debt burden in the long term.

Against that background, the UNCTAD principles, as well as the UNGA resolution seem to call for a broadening of the necessity defence in sovereign debt cases[883].

Principle 9, notably, endorses the idea that the debtor's obligations do not resume after the situation justifying necessity has ended, as highlighted by the wording "*can prevent the borrower's full repayment"*[884]. In addition, according to Howse[885], the principles do not require a non-participation of the sovereign in the occurrence of the event leading to necessity[886].

However, if principle 9 broadens *de lege ferenda* the necessity defence in sovereign debt cases, it seems, *de lege lata* that the customary standard remains unchanged. As rightfully pointed out by Waibel[887], the UNCTAD principles remain a soft law instrument that cannot by itself modify customary international law. Moreover, as highlighted earlier the voting patterns regarding the UNGA resolution and lack of sufficient practice seem to warrant the exclusion of the development of a new customary norm.

In addition to the customary necessity standard, specific necessity clauses are also inserted in Bilateral Investment Treaties. As highlighted in chapter 2, litigation before investment tribunals focused on the interpretation of article XI of the US-Argentina BIT reading:

> *"This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfilment of its obligations with respect to the*

[882] Waibel, 'Two Worlds of Necessity in ICSID Arbitration' (n 23) 643.
[883] UNCTAD (n 849) principle 9.
[884] A contrario, according to Waibel, the principle distinguishes between "the recognition of a state of economic necessity (the third sentence of Principle 9) and the availability of necessity as a legal defence (the fourth sentence of Principle 9)". Therefore, while principle 9 recognises that, economically, necessity might entail restructuring measures, legally, the UNCTAD principles do not attempt to modify the ambit of the necessity defence." Waibel, 'Out of Thin Air?' (n 25) 103-105.
[885] Howse (n 25) 387.
[886] The implications of principle 9 mention: "*A sovereign's inability to continue normal debt servicing is typically caused by acute financial distress. Sometimes the sovereign will have been the author of its own difficulties (for example, by pursuing imprudent macroeconomic policies); occasionally a sovereign predicament will have been abetted by reckless creditor behaviour. In other cases the crisis may have been precipitated by events beyond the sovereign's control (natural disasters or a general deterioration in international markets)*." UNCTAD (n 849) principle 9; Howse (n 25) 387.
[887] Waibel, 'Out of Thin Air?' (n 25) 87-99.

maintenance or restoration of international peace or security, or the Protection of its own essential security interests."[888]

While most arbitral tribunals opted for a narrow interpretation of the necessity standard[889], the *Continental Casualty* tribunal opted for a broader reading of the clause[890]. Instead of interpreting article XI of the US-Argentina BIT in light of the customary standard of necessity, the arbitral tribunal opted for a reading of necessity referencing the WTO Appellate body case-law[891].

The case involved a US based investment firm which held a large stake in an Argentinean insurance company. Following the Argentinean crisis, and in particular the South-American republic's decision to de-dollarize the Argentinean *peso*, the assets of the aforementioned insurance company plummeted in value, prompting it to sue[892]. The US firm alleged that the measures imposed by Argentina during the crisis violated several dispositions of the US-Argentina BIT, while Argentina argued, *inter alia*, that its liability was excluded by article XI of the BIT[893].

The *Continental Casualty* tribunal abandoned the 'only way' criteria required by the customary reading of necessity in favour of a balance-of-interests test. The tribunal justifies this departure from earlier arbitral case-law by highlighting textual similarities between article XI of the BIT and XX of the GATT. It decided that the necessity of a measure should be determined through "*a process of weighing and balancing of factors" which usually includes the assessment of the following three factors: the relative importance of interests or values furthered by the challenged measures, the contribution of the measure to the*

[888] Treaty between the United-States of America and the Argentine Republic concerning the Reciprocal Encouragement and Protection of Investment (Buenos Aires) artice XI.
[889] *CMS Gas Transmission Company v. The Republic of Argentina (Award)* (n 517); *LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc .v. Argentine Republic (Decision on liability)* (n 543); *Enron Corporation and Ponderossa Assets L.P. v Argentine Republic (Award)* (n 551); Reinisch and Binder (n 30); Reinisch, 'Necessity in Investment Arbitration' (n 555).
[890] *Continental Casualty Company v. The Argentine Republic* (n 591).
[891] See e.g. *Korea — Measures Affecting Imports of Fresh, Chilled and Frozen Beef* [2001] WTO Appelate Body DS 161; *Continental Casualty Company v. The Argentine Republic* (n 591).
[892] *Continental Casualty Company v. The Argentine Republic* (n 556) 37-66. For an overview of the factual background on the case, and an overall comment see notably Manu Misra, 'The Necessity Defense & Continental Casualty: Importation of WTO Principles at the ICSID' (2015) 2 McGill Journal of Dispute Resolution 129.
[893] *Continental Casualty Company v. The Argentine Republic* (n 556) 70.

realization of the ends pursued by it and the restrictive impact of the measure on international commerce"[894].

Regarding Argentina, the tribunal underlined that:

> *"within the economic and financial situation of Argentina towards the end of 2001, the Measures at issue (...) were in part inevitable, or unavoidable, in part indispensable and in any case material or decisive in order to react positively to the crisis, to prevent the complete break-down of the financial system, the implosion of the economy and the growing threat to the fabric of Argentinean society and generally to assist in overcoming the crisis. In the Tribunal's view, there was undoubtedly 'a genuine relationship of end and means in this respect.'"*[895]

Examining whether Argentina could have opted for less restrictive measures in order to solve its financial issues, the tribunal underlined that:

> *"it is not its mandate to pass judgment upon Argentina's economic policy during 2001-2002, nor to censure Argentina's sovereign choices as an independent state"*[896].

Finally, regarding the argument that Argentina had contributed to the development of its financial crises, the tribunal similarly underlined that:

> *"States are basically free to adopt economic and monetary policies of their choice; and this Tribunal is not subjecting past economic policies to any judicial, administrative or political review."*[897]

There are two key elements in the *Continental Casualty* reading of the necessity clause in the US-Argentina BIT.

First, the 'balance of interests' approach followed by the arbitral tribunal allows sovereigns to escape the rigid framework of the customary necessity standard. It allows the tribunal to take into account the interests of the debtor State and its population when deciding whether the BIT breaches were necessary. Second, regarding the "less restrictive measures" and the

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[894] ibid para 194, citing notably *Korea — Measures Affecting Imports of Fresh, Chilled and Frozen Beef* (n 891) para 164.
[895] *Continental Casualty Company v. The Argentine Republic* (n 556) para 197.
[896] ibid para 199.
[897] ibid para 224.

"non-contribution" arguments, relying on article XX of the GATT and the WTO case-law allow for the creation of regulatory room for manoeuvre for a debtor involved in a restructuring process[898]. In addition, it allows the arbitral tribunal to avoid having to second guess complex macro-economic decisions of the debtor[899].

Said interpretation of necessity is debated in the Investment arbitration case-law and scholarship[900]. Notably, there are doubts regarding the suitability of interpreting investment law dispositions in light of a trad agreement as both regimes pursue wildly different aims[901].

The common thread between necessity in the UNCTAD principles and the UNGA resolution and the *continental casualty* reading of the necessity defence, is that such an interpretation of necessity *de facto* limits the efficiency of the remedies available to creditors. As most sovereign debt crises occur in times of difficult economic circumstances, such interpretations effectively limit the likelihood that a sovereign's responsibility will be triggered for measures it has implemented during a restructuring process.

4.3.4 The Provision of Funds to the Debtor: Bail-outs by International Organisations

A final aspect of the anti-holdout model in international law can be found in the increased involvement of international institutions in the prevention and resolution of sovereign debt crises, through the provision of bailouts to overindebted sovereigns. This section will mostly focus on two institutions: the IMF, especially regarding the creation of a systemic risk exception in its rules on loan conditionality and the European Stability Mechanism.

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[898] Andrew Mitchell and Caroline Henckels, 'Variations on a Theme: Comparing the Concept of "Necessity" in International Investment Law and WTO Law' (2013) 14 Chicago Journal of international law 145–146 <https://chicagounbound.uchicago.edu/cjil/vol14/iss1/5>.
[899] Ibid. See also *LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc .v. Argentine Republic (Decision on liability)* (n 543).
[900] *Contra* ibid; *CMS Gas Transmission Company v. The Republic of Argentina (Award)* (n 517); *Enron Corporation and Ponderossa Assets L.P. v Argentine Republic (Award)* (n 551). See also Mitchell and Henckels (n 898) 148–151; Jose Alvarez and Tegan Brink, 'Revisiting the Necessity Defense: Continental Casualty v Argentina', *Yearbook on International Investment Law & Policy 2010-2011. Karl P Sauvant, ed.* (Oxford University Press 2012); Celine Levesque, 'The Inclusion of GATT Article XX Exceptions in IIAs: A Potentially Risky Policy' (*ResearchGate*) <https://www.researchgate.net/publication/297174751_The_inclusion_of_GATT_Article_XX_exceptions_in_IIAs_A_potentially_risky_policy> accessed 2 April 2019.
[901] Alvarez and Brink (n 900) 319; Misra (n 892) 139; Levesque (n 900).

4.3.4.1 The Increased Role of the IMF in Bailing-out Overindebted States

Prior to 2010, lending by the IMF was subjected to proof of the recipient's debt sustainability. Article V of the IMF's article of Agreement stipulated:

> *"The Fund shall adopt policies on the use of its general resources, including policies on stand-by or similar arrangements, and may adopt special policies for special balance of payments problems, that will assist members to solve their balance of payments problems in a manner consistent with the provisions of this Agreement and that will establish adequate safeguards for the temporary use of the general resources of the Fund."*[902]

The traditional reading of this disposition is that it prevents the IMF from lending available to States whose debt is unsustainable[903]. The IMF, defined sustainability as "*whether a country's debt can be serviced without an unrealistically large future correction in the balance of income and expenditure*"[904] .

This definition requires the solvency of the debtor[905], calculated through its debt-to-GDP ratio, but also takes into account liquidity constraints and the cost of financing. This last condition can prove problematic as the cost of financing tends to rise when its debt-to-GDP ratio and its liquidities are insufficient, making it more difficult to borrow from capital markets in order to repay already existing debt[906].

The logic behind tying bail-outs to debt sustainability is that, given the limited funding of the IMF, the fund ought to only make resources available to sovereigns if it is confident that the recipient will be able to reimburse the loan it has received[907]. If a sovereign's debt is unsustainable, *i.e.* if its debt to GDP ratio is such that its sovereign debt crisis is not caused by a lack of liquidities but by insolvency, then bailing out the debtor only serves to delay its inevitable default. This would lead to the Fund wasting resources that could have been better used by another State.

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902 Articles of Agreement of the International Monetary Fund (Bretton Woods) 1944, article V.
903 Anne Krueger and Sean Hagan, 'Sovereign Workouts: An IMF Perspective' (2005) 6 Chicago Journal of international law 203, 206-207.
904 IMF, 'Assessing Sustainability' <https://www.imf.org/external/np/pdr/sus/2002/eng/052802.pdf>, 3.
905 Whether the recipient's future balance can accommodate its debts Wyplosz (n 88) 3-4.
906 For an in-depth analysis of said borrowing conditions see ibid.
907 Krueger and Hagan (n 874) 207.

The bail-out norms on debt sustainability have undergone radical changes following the Greek and Eurozone crises. For Greece, IMF lending began in 2010, and, overall, the fund lent over €30 billion, or 27% of the total bail-out extended by the Troika[908]. The issue regarding the Greek bail-out was that, in 2010, there were heavy doubts, expressed by the IMF's staff itself that the Greek debt was sustainable[909].

However, as Greece's situation, and the potential effects of a Greek default were deemed exceptional, the fund opted to adapt its conditionality framework to limit the impact of a Hellenic default on global markets. It was understood at the time that a Greek default could have spill-over effects on the banking system of the Eurozone, leading to a broader financial crisis. Moreover, a default by Greece could have negatively affected the status of the Euro as a global currency, leading to destabilising effects for the other members of the currency union[910].

As a result, the IMF chose to alter its *ad hoc* lending policy, accepting to lend to Greece even though its debt was not sustainable "with a high probability"[911]. This exception in the fund's lending policy remained in place after the Eurozone crisis. Thus, at today's date, lending by the IMF is available for any State, even those with unsustainable debts, if their default can trigger a systemic shock to global financial systems[912].

The principal effect of this easing in the IMF's lending conditions is that it is now easier for large sovereign debtors[913] to access IMF lending in times of crisis as the sustainable nature of their debt will not be taken into consideration. This facilitates said State's access to liquidities enabling them to return to debt sustainability in an easier fashion.

4.3.4.2 The Creation of the European Stability Mechanism

As with the IMF, the EU normative framework on bailouts was altered following the Greek and Eurozone crises. Traditionally, article 125 of the TFEU had been read as preventing

908 Susan Schadler, 'Unsustainable Debt and the Political Economy of Lending: Constraining the IMF's Role in Sovereign Debt Crises' <https://www.cigionline.org/publications/unsustainable-debt-and-political-economy-lending-constraining-imfs-role-sovereign-debt> accessed 18 February 2019, 7-9.
909 ibid.
910 For an overview of the systemic risk created by a Greek debt default see in general: Niccolò Battistini, Marco Pagano and Saverio Simonelli, 'Systemic Risk, Sovereign Yields and Bank Exposures in the Euro Crisis' (2014) 29 Economic Policy 203; ibid; Black and others (n 9).
911 Schadler (n 908) 9–10.
912 Jeromin Zettelmeyer, Christoph Trebesch and G Mitu Gulati, 'The Greek Debt Restructuring: An Autopsy' (Social Science Research Network 2013) SSRN Scholarly Paper ID 2144932 <http://papers.ssrn.com/abstract=2144932> accessed 16 August 2016.
913 As those are more likely to trigger a systemic shock in case of failure.

bailouts of EU member States by EU institutions[914] or other members of the Union.[915] Following the Greek crisis, and the risk of contagion it posed to broader financial markets the Troika opted to bail Greece out, under strict austerity conditions, in apparent violation of article 125[916].

In addition from bailing Greece out, the Member States decided, in 2010 to establish two *ad hoc* institution to deal with the broader Eurozone crisis: the European Financial Stability Mechanism and the European Financial Stability Facility[917]. Both institutions, tasked with bailing out members of the European Union, were backed by funds from Eurozone members and authorised to borrow from capital markets to gather the sums necessary for their mission[918].

The EFSM can be defined as:

> *as "an intergovernmental agreement to provide financial assistance of up to EUR 60 billion subject to strong conditionality in the context of a joint EU and IMF support which will be on terms and conditions similar to those imposed by the IMF"*[919]

The EFSF, *a contrario*, is:

[914] For a discussion on the EU response to the Greek crisis see: Rodrigo Olivares-Caminal, 'The EU Architecture to Avert a Sovereign Debt Crisis' (2012) 2011 OECD Journal: Financial Market Trends 167; Rodrigo Olivares-Caminal, 'Sovereign Debt Defaults: Paradigms and Challenges' (2010) 11 Journal of Banking Regulation 91; Etienne de Lhoneux and Christos A Vassilopoulos, 'The ESM Treaty and the European Law: A Necessary Coexistence' in Etienne de Lhoneux and Christos A Vassilopoulos (eds), *The European Stability Mechanism Before the Court of Justice of the European Union: Comments on the Pringle Case* (Springer International Publishing 2014) <https://doi.org/10.1007/978-3-319-01478-4_4> accessed 7 March 2019; Paul Craig, '*Pringle* : Legal Reasoning, Text, Purpose and Teleology' (2013) 20 Maastricht Journal of European and Comparative Law 3.

[915] Article 125 reads: "*The Union shall not be liable for or assume the commitments of central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of any Member State, without prejudice to mutual financial guarantees for the joint execution of a specific project.* ***A*** *Member State shall not be liable for or assume the commitments of central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of another Member State, without prejudice to mutual financial guarantees for the joint execution of a specific project.*" Consolidated version of the Treaty on the Functioning of the European Union (Lisbon) 2007 (12012E/TXT) article 125.

[916] de Lhoneux and Vassilopoulos (n 885) 43. There were other EU dispositions which could arguably have been breached by the implementation of the ESM treaty, especially in regard to the competence *ratione materiae* of the EU institutions to create such a framework. For an analysis of those potential challenges see ibid. 37-68.

[917] de Lhoneux and Vassilopoulos (n 885) 1-8. See also Olivares-Caminal, 'The EU Architecture to Avert a Sovereign Debt Crisis' (n 885).

[918] Marcello Minenna and Dario Aversa, 'A Revised European Stability Mechanism to Realize Risk Sharing on Public Debts at Market Conditions and Realign Economic Cycles in the Euro Area' (2019) 48 Economic Notes 12118; de Lhoneux and Vassilopoulos (n 885) 2-3.

[919] Olivares-Caminal, 'The EU Architecture to Avert a Sovereign Debt Crisis' (n 885) 5.

"a temporary credit-enhanced SPV with minimal capitalization created to raise funds from the capital markets on its investment grade rating and provide financial assistance to distressed [Euro-area Member States] at lower interest rates than those available to the latter"[920]

Therefore, the function of the EFSM was to act as an institution bailing out members of the European Union, in collaboration with the IMF and on similar conditions[921]. The EFSF, on the other hand was a Special Purpose Vehicle whose task was to provide relief to Members of the Eurozone by raising money from capital markets[922].

Both *ad hoc* institutions were replaced in 2012 by the European Stability Mechanism (ESM)[923]. The ESM, established by treaty, is an organisation tasked with the bailing out of Members of the Eurozone, in liaison with ECB and the IMF[924]. The funds used the by ESM to fulfil its functions are drawn both from contributions by Members of the Eurozone and by the ESM itself, as the organisation has the ability to borrow from private entities[925].

In order to authorise the creation of the ESM, the TFEU required the introduction of an article 136 (3) reading:

"the Member States whose currency is the euro may establish a stability mechanism to be activated if indispensable to safeguard the stability of the euro area as a whole."[926]

The conformity of the creation of the ESM with existing EU law was challenged before the European Court of Justice[927]. Claimants argued that the creation of the ESM through treaty by Member States was *ultra vires* as the regulation of the monetary policy of the Euro-Area

[920] ibid 17.
[921] ibid 5.
[922] ibid 5.
[923] Treaty Establishing the European Stability Mechanism (Brussels); Olivares-Caminal, 'The EU Architecture to Avert a Sovereign Debt Crisis' (n 885) 13. On the creation of ESM see also Minenna and Aversa (n 889); de Lhoneux and Vassilopoulos (n 885).
[924] Treaty Establishing the European Stability Mechanism (Brussels), recital 8.
[925] ibid; Minenna and Aversa (n 918); Olivares-Caminal, 'The EU Architecture to Avert a Sovereign Debt Crisis' (n 914); Riegner (n 6) 136.
[926] Consolidated version of the Treaty on the Functioning of the European Union (Lisbon) article 136; de Lhoneux and Vassilopoulos (n 885) 45; Craig (n 885) 4.
[927] See *Thomas Pringle v Government of Ireland and Others* Court of Justice of the European Union C-370/12, Digit Rep Court Rep - Gen; Comments in: Craig (n 885); Etienne de Lhoneux and Christos A Vassilopoulos, 'The Pringle Judgment and Future Perspectives' in Etienne de Lhoneux and Christos A Vassilopoulos (eds), *The European Stability Mechanism Before the Court of Justice of the European Union: Comments on the Pringle Case* (Springer International Publishing 2014) <https://doi.org/10.1007/978-3-319-01478-4_5> accessed 7 March 2019.

is an exclusive competence of the EU itself[928]. In addition, claimants postulated that the establishment of the ESM contravened to article 125 of the TFEU, mentioned *supra*.

Regarding the first point, the CJEU underlined that the establishment of the ESM was not a matter of monetary policy but rather should be read as relating to economic policy *sensu lato*, on which the EU does not enjoy exclusive competence[929].

Regarding the TFEU's no-bailout clause, the Court of Justice underlined that the text of article 125 does not prohibit all kind of financial assistance by the EU or its Member States to other Member States[930]. Focusing on the object and purpose of article 125, the ECJ concluded that the actual aim of the article was to "*prohibit the EU and Member States from granting financial assistance as a result of which the incentive of the recipient Member State to conduct a sound budgetary policy is diminished*"[931].

In other words, according to the Court, article 125 enables the EU and its Member States to extend financial assistance to a Member of the Union as long as said assistance cannot be read by the Court as encouraging the recipient towards running budget deficits that would otherwise have been sanctioned by capital markets.

Against that background, the Court ruled that the establishment ESM did not breach the obligation contained within article 125 as it did not make the Mechanism "*liable for the commitments of the Member States*"[932]. It seems therefore that as long as the ESM did not act as guarantor to the Eurozone Member States[933], its creation did not breach what had previously been read as a no-bailout clause within the Treaty.

The creation of the ESM and the *Pringle* decision clearly indicates a move in international law towards facilitating bailouts of systemically important heavily indebted sovereigns. This array of international assistance to over-indebted debtor limits the likelihood of default once

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[928] *Thomas Pringle v Government of Ireland and Others.* (n 898) para 68; de Lhoneux and Vassilopoulos (n 898) 38-40; Craig (n 885) 5-6.
[929] *Thomas Pringle v Government of Ireland and Others.* (n 898) 68; de Lhoneux and Vassilopoulos (n 898) 38-40; Craig (n 885) 6.
[930] *Thomas Pringle v Government of Ireland and Others.* (n 898) para 135-136; de Lhoneux and Vassilopoulos (n 898) 52; Craig (n 885) 7-8.
[931] *Thomas Pringle v Government of Ireland and Others.* (n 898) para 136.
[932] ibid para 146.
[933] Craig (n 885) 8.

a restructuring has been agreed to and should thus lead to a broader acceptance of restructuring offers by creditors, as the default risk of sovereigns is lowered.

4.4 The Strengths and Weaknesses of the Anti-holdout model

After having reviewed the essential components of the anti-holdout model, and their implementation in international law, the third part of this thesis will now focus on addressing the strengths and weaknesses of this new regulatory model.

Overall, the main strengths of the anti-holdout model lie in the fact that it limits the costs of debt restructurings for most stakeholders, and encourages negotiations between States and their creditors, thus enhancing the legitimacy of the restructuring process as a whole.

For these reasons, the anti-holdout model appears to be more suited to the current contractual structure of sovereign debt. These improvements over the creditor protection model however, do not signify that there are no weaknesses in the way sovereign debt currently works. Notably, the current system for restructuring State debt heavily favours large institutional investors over retail holders of bonds, and the legal avenues via which the anti-holdout model has been implemented creates a risk of fragmentation of the law on sovereign debt. Finally, the current regulatory model does not encourage States to restructure their debts as early as possible.

4.4.1 The Strengths of the Anti-holdout model

4.4.1.1 A Faster Return to Debt Sustainability

The main strength of the anti-holdout model is that it facilitates sovereign debt restructurings. This shortens the average time needed to bring a sovereign back to debt sustainability and limiting the costs of restructuring processes for all parties involved.

This facilitation of sovereign debt restructurings is done via three main tools within the model. First, majority decision-making enables restructurings to proceed once a majority of creditors agree over a restructuring proposal. As the majority of debt titles are usually held by large institutional investors, who have an interest in seeing the debtor return to debt sustainability[934], majority decision-making creates a positive feedback loop between the

[934] See IMF, 'Sovereign Investor Base Dataset for Emerging Markets' (n 3).

creditors who have an interest in seeing the sovereign succeed in its restructuring and their debtor[935]. This holds true whether majority decision-making is implemented via the use of a CAC or via the use of good faith and the abuse of rights doctrine.

Beyond majoritarian decision making, the current model further facilitates sovereign debt restructurings by impeding attempts of holdout creditors to litigate over sovereign debt. These incentives against litigation, and these limits to the abilities of creditors to enforce their rights, limit the likelihood of enforcement attempts disrupting an agreed restructuring proposal. Moreover, with judicial enforcement of sovereign debt being more difficult, would-be holdouts are incentivised towards accepting a reasonable restructuring proposal, rather than seeking full payment before courts and tribunals.

Litigation over sovereign debt is disincentivised via several measures, both in domestic and international law. CACs prevent holdout litigation on the contractual rights arising from sovereign bonds[936]. Good faith and the abuse of rights doctrine, further disincentivise litigation by increasing the likelihood that international courts and tribunals will rule in favour of a sovereign whose restructuring proposal has been accepted by most creditors[937]. Similarly, a broader interpretation of the necessity defence, as advocated in *soft law*[938], and applied in *Continental Casualty*[939], increases the likelihood that a State in dire economic circumstances will be absolved of its international responsibility.

Disincentivising holdouts also depends upon limiting the availability of *fora* available for creditors. Notably, the current trend in IIAs towards the exclusion of sovereign debt litigation, and the narrower interpretation of article 25 of the ICSID convention put forwards in *Poštová*[940], may prevent holdout creditors from litigating sovereign debt before investment tribunals.

A final incentive against litigation can be found in the limitation of remedies available to creditors. Notably, the new drafting of the *pari passu*[941] clause and the rank of payment

[935] Buchheit and Reisner (n 256); Fisch and Gentile (n 73) 1059.
[936] International Monetary Fund (n 13); International Capital Market Association (n 678).
[937] E.g. *Mamatas et autres v. Greece* (n 18); *Alessandro Accorinti and others v. European Central Bank* (n 19).
[938] United Nations Conference on Trade and Development (n 16) principle 9; 'United Nations General Assembly, Sixty-Eitgh Session, Resolution towards the Establishment of a Multilateral Legal Framework for Sovereign Debt Restructuring Processes , A/RES/68/304' <http://www.un.org/en/ga/search/view_doc.asp?symbol=A/RES/68/304>, principle 1.
[939] *Continental Casualty Company v. The Argentine Republic* (n 591).
[940] Montanaro (n 453).
[941] International Monetary Fund (n 13).

interpretation of the clause[942] prevent holdouts from obtaining rateable payment as a remedy. Similarly, anti-vulture fund legislation[943] and a strengthening of sovereigns' immunities of execution[944] limit the ability of holdouts to obtain payment via domestic courts.

Beyond disincentivising litigation, the anti-holdout model improves the rapidity of sovereign debt restructurings by enabling debtors to better access the funds needed to maintain their liquidity. This is done either by diminishing sovereign's indebtedness, as majority decision-making lets a State obtain a haircut on all their bonds, or by providing sovereigns with funds via international institutions.

4.4.1.2 Increased Legitimacy of Restructuring Processes

The second strength of the anti-holdout model is that it increases the legitimacy of the decision reached during the debt workout.

The anti-holdout model incentivises both States and their creditors towards reaching amiable solutions to sovereign debt crises. For the sovereign, given that decisions to restructure benefit from majority agreements[945], negotiating with creditors is a quasi-necessary step to ensure that restructuring proposals will reach sufficient support to trigger a CAC, or lead to the conclusion that holdouts are acting in bad faith[946].

Moreover, the good faith principles, when apply to sovereign debt arguably leads to a judicially enforceable obligation by the sovereign to negotiate with its creditors. This could mean that a State failing to do so may become the target of litigation by disgruntled creditors.

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[942] *Export-Import Bank of the Republic of China v. Grenada* (n 28); Zamour (n 74).
[943] Loi du 12 juillet 2015 relative à la lutte contre les activités des fonds vautours.
[944] Debt Relief (Developping Countries) Act 2010; 'Loi Du 28 Avril 1999 Visant à Transposer La Directive 98/26/CE Du 19 Mai 1998 Concernant Le Caractère Définitif Du Règlement Dans Les Systèmes de Paiement et de Règlement Des Opérations Sur Titres.' (n 741); LOI n° 2016-1691 du 9 décembre 2016 relative à la transparence, à la lutte contre la corruption et à la modernisation de la vie économique; Loi visant à empêcher la saisie ou la cession des fonds publics destinés à la coopération internationale, notamment par la technique des fonds vautours.
[945] As reaching an agreement with the majority of the creditor base shelters the result of the negotiation from holdout enforcement. See also Goldmann, 'Putting Your Faith in Good Faith: A Principled Strategy for Smoother Sovereign Debt Workouts' (n 651) 130–131.
[946] ibid 130.

In addition, under the CETA agreement, a stay on enforcement is in place during negotiations[947], providing State and their creditors with a window during which they can peacefully negotiate.

These negotiations further the legitimacy of debt restructurings as they ensure that solutions to sovereign debt crises are acceptable for most creditors and that creditors have been involved in the decision-making process.

Finally, majority-decision making shrouds sovereign debt restructurings with a democratic appearance. While votes in CACs, and majorities for the purpose of good faith and the abuse of rights doctrine, are not quantified on a *per virem* basis, it is undeniable that majority decision making appears more democratic than unilateral 'take-it or leave-it' offers by the debtor.

This increase in legitimacy contributes towards rendering restructuring offers more acceptable to the creditor base, and to the debtor's population. As a result, it is likely that compliance with the decisions reached during the restructuring will increase, both for creditors and the sovereign debtor.

4.4.1.3 Management of sovereign defaults and restructuring risks

The final strength of the anti-holdout model is that it spreads the costs (and therefore the risks) of sovereign debt restructurings across the entirety of a State's creditor-base and not only towards the creditors likely to accept a haircut.

In effect this furthers the risk management aspects of the bond market, the main driving force behind the Brady plan which lead to its creation[948]. To recall, the main advantage of bonds over syndicated loans is that a secondary market enables a broader class of investor to gain exposure to the risks of sovereign indebtedness. Thus, when sovereigns fail on their bonds, they are less likely to take with them critically important financial institutions, as their default risk is spread across various creditor classes.

However, successful holdout creditors unbalance some of the risk distributing effects of the bond market. Indeed, these creditors can avoid the losses caused by sovereign debt

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[947] 'Comprehensive Economic and Trade Agreement between Canada, of the One Part, and the European Union and Its Member States, of the Other Part, 14 September 2016 (Brussels)' (n 832) annex 8-b.
[948] Monteagudo (n 8); Ghosal and Miller (n 158); Dellas and Niepelt (n 297).

restructuring by obtaining payment on the full value of their bonds. This means, in effect, that the costs of sovereign debt restructurings were only born by the creditor classes who accept debt restructuring, *i.e.* large financial institutions.

The anti-holdout model, because it seeks to prevent holdout enforcement and enables majority restructuring, spreads restructuring costs back to the entirety of a sovereign's creditor base. This means that, for most creditors, the costs of bringing the sovereign back to debt sustainability are lower, and thus restructuring more acceptable. Correlatively, the spread of restructuring costs also leads to a reduced exposure of important financial institutions to sovereign debt failures, thus strengthening the stability of the global financial system as a whole. This stabilising effect is furthered by the provision of bail-outs specifically designed to prevent sovereign failure from triggering systemic crises.

4.4.2 The Weaknesses of the Anti-holdout model

4.4.2.1 Fragmentation as a product of legal innovation

Fragmentation is a classic trope of international law[949]. It refers to the risk of legal contradictions created by the rise of specialised international legal regimes[950]. As international law specialises, both from a substantive and from a dispute settlement perspective, the likelihood that alike situations are not treated alike rises. From a substantive point of view fragmentation occurs when a same situation can be treated differently by two different legal regimes. This creates the need for conflict of law norms in international law[951]. From a dispute settlement perspective, the risk is that specialised *fora* might interpret international law in different ways[952].

[949] It should be noted that fragmentation, in the realm of sovereign debt law is not only apparent at the legislative level but also stems from decentralised contract drafting. Gulati and Gelpern in particular note divergences in the drafting of CACs and *pari passu* clauses in New-York. See Mitu Gulati and Anna Gelpern, 'Innovation After the Revolution: Foreign Sovereign Bond Contracts Since 2003' (2009) 4 Capital Markets Law Journal 85.
[950] Martti Koskenniemi, 'international law Commission: 58th Session. Report of the Study Group of the ILC: Fragmentation of international law: Difficulties Arising from the Diversification and Expansion of international law.' <http://legal.un.org/ilc/documentation/english/a_cn4_l682.pdf>.
[951] C Wilfred Jenks, 'The Conflict of Law-Making Treaties' (1953) 30 British Year Book of international law 401; Koskenniemi (n 959).
[952] Rosalyn Higgins, 'The ICJ, the ECJ, and the Integrity of international law' (2003) 52 The International and Comparative Law Quarterly 1; Olivier Delas and others, *Les juridictions internationales : complémentarité ou concurrence ?* (Emile Bruylant 2005). See also Riegner (n 6).

Sovereign debt restructurings, as a phenomenon, fall under the scope of a broad array of legal orders and under the potential jurisdiction of a number of international and domestic courts.

Notably, sovereign debt is subject to the contract law chosen in the bonds, usually New-York or English law[953], or alternatively the domestic law of the issuer[954]. Additionally, sovereign bonds could be subject to domestic legislation, such as legislation reinforcing sovereign immunities or the Belgian anti-vulture fund act[955]. The characterisation of sovereign debt as an investment leads to the applicability of International Investment law[956]. However, an expropriatory measure could similarly fall under the Human Rights Law[957], customary international law, or European Law[958].

From a dispute settlement perspective, different courts and tribunals have interpreted the law on sovereign debt in notoriously contradictory fashion.

The anti-holdout model, given that its implementation required both regulatory action by public entities and reversal of well-established case-law, further raises the likelihood of fragmentation. This thesis identifies two critical areas where risks of fragmentation are particularly high: the competence of arbitral tribunals on sovereign debt, and the adoption of new domestic law.

Regarding the competence of investment tribunals, risks of fragmentation arise from the interaction between the decentralised nature of the ICSID system and the internationality of the bond market. Reducing the likelihood that investment tribunals are competent for sovereign debt disputes either requires arbitral tribunals to interpret article 25 of the ICSID convention *à la Poštová*, or changes in BIT drafting[959].

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953 Das, Papaioannou and Trebesch (n 4) 142.
954 *Mamatas et autres v. Greece* (n 18); *Alessandro Accorinti and others v. European Central Bank* (n 19).
955 Debt Relief (Developping Countries) Act 2010; Loi visant à empêcher la saisie ou la cession des fonds publics destinés à la coopération internationale, notamment par la technique des fonds vautours; Loi du 12 juillet 2015 relative à la lutte contre les activités des fonds vautours; LOI n° 2016-1691 du 9 décembre 2016 relative à la transparence, à la lutte contre la corruption et à la modernisation de la vie économique.
956 *Abaclat and Others v. Argentine Republic* (n 17); *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17); *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17); Waibel, 'Opening Pandora's Box' (n 81).
957 *De Dreux-Brézé c. France* (n 419); *Thivet v. France* (n 419); *Malysh and others v Russia* (n 419); *Mamatas et autres v. Greece* (n 18).
958 *Alessandro Accorinti and others v. European Central Bank* (n 19); *Stefan Fahnenbrock et. al. C Hellenische Republic* (n 307).
959 On this question see Nakajima (n 871); Gallagher, 'Financial Crises and International Investment Agreements' (n 866).

Regardless of the avenue the anti-holdout model opts for, the law on sovereign debt risks entering a twilight zone during which States and investors cannot, in advance, know whether investment litigation on sovereign debt is likely.

Moreover, altering the drafting of BITs results in increasingly multiple drafting of 'sovereign debt clauses' in BITs. For example, at today's date, while some treaties explicitly include or explicitly exclude sovereign debt[960], others merely include: "*obligations, private or public titles or any other right to performances or services having economic value, including capitalized revenues*"[961] or similarly "*bonds, debentures, loans and other forms of debt, including rights derived therefrom*" [962].

In the current state of the case-law, it is uncertain whether the mere inclusion of debt instrument or bonds in the non-exhaustive list of investment covers sovereign bonds, or rather is designed as only applies to corporate bonds. It is particularly unclear given that some treaties precise that the bonds or debentures included in the definition of investment are those "*of an enterprise*"[963].

In addition to such drafting, some treaties include a catch-all provision reading "*any right of economic nature conferred under law or contract, as well as any license and concession granted in compliance with the applicable provisions applicable to the concerned economic activities, including the prospection, cultivation, extraction and exploitation of natural resources*"[964] or "*claims to money which has been used to create an economic value or. claims to any performance having an economic value*"[965].

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[960] For a BIT explicitly including sovereign debt see e.g. 'Agreement between Japan and the Kingdom of Saudi Arabia for the Promotion and Protection of Investment, Signed in Jeddah 2013.' Including in their definition of investment *bonds, debentures, loans and other forms of debt, including rights derived therefrom as well as securities issued by the government of a Contracting Party*".

[961] Treaty between the United-States of America and the Argentine Republic concerning the Reciprocal Encouragement and Protection of Investment (Buenos Aires).

[962] 'Agreement between Japan and the Republic of Uzbekistan for the Liberalization, Promotion and Protection of Investment, Signed in Tashkent 2008.'

[963] 'Agreement Between the Government of Canada and the Government of Burkina Faso for the Promotion and Protection of Investments 2015.'

[964] 'Agreement between Italy and Argentine Republic for the Promotion and Protection of Investment (Signed in Buenos Aires) 1990'; *Abaclat and Others v. Argentine Republic* (n 17); *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17); *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17).

[965] 'Treaty between the Federal Republic of Germany and the Democratic Socialistic Republic of Sri Lanka Concerning the Promotion and Reciprocal Protection of Investments, 2000.'

It should be noted that this catch-all provision can be included either in BITs broadly mentioning debt instruments in their definition of investment[966], or in those only mentioning the debt instruments of enterprises[967]. Here again, the interpretation of such treaties remains open. This multiplicity of drafting does not be appear to be diminished when analysing the BITs of a single State. For example, Japan's BITs include both explicit exclusions of sovereign debt[968], explicit inclusions of it[969], treaties featuring the catch-all provision without mentioning bonds as an investment[970] and treaties mentioning bonds as an investment but without catch-all provisions[971]. Similarly, while US BITs typically tend to exclude sovereign debt, Gallagher underlines that the US-Korea BIT does not explicitly exclude it[972].

The problem with this multiplicity of drafting becomes more apparent when it is combined with the internationality of the bond market. BITs *ratione personae* apply to the nationals of the sovereign signatories to the Treaty[973]. Bonds, however, can usually circulate across borders due to their transferability. *Ergo*, one issuer could first issue bonds in the US, under American law, but these bonds could be bought by an Italian National. At the domestic law level, this is not an issue, the law selected in the bonds, and the jurisdiction chosen by the bond, will apply without regard to the nationality of its holder. However, when litigation stems from BITs, creditors can litigate based on their nationality, putting the debtor in a position where it is nearly impossible to know in advance if international litigation is likely[974].

[966] 'Agreement between Italy and Argentine Republic for the Promotion and Protection of Investment (Signed in Buenos Aires) 1990' (n 964); *Abaclat and Others v. Argentine Republic* (n 17); *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17); *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17).

[967] 'Agreement between the Government of the Republic of China (Taiwan) and the Government of Saint Vincent and the Grenadines for the Reciprocal Promotion and Protection of Investments, Kingstown (2010)'.

[968] 'Agreement between Japan and the State of Israel for the Liberalization, Promotion and Protection of Invsement, Signed in Tokyo 2017.'

[969] 'Agreement between Japan and the Republic of Uzbekistan for the Liberalization, Promotion and Protection of Investment, Signed in Tashkent 2008.' (n 962).

[970] 'Agreement between Japan and the Arab Republic of Egypt Concerning the Encouragement and Reciprocal Protection of Investment, Signed in Tokyo 1977.'

[971] 'Agreement between the Governement of the Republic of Korea and the Government of Japan for the Liberalization, Promotion and Protection of Investment, Signed in Seoul 2002.'

[972] Gallagher, 'Financial Crises and International Investment Agreements' (n 864).

[973] Engela C Schlemmer, 'Investment, Investor, Nationality, and Shareholders' [2008] The Oxford Handbook of International Investment Law <http://www.oxfordhandbooks.com.ezproxy.lib.gla.ac.uk/view/10.1093/oxfordhb/9780199231386.001.0001/oxfordhb-9780199231386-e-2> accessed 17 April 2019.

[974] On this question see notably: Gallagher, 'Financial Crises and International Investment Agreements' (n 864).

The same issue arises when the anti-holdout model is implemented via domestic legislation. As highlighted *supra*, several domestic lawmakers took it upon themselves to implement domestic solutions to the collective action issues explored in this thesis. Notably, both Belgium[975] and the UK[976] reinforced the immunity of execution of economically distressed sovereigns, and both France[977] and Belgium[978] implemented legislation designed to limit vulture fund litigation.

As domestic pieces of legislation, the applicability of the aforementioned acts is limited *ratione loci*. These acts only apply to sovereign debt litigation occurring before the domestic courts of the sovereigns enacting them.

This limited applicability severely limits the practical usefulness of such laws, especially the French and Belgian anti-vulture fund dispositions. Indeed, since sovereign bonds, contractually tend to elect American and English courts for dispute settlement, litigation on sovereign debt usually occurs before said courts[979].

Here again, the problems lie with the internationality of the bond market and the seeming ubiquity with which holdout creditors seem able to search for attachable assets[980]. Fundamentally, unless legislation changes in the United-States or the United-Kingdom, domestic changes in litigation are unlikely to have a practical impact on holdout creditors and sovereign debt litigation as a whole.

4.4.2.2 Retail Investors and the Anti-holdout model

Retail investors are an understudied category of debt holders when it comes to understanding the contemporary law on sovereign debt. Individual holders of bonds are not only a growing part of the creditor base, with a recent IMF dataset indicating that they hold roughly 25% of all sovereign’s external debt[981], but are also a growing category of litigants. Notably, during the Argentine restructuring process, individual Italian holders of bonds sued Argentina

[975] Loi visant à empêcher la saisie ou la cession des fonds publics destinés à la coopération internationale, notamment par la technique des fonds vautours.
[976] Debt Relief (Developping Countries) Act 2010.
[977] LOI n° 2016-1691 du 9 décembre 2016 relative à la transparence, à la lutte contre la corruption et à la modernisation de la vie économique.
[978] Loi du 12 juillet 2015 relative à la lutte contre les activités des fonds vautours.
[979] Belle (n 721).
[980] Muir Watt (n 340).
[981] IMF, ‘Sovereign Investor Base Dataset for Emerging Markets’ (n 3).

before ICSID tribunals[982]. Likewise, individuals sued Greece before domestic German tribunals[983], the European Court of Justice[984], and the European Court of Human Rights[985].

Against that background, focusing on the effects of the anti-holdout model on small bondholders makes sense for two reasons.

First, retail investors, are a particularly vulnerable category of debt holders. Thus, understanding the effects of a restructuring on their financial health matters from a consumer protection perspective.

Second, and more fundamentally, while vulture fund litigation is a seemingly disappearing phenomenon, litigation by retail investors is a growing phenomenon. As litigation disrupts restructuring processes, incentivising retail investors against litigating is logical as it would promote more efficient restructuring processes. In order to understand why the anti-holdout model fails retail investors, one has to understand why they differ from vulture funds.

Vulture funds, as understood in this thesis, are arbitrageurs. They purchase sovereign bonds at their market value on the secondary bond market, and then realise them at a second, higher value, their judicial value, in a courthouse[986].

The restructuring protection model works as a tool to disincentivise vulture funds because it makes this financial gamble unrealisable. Before domestic court, CACs prevent holdout enforcement[987], and the enhanced *pari passu* prevents vulture funds from effectively coercing States into repaying vulture funds. With the domestic avenue for litigation closed, one could expect vulture funds to move towards international litigation. However, international litigation, as an avenue for dispute settlement is more uncertain[988]. In addition, arbitral tribunals are extremely expensive means of dispute settlement as opposed to domestic courts[989]. This, effectively, closes the window for arbitrage.

[982] *Abaclat and Others v. Argentine Republic* (n 17); *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17).
[983] *Stephan Fahnenbrock et al v Hellenische Republic* [2015] Court of Justice of the European Union C-226/13, C-245/13, C-247/13, C-578/13.
[984] *Alessandro Accorinti and others v. European Central Bank* (n 19).
[985] *Mamatas et autres v. Greece* (n 18).
[986] Fisch and Gentile (n 73); Blackman and Mukhi (n 73).
[987] Stolper and Dougherty (n 11).
[988] *Poštová banka, a.s. and Istrokapital SE v. Hellenic Republic (Award)* (n 17); *Mamatas et autres v. Greece* (n 18); *Alessandro Accorinti and others v. European Central Bank* (n 19).
[989] An OECD survey indicates an average of $8 million per case. David Gaukrodger and Kathryn Gordon, 'Investor-State Dispute Settlement: A Scoping Paper for the Investment Policy Community"' (2012) 2012

Retail investors operate following a different investing strategy. They purchase bonds as a savings device[990]. Litigation, for retail investors therefore performs a different economic function than it does for vulture funds. For vulture funds, litigation is a calculated investing strategy. For individuals, however, litigation is a way to potentially mitigate the costs of a debt restructuring.

In addition, as opposed to more sophisticated investors, individual holders of bonds have more to lose following a haircut. First, if studies conducted on shareholding hold true in the bond market[991], the position of retail investors tends to be more concentrated. This means that a loss on an individual's bonds will, comparatively, be more painful, the same loss for a bank or a pension fund. Retail investors are also unable to hedge their losses by accessing the derivatives market, as they lack the capital required for the purchase over-the-counter derivatives trading[992].

Moreover, as mentioned before, individuals are not economically incentivised to participate in the restructuring process. As opposed to institutional investors, they do not have a long-term relationship with the debtor and will therefore not benefit from its return to capital markets.

The fact that individuals suffer comparatively more losses than their more sophisticated counterparts is problematic in the restructuring protection model as majority decision-making means that smaller holders cannot prevent a loss on their bonds[993]. This problem is compounded by the fact that retail investors, or their representatives, are usually not invited to the restructuring negotiations, preventing them from impacting the final decision[994].

The fact that the creditors who have incentives towards restructuring hold the decision-making power during the restructuring process is a positive development as it speeds up the

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OECD Working Papers on International Investment <http://www.oecd.org/daf/inv/investment-policy/WP-2012_3.pdf>.

[990] Felix Salmon, 'Stop Selling Bonds to Retail Investors Essays' (2003) 35 Georgetown Journal of international law 837.

[991] It would make sense if retail investors' portfolio, as their shareholding was not sufficiently diversified. Tradionally, bonds are safer, less volatile investments reducing the need for diversification. If retail investors fail to sufficiently diversify their more volatile shareholding, one could reasonably expect the same issues to be carried over in the bond market, if not amplified. Barber and Odean (n 306).

[992] Wood, *Law and Practice of International Finance* (n 253) 427;440.

[993] International Capital Market Association (n 678); Gelpern, Heller and Setser (n 11).

[994] *Mamatas et autres v. Greece* (n 13) para 11-13.

restructuring process. The problem is that it also results in an amalgamation both vulture funds and retail investors under the holdout 'moniker', to the detriment of smaller holders.

The perfect example of this amalgamation can be found in the reasoning of the ECtHR in the *Mamatas* case[995]. The ECtHR in *Mamatas* relied on the notion of reasonableness to dismiss the claimants' assertion that their property rights had been violated. The court, in its reasoning notes the price at which Greek bonds were trading at the time of the restructuring, the market's acceptance of CACs and the fact that the applicants decided to hold on to their bonds rather than liquidating them. It then uses these findings to argue that the claimants had not acted as "*prudent and circumspect investors*", and therefore could not claim that their property rights had been unlawfully limited by Greece[996].

The problem with the Court's reasoning is not that it opted to sanction the retrofit CACs, as this measure was necessary to ensure the success of the Greek restructuring process. Rather, the decision by the Strasbourg Court to analyse the behaviour of retail investors under the same standard as sophisticated players within the sovereign debt market seems questionable.

The ECtHR, as the ECJ in *Accorinti*[997], underline that the claimants, should have been aware of the risk linked to the holding of Greek bonds given the price at which they were trading, and given the fact that even in 2009,Greece's debt to GDP ratio was high.

The argument that investors should have been aware, that the purchase of Greek bonds entailed significant risk seems artificial. The yield on 10-year Greek bonds in 2009, according to data gathered by the Bank of Greece oscillated between 4.52% in August, and 5.87% in March[998]. German 10-year bonds that same year yielded between 3.02% in March and 3.47% in June, according to data gathered by the St Louis Federal Reserve[999]. As a

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[995] *Mamatas et autres v. Greece* (n 18).
[996] *Mamatas et autres v. Greece* (n 13) para 54.
[997] *Alessandro Accorinti and others v. European Central Bank* (n 14) para 82.
[998] Comparing the Greek and German securities for that year makes more sense than comparing Greek bonds and 3 month US Treasuries, usually used as a benchmark for risk as it allows to minimise any differences linked to an exchange risk, indeed, in 2009, both Greece and Germany borrowed in Euro. Using German bonds as a benchmark for risk for Euro-denominated government securities can be justified by the fact that Germany is traditionally considered the safest borrower of the Eurozone. The figure quoted here are from https://www.bankofgreece.gr/Pages/en/Statistics/rates_markets/titloieldimosiou/titloieldimosiou.aspx?Year=2009
[999] https://fred.stlouisfed.org/series/IRLTLT01DEM156N; Heather D Gibson, Stephen G Hall and George S Tavlas, 'The Greek Financial Crisis: Growing Imbalances and Sovereign Spreads' (2012) 31 Journal of International Money and Finance 498.

further point of comparison, the yield on 10 Year treasury bonds that year oscillated between 2.48% and 2.60% according to data gathered by US Department of Treasury[1000].

Bond yields, of course, are not only a proxy for the riskiness of the investment, but also for its desirability and can be impacted by other factors such as global inflation[1001]. 2009 bond yields might be distorted by broader market trends that year, notably the 2008 financial crisis which brought investors seeking safe havens from global volatility towards government securities, hence reducing their yield[1002]. However, used as a rough approximation of risk assessment by market actors, the yield on Greek bonds highlight that investors, despite Greece's high debt to GDP ratio, did not consider the Greek government securities as a particularly reckless investment[1003].

Once the Greek restructuring was under way, and Greece's default was deemed unavoidable by institutional stakeholders and credit rating agencies, the value of Greek bonds plummeted[1004]. This meant that their holders already suffered consequential unrealised losses. At this point, were a retail investor to liquidate her position on Greek government securities, as suggested by the court, the losses would be realised. Logically, at this point, a prudent and circumspect *institutional* investor would liquidate. It would take in a loss and absorb it, either through gains in its portfolio, or through hedging. However, for a retail investor, selling at this point meant taking in a certain loss.

One can therefore argue that the decision of such a retail investor to hold on to her bonds, especially when the Greek government had provided assurances that individuals would be spared during the restructuring[1005], made economic sense. Contrary to the court's reasoning, the fact that individual holders act differently than the majority of bondholders does not mean that, given their specific circumstances, they act *unreasonably* or in bad faith.

Finally, given that for some retail investors, litigation is a mean to protect an investment, to guarantee that savings are kept safe, disincentivising litigation by making access to court

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[1000] https://www.treasury.gov/resource-center/data-chart-center/interest-rates/Pages/TextView.aspx?data=yield

[1001] Mr Manmohan S Kumar and Mr Emanuele Baldacci, *Fiscal Deficits, Public Debt, and Sovereign Bond Yields* (International Monetary Fund 2010).

[1002] Salvador Barrios and others, 'Determinants of Intra-Euro Area Government Bond Spreads during the Financial Crisis' (Directorate General Economic and Financial Affairs (DG ECFIN), European Commission 2009) 388 <https://ideas.repec.org/p/euf/ecopap/0388.html> accessed 8 May 2019.

[1003] On this question see also Gibson, Hall and Tavlas (n 999).

[1004] ibid.

[1005] *Mamatas et autres v. Greece* (n 18).

more difficult or more expensive might not be sufficient to prevent it. Specific provisions designed to make haircuts more palatable for retail investors are therefore required.

4.4.2.3 The Sovereign Debtor in the Anti-holdout model

the anti-holdout model mostly focuses on collective action issues between debtors and their creditor-base. While this approach is an appropriate response to the problems raised in the 1990s and 2000s by holdout litigation, it does not address one of the central issues of debt restructurings: the lack of incentives, for debtor governments, to restructure their debt when necessary[1006].

The problem with debtors, under the current model, is that faced with domestic political pressures, governments may prefer to delay inevitable restructurings. This renders debt workouts more expensive, and thus more painful for creditors and the debtor's population[1007].

For example, it is only following partial default on its bonds in November 2017 that Venezuela organised a rather unproductive meeting with its bondholders, despite having been plunged in a financial crisis for several years[1008]. Since this initial meeting, little efforts have been made by the Maduro government to resolve its debt crisis In the meantime, the living condition of Venezuela's population deteriorated as inflation rose to historically high levels[1009].

The anti-holdout model addresses the issues arising *after* the sovereign has opted to open negotiations and restructure its debt. However, nothing within the current regulatory model is designed to entice the debtor's government to restructure its debt when necessary. Such a situation is problematic, as later restructurings lead to higher costs not only for the sovereign's debtor, but also for its population.

[1006] Martin Guzman, Joseph Stiglitz and Jose Antonio Ocampo, 'Introduction', *Too Little, Too Late: The Quest to Resolve Sovereign Debt Crises, Guzman, Ocampo and Stiglitz (eds.)* (Columbia University Press 2016).
[1007] *Too Little, Too Late: The Quest to Resolve Sovereign Debt Crises* (n 72).
[1008] Buchheit and Gulati, 'How to Restructure Venezuelan Debt (¿Cómo Restructurar La Deuda Venezolana?' (n 5); 'Venezuela in "Selective Default"' (n 5); 'Venezuela Offers Chocolates but Little Else to Creditors' *Reuters* (13 November 2017) <https://www.reuters.com/article/us-venezuela-bonds-idUSKBN1DD0IG> accessed 7 May 2019.
[1009] For a recent overview see 'Venezuela's Inflation Tumbles to 9,586% in 2019: Central Bank' *Reuters* (4 February 2020) <https://www.reuters.com/article/us-venezuela-economy-idUSKBN1ZY2YQ> accessed 25 May 2020.

5. Conclusion

5.1 Overview

For most of its history, sovereign lending can be understood as a gamble by private entities that the sovereign to whom they have extended credit will choose to honour its contractual obligations. While mechanisms designed to increase the likelihood of repayments have nearly always been a feature of the sovereign/creditor relationship, actual judicial remedies guaranteeing repayment have been a historical exception rather than a rule. As such, economists sought to understand the sovereign debt puzzle by reference to either reputational games between States and their potential lenders[1010], or by explaining that States could improve their borrowing conditions by providing their creditors with credible commitment devices[1011].

As such, rights of creditors had been guaranteed via supersanctions[1012], gunboat diplomacy[1013], the pledging of securities[1014] and diplomatic protection[1015]. These means of protection were often inefficient as they subjected creditors to the political whims of their national State or failed to shield them from the debtor's regulatory powers.

A combination of factors from the 1970s onwards would see this situation change. First, as the '70s unfolded, bringing with them steep rates of inflation, the Bretton Woods institutional system started to show cracks and displayed an inability to face borrowing demands of LDCs[1016]. Bank syndicates entered this breach, re-opening private lending for developing sovereigns for the first time since the 1930s.

The law potentially applicable to sovereign debt, however, differed from the one in force in the 19th and early 20th century. First, the law of immunities had evolved to enable private entities to litigate against sovereigns before domestic courts for *acta de iure gestionnis*[1017]. Second, at the international level, from the 90s onwards, two new avenues had been opened

[1010] Eaton (n 185); Tomz (n 112).
[1011] North and Weingast (n 124); North (n 124); Oosterlinck, Ureche-Rangau and Vaslin (n 192); Mitchener and Weidenmier (n 91).
[1012] Mitchener and Weidenmier (n 91).
[1013] Waibel, *Sovereign Defaults before International Courts and Tribunals* (n 2) 29–35; Weidenmier (n 175).
[1014] Vizcarra (n 229).
[1015] Weidemaier, 'Contracting for State Intervention' (n 236).
[1016] Warren and Avery (n 248).
[1017] Delaume (n 82); Weidemaier, 'Sovereign Immunity and Sovereign Debt' (n 82).

to enable litigation by individuals and companies against sovereigns: human right courts[1018] and investment tribunals[1019].

During the following years, and up until the early 2000s, contractual design and court decisions showed a systematic bias towards favouring creditors. This bias, coupled with creditor heterogeneity, lead to collective action issues within the sovereign debt market, preventing sovereigns from efficiently restructuring their debts when necessary. These increased difficulties, led, in turn, to changes within the law on sovereign debt, at the contractual level, the domestic law level and the international level.

These evolutions were accompanied by a spectacular fragmentation of the law on sovereign debt, both within the case law and the scholarship. At the judicial level, domestic and international courts rendered several highly contradictory and highly controversial decisions, whether on necessity[1020], the interpretation of the *pari passu* clause[1021], the applicability of ISDS to sovereign debt[1022], or even the law on immunities[1023].

Approaches to sovereign debt were similarly fragmented within the legal scholarship on sovereign debt. Scholars have treated the social phenomenon that is sovereign debt in a divided way, falling on either side of the traditional domestic/international division of law. Methodologically, sovereign debt was examined through the lens of legal positivism, or law and economics, and focused on finding technical solutions to the problems plaguing the sovereign debt market. Alternatively, sovereign debt was approached in a highly political way, but few studies have provided a broad overview of how sovereign defaults and restructurings have been regulated.

[1018] *Mamatas et autres v. Greece* (n 18); *De Dreux-Brézé c. France* (n 419); *Thivet v. France* (n 419); *Malysh and others v Russia* (n 419).

[1019] *Fedax N.V. v. The Republic of Venezuela* (n 551); *Abaclat and Others v. Argentine Republic* (n 17); *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17); *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17).

[1020] *CMS Gas Transmission Company v. The Republic of Argentina (Award)* (n 517); *LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc .v. Argentine Republic (Decision on liability)* (n 543); *Enron Corporation and Ponderossa Assets L.P. v Argentine Republic (Award)* (n 551); *Continental Casualty Company v. The Argentine Republic* (n 591).

[1021] *Elliott Assocs., L.P. v. Banco de la Nacion* (n 28); *Elliott Assocs., L.P.* (n 323); *Export-Import Bank of the Republic of China v. Grenada* (n 28); *NML Capital, LTD., et al. v The Republic of Argentina* (n 28); *Republic of Nicaragua v LNC Investment LLC* (n 398).

[1022] *Abaclat and Others v. Argentine Republic* (n 17); *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17); *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17); *Poštová banka, a.s and ISTROKAPITAL SE v Hellenic Republic (Award)* [2015] ICSID ARB/13/8.

[1023] *Republic of Argentina v. Weltover, Inc.* (n 24); *Ordinanza* (n 25).

Understanding the last forty years of legal development on sovereign debt, and understanding what type of incentives the current regime on default and restructuring provides, requires systematizing these fragmented approaches. This thesis has done so by providing a law and economics-based framework via which legal norms on sovereign debt can be understood. This framework examines the incentives produced by the domestic and international norms on sovereign debt, and sorts said norms according to the type of behaviour they seek to encourage. Such an understanding of sovereign debt, and the criticisms of the current regime it leads to, are necessary, when the prospect of a global financial crisis and defaulting sovereigns has risen again following the Covid pandemic.

In order to understand sovereign debt, this thesis had to depart from traditional law and economics[1024] and acknowledge that the behaviour of market actors is not fully rational but *bounded* by external factors[1025]. Notably, that high transaction costs may have prevented contractual developments[1026]. Similarly, the democratic appearance of CACs may increase compliance with restructuring offers and participation to the restructuring process. In the same vein, a fully institutionalist reading of State behaviour [1027], would prevent understanding that governments, due to domestic political pressure, may not restructure when needed[1028].

The 'new law and economics' approach used here, treats the actors within the sovereign debt market as rationally *bounded*, but still influenceable by legal norms, either via their structural impact on the market, their effect as a pricing mechanism, or their legitimacy.

The net result of this approach is that one can systematise the law on sovereign defaults and restructurings as a succession between two distinct regulatory models: the creditor protection model and the anti-holdout model.

The creditor protection model relied on the idea that norms within the sovereign debt market should enable creditors to effectively enforce the obligations against the debtor. Such abilities should not be understood merely as favouring private interests over the interests of sovereigns and their populations, as the remedies act as judicial credible commitment

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[1024] E.g. Richard A Posner, *Economic Analysis of Law* (5th ed, Aspen Law & Business 1998); Cooter and Ulen (n 98); Trachtman (n 98).
[1025] Sunstein (n 139); Christine Jolls, Cass Sunstein and Richard Thaler, 'A Behavioral Approach to Law and Economics' [1998] Faculty Scholarship Series <https://digitalcommons.law.yale.edu/fss_papers/1765>.
[1026] Gulati and Scott (n 75); Weidemaier, Scott and Gulati (n 75).
[1027] Trachtman (n 98); March and Olsen (n 119).
[1028] *Too Little, Too Late: The Quest to Resolve Sovereign Debt Crises* (n 72).

devices[1029], incentivising creditors to lend. Thus, they enable sovereigns to borrow under better conditions.

To function, the creditor protection model required a combination of three elements: first, access to competent and independent jurisdictions by creditors; second a recognition of the sovereigns' obligations by said jurisdictions; finally, effective remedies to coerce the sovereign.

Attempts to put in place all those components explain much of how the law on sovereign debt, both international and domestic has developed. Recognising that debt restructurings are *acta de iure gestionnis*[1030], forum selection clauses in sovereign bonds, and the *Abaclat*[1031], *Ambiente*[1032] and *Alemanni*[1033] decisions let creditors access independent domestic and international jurisdictions. Choice-of-law clauses[1034], currency clauses[1035] and a narrow reading of the necessity defence[1036] ensured creditors that the obligations arising from the sovereign debt relationship were recognised by courts and tribunals and were protected from the sovereign's regulatory reach. Finally, changes in the law of immunities and the rateable payment interpretation of the *pari passu*[1037] clause provided creditors with variably efficient ways to coerce sovereigns into fulfilling their obligations.

While these remedies did not guarantee that States would honour their obligations, they heavily favoured creditors and increased the chances of them being able to obtain payment. Thus, they provided a tax on defaulting, repudiating, or restructuring, and strategically enabled creditors to sue. In addition, these remedies ensured that sovereigns could not renege on their debts and should therefore respect the rule of law, thus legitimising the actions of litigating creditors.

Such a situation was not problematic when the main contractual instruments for sovereign indebtedness were syndicated loans. Given the contractual structure of bank syndicates, and

[1029] North (n 124); North and Weingast (n 124).
[1030] *Republic of Argentina v. Weltover, Inc.* (n 24).
[1031] *Abaclat and Others v. Argentine Republic* (n 17).
[1032] *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17).
[1033] *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17).
[1034] Choi, Gulati and Posner (n 114).
[1035] Flandreau and Sussman (n 114); Eichengreen, Haussman and Panizza (n 114).
[1036] *LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc .v. Argentine Republic (Decision on liability)* (n 543); *CMS Gas Transmission Company v. The Republic of Argentina (Award)* (n 517); *Enron Corporation and Ponderossa Assets L.P. v Argentine Republic (Award)* (n 551).
[1037] *Elliott Assocs., L.P. v. Banco de la Nacion* (n 28); *Elliott Assocs., L.P.* (n 323); *NML Capital, LTD., et al. v The Republic of Argentina* (n 28).

given that large banks are in a long term client relationship with sovereign debtors, actors within the syndicated sovereign debt market had no interest in systematically suing restructuring sovereigns[1038]. However, while the club-like nature of syndicated lending enabled lenders to coordinate during restructurings, and disincentivised reckless enforcement, it created a system where critically important financial institutions were heavily exposed to default risks of LDCs[1039]. When this system came to a halt during the Latin American crisis, sovereign indebtedness took the form of bonds, whose transferability enabled risk to be spread to broader classes of creditors.

This heterogeneity of the bond market proved to be a double edge sword as it brought creditors which lacked the incentives to allow States to restructure their debts when needed: vulture funds and retail investors[1040].

These two groups of creditors would seize the remedies made available under the creditor protection model and heavily disrupt several restructuring processes, leading to increased uncertainty as to the success of much needed debt restructurings.

This lead in the development of the second model, the anti-holdout model. The anti-holdout model seeks to improve upon the efficiency of sovereign debt law by providing the sovereign and its creditors with legal tools to facilitate debt restructurings. Thus, it seeks to disincentivise holding out and litigating reasonable restructuring offers.

It relies on three key components: majoritarian decision-making during restructurings, incentives against holding out from restructuring offers, and the provision of funds to improve the debtor's liquidity.

Notably, the insertion of Collective Action Clauses in sovereign bonds[1041], and reliance on good faith or good faith-like reasoning in adjudication[1042] promote majority decision-making. The rank of payment reading of the *pari passu* clause[1043], anti-vulture fund legislation[1044], a

[1038] Wood, 'Essay' (n 254).
[1039] Monteagudo (n 8).
[1040] Dellas and Niepelt (n 297); Ghosal and Miller (n 158).
[1041] International Monetary Fund (n 13); International Capital Market Association (n 678); International Monetary Fund (n 674).
[1042] United Nations General Assembly, 'Resolution 69/319: Basic Principles on Sovereign Debt Restructuring Processes' (n 22); UNCTAD (n 878).
[1043] *NML Capital, LTD., et al. v The Republic of Argentina* (n 28); *Export-Import Bank of the Republic of China v. Grenada* (n 28); *Republic of Nicaragua v LNC Investment LLC* (n 398); Zamour (n 74).
[1044] Loi du 12 juillet 2015 relative à la lutte contre les activités des fonds vautours.

strengthening of immunities of execution[1045], reliance on good faith and the abuse of rights doctrine and a more generous reading of the economic necessity defence[1046] have reduced the efficiency of remedies available to creditors. This increases the likelihood that they will accept restructuring offers.

Similarly, CACs prevent a minority of holdouts from suing the debtor for breach of contract if a majority of creditors has agreed to a restructuring offer.

Finally, the systemic risk exception in IMF conditionality as wells as the creation of ESM[1047] have created new venues via which sovereigns can bolster their liquidity during crises thus limiting private exposure to default.

Most of these developments, are essentially taxes on litigation, they lower the odds of success before courts without changing the pay-off. Moreover, the insertion of CACs also restructures the creditor/debtor relationship by enabling the latter to restructure by majority decision making. Finally, the use of majority processes, and reliance on quasi-natural law principles, such as good faith and the abuse of rights, provides legitimacy to sovereigns refusing to repay holdouts.

The main advantage of the anti-holdout model is that it facilitates debt restructurings, thus limiting the costs of reducing a sovereign's over-indebtedness, both for the sovereign itself, but also for its population and most of its creditors.

Despite these strengths, there remain some weaknesses in the current regulatory model for sovereign debt. First, the system as it is currently designed relies upon the idea that prompt restructurings are efficient. Research has shown that States restructuring too late is one of the main sources of costs during sovereign debt workouts[1048]. However, sovereign debt law, as it currently stands, does little to encourage sovereign to act as early as possible.

[1045] Debt Relief (Developping Countries) Act 2010; 'Loi Du 28 Avril 1999 Visant à Transposer La Directive 98/26/CE Du 19 Mai 1998 Concernant Le Caractère Définitif Du Règlement Dans Les Systèmes de Paiement et de Règlement Des Opérations Sur Titres.' (n 741) 208; Loi visant à empêcher la saisie ou la cession des fonds publics destinés à la coopération internationale, notamment par la technique des fonds vautours; LOI n° 2016-1691 du 9 décembre 2016 relative à la transparence, à la lutte contre la corruption et à la modernisation de la vie économique.
[1046] *Continental Casualty Company v. The Argentine Republic* (n 591).
[1047] Treaty Establishing the European Stability Mechanism (Brussels).
[1048] See *Too Little, Too Late: The Quest to Resolve Sovereign Debt Crises* (n 72).

Similarly, while the current model is designed to disincentivise holding out, it does little to ensure that retail investors have an interest in accepting a reasonable restructuring offer by the sovereign. It therefore fails from a consumer protection perspective, and from an anti-holdout perspective.

Finally, the way via which legal innovation has been advanced in the sovereign debt market, via a disparate range of legal instruments and contradictory court decisions, raises the possibility of fragmentation. This added fragmentation leads to added uncertainty in times of restructuring.

The paradigm-mapping exercise pursued in the pages of this thesis was necessary because understanding these blind-spots in the current regulatory model required moving away from a narrow technical lens when assessing the norms on sovereign debt. It also required a model of sovereign debt regulation which transcended the domestic/international legal boundary to fully map the sets of incentives applicable to sovereigns and their creditors.

In highlighting issues created by the move away from the creditor protection model and towards an anti-holdout model, this thesis should not be regarded as discrediting recent legal developments. Rather, it understands these issues as unforeseen consequences of a model which improves on a previously dire situation.

Finally, avenues to improve upon those blind spots can be developed and will briefly be examined the next, final section.

5.2 Moving Forward: potential solutions to improve upon the contemporary regulatory model

5.2.1 Reducing Fragmentation: Regional Agreements and Sovereign Debt

The classic solution for fragmentation is the creation of multilateral conventional instruments. An international mechanism for sovereign debt restructuring has been, regularly suggested[1049]. Notably, in the early 70s, the Group of 77 suggested the instigation of an

[1049] Kenneth Rogoff and Jeromin Zettelmeyer, 'Bankruptcy Procedures for Sovereigns: A History of Ideas, 1976–2001' (2002) 19 IMF Staff Paper <https://www.imf.org/External/Pubs/FT/staffp/2002/03/pdf/rogoff.pdf>.

International Debt Commission, tasked with assessing the debt of developing states and establishing recommendations to tackle over indebtedness[1050]. Similarly, scholars since, at least the 1980s have suggested the creation of a multilateral framework for sovereign debt restructuring, either centred on the IMF[1051], or independent[1052].

At today's date, the core of the discussion on an international mechanism for sovereign debt restructuring centres on Anne Krueger's proposal for a Sovereign Debt Restructuring Mechanism[1053], operating in collaboration with the IMF[1054]. The establishment of such a multilateral system runs into two issues, one is political, the other legal.

Politically, 'creditor states' have systematically opposed the creation of such mechanisms[1055]. As previously highlighted, the same creditor states voted against the recent UN general assembly resolution on sovereign debt, indicating that their opposition to a public international law-based framework for sovereign debt resolution remains strong[1056]. Given the opposition of creditor states, the establishment of such a treaty-based international mechanism to restructure sovereign debt seems unlikely.

Moreover, legally, the creation of an additional instrument governing sovereign debt restructuring will not help reduce the fragmentation of the current regime. Fragmentation will remain unless said new multilateral instrument implicitly or explicitly repeals all other international norms applicable to sovereign debt restructurings. Rather, the creation of an additional instrument applicable to sovereign debt would only lead to the creation of additional conflict between norms. In addition, unless said multilateral instrument is made directly applicable, it does not seem that it would equally apply to creditors acting before domestic courts.

[1050] ibid; Charles Lipson, 'The International Organization of Third World Debt' (1981) 35 International Organization 603.
[1051] Jeffrey D Sachs, 'International Lender of Last Resort? What Are the Alternatives?' (1999) 43 Conference Series ; [Proceedings] 181.
[1052] See e.g. Rogoff and Zettelmeyer (n 1049).
[1053] Krueger (n 76).
[1054] ibid.
[1055] See in general Ocampo (n 32); Euliss (n 76); Mooney (n 76).
[1056] United Nations General Assembly, 'Resolution 69/319: Basic Principles on Sovereign Debt Restructuring Processes' (n 22). It should be noted that creditor States do not oppose all developments towards facilitating debt restructuring. Rather, their opposition seems to focus on the establishment of mechanisms to that effect in international law, contractual modifications being therefore preferred. See Mooney (n 76). On the role of creditor States within the development of the law on sovereign debt, and its links to sovereign equality see Klabbers (n 23) 247.

Against that background, it does not seem that the drafting of an international treaty on sovereign debt is the solution to the fragmentation issues that contemporary sovereigns face when restructuring their debt.

A possible way to reduce the legal uncertainty created by the combination between the international nature of the bond market and drafting variation in BITs could be found in regional trade and investment agreements. Indeed, the multilateral nature of these instruments enables them to apply equally to bondholders of several nationalities, therefore overall reducing the number of possible drafting variations.

For example, the already mentioned CETA treaty explicitly applies to sovereign bonds[1057]. CETA defines investments as:

> *"Every kind of asset that an investor owns or controls, directly or indirectly, that has the characteristics of an investment, which includes a certain duration and other characteristics such as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk. Forms that an investment may take include:*
>
> *(…)*
>
> *shares, stocks and other forms of equity participation in an enterprise; bonds, debentures and other debt instruments of an enterprise; (…)*
>
> *claims to money or claims to performance under a contract;"*[1058]

This broad definition of investment, featuring the catch-all provision displayed in the Argentina-Italy BIT at stake in the *Abaclat*[1059], *Alemanni*[1060] and *Ambiente*[1061] decisions is further developed regarding sovereign debt by Annex X.17, on CETA's applicability to sovereign debt. Annex X explicitly excludes sovereign bonds from the ISDS dispositions of

[1057] 'Comprehensive Economic and Trade Agreement between Canada, of the One Part, and the European Union and Its Member States, of the Other Part, 14 September 2016 (Brussels)' (n 862).
[1058] ibid.
[1059] *Abaclat and Others v. Argentine Republic* (n 17).
[1060] *Giovanni Alemanni and Others v. The Argentine Republic (Decision on Jurisdiction and Admissibility)* (n 17).
[1061] *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (n 17).

CETA, except for cases related to MFN and National Treatment dispositions within the treaty[1062]. A similar exclusion of sovereign debt features in the NAFTA agreement[1063].

Mega-regionals reduce the uncertainty linked towards adjudicating sovereign debt through ISDS at two different levels.

The multilateral nature of the instrument reduces the overall number of potential instruments applying to a single bond issue or restructuring. This facilitates the task of States and their creditors in ascertaining whether international litigation is possible on sovereign debt. Indeed, as they replace multiple pre-existing BITs, mega-regionals reduce the overall number of potentially applicable BITs to a single debtor.

This advantage of regional trade and investment agreements is tempered by the fact that, for the near-foreseeable future, their use is unlikely to fully replace the already existing BIT system. Indeed, while the overall use of regional agreement is on the rise, and while the overall number of newly concluded BITs is falling, the current system for the adjudication of investment disputes remains BIT-centric.

The second advantage of regional agreements is that compared to BITs, they usually feature more detailed dispositions on sovereign debt. This is easily explained by the fact that, if one wants to introduce reform regarding ISDS application to sovereign debt, doing so via multilateral regional agreements entails less transaction costs. Adding dispositions limiting the applicability of international investment agreements to sovereign debt involves a certain cost, linked to the fact that the sovereigns signing the treaty have to negotiate the exact content of said dispositions. Moreover, from a reputational or a credible commitment point of view, a State's willingness to prevent litigation on its own debt may be perceived badly by its creditors. In a BIT, these costs are incurred by the two signatories alone, however, in a regional agreement, the same cost can be spread across all the parties to the treaty.

[1062] 'Comprehensive Economic and Trade Agreement between Canada, of the One Part, and the European Union and Its Member States, of the Other Part, 14 September 2016 (Brussels)' (n 862).
[1063] 'North-American Free Trade Agreement', article 1139.

5.2.2 Incentivising Retail Investors against Litigating: GDP-Linked Bonds and Representation

The position of retail investors within the restructuring protection model creates a conundrum. On the one hand, litigation makes restructuring more complex and expensive, it hurts the interests of most stakeholders and therefore, when possible, should be avoided[1064]. On the other hand, preventing reasonable litigation by retail investors might lead them to exit the sovereign debt market, leading to higher borrowing costs for smaller economies or to higher concentration of risk in key players within the financial system.

A potential solution to this conundrum would be to strengthen the path dependency between retail investors and the borrower. The problem with retail investors, from a game theoretical perspective, is that they play a single round of the prisoner's dilemma game. If one could turn them into repeat players, it would incentivise them towards accepting restructuring proposals without potentially leading to their exit from the sovereign debt market.

A potential solution could come from the use of GDP-linked bonds. GDP-linked bonds are floating rate bonds, with a rate tied to the GDP of the issuer[1065]. In other words, the pay-off on GDP-linked bonds rises when the debtor does well economically. Restructurings usually involve a menu of options for creditors, for example, bonds with extended maturity, a reduced interest rate or a reduced principal compared to the securities swapped during the restructuring[1066].

Systematically adding GDP-linked bonds to this menu, hence making them available for retail investors, would entice them into accepting a restructuring offer and would dissuade them from litigating once the swap has occurred. Regarding the first point, GDP-linked bonds could be used as a sweetener as the size of the haircut on the initial bonds would be reduced with the floating rate going up during periods of economic growth for the debtor. Basically, GDP-linked bonds allow for a haircut, *ab initio*. However, if this haircut is

[1064] See e.g. Julian Schumacher, Christoph Trebesch and Henrik Enderlein, 'Sovereign Defaults in Court: The Rise of Creditor Litigation 1976-2010' [2012] SSRN Electronic Journal <http://www.ssrn.com/abstract=2189997> accessed 17 October 2016.

[1065] David Barr, Oliver Bush and Alex Pienkowski, 'GDP-Linked Bonds and Sovereign Default' in Joseph E Stiglitz and Daniel Heymann (eds), *Life After Debt: The Origins and Resolutions of Debt Crisis* (Palgrave Macmillan UK 2014) <https://doi.org/10.1057/9781137411488_16> accessed 1 March 2019.

[1066] Das, Papaioannou and Trebesch (n 4) 7.

successful and creates economic growth for the debtor, then the rate of the bonds rises, paying for part of the debt write-off[1067].

Second, because the floating rate is linked to economic growth in the debtor's economy[1068], holders of GDP-linked bonds are incentivised towards creating said economic growth. As litigation creates uncertainty during a restructuring process, holders of GDP-linked bonds should be incentivised against litigating.

Fundamentally, the use of GDP-linked bonds could allow debt issuers to create a long-term commitment between themselves and retail investors. Retail investors would thus be financially invested in the success of the restructuring process and incentivised towards voluntarily participating to it.

In addition to GDP-linked bonds, ensuring the participation of representatives of retail investors to negotiations could strengthen the legitimacy of the restructuring agreement, and thus act as an incentive for retail investors to accept the result of negotiations.

Direct participation of retail investors to the restructuring process is impossible given the number of small bondholders and the difficulties in inviting them all individually. However, ensuring the participation of legal representatives of small bondholders to the restructuring process could help achieve a similar effect.

Several model of creditor representation have been envisaged for sovereign bonds[1069]. Trustees for example are legal representatives of creditors, given power to trigger enforcement on the bonds in case of defaults[1070]. Trustees are a regular feature of modern bond issues with BNY Mellon acting as a trustee on some of Argentina's restructure bonds and a trust a trust indenture being put in place for Ecuador's bonds during its 2008 default[1071]. The advantage of trustees is that they can act both as representative of creditors, and therefore directly participate in the restructuring negotiations, while also wielding judicial powers.

[1067] Barr, Bush and Pienkowski (n 1033) 247.
[1068] While a State's GDP is not a perfect measure of its economy, it is one of the few values that is easily usable as an easy economic indicator for economic growth. ibid.
[1069] For an overview of creditor representation during the Argentinean practice see Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 136–142.
[1070] Buchheit, 'Trustees versus Fiscal Agents for Sovereign Bonds' (n 319) 410.
[1071] See Mitu Gulati and Lee Buchheit, 'The Coroner's Inquest: Ecuador's Default and Sovereign Bond Documentation' [2009] International Financial Law Review 22.

Their issue, when focusing on retail investor participation *in specifis*, is that usually trust indentures or trust deeds are set for the whole of a bond issue[1072]. Trustees, as such, act as collective action clause in that they represent the majority of the bondholders, which is constituted by large players on the sovereign debt market.

Creditor Committees could therefore provide a better framework through which retail investor protection could be achieved. Creditor Committees are committees designed to represent the interest of bondholders following an event of default. As opposed to trustees they do not act as representatives of all the holders of a specific issue, but rather as *ad hoc* institutions designed for the representation of specific groups of holders[1073]. Dispositions for the creation of creditor committees can be included directly in the bond documentation, ensuring the existence of a legal framework for the creation of such committees prior to any default.

In this case, the ICMA provides bond issuers with a standardised clause for the formation and management of such committees. The problem with the ICMA standardised clause, however, is that it requires the participation of 30% of bondholders for the creation of a committee. In practice, some issuers have favoured different required participation threshold, some as low as 25%, some as high as 50%[1074].

To encourage the participation of retail investors, a low required participation threshold might be more beneficial as it would broaden the potential issues in which such committees could be set up. In cases where several creditor committees are set up, a steering group has to be established, enabling them to coordinate their actions. A more systematic set up of creditor committees representing the interests of retail investors could strengthen the legitimacy of the decisions made during a restructuring process, and ensure that options for retail investors are at least considered during the restructuring negotiations.

[1072] Buchheit, 'Trustees versus Fiscal Agents for Sovereign Bonds' (n 377).

[1073] See Michael Waibel, 'Engagement between Creditors and Sovereign Debtors: Guidance on Setting up Creditor Committees (EMTA Special Seminar: Further Improvements in the Market-Based Approach to Sovereign Debt Restructuring)'; Buchheit, 'Use of Creditor Committees in Sovereign Debt Workouts' (n 233).

[1074] See Michael Waibel, 'To Formalize or Not to Formalize: Creditor–Debtor Engagement in Sovereign Debt Restructurings' (2018) 13 Capital Markets Law Journal 452.

5.2.3 Incentivising States towards Restructuring Unsustainable Debts: A Contractually Enforceable Obligation to Restructure

If the legal framework on sovereign debt is to be economically efficient, it has to provide incentives for the debtor to undertake politically difficult debt restructurings as soon as possible.

Under the current system, the decision to kickstart debt restructurings lies firmly in the debtor's hands, up until an event of default, as defined by the bonds' documentation. Typically, events of defaults are defined as a breach of one of the bond's clauses[1075], usually events of default will be triggered by a missed payment on the bonds[1076].

The problem with this definition, or with the reliance on events of default to trigger creditor's remedies[1077], is that they ignore situations in which no contractual dispositions have been breached despite the fact that the debtor's debt burden is unsustainable[1078].

Therefore, as long as the debtor has sufficient liquidity to meet short-term payment obligations, creditors are unable to force the State to restructure its debt. Given that events of defaults, as traditionally understood, do not allow creditors to rely on their contractual remedies prior to breach of contract, an expansion of the definition seems necessary.

Ams *et al*.[1079] have suggested redefining events of defaults via the use of three different legal categories:

- Technical defaults, defined as events of defaults as contractually defined, but not constitutive of default under reputable third-party norms, e.g. credit rating agencies or CDSs[1080].

[1075] Julianne Ams and others, 'Chapter 7: Sovereign Default', *Sovereign Debt: A Guide for Economists and Practitioners* (IMF) <https://www.imf.org/~/media/Files/News/Seminars/2018/091318SovDebt-conference/chapter-7-sovereign-default.ashx>.
[1076] For an overview of the potential events of default arising from a standard bond issuance see Olivares-Caminal, *Legal Aspects of Sovereign Debt Restructuring* (n 5) 3.
[1077] In addition to litigation or payment acceleration, events of default also determine when creditor committees can be set up. Buchheit, 'Use of Creditor Committees in Sovereign Debt Workouts' (n 233); Waibel, 'Engagement between Creditors and Sovereign Debtors: Guidance on Setting up Creditor Committees (EMTA Special Seminar: Further Improvements in the Market-Based Approach to Sovereign Debt Restructuring)' (n 1073).
[1078] Ams and others (n 1075).
[1079] ibid 3.
[1080] ibid.

- Contractual defaults, defined as events of defaults that also constitute a default under reputable third-party norms[1081].
- Sustentive defaults, which count as defaults under reputable third-party norms but not as an event of default *in contractu*.[1082]

The problem of this expanded definition of default is that it still relies on, either a financial default, the fact that the State has not repaid part of its original debt, or a breach of contract. Hence, it does not allow for pre-emptive remedies available to creditors when default has not yet occurred but seems inevitable.

Designing such a remedy runs into two main potential issues. If the conditions for the use of the remedy are too narrow, the remedy is potentially useless. If they are too wide, they could potentially allow creditors to disturb a debt arrangement without proper cause.

Against that background, this thesis suggests the use of an automatic negotiation obligation, tied to external appraisals of debt sustainability. Its purpose is to create, for the State, an obligation to convene a meeting of bondholders or their representatives once a substantial downgrade in the likelihood of its debt repayment has been pronounced. Failure to convene such a meeting should, in turn, be constitutive of a breach of contract, hence creating an event of default.

The first step would be to implement into sovereign bonds themselves such an obligation to negotiate in case of doubts on the sustainability of the issuer's debt. Two external sources could be provided for an appraisal of debt sustainability.

First, the IMF's Debt Sustainability Analysis (DSA). The IMF's DSA has several advantages for the purpose of using it as an indicator of debt repayment triggering an obligation to negotiate. First, it is conducted by an independent third party, the IMF. It is also standardised and conducted regularly[1083]. The IMF's DSA takes into account several variables influencing debt sustainability such as the debtor's GDP, inflation, interests and exchange rates. It correlates said variables with the debt-to-GDP ratio of the issuer, and issues a series of stress tests[1084]. The IMF, in collaboration with the World Bank also takes into account the quality

[1081] ibid.
[1082] ibid.
[1083] On the DSA see Wyplosz (n 88) 2.
[1084] ibid 3-6.

of the economic and political institutions of the debtor[1085]. The results are then published by the IMF, with a label applied to each issuer, ranging from “low risk” to “high risk” or “debt distress”.

One could imagine the obligation of the issuer to organise a meeting of bondholders to be linked with either a DSA going from medium to high risk or from high risk to debt distress.

A second source for the appraisal of a State’s debt sustainability could come from credit rating agencies. There are several advantages on the use of credit rating agencies. First, as opposed to the IMF they are not perceived as political institutions. Their credit rating is also more nuanced than the 5 steps scale of the IMF. Moreover, according to Reinhart, credit rating agencies have a good track record in predicting default[1086]. In addition, rating is performed on separate bond issues and not the debt as a whole, allowing for added flexibility. There are however two main issues with the use of credit rating agencies[1087]. As private entities CRAs are funded by the issuer, raising potential questions of conflict of interests[1088]. Second, there are issues regarding the transparency of their methodologies[1089].

Using the automatic negotiation process, once a downgrade in debt sustainability outlook has occurred, the issuer has a legal obligation to convene a meeting of bondholder or their representative. Thus, under this system, a mere downgrade does not trigger an event of default, meaning that creditors could not use this opportunity to demand payment acceleration, or sue; similarly it could not lead to a contamination of the issuer’s other instruments via cross-default clauses.

This meeting should be convened within a limited time window, and its purpose is to give representatives of the issuer an opportunity to propose solutions to prevent an eventual default. The downgrade in debt sustainability should also be linked to the ability to create creditor committees. At the end of these negotiations, a vote should take place, on the same majorities as CACs either demanding a debt restructuring, or refusing it. If a qualified

[1085] ibid 11.
[1086] They are however more problematic when it comes to predicting currency crises. Carmen M Reinhart, ‘Default, Currency Crises, and Sovereign Credit Ratings’ (2002) 16 The World Bank Economic Review 151.
[1087] John Patrick Hunt, ‘Credit Rating Agencies and the Worldwide Credit Crisis: The Limits of Reputation, the Insufficiency of Reform, and a Proposal for Improvement’ (2009) 2009 Columbia Business Law Review 109; Lynn Bai, ‘On Regulating Conflicts of Interest in the Credit Rating Industry’ (2010) 13 New York University Journal of Legislation and Public Policy 253.
[1088] On potential conflict of interests in CRAs see Bai (n 1087); Franklin Strier, ‘Rating the Raters: Conflicts of Interest in the Credit Rating Firms’ (2008) 113 Business and Society Review 533.
[1089] See Hunt (n 1087).

majority of creditors agrees that a restructuring is necessary, then a second round of negotiations should occur to determine the size of the haircut.

Failure by the State to negotiate, at either of these stages would be characterised as a breach of contract, hence leading to an event of default and enabling creditors to accelerate payment or seek judicial enforcement.

The advantage of such a solution is that it would allow for negotiations to occur automatically in cases where doubts are expressed on the likelihood that the debt will be repaid, without these doubts being considered events of default. Moreover, it also relies on pre-existing mechanisms and institutions, making it relatively easy to put in place and also synergises with the use of CACs and Creditor Committees, thus ensuring the representation of most creditors.

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Annex 1: List of Treaties explicitly excluding sovereign debt

The following list has been compiled by the author relying on the UNCTAD Bilateral Investment Treaty Database. It only encompasses the Bilateral Trade and Investment Agreements, in force in 2018.

Acuerdo Entre El Gobierno De Los Estados Unidos Mexicanos Y El Gobierno De La Republica Argentina Para La Promocion Y Proteccion Reciproca De Las Inversiones, 1995.

Agreement Between The Government Of Australia The Government Of The United Mexican States And On The Promotion And Reciprocal Protection Of Investments, 1996.

Agreement Between The Republic Of Austria And Bosnia And Herzegovina For The Promotion And Protection Of Investments, 1998.

Agreement Between The Republic Of Austria And The Republic Of Cuba For The Promotion And Protection Of Investments , 1998.

Agreement Between The Republic Of Austria And Georgia For The Promotion And Protection Of Investments, 1999.

Agreement Between The Republic Of Austria And The Republic Of Guatemala For The Promotion And Protection Of Investments, 1999.

Agreement Between The United Mexican States And The Republic Of Austria On The Promotion And Protection Of Investments, 1999.

Agreement Between The Government Of The Republic Of Croatia And The Government Of The Republic Of Azerbaijan On The Promotion And Reciprocal Protection Of Investments, 2000.

Agreement Between The Government Of The Kingdom Of Bahrain And The Government Of The United Mexican States On The Promotion And Reciprocal Protection Of Investments, 2000.

Agreement Between The Government Of The United Mexican States And The Government Of The Republic Of Belarus On The Promotion And Reciprocal Protection Of Investments, 2000.

Agreement Between The Government Of Canada And The Government Of The Republic Of Benin For The Promotion And Reciprocal Protection Of Investments, 2000.

Accord Entre L'union Economique Belgo-Luxembourgeoise, D'une Part, Et Le Gouvernement De La République Du Perou, D'autre Part, Concernant L'encouragement Et La Protection Reciproques Des Investissements, 2001.

Acuerdo De Cooperación Y Facilitación De Inversiones Entre La República Federativa Del Brasil Y La República De Chile, 2002.

Acordo De Cooperação E Facilitação De Investimentos Entre A República Federativa Do Brasil E A República Da Colômbia, 2005.

Investment Cooperation And Facilitation Agreement Between The Federative Republic Of Brazil And The Republic Of Malawi, 2005.

Acordo De Cooperação E Facilitação De Investimentos Entre A República Federativa Do Brasil E Os Estados Unidos Mexicanos, 2005.

Canada - Honduras Fta (2013), 2005.

Agreement Between The Government Of Canada And The Government Of The Hong Kong Special Administrative Region Of The People's Republic Of China For The Promotion And Protection Of Investments, 2006.

Agreement Between Canada And The Hashemite Kingdom Of Jordan For The Promotion And Protection Of Investments, 2006.

Agreement Between Canada And The State Of Kuwait For The Promotion And Protection Of Investments, 2006.

Agreement Between Canada And Mali For The Promotion And Protection Of Investments, 2006.

Agreement Between Canada And Mongolia For The Promotion And Protection Of Investments, 2006.

Agreement Between Canada And The Republic Of Peru For The Promotion And Protection Of Investments, 2007.

Agreement Between Canada And The Federal Republic Of Senegal For The Promotion And Protection Of Investments, 2007.

Agreement Between Canada And The Republic Of Serbia For The Promotion And Protection Of Investments, 2007.

Agreement Between The Government Of Canada And The Government Of The United Republic Of Tanzania For The Promotion And Reciprocal Protection Of Investments, 2008.

Investment Agreement Between The Government Of The Hong Kong Special Administrative Region Of The People’s Republic Of China And The Government Of The Republic Of Chile, 2008.

Accuerdo De Inversion Entre La Republica De Chile Y La Republica Oriental Del Uruguay, 2008.

Bilateral Agreement For The Promotion And Protection Of Investments Between The Government Of The Republic Of Colombia And The Government Of The People's Republic Of China, 2009.

Colombia - Costa Rica Fta, 2009.

Agreement For The Promotion And Protection Of Investments Between The Republic Of Colombia And The Republic Of India, 2010.

Colombia - Korea, Republic Of Fta, 2010.

Acuerdo Entre El Reino De España Y La República De Colombia Para La Promoción Y Protección Recíproca De Inversions, 2011.

Bilateral Agreement For The Promotion And Protection Of Investments Between The Government Of The United Kingdom Of Great Britain And Northern Ireland And Republic Of Colombia, 2012.

Convenio Entre El Gobierno De La Republica Del Peru Y El Gobierno De La Republica De Cuba Sobre La Promocion Y Proteccion Reciproca De Inversiones, 2013.

Agreement Between The Czech Republic And The United Mexican States On The Promotion And Reciprocal Protection Of Investments, 2013.

Agreement Between The Republic Of Guatemala And The Republic Of Trinidad And Tobago On The Reciprocal Promotion And Protection Of Investments, 2013.

Agreement Between The Government Of The United Mexican States And The Government Of The Republic Of Iceland On The Promotion And Reciprocal Protection Of Investments, 2013.

Agreement Between The Government Of The United Mexican States And The Government Of The Republic Of India On The Promotion and Protection Of Investments, 2013.

Agreement Between Japan And The Republic Of Peru For The Promotion, Protection And Liberalisation Of Investment, 2014.

Agreement Between Japan And Ukraine For The Promotion And Protection Of Investment, 2014.

Agreement Between Japan And The Oriental Republic Of Uruguay For The Liberalization, Promotion And Protection Of Investment, 2014.

Agreement Between The Government Of The United Mexican States And The Government Of The State Of Kuwait On The Promotion And Reciprocal Protection Of Investments, 2014.

Agreement On Promotion, Encouragement And Reciprocal Protection Of Investments Between The Kingdom Of The Netherlands And The United Mexican States, 2014.

Pacific Alliance Additional Protocol, 2014.

Mexico - Panama Fta, 2015.

Agreement Between The Portuguese Republic And The United Mexican States On The Reciprocal Promotion And Protection Of Investments, 2015.

Agreement Between The United Mexican States And The Slovak Republic On The Promotion And Reciprocal Protection Of Investments, 2015.

Agreement On The Promotion And Reciprocal Protection Of Investments Between The United Mexican States And The Kingdom Of Spain, 2015.

Agreement Between The Government Of The Kingdom Of Sweden And The Government Of The United Mexican States Concerning The Promotion And Reciprocal Protection Of Investments, 2015.

Agreement Between The Swiss Confederation And The United Mexican States On The Promotion And Reciprocal Protection Of Investments, 2015.

Acuerdo Entre El Gobierno De Los Estados Unidos Mexicanos Y El Gobierno De La Republica De Trinidad Y Tobago Para La Promoción Y Protección Recíproca De Las Inversiones , 2016.

Agreement Between The Government Of The United Kingdom Of Great Britain And Northern Ireland And The Government Of The United Mexican States For The Promotion And Reciprocal Protection Of Investments, 2016.