Inter-creditor Equity in Sovereign Debt Restructuring

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Yanying Li
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1 Introduction

(1.1) This dissertation explores the relationship among creditors in sovereign debt restructuring and specifically focuses on the issue of inter-creditor equity. At the outset, it should be mentioned that the phrase "sovereign debt restructuring" refers to the methods through which sovereign debtors (being sovereign States) obtain debt relief. The word "equity" is to be understood as the state or quality of being just and fair. In the context of inter-creditor equity it therefore means a just and fair treatment of each creditor.

(1.2) The topic of sovereign debt concerns a broad range of issues in various legal and financial subjects, such as insolvency law, contract law, public international law, private international law and international finance. Whereas contract law deals with the contractual relationship between two or more parties, insolvency law focuses on the debtor-creditor dynamics. Public international law covers issues arising out of the fact that the debtor is a sovereign State. Private international law addresses the potential conflicts of law issues when it comes to the enforcement of a foreign agreement or judgment. Last but not least, international finance is relevant because it explains the position of sovereign lending and borrowing in the context of public finance as well as different forms of lending transactions. This dissertation takes a limited approach and chooses insolvency law as its main focus.

(1.3) At present, there is no international insolvency regime governing sovereign debt defaults with rules designed to address the scenario in which creditors cannot get paid in full. Instead, sovereign debt defaults are dealt with using an *ad hoc*, individual case-by-case approach in which most rules are invented along the way. In practice, the sovereign debtor is compelled to seek debt relief from creditors before or shortly after the default, via an extension of the maturity of a creditor's claim, and/or a reduction of the value of this claim. Such relief is obtained by renegotiating the relevant debt instruments (mostly contracts) with different types of creditors, including multilateral financial institutions, governments, commercial banks and bondholders.

(1.4) Renegotiations with multilateral institutions are often conducted in an *ad hoc* manner. Renegotiations with governments who are members of the Paris Club are conducted through the Club's processes. The Paris Club is an informal group of official creditors with 19 permanent members and a small secretariat in Paris. It functions as such since the 1950s. Countries that are not members of the Paris Club renegotiate with the sovereign debtor on an *ad hoc* basis. Renegotiations with commercial banks are either purely *ad hoc* or conducted through the London Club, an informal group of commercial banks with no fixed membership and no secretariat. The London Club functions in this role since the 1980s. Renegotiations with bondholders are conducted through exchange offers prepared by the sovereign debtor. Occasionally bondholder committees are formed on an *ad hoc* basis to facilitate the negotiation process. Given that the total amount of the debt relief required to recover from a crisis is rather certain, the fact that a particular creditor grants lesser debt relief implies that other creditors must grant more. Against this background, the issue of inter-creditor equity arises.

(1.5) The issue of inter-creditor equity is closely linked with the outcome of sovereign debt restructuring because creditors may not be willing to grant debt relief if they know that other creditors may get paid in full. Importantly, following the issuance of an injunction by a US district court in *NML Capital Ltd. v. Republic of Argentina* in 2012,[1] which prevented Argentina from paying those bondholders who granted debt relief unless the holders of original bonds were to be paid in full, a need has arisen for the introduction of changes in the way presently issues are resolved, i.e. legal reform in the area of inter-creditor equity in sovereign debt restructuring. In April 2013 and September 2014, the International Monetary Fund ("IMF") published several proposals to strengthen the current contractual framework to address collective action problems in sovereign debt restructuring. In September 2014, the United Nations ("UN") General Assembly went further and passed a resolution to establish a multilateral legal framework for sovereign debt restructuring processes. These reform initiatives are still under way.

(1.6) As listed below, this dissertation consists of three published articles, one forthcoming book chapter and one unpublished article:

1. Question the Unquestionable Beauty of a Collective Proceeding for All Sovereign Debt Claims (peer-reviewed journal *International Insolvency Review* Vol. 22: 85–105 (2013); re-published in *Norton Journal of Bankruptcy Law and Practice* Vol. 22, No. 5: 551- 576 (2013))

2. Policy Implication of Poštová Tribunal's Jurisdiction Over Sovereign Bonds: Bankruptcy Cram-Down and ICSID Arbitration (*Norton Journal of Bankruptcy Law and Practice* Vol. 23, No. 5: 604- 633 (2014))

1 See *NML Capital, Ltd. v. Republic of Argentina*, No. 12-105-(L) (2d Cir. 26 Oct. 2012); *NML Capital, Ltd. v. Republic of Argentina*, 08 Civ. 6978 (TPG), 09 Civ. 1707 (TPG), 09 Civ. 1708 (TPG) (S.D.N.Y., 21 Nov. 2012).

3. New IMF Initiative Revives Old Inter-Creditor Issues (peer-reviewed journal *Tijdschrift voor Insolventierecht* Vol. 19, No. 5: 177- 186 (2013))

4. The Missing Element of a Single Limb Voting Procedure: Fair and Equitable Treatment Standard in Sovereign Debt Restructuring (*Forthcoming* book chapter in: R. Hoffmann (eds.), International Investment Law and the Global Financial Architecture, Elgar Publishing 2015)

5. Settlement of Sovereign Debt Disputes: the Present State of Law and Perspectives of Further Development (unpublished)

(1.7) I chose the format of articles (instead of monograph) for my dissertation because it allows me to publish work at an early stage of my Ph.D study. I started this research on sovereign debt restructuring in 2012, i.e. the year in which Greece initiated the debt restructuring process with its private creditors. In response to the Greek crisis, the United Nations General Assembly, the International Monetary Fund, the International Capital Market Association have proposed various possible solutions to improve the current market practice or the existing legal framework. Thanks to this article format, I was able to publish some contemporaneous comments on these initiatives, which attracted invitations to speak at conferences on this topic. Another reason for choosing this article format is because it allows the Ph.D process to be divided into manageable units, thereby reducing the likelihood of losing control of the research. It allows me to easily manage my research and gain some work experience in the meantime.

(1.8) One key disadvantage of the article format is that dissertations consisting of articles develop less often into a standard work on a particular topic than monograph dissertations. The structure of dissertations consisting of articles is often not so clear and the logic between each article is not so obvious. Within my research I have been confronted with many complex and continuously changing issues related to sovereign debt restructuring. Well-known cases such as debt restructuring of Russia, Ecuador, Argentina and Greece are the cradle of many other questions that I have not touched upon in my dissertation, such as – within the context of inter-creditor equity in sovereign debt restructuring –the priority status of new financing, the nature of different types of commercial debt, the *de facto* preferred creditor status of multilateral lenders, and so on. I have also avoided discussions concerning the political aspects of sovereign debt restructuring. The selection I have made focuses on the core issues regarding inter-creditor equity in the context of domestic insolvency law. It is largely inspired by international news coverage on the legal reform of sovereign debt restructuring in the past three years and is in itself enough to demonstrate the different aspects of sovereign debt restructuring.

(1.9) It is worth clarifying that in this dissertation all articles that have been published or accepted for publication are kept the same way as they appear in the journals. To assist the readers, I have added a Table of Legislation, Table of Cases and Bibliography (i.e. books, consultation documents, journal articles etc) at the end of this dissertation. I have not included the news items I cited in each chapter. In this dissertation, the term 'privately held bonds' means sovereign bonds held by private creditors.

(1.10) This dissertation employs descriptive and evaluative analysis. Descriptive analysis is used in connection with the principles on inter-creditor issues in proposals for reform, the fundamental principles of domestic insolvency law for consumers, companies and municipalities[2] as well as the case law from US bankruptcy courts regarding financially distressed municipalities. Evaluative analysis is used to assess the desirability of the introduction of the above-mentioned principles to sovereign debt restructuring processes.

Research question

(1.11) All articles in this dissertation concern the central research question, which is

> *How to design a multilateral legal framework for sovereign debt restructuring that ensures inter-creditor equity.*

(1.12) This research question is divided into the following six sub-questions:

1) Whether a collective proceeding for all claims is desirable for sovereign debt restructuring;
2) How to protect the interest of minority bondholders in respect of the approval of a debt adjustment plan;
3) Whether claims in a pre-default context should be treated as accelerated for voting purposes through the operation of one-tier aggregated collective action clauses ("CACs");
4) How to design rules regarding the ranking between government creditors and private creditors;

2 The fundamental principles of domestic insolvency law discussed in this dissertation are mainly those addressed in the UNCITRAL Legislative Guide on Insolvency Law (2004). Also see generally B. Wessels, 'Insolvency Law', in: Jan M. Smits (ed.), Elgar Encyclopedia of Comparative Law, 2nd ed., Edgar Elgar, Cheltenham, UK – Northampton, MA, USA London, 2012, pp. 383-407; I. Fletcher, The Law of Insolvency (Sweet & Maxwell, 2009) and T. Jackson, The Logic and Limits of Bankruptcy Law (Harvard 1986).

5) Whether investment arbitration could serve as an appropriate forum to develop a safeguard provision for CACs with a single-limb voting procedure; and
6) What is the most desirable mechanism for the settlement of sovereign debt disputes concerning inter-creditor equity?

(1.13) In the context of domestic insolvency law for consumers, companies and municipalities, inter-creditor equity is ensured through a collective proceeding in which all creditors get paid in a certain order of priority (liquidation) or get paid in accordance with a plan of debt adjustment approved by a majority of creditors (reorganization). Sub-questions (1) and (2) search for a solution to ensure inter-creditor equity in the sovereign debt context. In light of the recent reform proposals put forward by the IMF and the UN, this dissertation also provides extensive contemporaneous comments on issues regarding inter-creditor equity in these proposals. Within the framework of the central research question, sub-question (3) discusses whether claims in a pre-default context should be treated as accelerated for voting purposes through the operation of one-tier aggregated collective action clauses. Sub-question (4) deals with how to design rules regarding the ranking between government creditors and private creditors. Sub-question (5) investigates whether investment arbitration could serve as an appropriate forum to develop a safeguard provision for CACs with a single-limb voting procedure. Sub-question (6) explores the most desirable mechanism for the settlement of sovereign debt disputes concerning inter-creditor equity. It is worth noting that the titles of these chapters reflect the titles of original articles that have been published in law journals and books.

Summary of research

(1.14) Chapter 2, entitled "*Question the Unquestionable Beauty of a Collective Proceeding for All Sovereign Debt Claims*," discusses inter-creditor equity and the establishment of a legal framework for sovereign debt restructuring in a general context without distinguishing the type of creditors. It begins with a description of various reform proposals addressing the relationship between multilateral, bilateral and commercial creditors and the different views expressed in these proposals, ranging from equal treatment to separate treatment to comparable treatment. While studying and analyzing these different views, I noticed that nearly all proposals envisage a "collective" proceeding that would include "all" sovereign debt claims without explaining any reasons for such a vision, partly because this is the form that all national bankruptcy proceedings take. I adopted a critical approach and questioned the application of the fundamental theory of collectivity in bankruptcy law to the context of financially distressed sovereign States. I discussed the issue of collectivity from two distinctive aspects: (1) the desirability of a collective proceeding, and (2) the inclusion of all claims in sovereign debt restructuring.

(1.15) In assessing the desirability of a collective proceeding, I explained that the need for a collective proceeding in national bankruptcy law is justified by two main theories – the common pool problem and the creditors' bargain theory. The common pool problem refers to the situation in which self-interested creditors have every incentive to collect as many of the debtor's assets as quickly as they can, because the creditors who are first to collect suffer none of the deleterious effects of their collection actions. Thus, the creditors' pursuit of their collection remedies is viewed as analogous to the overfishing of a common pool. According to the creditor's bargain theory, a collective proceeding is only desirable when it is in the best interests of both unsecured and secured creditors, and that secured creditors would only agree to be included in the same proceeding as unsecured creditors if their rights are well preserved through priority rules.

(1.16) With respect to the inclusion of "all" claims, I identified the scope of creditors affected by inter-creditor equity by discussing the "temporary" nature of the sovereign debt crisis and the "alive" feature of the limited pool of sovereign assets. I observed that where the pool of assets is constantly replenished, the issue of inter-creditor equity does not concern all creditors because the fact that certain creditors grant lesser debt relief does not necessarily require other creditors to grant more. I also discussed the reasons for non-applicability of the automatic acceleration principle in national bankruptcy law in the sovereign debt context through its analysis of the non-liquidable nature of sovereign debtors and the legislative motivation for the adoption of the automatic acceleration principle for municipal debtors in US Chapter 9 on municipality bankruptcy.

(1.17) Chapter 3 "*Policy Implication of Poštová Tribunal's Jurisdiction Over Sovereign Bonds: Bankruptcy Cram-Down and ICSID Arbitration*" focuses on the issue of inter-creditor equity in the context of sovereign bond restructuring. Given the significant number of bondholders involved in each restructuring, it is virtually impossible for the sovereign debtor to engage in direct negotiation with each individual bondholder. In practice, sovereign bond restructurings are conducted through exchange offers or amendments of the original contract terms. Under the exchange offer approach, the sovereign debtor invites bondholders to exchange their bonds for new bonds of lesser value. With respect to the amendment of the original contract terms, collective action clauses have been introduced into sovereign bond documentation to facilitate the process. CACs could enable a qualified majority of bondholders to bind all holders of the same bond issuance to a change of the contract terms, including a change to the maturity date as well as to the amount of interest and principal.

(1.18) Following the Greek debt restructuring, *Poštová* Banka A.S. (a Slovak entity) and its shareholder Istrokapital S.E. (a Cypriot entity) initiated arbitration against Greece in May 2013 at the International Centre for Settlement of Investment Disputes, pursuant to the bilateral investment treaties concluded between Greece and Slovakia as well as Greece and Cyprus. The claimants contend that they purchased Greek bonds in 2010 and were forced to exchange their bonds for new securities of substantially lesser value. They allege that the forcible bond exchange was carried out through the newly adopted Greek Bondholder Act that retroactively and unilaterally amended the bond terms by inserting a CAC into outstanding Greek-law bonds. According to the claimants, the CAC allows the imposition of new terms upon bondholders against their consent if a supermajority of other bondholders consent. This case is currently pending.

(1.19) In this chapter I demonstrated that what the Greek Bondholder Act introduced was not an ordinary CAC but something similar to cram-down procedures in national insolvency law. Notably, the Act enables a qualified majority of bondholders to bind all holders of the affected domestic debt to the restructured terms even where the needed majority of creditors for the restructuring would not be attained within a single bond issue. Put differently, the Act eliminates the power of a creditor or a group of creditors to obtain a blocking position in an individual issuance. As a result, I argued that the Act shares some elements of the cram-down procedure in US Chapter 9 on municipality bankruptcy, under which an impaired class could be forced to accept a proposed plan. However, I also pointed out that the elimination of the power of a creditor to obtain a blocking position in an individual issuance would only resemble the craw-down procedure if claims of an individual issuance differ from that of other issuances so that they constitute a particular class by themselves.

(1.20) Then I provided a detailed description of the safeguard provision for the cram-down procedure in US Chapter 9 on municipality bankruptcy. Such a provision prohibits unfair discrimination against each impaired dissent creditor class and also incorporates the fair and equitable treatment principle. To quote the language of that provision, the court shall confirm the plan under the cram down procedure "if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan." With the safeguard provision in mind, I noted that foreign investors are entitled to initiate arbitration under most investment treaties against the host country directly for alleged breaches of treaty obligations through arbitration clauses, which often include fair and equitable treatment principle. The principle of fair and equitable treatment in this context has been interpreted by arbitral tribunals as covering two notions that are similar to the safeguard provision under municipality bankruptcy law: (a) prohibition of unfair discrimination, and (b) legitimate expectations and the obligation of proportionality.

(1.21) Chapter 4 "*New IMF Initiative Revives Old Inter-Creditor Issues*" provides extensive comments on the IMF's staff paper on "Sovereign Debt Restructuring – Recent Developments and Implications for the Fund's Legal and Policy Framework" dated 26 April 2013. The staff paper was prepared in response to recent debt restructurings, including the largest restructuring in history in Greece, as well as ongoing litigations brought by Argentine bondholders. It does not provide concrete reform proposals, but identifies four issues to be studied further through follow-up staff papers: (1) the staff's observation that debt restructurings have often been too little and too late; (2) the collective action problem in sovereign debt restructurings, especially in pre-default contexts; (3) the growing role and changing composition of official lending that call for a clearer framework for official sector involvement; and (4) the IMF's lending into arrears policy that the collaborative, good faith approach should be adopted to resolve external private arrears.

(1.22) In this chapter I discussed inter-creditor equity in relation to the second and third issues. The second issue concerns the collective action problem in sovereign debt restructuring, especially in pre-default contexts. The collective action problem refers to the situation in which creditors will become less willing to accept the restructuring offer when other creditors may be able to recover their claims in full, even though it would be in the collective best interest of all creditors to agree to a restructuring as soon as possible. In essence, it is a problem that arises out of the concern of inter-creditor equity. According to the staff paper, there is merit in designing a more robust form of aggregated CACs for international sovereign bonds to overcome this collective action problem. The paper notes that only four countries have included aggregation clauses in their sovereign bonds to date – Argentina, the Dominican Republic, Greece and Uruguay. These aggregation clauses contain a two-tier voting system: (1) 75 (Greece) or 85 (Argentina, the Dominican Republic and Uruguay) percent of the aggregated outstanding principal of all series to be affected, and (2) 66⅔ percent of the outstanding principal of each individual series to be affected. However, the paper emphasizes that the two-tier aggregation clauses have limitations. For instance, it still enables a creditor or a group of creditors to obtain a blocking position in a particular issue. In order to address this limitation, the paper suggests that the two-tier voting thresholds in the existing aggregation clauses could be replaced with one-tier voting threshold, which disallows blocking minorities in single bond series.

(1.23) An aggregation clause with one-tier voting threshold that disallows blocking minorities in single bond series, in my view, may present the risk of discriminating minorities with different maturities by empowering majorities to impose an agreement on minorities in a pre-default context. For instance, creditors holding long-term maturity bonds may impose an unfavorable treatment on creditors with short-term maturity bonds, and vice versa. This problem does not exist in a post-default context, because all claims will be accelerated and considered to have the same maturity, i.e., all due and payable.

(1.24) The third issue in the staff paper relates to the growing role and changing composition of official lending that call for a clearer framework for official sector involvement. In this respect, I found the IMF's position on the issue of inter-creditor equity self-contradictory. On the one hand, the IMF maintains that the debtor and creditors should have the freedom to negotiate the debt restructuring strategy, thereby assuming that debt negotiation is a matter that concerns only the debtor and creditor(s) in the negotiation, but not other creditors outside the negotiation. On the other hand, the IMF is worried about the growing number of creditors that are non-Paris Club members as well as the uneven debt negotiation practices across country cases, which indicates its concern for inter-creditor equity. In my view, this self-contradictory position is explained by the fact that the IMF is a multilateral lender itself. Against this background, I discussed how rules regarding the ranking between official bilateral creditors and private creditors should be developed.

(1.25) Chapter 5, entitled "*The Missing Element of a Single Limb Voting Procedure: Fair and Equitable Treatment Standard in Sovereign Debt Restructuring*," criticizes the recent reform initiative advocated by the IMF in its paper on "Strengthening the Contractual Framework to Address Collective Action Problems in Sovereign Debt Restructuring" dated 2 September 2014. The staff paper suggests a few contractual reforms designed to tackle collective action problems so as to achieve orderly sovereign debt restructurings. Among other things, the paper advocates in favor of a single CAC with a menu of voting procedures, including (1) a series-by-series voting procedure, (2) a two-limb aggregated voting procedure, and (3) a single-limb voting procedure with the possibility for sub-aggregation. Given that the CAC's function is to enable a qualified majority of bondholders to bind all holders of the same series to an amendment of the bond terms, different voting procedures permit different levels of influence that minority bondholders could potentially exercise over the restructuring process. Under options (1) and (2), for example, a creditor or a group of creditors could obtain a blocking position in a particular series and effectively prevent the operation of CAC in that series. By contrast, a single-limb voting procedure in option (3) will enable contract terms to be amended on the basis of a single vote across all affected instruments, thereby limiting the ability of holdout creditors to undermine the restructuring process. As explained in the staff paper, the success of the newly adopted Greek Bondholder Act in the 2012 debt restructuring prompted the introduction of this single-limb voting procedure.

(1.26) In this chapter I analyzed the nature of the single-limb voting procedure and emphasized its resemblance to cram-down procedures in bankruptcy law. Whereas the cram-down procedure in the US municipality bankruptcy contains a safeguard provision which ensures minimum protection for each impaired dissent creditor class through the prohibition of unfair discrimination and through the inclusion of the fair and equitable treatment principle, the single-limb voting procedure is silent about creditor protection in this context. In searching for a safeguard provision for the single-limb voting procedure, I discovered the similarities between the safeguard provision for cram-down procedures and the fair and equitable treatment principle under investment treaties. I also noted that not all sovereign debt claims could be brought to investment treaty tribunals. While a mere breach by a state of a contract with foreign investors does not violate international law, a sovereign act of a State contrary to such a contract may do so. Hence, arguably claims concerning the enactment of the Greek Bondholder Act may be brought before investment treaty tribunals, but not claims arising out of the contractual operation of CACs with a single-limb voting procedure in sovereign bonds.

(1.27) Chapter 6 on "*Settlement of Sovereign Debt Disputes: the Present State of Law and Perspectives of Further Development*" explores the issue concerning the search for an appropriate forum to apply the safeguard provision identified in Chapter 5 in a broader context. This chapter was prepared after the adoption of the UN Resolution "Towards the establishment of a multilateral legal framework for sovereign debt restructuring processes" on 9 September 2014. This resolution decides to elaborate and adopt a multilateral legal framework for sovereign debt restructuring processes with a view to increasing the efficiency, stability and predictability of the international financial system and achieving sustained, inclusive and equitable economic growth and sustainable development.

(1.28) In this chapter I described the *status quo* of the settlement of sovereign debt disputes, including cases at domestic courts filed under the dispute resolution clauses in bonds or loan contracts as well as cases before investment arbitration tribunals initiated pursuant to investment treaties. Having analysed the *status quo*, I pointed out that judges in domestic courts do not address the concept of insolvency of a sovereign State. These judges would not be able to analyze the key issue of how much should creditors get paid if not the full amount, because the contract law applicable to a particular dispute does not contain similar principles as bankruptcy law. With respect to claims arising out of *pari passu* clauses, judges interpret these clauses on the basis of their wording. Most *pari passu* clauses provide that bonds of that particular issue shall rank equally among themselves. Some also state that the debtor's payment obligation under that particular issue shall rank equally with all other existing and future unsubordinated and unsecured external indebtedness. These judges would not analyze the nature of debt giving rise to the claims and determine whether these claims should receive equal treatment as bankruptcy judges do. Furthermore, I discussed the jurisdiction of investment treaty tribunals and emphasized that arbitral tribunals established under investment treaties have no jurisdiction where the claim at stake is a pure contract claim, as opposed to a claim that allegedly breaches the obligations specified in investment treaties. A claim is not viewed as a pure contract claim where the circumstances and/or the behavior of the host State appear to derive from its exercise of sovereign State power.

(1.29) With the aim to explore the perspective of further development in the field of settlement of sovereign debt disputes, a comparison is made between the characteristics of mediation, arbitration and adjudication, and then assesses the applicability of these methods to disputes arising from sovereign debt matters. In respect of mediation, I presented the only example of sovereign debt mediation involving Argentina. I also discussed several examples of municipal debt mediation in the US involving cities such as Stockton and Detroit. Then follows a summary of a couple of academic proposals in favor of the establishment of an arbitral tribunal for sovereign debt disputes. I also offered examples of the Tribunal concerning the Bank for International Settlements and the Iran-US Claims Tribunal. As regards sovereign debt adjudication, which refers to an international insolvency court for sovereign States. After recounting the attempts made by the IMF from 2001 to 2003 to establish a treaty-based framework to restructure sovereign debt – the Sovereign Debt Restructuring Mechanism, I provided an overview of the International Tribunal for the Law of the Sea as a recent example of newly established specialized tribunals. In this chapter the question of whether it would be advisable to follow the development in the field of the law of the sea by establishing a specialized international insolvency tribunal to settle sovereign debt disputes is also assessed.

Conclusions

(1.30) Having introduced the chapters which contain a description and evaluation of my research question, I now formulate the responses to the central question and the sub-questions set out at the beginning of the introduction of my research. For ease of reference, these questions are:

1) Whether a collective proceeding for all claims is desirable for sovereign debt restructuring;
2) How to protect the interest of minority bondholders in respect of the approval of a debt adjustment plan;
3) Whether claims in a pre-default context should be treated as accelerated for voting purposes through the operation of one-tier aggregated collective action clauses ("CACs");

4) How to design rules regarding the ranking between government creditors and private creditors;
5) Whether investment arbitration could serve as an appropriate forum to develop a safeguard provision for CACs with a single-limb voting procedure; and
6) What is the most desirable mechanism for the settlement of sovereign debt disputes concerning inter-creditor equity?

(1.31) My response to sub-question (1) is that the principle of collectivity in bankruptcy law should not apply to the sovereign debt context. I discussed in Chapter 2 the issue of collectivity from two distinctive aspects: (1) the desirability of a collective proceeding, and (2) the inclusion of all claims in sovereign debt restructuring. In assessing the desirability of a collective proceeding, reference was made to the two main theories that justify the need for a collective proceeding in national bankruptcy law – the common pool problem and the creditors' bargain theory. Relying on the empirical data concerning the number of instances of litigation against sovereign debtors in the US and UK courts between 1976 and 2010, I argued that a small number of individual actions that may diminish the debtor's pool of assets couldn't be compared with the overfishing situation in a common pool. Given the incomparably different nature of multilateral/bilateral claims, I found it impossible to weigh political and financial considerations and to devise a priority order between multilateral/bilateral claims and commercial claims. Based on the creditors' bargain theory, the suggestion has been made that multilateral/bilateral claims and commercial claims should not be included in a collective proceeding. Furthermore, in my view the conflict of interest among creditors exists only during the temporary period when there are not enough assets for everyone. Thus, I advised against the inclusion of all claims in sovereign debt restructuring.

(1.32) Chapter 3 responds to sub-question (2) of how to protect the interest of minority bondholders in respect of the approval of a debt adjustment plan. In the context of the Greek debt restructuring, I found that the Greek Bondholder Act shares some elements of the cram-down procedure in US Chapter 9 on municipality bankruptcy. Given that the Act would only resemble the craw-down procedure if claims of an individual issuance differ from that of other issuances so that they constitute a particular class by themselves, I looked into the UNCITRAL Legislative Guide on Insolvency Law for guidance. The Legislative Guide provides that ordinary unsecured creditors can be divided into different classes based upon the different nature of debts giving rise to the claims. To apply this criterion to the Greek debt restructuring, it is my argumentation that the nature of an individual issuance differs from that of other issuances with different maturities. Due to different residual maturities involved, the same restructuring term extended to all bondholders implies large differences in the present value haircut across the existing bonds. Therefore, in my view, the Act functions in the same way as the cram-down procedure in US Chapter 9 on municipality bankruptcy. In light of the similarities between the safeguard provision for the cram-down in municipality bankruptcy and the fair and equitable treatment principle under investment treaties, I advocated that investment arbitration is an appropriate forum to develop a safeguard provision for cram-downs in the context of sovereign debt restructuring.

(1.33) In respect of sub-question (3), I considered it inappropriate to treat claims in a pre-default context as accelerated for voting purposes in the context of one-tier aggregated CACs. Unlike the pre-pack arrangements in the non-sovereign context, it is explained in Chapter 4 that unsecured creditors holding sovereign bonds may have less incentive to voluntarily agree on the acceleration of their claims, simply because the likelihood of a general default and insolvency in the sovereign debt context is comparatively small. Given that sovereign debtors can raise revenue through taxation, the pool of assets, although limited, is not still but alive. In addition, States can never be liquidated, thus rendering sovereign debt crisis merely temporary. When the debt crisis is over in a few years, the sovereign debtor will again be able to repay everyone. Therefore, I suggested that claims in a pre-default context should not be treated as accelerated for voting purposes through the operation of one-tier aggregated CACs.

(1.34) Chapter 4 also addresses sub-question (4) of how to design rules regarding the ranking between government creditors and private creditors. In my view, such rules should be developed in a realistic way. As it is impossible to weigh political considerations, the differences between official creditors and private creditors are simply non-comparable. As a result, I advocated in favor of the separate treatment of official and private creditors as well as a general rule that does not specify details of separate treatment, but simply requires all creditors to take a loss in order to contribute to the recovery of debt crisis. It should be emphasized that in my view not all creditors do need to be treated equally, but in a manner that reflects the different bargains they have struck with the debtor.

(1.35) My response to sub-question (5) of whether investment arbitration could serve as an appropriate forum to develop a safeguard provision for CACs with a single-limb voting procedure is provided in Chapter 5. I advocated in favor of a safeguard procedure to ensure that any amendment of the contract terms imposed by majority bondholders in the context of the single-limb voting procedure is fair and equitable with respect to minority bondholders who have voted against the amendment. My conclusion is that investment arbitration could serve as an appropriate forum to develop a safeguard provision for the single-limb voting procedure but not as an appropriate forum to apply the safeguard provision once developed, because not all sovereign debt claims can be filed before investment treaty tribunals. In my view, the search for an appropriate forum to apply the safeguard provision constitutes an entirely different issue and merits careful consideration and discussion elsewhere.

(1.36) Chapter 6 answers sub-question (6) regarding the most desirable mechanism for the settlement of those sovereign debt disputes that cannot be filed before investment treaty tribunals. I noted that one key shortcoming of mediation is that it has no set procedure and could in theory continue indefinitely if the parties refuse to compromise. This is particularly unfavorable for disputes arising out of sovereign debt restructurings, because a delay in the resolution of the disputes could have serious impact on the debtor country's economy. Given that the start-up and operational costs needed for a specialized tribunal will certainly be significantly higher than that necessary for the conduct of an arbitral proceeding, I argued that the benefits a specialized tribunal could bring may not outweigh the costs involved in creating such a tribunal. I concluded that arbitration, preferably modelled after the tribunal concerning the Bank for International Settlements, is the most suitable mechanism for this purpose.

(1.37) As I indicated earlier, the central question of the theme of inter-creditor equity in sovereign debt restructuring – How to design a multilateral legal framework for sovereign debt restructuring that ensures inter-creditor equity – is answered through sub-questions (1)-(6). In short, I argued that a multilateral legal framework for sovereign debt restructuring should not take the form of a collective proceeding and should not include claims with all kinds of maturities. In the context of a cram-down procedure, a safeguard procedure should be favored to ensure that any amendment of the contract terms imposed by majority bondholders is fair and equitable with respect to minority bondholders who have voted against the amendment. In my view, investment arbitration could serve as an appropriate forum to develop such a safeguard provision. A new arbitral tribunal, preferably modelled after the tribunal concerning the Bank for International Settlements, could apply the safeguard provision once developed, because not all sovereign debt claims can be filed before investment treaty tribunals.

(1.38) With respect to the meaning of 'fair and equitable', Chapter 3 discusses in detail how US bankruptcy courts and international investment tribunals interpret this term. In the context of municipality bankruptcy in the US, the term 'fair and equitable' requires that the amount to be received by dissenting creditors under a plan is "all that they can reasonably expect in the circumstances'. Similarly, the fair and equitable principle in the context of investment treaties refers to the concept of legitimate expectations and the obligation of proportionality.

(1.39) These results reflect significantly different theoretical underpinnings and solutions of which I feel that they may influence future research and global theoretical debate as well as may serve as clear arguments for concrete answers in (global) practice. In this way it is hoped that my study provides useful material to contribute to the establishment of a more predictable and structural multilateral legal framework for inter-creditor equity in sovereign debt restructuring.

2 Question the Unquestionable Beauty of A Collective Proceeding for All Sovereign Debt Claims[1]

2.1 Introduction

(2.1) Despite the efforts to reform the sovereign debt restructuring process undertaken by the International Monetary Fund ("IMF") in 2003, the restructuring practice is currently facing new challenges. In early 2012, both EU member States and the European Central Bank ("ECB") managed to claim priority status unilaterally in the middle of the current Eurozone crisis. In October 2012, a US court in *NML Capital Ltd. v. Republic of Argentina* granted injunctions in relation to Argentina's breach of the *pari passu* clause, which provides that the payment obligation of the debtor under that particular bond issue shall rank equally with all other existing and future unsubordinated and unsecured external indebtedness. How would the sovereign debt community react to these events? To date, nearly all literature on sovereign debt issues has focused on deterring holdout behavior in foreign bonds restructuring, from a majority voting system to a stay on enforcement.[2] However, these new challenges are likely to shift the attention from holdout behavior to inter-creditor relations,

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1 This chapter was prepared for the Annual Meeting of the Academic Forum of INSOL International (18-19 May 2013). It has been published in *International Insolvency Review* Vol. 22: 85–105 (2013) and re-published in *Norton Journal of Bankruptcy Law and Practice* Vol. 22, No. 5: 551- 576 (2013). The author is very grateful to Professor Bob Wessels, Professor Mitu Gulati and Professor Rolef de Weijs for their helpful comments on an earlier draft.

2 L. Buchheit at al., "The Problem of Holdout Creditors in Eurozone Sovereign Debt Restructurings" (Jan. 2013), available at http://ssrn.com/abstract=2205704 (last viewed 11 Mar. 2013); W. Weidemaier & M. Gulati, "A People's History of Collective Action Clauses" (Nov. 2012), available at http://ssrn.com/abstract=2172302 (last viewed 11 Mar. 2013); S. Hagan, "Designing a Legal Framework to Restructure Sovereign Debt", 36 Geo. J. Int'l L. 299 (2005); J. Eaton, Chapter 15 "Standstills and an International Bankruptcy Court", in: Fixing Financial Crises in the 21st Century (2004); S. Schwarcz, "Idiot's Guide" to Sovereign Debt Restructuring, 53 Emory Law Journal (2004) pp. 1189-1218; IMF, "The Design of the Sovereign Debt Restructuring Mechanism-Further Considerations", prepared by the Legal and Policy Department and Review Departments (Nov. 2002); K. Rogoff & J. Zettelmeyer, "Early Ideas on Sovereign Bankruptcy Reorganization: A Survey", IMF WP02/57 (Mar. 2002); J. Sachs, "Do We Need an International Lender of Last Resort?" Frank D. Graham Lecture at Princeton University, Vol. 8 (Apr. 1995), available at h*ttp://www.earth.columbia.edu/sitefiles/file/about/director/pubs/intllr.pdf* (last viewed 11 Mar. 2013).

which is considered to be one of the key elements of an effective insolvency law.[3]

(2.2) Unfortunately only very few scholars have so far discussed inter-creditors issues in a detailed fashion. Buchheit, Gelpern and Wood provide an excellent overview of contractual provisions in sovereign debt instruments that serve the purpose of ensuring equal treatment within certain groups of creditors (i.e. Paris Club members, commercial banks, bondholders).[4] Wood studies the priority ladder in national bankruptcy law and reveals an existing *de facto* priority ladder in the sovereign debt context, which follows the order of super-priority claims such as set-off, security interests and trusts, priority claims such as IMF loans, and *pari passu* claims.[5] The *status quo*, however, presents an ambiguous picture of inter-creditor relations and leaves a number of issues wide open such as the scope of priority claims, the relationship between multilateral, bilateral and commercial creditors, and the status of new financing. The need to develop substantive legal principles in this context has recently been emphasized by the Dutch government and the Permanent Court of Arbitration ("PCA")[6] in their project on "Sovereign Debt and Arbitration".[7]

3 Key objectives of an effective and efficient insolvency law specified by the United Nations Commission on International Trade Law ("UNCITRAL") Legislative Guide on Insolvency Law include the recognition of existing creditor rights and the establishment of clear rules for ranking of priority claims, and the equitable treatment of similarly situated creditors. See UNCITRAL Legislative Guide on Insolvency Law (2004), available at http://www.uncitral.org/pdf/english/texts/insolven/05-80722_Ebook.pdf (last viewed 11 Mar. 2013), at 11-13.

4 L. Buchheit, "The Search for Intercreditor Parity", 8 L. & Bus. Rev. Am. 73 (2002); A. Gelpern, "Building a Better Seating Chart for Sovereign Restructurings", Emory L. J. 53 (2004); P. Wood, "Sovereign insolvency: the bankruptcy ladder of priorities and the pari passu clause", Tijdschrift voor Financieel Recht (Mar. 2012).

5 P. Wood, "Sovereign insolvency: the bankruptcy ladder of priorities and the pari passu clause", *supra* note 4, at 64.

6 Established by the 1899 and 1907 Conventions for the Pacific Settlement of International Disputes, the PCA is an intergovernmental organization that works to facilitate the resolution of international disputes through arbitration and other processes.

7 Since 2000, several non-governmental organizations ("NGOs") focused on sovereign debt matters have actively advocated for the establishment of an arbitral tribunal for sovereign debt matters, which would function as an international insolvency court. See Jubilee, "Chapter 9/11? Resolving international debt crises – the Jubilee Framework for international insolvency", Jan. 2002, available at http://probeinternational.org/library/wp-content/uploads/2011/02/9-11.pdf (last viewed 7 Jan. 2013); Erlassjahr, "Resolving Sovereign Debt Crises – Towards a Fair and Transparent International Insolvency Framework", Sep. 2010, available at http://www.erlassjahr.de/english/towards-an-international-insolvency-framework.html (last viewed 7 Jan. 2013), and AFRODAD, "Fair and Transparent Arbitration on Debt", 2002, available at http://www.afrodad.org/Publications/FTA/fta%20issues%20paper%202002.pdf (last viewed 7 Jan. 2013). In response to their proposals, the Netherlands government invited the PCA to initiate a project to promote and facilitate the settlement of disputes arising out of international loan agreements. The interim conclusion of this project also refers to the need to develop substantive legal principles in this respect. See

(2.3) Having acknowledged the challenges involved in discussing all open issues about inter-creditor relations at once, the author intends, in this paper, to focus on the relationship between multilateral, bilateral and commercial creditors. The author starts with various proposals touching upon this issue and the different views expressed, ranging from equal treatment to separate treatment to comparable treatment. While studying these different views, the author notices that nearly all proposals envisage a "collective" proceeding that would include "all" sovereign debt claims without explaining any reasons for such a vision, partly because this is the form that all national bankruptcy proceedings take.[8] The main purpose of this paper is to take the unusual route of questioning the unquestionable beauty of a collective proceeding for all sovereign debt claims.

(2.4) This paper is structured as follows: Part II provides an introduction to the context and new developments in sovereign debt restructurings. Part III analyses inter-creditor issues in sovereign debt restructurings with a focus on the concept and *status quo*. In exploring solutions to inter-creditor issues, Part IV starts with a summary of the existing proposals relating to inter-creditor issues and moves on to discuss the appropriateness of a collective proceeding for all claims. First, the author argues that the automatic acceleration principle in national bankruptcy law should not apply to the sovereign debt context because of the "temporary" nature of the sovereign debt crisis, the "alive" feature of the limited pool of sovereign assets and the "non-liquidable" fact of the sovereign debtor. Second, the author argues that a collective proceeding is not the most desirable form of proceeding due to the absence of the common pool problem in the context of sovereign debt and the incomparably different natures of multilateral/bilateral claims that renders the design of a priority order between multilateral/bilateral claims and commercial claims impossible. Part V concludes this paper.

"Arbitration and Sovereign Debt", Paper prepared by the Steering Committee of the Netherlands Government and the Permanent Court of Arbitration, Jul. 11, 2012, at para. 2, available at http://www.slettgjelda.no/filestore/ArbitrationandSovereignDebt.pdf (last viewed 7 Jan. 2013).

8 C. Paulus, "A Resolvency Proceeding for Defaulting Sovereigns", IILR 2012; A. Dickerson, "A Politically Viable Approach to Sovereign Debt Restructuring", 53 Emory L. J. (2004), pp.997-1041; K. Berensmann & F. Schroeder, "A proposal for a new international debt framework (IDF) for the prevention and resolution of debt crisis in middle-income countries", Discussion Paper 2/2006; Erlassjahr, "Resolving Sovereign Debt Crises – Towards a Fair and Transparent International Insolvency Framework", Sep. 2010, available at http://www.erlassjahr.de/english/towards-an-international-insolvency-framework.html (last viewed 7 Jan. 2013); P. Bolton & D. Skeel, "Inside the Black Box: How should a Sovereign Bankruptcy Framework be Structured?", Emory L. J. 53. 763 (2004); S. Schwarcz, "Idiot's Guide" to Sovereign Debt Restructuring, 53 Emory L. J. (2004) pp. 1189-1218.

2.2 SOVEREIGN DEBT RESTRUCTURINGS

2.2.1 The Context

(2.5) The current practice of sovereign lending and borrowing is unprecedented. For two centuries, sovereign debtors borrowed from one or more, but not all, of the following sources: commercial banks, bondholders, governments and multilateral institutions. It was not until the early 1990s that all four types of creditors began to play an active role in the sovereign debt market.[9] While commercial banks and bondholders form the "private sector" creditor group, the "public sector" creditor group is composed of governments ("bilateral creditors") and multilateral institutions such as the IMF, the World Bank and other regional banks (collectively, "multilateral creditors").

(2.6) With debt comes the possibility of default, and sovereigns are no exception to this axiom. At present, there is no international insolvency regime governing sovereign debt defaults, comprised of rules designed to cope with the scenario in which creditors cannot be fully satisfied. Instead, sovereign debt defaults are dealt with using an *ad hoc*, individual case-by-case approach in which most rules are invented along the way. In practice, in order to avoid an eternal default, the sovereign debtor is compelled to seek debt relief from creditors before or shortly after the eve of default, via an extension of maturity, and/or a reduction of the value of the claim. Such relief is obtained by renegotiating the relevant debt instruments with individual creditors. The rationale for renegotiation is that all participants in the sovereign borrowing and lending activities, both debtor and creditors, should share the risk of insolvency.

(2.7) Renegotiations with multilateral creditors are often conducted in this *ad hoc* manner. Renegotiations with bilateral creditors who are members of

9 Following the first issuance of international bonds by Barings in 1817, bonds were the primary means of international long-term lending to States for more than 100 years until the 1930s. Bank lending was often limited to the form of short-term trade financing or interbank credit lines. The Great Depression in the 1930s shut down the bond market. At that time, States began to lend money to one another through loans, grants, and export credits. Since 1944, the IMF, World Bank and many regional development banks have been established to achieve international economic cooperation, and joining the sovereign debt creditor group. Also after the Second World War, long-term borrowing from commercial banks to sovereign States began to grow rapidly, and peaked in the 1970s. A wave of bank loan defaults in the 1980s triggered a new debt crisis, and in the early 1990s, banks agreed to exchange bad loans for Brady bonds. As a result, bond finance, largely dormant for more than sixty years, has again dominated foreign sovereign borrowing. See A. Gelpern and M. Gulati, "Public Symbol in Private Contract: a Case Study", (2006) 84 Wash. U. L. Rev. 1627, at 1632-1633; L. Rieffel, "The Bank Advisory Committee Process", Chapter 6 in Restructuring Sovereign Debt: The Case for Ad Hoc Machinery (2003, Brookings), at 96.

the Paris Club are conducted through the Club's processes. The Paris Club is an informal group of official creditors with 19 permanent members and a small secretariat in Paris.[10] Countries that are not members of the Paris Club renegotiate with the sovereign debtor on an *ad hoc* basis. Renegotiations with commercial banks are either purely *ad hoc* or conducted through the London Club, an informal group of commercial banks with no fixed membership and no secretariat.[11] Renegotiations with bondholders are conducted through exchange offers prepared by the sovereign debtor. Occasionally bondholder committees are formed on an *ad hoc* basis to facilitate the process.[12]

(2.8) From November 2001 through April 2003, the IMF proposed a reform to the contemporary international financial architecture by introducing a treaty-based framework to restructure sovereign debt –the Sovereign Debt Restructuring Mechanism ("SDRM").[13] The key feature of the SDRM is a majority voting system, which binds all creditors to a restructuring agreement that has been accepted by a qualified majority.[14] Whereas this proposal was eventually shelved due to a lack of sufficient support from the IMF member States,[15] the idea of a majority voting system survived. Collective Action Clauses ("CACs"), a contractual approach to implementing a majority voting system, gained broad support from market participants and sovereign debtors.[16]

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10 Paris Club official website, available at http://www.clubdeparis.org/sections/composition/membres-permanents-et/membres-permanents, (last viewed 13 Dec. 2012). See generally E. Cosio-Pascal, "The Emerging of a Multilateral Forum for Debt Restructuring: The Paris Club", UNCTAD/OSG/DP/2008/7, Discussion Papers No. 192, available at http://unctad.org/en/Docs/osgdp20087_en.pdf (last viewed 7 Jan. 2013).

11 L. Rieffel, "The Bank Advisory Committee Process", *supra* note 9, at 103.

12 For a discussion of the use of creditors' committees in the Congo debt restructuring, see M. Richards, "The Republic of Congo's Debt Restructuring: Are Sovereign Creditors Getting Their Voice Back?", (2010) 73 Law & Contemp. Probs 273-299. Creditors' committees were also organized in the Greek debt restructuring, see J. Zettelmeyer, C. Trebesch and M. Gulati, "The Greek Debt Exchange: An Autopsy" (2012), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2144932 (last viewed 13 Dec. 2012).

13 S. Hagan, "Designing a Legal Framework to Restructure Sovereign Debt", *supra* note 2, at 300-301.

14 IMF, "The Design of the Sovereign Debt Restructuring Mechanism-Further Considerations", *supra* note 2, at para. 8.

15 An amendment of the IMF's Articles of Agreement needs the approval of three-fifths of member States, holding eighty-five percent of the total voting power. See Articles of Agreement of the International Monetary Fund, as amended, art. XXVIII(a), available *at* http:// www.imf.org/external/pubs/ft/aa/aa28.htm (last viewed 11 Mar. 2013).

16 In fact, CACs in bonds governed by English law began to appear in 1980s. What the SDRM initiative encouraged was the inclusion of such clauses in bonds governed by New York law and others. Countries such as Mexico, Brazil, Belize, Guatemala, Venezuela, Uruguay were among the first group to include CACs in their New York law bonds. More recently, the Treaty Establishing the European Stability Mechanism ("ESM") also forces the inclusion of CACs, as of 1 January 2013, in all euro-area government securities with maturity above one year. In addition, the model CAC prepared includes an aggregation feature – referred to as cross-series modification – that permits changes to bind more than one series of bonds.

2.2.2 New Developments

(2.9) In October 2012, a US federal appellant court in *NML Capital Ltd. v. Republic of Argentina* affirmed the trial court's decision to issue injunctions designed to remedy Argentina's breach of the *pari passu* clause in certain bonds, which arose from the fact that it had issued new debt pursuant to exchange offers in 2005 and 2010 and was making the required payments on this new debt, but had declared that it would make no payments to those still holding the old bonds.[17] In February 2013, a second arbitral tribunal[18] at the Inter-

See generally Cliffford Chance newsletter, "Euro area member states take collective action to facilitate sovereign debt restructuring", Dec. 2012, available at http://www.cliffordchance.com/publicationviews/publications/2012/12/euro_area_memberstatestakecollectiveactiont.html (last viewed 7 Jan. 2013); M. Bradley & M. Gulati, "Collective Action Clauses for the Eurozone: An Empirical Analysis" (Oct. 2011), available http://ssrn.com/abstract=1948534 (last viewed 11 Mar. 2013); R. Quarles, "Herding cats: collective-action clauses in sovereign debt the genesis of the project to change market practice in 2001 through 2003", Law & Contemp. Probs (Sept. 2010); J. Drage & C. Hovaguimian, "Collective Action Clauses (CACS): an analysis of provisions included in recent sovereign bond issues" (Nov. 2004).

17 The pari passu clause in dispute provided that securities shall at all times rank *pari passu*, and that the Argentina's payment obligations under the bonds shall at all times rank equally at least equally with all its other present and future unsecured and unsubordinated securities. The appellant court explained that the clause protected against two different forms of discrimination: the issuance of other superior debt and the giving of priority to other payment obligations. It affirmed the injunctions issued by the trial court that requires Argentina to make ratable payments to plaintiffs concurrent with or in advance of its payments to holders of old bonds, and asked the trial court to further clarify how does the payment formula in the injunction intend to operate. The trial court clarified, in a subsequent order issued on 21 November 2012, that the payment formula in the injunction is intended to operate as follows: whenever Argentina pays any amount due under the terms of the exchange bonds, it must concurrently or in advance pay plaintiffs the same *percentage* of the amount due to them. See *NML Capital, Ltd. v. Republic of Argentina,* No. 12-105-(L) (2d Cir. 26 Oct. 2012); *NML Capital, Ltd. v. Republic of Argentina*, 08 Civ. 6978 (TPG), 09 Civ. 1707 (TPG), 09 Civ. 1708 (TPG) (S.D.N.Y., 21 Nov. 2012). For a discussion of this case, see Global Law Intelligence Unit, Allen & Overy LL.P, "The pari passu clause and the Argentine case", 27 Dec. 2012; W. Weidemaier, "Sovereign Debt After NML v. Argentina", Capital Markets Law Journal (forthcoming), available at http://ssrn.com/abstract=2199655 (last viewed 10 Mar. 2013).

18 Between 2006 and 2008, three groups of bondholders initiated arbitration at the ICSID against Argentina under investment treaties that grant foreign investors certain treaty protections with respect to the host country's behavior (i.e. *Abaclat and others v. Argentine Republic*, ICSID Case No. ARB/07/5; *Giovanni Alemanni and others v. Argentine Republic*, ICSID Case No. ARB/07/8; and *Ambiente Ufficio S.p.A. v. Argentine Republic*, ICSID Case No. ARB/08/9). In August 2011, the arbitral tribunal in *Abaclat* upheld its jurisdiction by a majority decision. One of the jurisdictional issues is whether bonds qualify as investment and could enjoy the protection offered by investment treaties. The word "investment" is not defined in the ICSID Convention, but the definition of investment in the applicable treaty in *Abaclat* does include sovereign bonds. Nevertheless, Argentina raised jurisdictional challenge, arguing that ICSID proceedings are not appropriate in the context of sovereign debt restructuring. Views of the members of the Tribunal differed. One member would have declined jurisdiction, explaining that the intervention of ICSID tribunals in sovereign

national Center for Settlement of Investment Disputes ("ICSID"), constituted pursuant to the Argentina-Italy bilateral investment treaty, dismissed jurisdictional challenges raised by Argentina and upheld its jurisdiction in the matter initiated by holdout bondholders.[19] Importantly, the bondholders' remarkable success in these events cannot be underestimated as it introduces a brand new battlefield against sovereign debtors.

(2.10) The term "brand new" is used because the last time sovereign debtors encountered numerous foreign bondholders was before the Great Depression shut down the international bond market in the 1930s, and at that time, sovereign debtors still enjoyed absolute sovereign immunity.[20] From the mid-20th century onwards, the notion of sovereign immunity shifted from the absolute theory to the restrictive theory permitting States to enjoy immunity for their public, but not private, acts.[21] Following the revival of the international bond

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debt disputes raises international public policy issues about the workability of future sovereign debt restructurings. However, the majority of the Tribunal, in finding jurisdiction, reasoned that policy concerns are for States, not for the Tribunal, to consider when negotiating investment treaties, and that the appropriateness of ICSID proceedings in this context is irrelevant. See *Abaclat and others v. Argentine Republic*, ICSID Case No. ARB/07/5, Decision on Jurisdiction and Admissibility (Aug. 2011), at para. 550; *Abaclat and others v. Argentine Republic*, ICSID Case No. ARB/07/5, Georges Abi-Saab's Dissenting Opinion of October 28, 2011, at para. 271.

19 *Ambiente Ufficio S.p.A. v. Argentine Republic*, (ICSID Case No. ARB/08/9), Decision in Jurisdiction and Admissibility (Feb. 2013). Co-arbitrator Santiago Torres Bernárdez dissented but has yet to issue a separate opinion.

20 Since the doctrine of absolute sovereign immunity did not permit States be sued in foreign courts without their express consent, disappointed private lenders to foreign States had very few options other than to seek the help of their own governments, known as "diplomatic protection". During that period, creditor States have often been debt collectors for money lent by their nationals to other governments through pressuring debtor State into payment or settlement by means of superior bargaining power, the use of power politics (including the use of force) or arbitration and adjudication at international courts and tribunals. A few case examples are *French Company of Venezuelan Railroads Case* (1905); *Canavero Claim* (Italy v. Peru, PCA, 1912); *French Claims Against Peru* (PCA, 1921); *Payment of Various Serbian Loans Issued in France* (PCIJ, 1929); *Payment in Gold of Brazilian Federal Loans Contracted in France* (PCIJ, 1929); *Societe Commerciale De Belgique* (Belgium v. Greece, PCIJ, 1939). See generally M. Waibel, Sovereign Defaults before International Courts and Tribunals (2011, Cambridge); L. Buchheit, "The Role of the Official Sector in Sovereign Debt Workouts", 6 Chi. J. Int'l L. 333 (2005); E. Borchard, State Insolvency and Foreign Bondholders, General Principles Volume I (1951).

21 Quite a few States have passed statutes codifying the restrictive theory of sovereign immunity. Examples include the Sovereign Immunities Acts of the United States. (1976), United Kingdom (1978), Singapore (1979), Pakistan (1981), South Africa (1981), Canada (1982), and Australia (1985). See generally H. Fox, The Law of State Immunity (2008, Oxford). Moreover, Austria, France, Iran, Japan, Kazakhstan, Lebanon, Norway, Portugal, Romania, Saudi Arabia, Spain, Sweden and Switzerland have ratified the United Nations Convention on Jurisdictional Immunities of States and Their Property (not yet in force) signed in December 2004, which recognizes the restrictive theory of sovereign immunity. See the Status of the United Nations Convention on Jurisdictional Immunities of States and Their Property,

market in the early 1990s, when banks agreed to exchange bad loans for Brady bonds, sovereign debtors are again facing numerous foreign bondholders, possibly one-time investors with less incentive to accept the debt restructuring offer. This time it is allowable to sue sovereign debtors in national courts; however, statistics show that foreign bondholders did not run crazily to the courthouse.[22] The reason for this may be associated with certain enforcement problems that bondholders with a favorable court judgment may still encounter: (1) there is currently no international convention dealing with the recognition and enforcement of foreign court judgments; and (2) attaching property both in the sovereign debtor's territory and abroad present problems. Nevertheless, despite great controversy, Argentine bondholders solved both problems in their recent episodes. The ICSID arbitral tribunals' willingness to embrace sovereign debt claims offers bondholders a better enforcement regime, as specified in the ICSID Convention.[23] More alarmingly, the injunction granted by the US court in *NML Capital Ltd.* renders asset searches unnecessary.[24]

(2.11) Despite the significant implications of these episodes for future sovereign debt restructurings, the solution should not exclusively focus on deterring holdouts. First, not all holdout creditors are aggressive vulture funds. The claimants in ICSID sovereign debt arbitrations against Argentina are frustrated bondholder themselves,[25] whose interests need protection. Second, the *NML Capital Ltd.* injunction was granted on the basis of the *pari passu* clause dealing with inter-creditor relations. The court mentioned that the operation of the *pari passu* clause as a constraint on Argentina as payor makes sense in the context of sovereign debt, because when sovereign debtors default they do not enter insolvency proceedings (where the legal rank of debt determines the order in which creditors will get paid).[26] In the view of the author, these

availableathttp://treaties.un.org/pages/ViewDetails.aspx?src=TREATY&mtdsg_no=III-13&chapter=3&lang=en (last viewed 11 Mar. 2013).

22 Schumacher provides an excellent dataset of sovereign debt litigations filed in the UK and U.S. courts between 1976 and 2010. Schumacher et al., "Sovereign Defaults in Court: The Rise of Creditor Litigation 1976-2010", available at http://dx.doi.org/10.2139/ssrn.2189997 (last viewed 11 Mar. 2013), at 8.

23 The ICSID Convention requires its 147 Member States to recognize and enforce an arbitral award rendered pursuant to the Convention as if it were a final judgment of a court in that State. See Art. 54(1), ICSID Convention, available at https://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp (last viewed 14 Dec. 2012).

24 Schumacher describes the current sovereign debt litigation environment as a hunt for assets. See Schumacher et al., "Sovereign Defaults in Court: The Rise of Creditor Litigation 1976-2010", *supra* note 22, at 8.

25 In *Abaclat*, claimants are over 180,000 bondholders (mostly Italian) at the time of initiation. See *Abaclat and others v. Argentine Republic*, Decision on Jurisdiction and Admissibility, *supra* note 18, at paras. 1, 3. In *Ambiente*, claimants are 119 Italian bondholders at the time of initiation. See *Ambiente Ufficio S.p.A. v. Argentine Republic*, Decision in Jurisdiction and Admissibility, *supra* note 19, at 113.

26 *NML Capital, Ltd. v. Republic of Argentina* (2d Cir. 26 Oct. 2012), *supra* note 17, at 19.

two episodes are likely to shift attention from deterring holdouts to crystalizing inter-creditor issues.

(2.12) Furthermore, the recent Eurozone episode also calls attention to inter-creditor issues. The newly concluded Treaty Establishing the European Stability Mechanism ("ESM") states that ESM loans will enjoy preferred creditor status in a similar fashion to those of the IMF, while accepting the IMF's preferred creditor status over the ESM.[27] On 6 September 2012, the ECB relinquished the preferred creditor status it had previously claimed in the event of a future debt restructuring of bonds acquired in its newly launched Outright Monetary Transactions ("OMT") program.[28] This episode has aptly illustrated the great uncertainty associated with certain creditors' unilateral claims of preferred status.

2.3 Inter-creditor Issues in Sovereign Debt Restructurings

2.3.1 The Concept of Inter-creditor Issues

(2.13) Given that renegotiations necessarily imply a certain degree of debt relief, they are certainly not creditors' favorite activities. When a sovereign debtor is financially sound, renegotiation is only a matter between the debtor and a particular creditor. The creditor does not need to know the identities of other creditors. However, the situation changes when a sovereign debtor encounters serious financial distress and does not have enough money to repay everyone. Under such circumstances, creditors awaken to the reality that sovereign lending activities are not risk-free and that they may have to take a loss. It is often said that, in the time of crisis, creditors should make "contributions" to help the debtor recover. Given that the total amount of contribution needed by the debtor to recover from the crisis is certain, the fact that a particular creditor makes a lesser contribution means that other creditors must make a larger one.

27 Treaty Establishing the European Stability Mechanism, Preamble, at para. 13.

28 The ECB announced that "it accepts the same (pari passu) treatment as private or other creditors with respect to bonds issued by euro area countries and purchased by the Eurosystem through Outright Monetary Transactions". Under the OMT program, the ECB buys short-term (one to three year) bonds of Eurozone countries in the secondary market, in unlimited amounts, in order to suppress the yields on those instruments. See ECB Press Release, 6 September 2012 – Technical features of Outright Monetary Transactions. It has been suggested that the uncertainty surrounding these events might have a potentially destabilizing effect on the market. See Global Law Intelligence Unit, Allen & Overy LL.P, "How the Greek debt reorganization of 2012 changed the rules of sovereign insolvency" (Sept. 2012), at 31.

(2.14) Therefore, as soon as the news of the debtor's financial distress spreads, creditors immediately want to find out who the other creditors are, whether they will be willing to make contributions and how large these might be. This change of attitude towards other creditors is referred to as the "conflict of interest issue among creditors" or "inter-creditor issues".

2.3.2 The Status Quo

2.3.2.1 Treatment Within the Same Group

(2.15) As far as the public sector is concerned, multilateral and bilateral creditors enjoy different treatment within their respective groups. Negotiations with multilateral creditors are conducted on an *ad hoc* and individual basis. Each multilateral creditor is responsible for its own negotiation process with the debtor and has no influence over other multilateral creditors' negotiation processes. Bilateral creditors within the Paris Club support the principle of equal treatment within the Club. All Paris Club decisions are taken based on consensus, in the form of so-called "Agreed Minutes". Although the Agreed Minutes are not binding, they guide the future bilateral negotiations that result in changes to the debt contracts.[29] In practice, driven by a mutual interest in avoiding disproportionate repayment of loans, all Paris Club members fully respect the commitments made through the Agreed Minutes.[30] However, such a principle does not apply to bilateral creditors outside the Paris Club, such as China, who are responsible for their own negotiations.

(2.16) In the private sector, commercial banks and bondholders all enjoy equal treatment within their groups but to a different extent. Commercial banks have employed the "mandatory repayment clause", which requires pro rata payments to all lenders in the event of a prepayment to any lender.[31] This clause excludes certain categories of claims, such as IMF debt, trade debt, foreign exchange contract obligations, interest and other agreed categories.[32] In addition, certain bank syndications also contain the "pro rata sharing clause", which provides that any bank receiving a greater proportion of its share must pay the excess to the agent bank who then redistributes to all banks on a pro rata basis.[33] The purpose of this clause is to share individual receipts, such as

29 E. Cosio-Pascal, *supra* note 10, at 12.
30 *Ibid.*, at 13.
31 M. Wright, "The Pari Passu Clause in Sovereign Bond Contracts: Evolution or Intelligent Design?", 1 Hofstra L. Rev. 40 (2011), at 5; L. Buchheit, "The Search for Intercreditor Parity", *supra* note 4, at 76.
32 P. Wood, "Sovereign insolvency: the bankruptcy ladder of priorities and the pari passu clause", *supra* note 4, at 69.
33 *Ibid.*

receipts by set-off, proceeds of litigation, individual guarantees or direct payments by the debtor.[34] Private bondholders have over the years expanded the use of the "*pari passu* clause" in the bond contracts, which provides, in part, that the bonds of that particular issue shall rank equally among themselves.[35]

2.3.2.2 Treatment Among Different Groups

a. Contractual Provisions

(2.17) Two types of contractual provisions in sovereign debt instruments address issues concerning treatment among different creditor groups: the "negative pledge clause" and the "*pari passu* clause". The "negative pledge clause" restricts the sovereign debtor's ability to grant security interests in its property to secure other creditors. The clause provides that if the debtor issues new debt and grants new creditors a security interest in the debtor's assets, the debtor has to grant old creditors an equivalent security interest.[36] While such a clause appears in both bank loan agreements and bond contracts, in the case of bonds the negative pledge generally only applies to security for bonds and other debt that is capable of being listed or traded on a market.[37]

(2.18) Besides ensuring the equal ranking of all bonds of that particular issue, the "*pari passu* clause" in most bond contracts also provides, in its second part, that the debtor's payment obligation under that particular issue shall rank equally with all other existing and future unsubordinated and unsecured external indebtedness.[38] On many occasions, the *pari passu* treatment in bond contracts is further limited to other bonds and tradable debt instruments.[39] Over the past decade, the *pari passu* clause has become a litigation tool for bondholders who refused to accept the exchange offer, and the meaning of

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34 *Ibid.*

35 The usage of *pari passu* clauses in unsecured bonds issued from 1960 to 2011 is recorded as follows: 123/144 (1960-1979), 429/464 (1980-1999), and 684/691 (2000-2011). See M. Gulati and R. Scott, The Three and a Half Minute Transaction: Boilerplate and the Limits of Contract Design (2012, Chicago), Appendix 7.

36 *Ibid.*, at 34. M. Wright, *supra* note 31, at 6.

37 One limitation of the negative pledge clause is that it does not catch various forms of quasi-security or title finance which, although not security in legal form, may be security in substance. P. Wood, "Sovereign insolvency: the bankruptcy ladder of priorities and the pari passu clause", *supra* note 4, at 69-70.

38 Wood lists a few examples of the pari passu clause in sovereign bonds, e.g. Pakistan (15 November 1999), Ecuador (27 July 2000), Ukraine (8 February 2001), Russian (25 February 2004), Argentina (10 January 2005), and Dominican Republic (20 April 2005). *Ibid.*, at 66-67.

39 Global Law Intelligence Unit, Allen & Overy LL.P, "The pari passu clause and the Argentine case" (27 Dec. 2012), at 7.

this clause has always remained controversial.[40] A narrow interpretation of this clause holds that all claims legally rank equally; in contrast, a wider interpretation suggests that the debtor must pay all its creditors ratably.[41]

(2.19) Despite Argentine bondholders' success in the recent *NML Capital Ltd.* decision which finds Argentina in breach of the *pari passu* clause, the meaning of this clause is far from being settled. It is not clear whether the US court in *NML Capital Ltd.* chose the narrow or the wider interpretation because it held that a combination of Argentina's actions breached the clause.[42] Furthermore, the court left the issue of whether payments to multilateral creditors would breach the *pari passu* clause entirely open, simply noting that the plaintiffs had not argued that preferential payments to the IMF made by Argentina could similarly entitle the plaintiffs to rateable payments.[43] Nevertheless, what is clear is that the history of the *pari passu* clause indicates that its introduction was intended, at least in part, as a tool for preserving inter-creditor equity and fairness in negotiations.[44]

b. Creditor Policies

(2.20) In the 1980s, commercial banks routinely imposed conditions for the restructuring of their loans, which involved a corresponding restructuring of the Paris Club debt.[45] Paris Club members have actively advocated that a sovereign debtor may not accept less debt relief from its non-Paris Club creditors than the amount agreed with the Paris Club. This is referred to as the comparability of treatment principle.[46] The principle, in essence, forbids

40 For a discussion of relevant case law, see P. Wood, Sovereign insolvency: the bankruptcy ladder of priorities and the pari passu clause, Tijdschrift voor Financieel Recht, March 2012, pp. 60 – 70, at 65-66; M. Gulati and R. Scott, The Three and a Half Minute Transaction: Boilerplate and the Limits of Contract Design (2012, Chicago), at 20-26.

41 Global Law Intelligence Unit, Allen & Overy LL.P, *supra* note 17, at 8.

42 Those actions included executive-declared moratoriums on payments on the old bonds which had been renewed each year, the fact that Argentina had not made a single payment on the old bonds for six years while timely servicing the new bonds, that Argentina enacted the Lock Law and that Argentina had stated in the prospectuses for the new bonds that it had no intention of making any payments on the old bonds and classified the old bonds as a separate category from the new bonds in its SEC filings. *Ibid.*, at 11.

43 *NML Capital, Ltd. v. Republic of Argentina,* (2d Cir. 26 Oct. 2012), *supra* note 17, at 21; Global Law Intelligence Unit, Allen & Overy LL.P, *supra* note 17, at 12.

44 M. Wright, *supra* note 31, at 4.

45 L. Buchheit, "The Search for Intercreditor Parity", *supra* note 4, at 78.

46 Non-Paris Club creditors include all external creditors except multilateral creditors. The Paris Club explains that non-Paris Club official bilateral creditors grant loans generally similar to those provided by Paris Club creditors. Consequently, non-Paris Club official bilateral creditors often restructure on terms very similar to those agreed with the Paris Club. These creditors may also participate in Paris Club treatments and, under these circum-

other creditors from making a lesser contribution than Paris Club creditors – although the Club considers certain mitigating factors to justify a deviation from the principle.[47] A controversial issue arises with respect to the willingness of Paris Club members to contribute proportionally when other creditor groups make larger contributions.[48] However, it is worth noting that the Paris Club considers on a case-by-case basis whether mitigating factors exist to justify a deviation from the comparability of treatment principle in respect of a particular creditor or debt instrument – although no explanation is provided as to what the "mitigating" factors entail.[49]

2.4 Exploring Solutions to Inter-creditor Issues

2.4.1 Existing Proposals

(2.21) Proposals in favor of a legal framework for sovereign debt workouts advanced by both economists and legal scholars started to emerge in the 1980s.[50] Notably, not all proposals focus on inter-creditor issues in sovereign debt workouts. The IMF's famous SDRM proposal, for instance, identifies the range of claims that could potentially be restructured under the mechanism, but leaves it to the debtor to decide which subset of eligible claims would need to be restructured in a particular case.[51] It nevertheless mentions that debt owed to an international organization could not be restructured under the SDRM;[52] the claims of official bilateral creditors would be excluded from the

stances, apply exactly the same treatment as that applied by Paris Club creditors. See Paris Club official website, *supra* note 10.

47 *Ibid.*

48 L. Buchheit, "The Search for Intercreditor Parity", *supra* note 4, at 76.

49 See Paris Club official website, *supra* note 10; L. Rieffel, "What Is Broken? What Fixes Make Sense?", Chapter 12 in Restructuring Sovereign Debt: The Case for Ad Hoc Machinery (2003, Brookings), at 282.

50 For a summary of proposals, see Das et al., "Sovereign Debt Restructurings 1950–2010: Literature Survey, Data, and Stylized Facts", IMF WP 12/203, at 87-95; Berensmann & Herzberg, "Sovereign Insolvency Procedures – A Comparative Look at Selected Proposals", Journal of Economic Surveys (2009) Vol. 23, No. 5, pp. 856–881.

51 Examples of eligible claims are listed as follows: (1) repayment of money lent or credit advances; (2) receipt of deferred purchase price of goods or services; (3) payments under bonds, notes or similar instruments; (4) amounts payable under interest rate and current swaps, and other financial derivatives; (5) the right of an issuing bank to be reimbursed for payments made under a letter of credit, bankers acceptance or bond; (6) payments due under leases; (7) guarantees or insurance contracts (direct or indirect) of the indebtedness of another party, and (8) court judgments requiring payment for liability on eligible claims, etc. See IMF, "The Design of the Sovereign Debt Restructuring Mechanism-Further Considerations", *supra* note 2, at 13 &18.

52 *Ibid.*, at 22-23.

SDRM or, alternatively, restructured within the SDRM as a separate class.[53] This section summarizes the discussion of inter-creditor issues in recent proposals.

2.4.1.1 Soft Law Approach

(2.22) According to Gelpern, inter-creditor issues could be addressed by allowing the sovereign debtor to impose priority rules on creditors unilaterally or by contract, to disclose the rankings at the time of borrowing and to comply with its commitments.[54] This proposal gives international financial institutions, like the IMF, a role in monitoring the sovereign debtor's compliance with such obligations. Amongst other things, the IMF could report whether the priorities States disclose in advance are consistent with the "general principles for according priority agreed among the official sector, the borrowers, and the private creditors".[55] In case of any violation, creditors would follow the old path of suing the sovereign debtor in national courts.[56]

(2.23) The Joint Public–Private Sector Committee[57] organized by the Institute of International Finance recently proposed a new version of the Principles for Stable Capital Flows and Fair Debt Restructuring. The principle dealing with inter-creditor issues stipulates that the sovereign debtor should "avoid unfair discrimination among affected creditors", including "seeking rescheduling from all official bilateral creditors."[58] It further provides that in keeping with general practice, short-term trade-related credits and inter-bank advances should be excluded from the restructuring plan and treated separately if

53 *Ibid.*, at 23-25.
54 A. Gelpern, *supra* note 4, Emory L. J. 53: 1119–1160 (2004), at 1153.
55 *Ibid.*, at 1158.
56 *Ibid.* Gelpern argues that this approach would encourage transparency and advance planning by the debtor, improve incentives for risk assessment by the creditors and introduce a multilateral policy check on governments' unilateral decisions in crisis.
57 The Institute of International Finance's *Joint Committee on Strengthening the Framework for Sovereign Debt Crisis Prevention and Resolution* is a public-private sector initiative launched under the auspices of the Co-Chairs of the Group of Trustees. The Joint Committee is chaired by Jean Lemierre, Senior Advisor to the Chairman, BNP Paribas and Co-Chair of the IIF Special Committee
on Financial Crisis Prevention and Resolution; Thomas Wieser, President, Eurogroup Working Group; David Mulford, Vice-Chairman International, Credit Suisse Group; and Gerardo Rodríguez Regordosa, Undersecretary of Finance and Public Credit, Mexico. It comprised 35 prominent representatives from the public and private sectors with extensive experience in sovereign debt restructuring in the Euro Area and elsewhere. The report was endorsed by the Group of Trustees during their Annual Meeting in Tokyo on October 14, 2012. See Report of the Joint Committee on Strengthening the Framework for Sovereign Debt Crisis Prevention and Resolution (Oct 2012), available at http://www.iif.com/press/press+393.php, last viewed 11 Mar. 2013), at 5-6. Information about the old version of the principles is available at http://www.iif.com/press/press+3.php (last viewed 9 Mar .2013).
58 *Ibid.*, at 22.

necessary.[59] The note to this principle explains that the goal of avoiding unfair discrimination among affected creditors could be achieved through treating all creditors fairly and providing "comparable treatment to all creditors".[60] It stresses that no creditor group should be "excluded ex ante from participating in debt restructuring" and any such arrangement should be "discussed and agreed to among all creditors on the basis of adequate justification".[61]

2.4.1.2 Hard Law Approach

(2.24) Berensmann and Schroeder endorsed the old version of the Principles for Stable Capital Flows and Fair Debt Restructuring proposed by the Institute of International Finance, and suggested a statutory approach to implement such principles. The old version of the principle dealing with inter-creditor issues provides that the sovereign debtor should "guarantee equal treatment of all creditors".[62] In connection with this, Berensmann and Schroeder proposed that all creditors (i.e. private, bilateral, multilateral) should participate in the restructuring negotiations under a newly established International Debt Framework Commission, with a few exceptions made for creditors with new financing and those holding trade credits.[63] The non-governmental organization German Debt Network (Erlassjahr) followed a similar approach. Its proposal states that in principle all creditors need to be treated equally, and preferred creditor status can only be granted by mutual consent.[64] It emphasizes "all claims on a sovereign need to be treated in one single process".[65]

(2.25) Paulus discussed the current "sectoral treatment of creditors" in sovereign debt workouts and emphasized the need for "a comprehensive solution".[66] To that end, Paulus advocated "an all-encompassing resolvency proceeding all claims should be included"[67] and envisaged a single forum.[68] His proposal suggests that different creditor groups could be treated differently and allows small creditors be packed into a separate group receiving full payment while other groups, such as institutionalized creditors, take haircuts.[69]

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59 *Ibid.*
60 *Ibid.*, at 26.
61 *Ibid.*
62 K. Berensmann & F. Schroeder, *supra* note 8, at 11.
63 *Ibid.*, at 14.
64 Erlassjahr, *supra* note 8, at 12.
65 *Ibid.*, at 16.
66 C. Paulus, *supra* note 8, at 6.
67 *Ibid.*, at 16.
68 Paulus mentions that "before it comes to the voting the debtor and its creditors have to sit at the same table and discuss the proposed plan". *Ibid.*, at 13.
69 *Ibid.*

(2.26) Bolton and Skeel addressed issues concerning the ranking for unsecured sovereign debt and proposed a "first-in-time" rule. According to this rule, when a sovereign debtor files for debt restructuring, "all unsecured debt would be classified by date of issue and earlier issues would have higher priority over later issues".[70] In order to avoid the creation of too many classes, they suggested that either each class must be of "a minimum size in value relative to the total value of outstanding debt" or "issues within any given fiscal year" should be put together in a single class.[71]

(2.27) Schwarcz drafted a Model Sovereign Debt Convention dealing with the sovereign debt restructuring process. Art. 6 of the Model Convention states that a debt restructuring plan shall designate classes of claims in accordance with Art. 7(3), specify the proposed treatment of each class and provide the same treatment for the same class.[72] Art. 7(3) provides that each class shall consist of claims against the sovereign debtor that are *pari passu* in priority, "provided that (a) *pari passu* claims need not all be included in the same class, and (b) claims of governmental or multigovernmental entities each shall be classed separately".[73] Art. 4 of the Model Convention requires the sovereign debtor to "notify all of its known creditors of its intention to negotiate a [p]lan under this Convention".[74]

(2.28) Similarly, Dickerson's proposal also requires the sovereign debtor to notify all creditors, disclose all claims, and explain the intended treatment of those claims.[75] It expresses the need to "ensure that all claims will be dealt with in an efficient, predictable, collective proceeding".[76]

2.4.1.3 Observations

(2.29) It appears from the proposals discussed above that inter-creditor issues in sovereign debt workouts are far from being settled. To begin with, not all proposals touch upon issues concerning the ranking of different claims. Among those that discuss the ranking issue, most of them address it in a rather ambiguous way. For instance, the Principles for Stable Capital Flows and Fair Debt Restructuring provide that sovereign issuers should treat all creditors fairly and provide comparable treatment to all creditors. However, the terms "fairly" and "comparable treatment" are not defined. Berensmann and Schroeder and the German Debt Network proposed equal treatment of all

70 P. Bolton & D. Skeel, *supra* note 8, at 799.
71 *Ibid.*
72 S. Schwarcz, *supra* note 8, at 1216.
73 *Ibid.*, at 1217.
74 *Ibid.*, at 1216.
75 A. Dickerson, *supra* note 8, at 1030.
76 *Ibid.*, at 999.

creditors without giving sufficient reasons. Furthermore, a few proposals discussing the ranking issue do not provide a complete picture. Bolton and Skeel advocated a "first-in-time" rule for the ranking of unsecured debt. Schwarcz touched upon the relationship between private claims and bilateral/ multilateral claims, suggesting that bilateral/multilateral claims should be classed differently from private claims.

(2.30) Despite the uncertainty of the ranking issue, nearly all proposals envisage a "collective" proceeding that would include "all" sovereign debt claims. Paulus employs the term "an all-encompassing resolvency proceeding all claims should be included". Dickerson mentions that "all claims" should be dealt with in an efficient, predictable, "collective" proceeding. Berensmann and Schroeder propose that "all" creditors should participate in the restructuring negotiations under a newly-established International Debt Framework Commission. German Debt Network emphasizes the need for "all" claims to be treated in a "single" forum. The Principles for Stable Capital Flows and Fair Debt Restructuring provide fair and comparable treatment for "all" creditors. Although Bolton and Skeel do not explicitly mention a collective proceeding for all claims, their detailed discussion concerning national bankruptcy law and claim classification implies a single process for all claims. Schwarcz's extensive discussion of claim classification also calls for a similar conclusion. In this respect, it is observed that the issue of whether a collective proceeding including all claims is the appropriate forum for sovereign debt workouts has never attracted attention in any proposal. These proposals either take a collective proceeding for all claims for granted without explaining any reason for this, or discuss directly issues involved in a collective proceeding including all claims (i.e. claim classification), thereby assuming the appropriateness of such a process. The paragraphs below intend to fill this gap by exploring the reasons behind a collective proceeding for all claims in national bankruptcy law and the rationale for borrowing (or not) such a concept for discussions concerning a legal framework for sovereign debt restructuring.

2.4.2 Treatment of All or Partial Claims

2.4.2.1 Creditors Affected by Inter-creditor Issues

(2.31) As mentioned above, inter-creditor issues are caused by the conflict of interests among creditors. The reason for such a conflict lies with a limited pool of assets that is insufficient for everyone's satisfaction so that creditors have to take a loss and contribute to the debtor's recovery. It is widely accepted that a lesser contribution made by any individual creditor requires that other creditors contribute more. However, this theory only makes sense in the situation of a still pool.

(2.32) By contrast, in the context of sovereign debt, the debtor can always raise revenue through taxation. Therefore, the pool of assets, although limited, is not still but alive. In other words, the pool is dynamic, with money going in and out on a daily basis. In addition, a sovereign State can never be liquidated, thus rendering the crisis merely temporary. Indeed, because the State will ultimately recover, the pool here will never become still. In a still pool, the interests of all creditors are conflicted. By contrast, where the pool of assets is constantly replenished, the ability of individual creditors to make a lesser contribution does not necessarily require other creditors to contribute more.[77] The conflict of interest exists only during the temporary period when there are not enough assets for everyone. During this period, the concerned creditors are those holding claims with maturities before the end of the crisis period. Taking Greece as an example, the financial crisis is severe but will eventually end in X years. Thus, a conflict of interest exists only among creditors holding claims with maturities in the next X years. It follows that inter-creditor issues are only relevant for creditors holding claims that will mature in the next X years. Therefore, any rules designed to address inter-creditor issues should not include all claims.

(2.33) Because the task of identifying "X" is extremely complex, if not impossible, the practical solution is to allow the debtor to determine its anticipated date of recovery from the crisis, after considering the debt sustainability analysis provided by international financial institutions. Giving the debtor the freedom to determine X will not be problematic, as it only intends to address the conflict of interests among creditors, but not to make the restructuring process necessarily easier for the debtor.

2.4.2.2 Inappropriateness of the Automatic Acceleration Principle

(2.34) Needless to say, the proposal that inter-creditor issues only exist among creditors holding claims with maturities in the next X years challenges the basic principle of national bankruptcy law that all claims become due upon the filing of bankruptcy ("automatic acceleration principle"). Different national bankruptcy legislations may use different terms for this principle, but it basically refers to the situation that all claims are allowed in a bankruptcy proceeding regardless of the maturity date. The author argues that this principle

77 It is argued that taking assets out of a live pool does not necessarily lead to a situation where fewer assets are available for other creditors, provided that the debtor can coordinate the rate at which assets increase, relative to the rate at which assets are attached by creditors. See S. Block-Lieb, "Fishing in Muddy Waters: Clarifying the Common Pool Analogy As Applied to the Standard for Commencement of a Bankruptcy Case", 42 Am. U. L. Rev. 337 (1993), at 381.

should not be applied to any future legal framework for sovereign debt restructurings for the reasons outlined below.

(2.35) First, the rationale for this basic principle derives from the liquidation scenario, and should not be applied to sovereign States where liquidation is not a possibility. In liquidation, the company will eventually be liquidated and dissolved; thus, all creditors must be able to make their claims immediately instead of years later, according to the maturity date.[78] This principle makes sense under the contract law theory that the debtor's repayment obligations cannot be assigned to a new entity without the creditor's permission unless the original debtor remains responsible.[79] It is argued that, from a contract law perspective, the continuation of a debtor's contractual obligation beyond its liquidation is equivalent to a delegation of that obligation to a new entity.[80] However, because the original debtor does not exist beyond liquidation, such a delegation of the repayment obligation is prohibited, and all claims become due and payable immediately. The principle also applies in reorganization on the basis that a company may still be liquidated if the reorganization plans fail.[81] In the absence of any possibility of liquidation, the principle that all claims are automatically accelerated simply should not apply to sovereign States. However, this rule would not affect creditors' ability to accelerate claims pursuant to the terms of the debt contract.

(2.36) Second, the fact that the US municipal bankruptcy law[82] does not differentiate between the municipal debtor and other types of debtors on this point does not mean that the automatic acceleration principle is appropriate for States. The principle that all claims with different maturity dates are allowed in a domestic bankruptcy proceeding is to be found in the definition of "claim" contained in the general provisions of the US bankruptcy law, which apply to all types of debtors. The US Code defines claim as "right to payment, whether or not such right is […] matured, unmatured […]".[83] This broad definition contemplates that all legal obligations of the debtor, no matter how remote, will be addressed in the bankruptcy proceeding.[84] The US Code explains that the reason for such a broad definition is that it "permits the

78 T. Jackson, "Determining Liabilities and the Basic Role of Nonbankruptcy Law", Chapter 2 in The Logic and Limits of Bankruptcy Law (1986, Harvard), at 38.

79 *Ibid.*

80 *Ibid.*

81 Notably, in reorganization proceedings, Section 1124 (2)(b) of the U.S. Code allows the debtor to "reinstat[e] the maturity of such claim or interest as such maturity existed before such default". *Ibid.*, at 40.

82 11 U.S.C. § 901-946.

83 11 U.S.C. § 101.

84 11 U.S.C.A. § 101.

broadest possible relief in the bankruptcy court".[85] But this presumption does not hold water in the context of sovereign debt restructuring. In the recent successful Greek restructuring, all creditors holding claims with maturities between 0 (20 March 2012) to 45 years (25 July 2057) were offered the same deal, which provides that the latest repayment date is 2042.[86] Accordingly, the bonds with the longest maturity (2057) will actually be paid before they become due (2042); the present value haircut implicit in the restructuring for this bond was -26.5.[87] This negative figure indicates that these bondholders suffered no loss at all; instead, their positions improved through the inclusion of their claims in the restructuring process. This finding contradicts the theory that the inclusion of all creditors in the bankruptcy proceeding necessarily contributes to the broadest possible relief for the debtor.

(2.37) To summarize, the author argues that the "temporary" nature of a sovereign debt crisis and an "alive" pool of sovereign assets put the fundamental principle of automatic acceleration adopted from national bankruptcy law in doubt. An analysis of the underlying reasons for such a principle further demonstrates its inappropriateness for sovereign debtors. Therefore, any future rules for inter-creditor issues should not address all sovereign debt claims, but only those claims which are relevant.

2.4.3 Collective or Non-collective Proceeding

2.4.3.1 Need for a Collective Proceeding in National Bankruptcy Law

(2.38) The need for a collective proceeding in national bankruptcy law is justified by two main theories – the common pool problem and the creditors' bargain theory. Scholars describe the creditors of a debtor with a limited pool of assets not enough for everyone as enmeshed in a common pool problem.[88]

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85 *Ibid.*

86 All creditors were offered (i) One and two year notes issued by the European Financial Stability Facility ("EFSF"), amounting to 15 per cent of the old debt's face value; (ii) 20 new government bonds maturing between 2023 and 2042, amounting to 31.5 per cent of the old debt's face value, with annual coupons between 2 and 4.3 per cent; (iii) A GDP-linked security which could provide an extra payment stream of up to one percentage point of the face value of the outstanding new bonds if GDP exceeds a specified target path (roughly in line with the IMF's medium and long term growth projections for Greece). See J. Zettelmeyer, C. Trebesch and M. Gulati, *supra* note 12, at 6.

87 *Ibid.*, at 17.

88 Susan Block-Lieb, "Congress's Temptation to Defect: A Political and Economic Theory of Legislative Resolutions to Financial Common Pool Problems", 39 Ariz. L. Rev. 801, pp. 802-803 (1997); See also T. Jackson, The Logic and Limits of Bankruptcy Law (1986), pp. 12-13; D. Baird & T. Jackson, Cases, Problems and Materials on Bankruptcy, 20-30 (2d ed.

They compare the debtor's assets to a jointly-owned pool of fish, and the debtor's creditors to self-interested fishermen. They view the creditors' pursuit of their remedies in terms of attachment, garnishment, execution and levy as analogous to the overfishing of a common pool: self- interested creditors have every incentive to collect as many of the debtor's assets as quickly as they can, because the creditors who are first to collect suffer none of the deleterious effects of their collection actions.[89] With this observation they make a powerful case for the need for some form of a collective bankruptcy remedy.[90]

(2.39) Moreover, the creditors' bargain theory holds that it is in the creditors' best interest to agree *ex ante* on binding collective procedural rules. The argument is that unsecured creditors prefer a collective system that treats them alike, because it reduces the costs associated with individual creditors' actions, increases the aggregate pool of assets and avoids a piecemeal dismantling of a debtor's business, as well as enhances administrative efficiencies.[91] However, fully secured creditors are not direct beneficiaries of any of these advantages, because they can easily remove the collateral from the debtor's estate.[92] Thus, unsecured creditors have a strong interest in including secured creditors in the collective proceeding, in order to prevent actions by them that diminish the aggregate estate.[93] Unsecured creditors are therefore willing to give secured creditors at least some benefit in exchange for their agreement to join in the collective proceeding. Secured creditors have no reason to object to inclusion if left as well off as before.[94] The result is a collective system that includes both secured and unsecured creditors, with the rights of secured creditors preserved through a priority position in the order for the distribution of assets.

2.4.3.2 Absence of the Need for a Collective Proceeding in the Sovereign Debt Context

(2.40) To begin with, the so-called common pool problem does not exist in the sovereign debt context. Litigation against a sovereign debtor in national courts is not an easy undertaking. Sovereign debt creditors holding a favorable judgment may still encounter problems with enforcement. Whereas attempts to attach property in the sovereign debtor's territory may face objections based

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1990); T. Jackson & R. Scott, "On the Nature of Bankruptcy: An Essay on Bankruptcy Sharing and the Creditors' Bargain", 75 Va. L. Rev. 155, 178 (1989).

89 Thomas Jackson, The Logic and Limits of Bankruptcy Law (1986), p. 13.

90 Susan Block-Lieb, "Fishing in Muddy Waters: Clarifying the Common Pool Analogy As Applied to the Standard for Commencement of a Bankruptcy Case", *supra* note 77.

91 T. Jackson, "Bankruptcy, Non-Bankruptcy Entitlements, and The Creditors' Bargain" (1982) 91 Yale L. J. 857, at 864, 866.

92 *Ibid.*, at 868.

93 *Ibid.*, at 869.

94 *Ibid.*, p. 870.

on public policy, efforts to enforce the judgment abroad may fail due to the sovereign's lack of attachable assets in foreign countries and the principle that certain assets located abroad cannot be attached due to their special characteristics (i.e. diplomatic missions, central bank reserves, military assets etc.).[95] Due to these difficulties and uncertainties, the number of court litigation against sovereign debtors is relatively small.

(2.41) Schumacher recently conducted empirical research concerning sovereign debt litigation filed against debtor governments in the US and UK courts between 1976 and 2010.[96] This research shows that only 108 cases were filed in the US and the UK by foreign banks, bondholders and other commercial creditors during this period, and that these cases only relate to 29 of the 180 sovereign debt restructurings with private creditors (16%).[97] It further reveals that only 27 out of 69 debtor governments have been sued.[98] It is worth noting that the number of creditors who manage both to obtain a favorable judgment and to enforce that judgment is even smaller. The author argues that such a small number of individual actions which may diminish the debtor's pool of assets cannot be compared with the overfishing situation in a common pool. Although the recent *NML Capital Ltd.* decision is likely to encourage future litigation against sovereign debtors, it is still too early to gauge that effect. Any decision to implement a collective proceeding should be balanced against the actual need and costs involved.

(2.42) Turning to the creditors' bargain theory, as discussed above a collective proceeding is only desirable when it is in the best interests of both unsecured and secured creditors, and secured creditors would only agree to be included in the same proceeding as unsecured creditor if their rights are well preserved through priority rules. In the sovereign debt world, however, whether creditors are secured or not is not a major difference between them as a result of the negative pledge clause which restricts the debtor's ability to grant security interests in its property to secure other creditors. One unique feature of the sovereign debt context is the involvement of multilateral and bilateral creditors. While commercial creditors lend for profit, multilateral and bilateral creditor lend for a wide variety of purposes, except making a profit. The rationale for multilateral lending relates to information provision in terms of monitoring government policies in recipient countries and the exercise of conditionality

95 R. Olivares-Caminal, Legal Aspects of Sovereign Debt Restructuring (2009, Sweet & Maxwell), at. paras. 2-001, 2-002, 2-004.
96 Schumacher et al., *supra* note 22.
97 *Ibid.*, at 3.
98 *Ibid.*

aimed at changing governmental policies.[99] Similarly, bilateral creditors often extended to advance political and social objectives, such as ensuring that domestic exporters are not disadvantaged by financial support offered by other governments, or sharing the costs of building infrastructure projects that can help the debtor achieve higher rates of economic growth.[100]

(2.43) Given the non-comparable differences between multilateral/bilateral creditors and commercial creditors, it seems extremely difficult, if not impossible, to weigh political and financial considerations and to devise a priority order between them. Such difficulty is acknowledged in the sovereign debt framework proposals put forward by the IMF and Schwarcz, in which the term "separate" is used to describe the treatment for multilateral and/or bilateral creditors.[101] Importantly, separate treatment does not necessarily violate the equitable treatment principle in national bankruptcy law, which basically ensures the fair treatment of creditors with similar legal rights so that assets are distributed according to the creditors' ranking.[102] That is, all creditors do not need to be treated equally, but "in a manner that reflects the different bargains they have struck with the debtor".[103]

(2.44) In light of the foregoing, the author argues that a collective proceeding is not the most desirable form of proceeding due to the absence of the common pool problem in the context of sovereign debt and the incomparably different nature of multilateral/bilateral claims that renders the design of a priority order between multilateral/bilateral claims and commercial claims impossible. In the view of the author, the inapplicability of a collective proceeding offers two possibilities: several separate collective proceedings or a non-collective proceeding. Whereas collectivity is considered to be the easiest way to ensure equal treatment, a similar result can arguably be achieved through the implementation of mandatory rules to the same effect and legal sanctions against violation of these rules. The ultimate choice largely depends on an analysis

99 D. Rodrik, "Why is There Multilateral Lending?", NBER Working Paper No. 5160 (June 1995), at 2. Crippa discusses the human right issues involved in projects financed by multilateral development banks. See L. Crippa, "Multilateral Development Banks and the Human Right Responsibility", 3 Am. U. Int'l L. Rev. 25 (2010): 531-577.

100 L. Rieffel, "What Is Broken? What Fixes Make Sense?", *supra* note 49. It is worth noting that China as a major bilateral lender to developing countries has a different approach towards bilateral lending. For example, Chinese loans generally do not require any change of national economic policies. See M. Mattlin & M. Nojonen, "Conditionality in Chinese bilateral lending", BOFIT Discussion Papers (14/2011); E. Downs, "INSIDE CHINA INC.: China Development Banks' Cross-border Energy Deals", The John L. Thornton China Center at Brookings (2011).

101 IMF, "The Design of the Sovereign Debt Restructuring Mechanism-Further Considerations", *supra* note 2, at 23-25. S. Schwarcz, *supra* note 2, at 1217.

102 UNCITRAL, *supra* note 3, at 11.

103 *Ibid.*

evaluating the benefits and costs involved for collective proceedings within a smaller circle.

2.4 CONCLUSION

(2.45) In light of recent creditor episodes, the *NML Capital Ltd.* decision in particular, the time for academic attention to shift from holdout concerns to inter-creditor issues has become ripe. This paper details the concept and *status quo* of inter-creditor issues in sovereign debt restructurings and explores possible solutions to inter-creditor issues. Notably, it questions the unquestionable beauty of a "collective" proceeding for "all" sovereign debt claims.

(2.46) With respect to "all" claims, this paper identifies the scope of creditors affected by inter-creditor issues by discussing the "temporary" nature of the sovereign debt crisis and the "alive" feature of the limited pool of sovereign assets. It maintains that where the pool of assets is constantly replenished, inter-creditor issues do not concern all creditors because the ability of individual creditors to make a lesser contribution does not necessarily require other creditors to contribute more. To further support this argument, the paper discusses the reasons for non-applicability of the automatic acceleration principle in national bankruptcy law in the sovereign debt context through its analysis of the non-liquidable nature of sovereign debtors and the legislative motivation for the adoption of the automatic acceleration principle for municipal debtors in US chapter 9 bankruptcy.

(2.47) Turning to a "collective" proceeding, this paper explains the theories in favor of such a proceeding in national bankruptcy law, namely, the common pool problem and the creditor's bargain theory. It uses empirical data concerning the number of litigation against sovereign debtors in the US and UK courts between 1976 and 2010 to argue that the common pool problem does not exist in the sovereign debt context. Moreover, it explains that, according to the creditor's bargain theory, a collective proceeding is only desirable when it is in the best interests of both unsecured and secured creditors, and that secured creditors would only agree to be included in the same proceeding as unsecured creditors if their rights are well preserved through priority rules. It analyses the incomparably different nature of multilateral/bilateral claims and argues that it is almost impossible to weigh political and financial considerations and to devise a priority order between multilateral/bilateral claims and commercial claims. Therefore, multilateral/bilateral claims and commercial claims should receive separate treatment and should not be included in a collective proceeding.

3 Policy Implication of Poštová Tribunal's Jurisdiction over Sovereign Bonds: Bankruptcy Cram-down and ICSID Arbitration[1]

3.1 Introduction

(3.1) Following the Greek debt restructuring in spring 2012, *Poštová* Banka A.S. (a Slovak entity) and its shareholder Istrokapital S.E. (a Cypriot entity) initiated arbitration against Greece in May 2013 at the International Centre for Settlement of Investment Disputes ("ICSID"), pursuant to the bilateral investment treaties concluded between Greece and Slovakia as well as Greece and Cyprus.[2] The claimants contend that they purchased Greek bonds in 2010 and were forced to exchange their bonds for "new securities of substantially lesser value".[3] They allege that the forcible bond exchange was carried out through the newly adopted Greek Bondholder Act that "retroactively and unilaterally" amended the bond terms by inserting a so-called "Collective Action Clause" ("CAC') into outstanding Greek-law bonds.[4] According to the claimants, the CAC allows "the imposition of new terms upon bondholders against their consent if a supermajority of other bondholders consent."[5] This case is currently pending and the parties agreed to bifurcate jurisdiction from the merits.[6] They further agreed that a hearing on jurisdiction would take place in July 2014 and a decision would be issued by November 15, 2014.[7]

(3.2) This paper explores the policy implication of the *Poštová* tribunal's jurisdiction over sovereign bonds. It should be mentioned at the outset that *Poštová* is not the first ICSID arbitration that involves sovereign bonds. Between

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1 This chapter has been published in *Norton Journal of Bankruptcy Law and Practice* Vol. 23, No. 5: 604- 633 (2014). The author is very grateful to Professor Bob Wessels for his helpful comments on an earlier draft.

2 *Poštová banka, a.s. and ISTROKAPITAL SE v. Hellenic Republic* (ICSID Case No. ARB/13/8), available at official website of the International Centre for Settlement of Investment Disputes, https://icsid.worldbank.org/ICSID/FrontServlet?requestType=GenCaseDtlsRH&actionVal=ListPendin (last visited 26 Feb 2014).

3 Investment Arbitration Reporter on "Bondholders' claim against Greece is registered at ICSID, as mandatory wait-period expires on another threatened arbitration", available at http://www.iareporter.com/articles/20130530_2 (last visited 26 Feb 2014).

4 *Ibid.*

5 *Ibid.*

6 *Poštová banka, a.s. and ISTROKAPITAL SE v. Hellenic Republic*, Procedural Order No.1 dated 20 December 2013, para. 14.1.

7 *Ibid.*

2006 and 2008, three groups of bondholders have brought arbitrations at ICSID against Argentina following the debt crisis.[8] All three cases are still pending and two of them (i.e. *Abaclat* and *Ambiente*) have come to the stage where the tribunal issued a decision on jurisdiction and admissibility upholding jurisdiction over the claims regarding sovereign bonds. Only one of these decisions (i.e. *Abaclat*) addressed the policy implication of ICSID tribunals' jurisdiction over sovereign bonds, as the respondent in the other case did not raise the issue.[9] In *Abaclat*, the majority found that policy reasons are for States to take into account when negotiating investment treaties but not for the tribunal to consider when deciding a case, stating that "[w]hether or not ICSID is the best way to deal with a dispute relating to these bonds and security entitlements in the context of foreign debt restructuring is irrelevant."[10] On the other hand, the dissenting opinion provides that "the present case raises, in an acute manner, an international public policy issue about the workability of future sovereign debt restructuring, should ICSID tribunals intervene in sovereign debt disputes."[11]

(3.3) Interestingly, what happened during the Greek debt restructuring and the policy considerations facing the *Poštová* tribunal differ significantly from the situation in *Abaclat*. Given that there was no CAC in the Argentina bonds and the claimants in *Abaclat* simply refused to participate in the restructuring and were in no way forced to accept the offer, the unspoken policy choices for the *Abaclat* tribunal were either a result that potentially threatens the workability of future sovereign debt restructuring or a result that gives bondholders, who have the possibility to go to national courts, an addition channel for remedy, thereby ensuring better creditor protection.[12] By contrast, the

8 *Abaclat and others v. Argentine Republic* (ICSID Case No. ARB/07/5); *Giovanni Alemanni and others v. Argentine Republic* (ICSID Case No. ARB/07/8); and *Giordano Alpi and others v. Argentine Republic* (ICSID Case No. ARB/08/9). See ICSID official website, available at http://icsid.worldbank.org/ICSID/FrontServlet?requestType=GenCaseDtlsRH&actionVal=ListPendin (last visited 26 Feb 2014).

9 *Ambiente Ufficio S.p.A. and others v. Argentine Republic*, Decision on Jurisdiction and Admissibility dated 8 February 2013.

10 *Abaclat and others v. Argentine Republic*, Decision on Jurisdiction and Admissibility of 4 August 2011, para. 550.

11 *Abaclat and others v. Argentine Republic*, Georges Abi-Saab's Dissenting Opinion of 28 October 2011, para. 271.

12 Outside the courtroom, policy implications of investment treaty tribunals' jurisdiction over sovereign bonds have been discussed quite extensively. Arguments in favor of ICSID's involvement include a better creditor protection and a healthier sovereign debt market. Opposite views concern the degree of the involvement of creditor governments and international institutions at the time of crisis, the competence of any international tribunal to determine debt-related issues, as well as creditors' incentives to hold out thereby disrupting the debt restructuring negotiations. See E. Norton, "International Investment Arbitration and the European Debt Crisis", 13 Chi. J. Int'l L. 291 (2012), pp. 6-7; F. Suescun de Roa, "Investor-State Arbitration in Sovereign Debt Restructuring: The Role of Holdouts", Journal

policy choices are different in the context of CACs. It has been argued that the fact that ICSID tribunals hear treaty claims concerning sovereign bonds despite the legitimate exercise of CACs would make CACs a must less effective tool in binding non-participating bondholders, thereby creating a significant legal gap in the international community's collective action policy.[13]

(3.4) This paper addresses the same issue from the prospective of non-participating bondholders, and argues that, if the *Poštová* tribunal refuses to hear treaty claims concerning sovereign bonds, it would create a significant gap concerning creditor protection under the current regime of sovereign debt restructuring. The paper is structured as follows: Part II gives an overview of the Greek debt restructuring; Part III analyses the nature of the Greek Bondholder Act adopted by the Greek legislature in order to facilitate the restructuring process, and finds that what the Act introduced was not an ordinary CAC but something similar to cram-down procedures in bankruptcy law; Part IV describes the safeguard provision for cram-down procedures in bankruptcy law, which includes the prohibition of unfair discrimination and the fair and equitable treatment principle; and Part V argues that ICSID arbitration is the best forum to develop a safeguard provision for cram-downs in the context of sovereign debt restructuring, due to the similarities between the safeguard provision for cram-down procedures in bankruptcy law and the fair and equitable treatment principle under investment treaties. Part VI concludes this paper.

3.2 Greek Debt Restructuring

(3.5) In February 2012, Greece announced a plan to restructure over € 200 billion in privately held Greek bonds. The restructuring offer was directed at the holders of all sovereign bonds issued prior to 2012 (total face value of € 195.7 billion) and 36 sovereign-guaranteed bonds issued by public enterprises (total face value of just under € 10 billion).[14] These holders were offered a

of International Arbitration, (Vol. 30 Issue 2, 2013) pp. 131 – 154; M. Waibel, Sovereign Defaults Before International Courts and Tribunals (Cambridge 2011), pp. 317, 323, 326; K. Gallagher, "The New Vulture Culture: Sovereign Debt Restructuring and Trade and In- vestment Treaties", Working Paper No 02/2011 (International Development Economics Associates (IDEAs) 2011), p. 10; M. Waibel, "Opening Pandora's Box: Sovereign Bonds in International Arbitration",
101 Am J Intl L 711, 713 (2007); UNCTAD, "Sovereign Debt Restructuring and International Investment Agreements", IIA Issues Note No.2 of July 2011, p. 8.

13 M. Waibel, "Opening Pandora's Box: Sovereign Bonds in International Arbitration", *supra* note 12, p. 736.

14 J. Zettelmeyer, C. Trebesch and M. Gulati, "The Greek Debt Exchange: An Autopsy", Peterson Institute for International Economics Working Paper No. 2013-13-8, p.5, available at SSRN: http://ssrn.com/abstract=2144932 (last visited 26 Feb 2014).

swap of their old bonds with a package of new ones comprised of (1) English-law bonds maturing between 2023 and 2042 issued by Greece with a face value equal to 31.5% of the face amount of the old bonds, (2) English-law EFSF (European Financial Stability Facility) notes with a maturity date of one or two year from the date of closure of the restructuring with a face value equal to 15% of the face amount of the old bonds, and (3) detachable GDP-linked securities issued by Greece under English law having a notional amount equal to the face amount of each holder's new bonds.[15]

(3.6) Among all targeted bonds, nearly 91% of the sovereign bonds had been issued under the Greek law, and the guarantee bonds were about evenly divided foreign and Greek law issues.[16] While the English-law bonds contain the Collective Action Clauses that enable a qualified majority to bind all holders in the same series to a change of the payment terms, the Greek-law sovereign bonds do not contain any CAC.[17] On 23 February 2012, the Greek legislature introduced a collective action procedure by passing the Greek Bondholder Act (4050/12), under which the proposed amendment of bond terms will bind holders of all Greek-law bonds, "if at least two thirds by face amount of a quorum of these bonds, voting collectively without distinction by series, approve the proposed amendments."[18] It further provides that "[o]ne half by face amount of all the Republic's bonds subject to the collective action procedure will constitute a quorum for these purposes."[19]

(3.7) On 9 March 2012, the Greek Ministry of Finance announced that out of the € 177.3 billion Greek-law bonds, € 146.2 billion had accepted the exchange offer and proposed amendment, € 5.9 billion had consented to the amendment without tendering their bonds, and € 9.3 billion had voted against the amendment.[20] Thus, the quorum and voting thresholds for amending the Greek-law bonds under the Greek Bondholder Act were easily met. Through the implementation of the Act, the proposed amendment became binding on all holders of Greek-law bonds.[21] While € 6.4 out of € 6.7 billion in Greek-law guaranteed debt was tendered for exchange, only € 13.1 out of € 21.6 billion foreign-law bonds had accepted the offer and consented to the proposed amendment.[22] Overall, Greece restructured approximately € 199

15 Hellenic Republic Ministry of Finance, Press Release dated 24 Feb 2012.
16 J. Zettelmeyer, C. Trebesch and M. Gulati, *supra* note 14.
17 J. Zettelmeyer, C. Trebesch and M. Gulati, *supra* note 14, pp. 6-7.
18 Hellenic Republic Ministry of Finance, *supra* note 15.
19 *Ibid.*
20 Hellenic Republic Ministry of Finance, Press Release dated 9 Mar 2012.
21 *Ibid.*
22 *Ibid.*

billion (96.9%) of the total face amount of bonds eligible to participant in the exchange.[23]

3.3 Hidden Nature of the Greek Bondholder Act

(3.8) This section analyses the nature of the Greek Bondholder Act, which, according to the claimants in *Poštová*, has retroactively and unilaterally amended the bond terms by inserting a CAC into outstanding Greek bonds. Is the Act in fact a CAC, an aggregated CAC or something else?

(3.9) Article 4 of the Greek Bondholder Act (Law No. 4050/2012) provides as follows:

> "A Bondholder's participation in the procedure is made with the whole or part of the principal amount outstanding of eligible titles it holds, as specified in the invitation. For the modification of the eligible titles, it is required the participation in the procedure (quorum) of at least one half (½) of the *aggregate principle amount outstanding of all eligible titles that are specified in the relevant invitation* ("participating principal amount") and a qualified majority in favour of the modification of at least two thirds (⅔) of the participating capital."[24]

3.3.1 Greek Bondholder Act = CAC?

(3.10) As the name suggests, the CAC enables a qualified majority of bondholders to bind all holders of the same bond issuance to a change of the contract terms, including the maturity date as well as the amount of interest and principal.[25] It began to appear in bonds governed by English law in the

23 Hellenic Republic Ministry of Finance, Press Release dated 25 Apr 2012.

24 An unofficial English translation of Law No. 4050/2012 is available at http://www.iiiglobal.org/component/jdownloads/finish/625/5899.html (last visited 26 Feb 2014).

25 Strictly speaking, the term CACs include two types of clauses: (1) "majority restructuring" provisions, which enable a qualified majority of bondholders to bind all holders to the same bond issuance to the financial terms of a restructuring; and (2) "majority enforcement" provisions, which allows a qualified majority of bondholders to limit the ability of a minority bondholders to enforce their rights following a default. The former type, "majority restructuring" provisions, is most frequently employed in practice. See IMF, "Collective Action Clauses in Sovereign Bond Contracts –Encouraging Greater Use" (Prepared by the Policy Development and Review, International Capital Markets and Legal Departments), Jun. 2002, available at http://www.imf.org/external/np/psi/2002/eng/060602a.htm (last visited 26 Feb 2014). The typical threshold for a qualified majority is 75%. See M. Bradley & M. Gulati, "Collective Action Clauses for the Eurozone: An Empirical Analysis", March 2013, p. 5, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1948534 (last visited 26 Feb 2014).

1980s.[26] In the wake of the Mexican crisis in 1995 and the Argentine default in 2001, the IMF began pushing for the adoption of CACs in sovereign bonds governed by New York law to facilitate the restructuring of sovereign bonds held by numerous and largely anonymous creditors.[27] Countries such as Mexico, Brazil, Belize, Guatemala, Venezuela, Uruguay were among the first group to include CAC in their New York law bonds.[28]

(3.11) In 2004, following on the shift to CACs in the New York market, the International Primary Market Association (IPMA) promulgated a set of recommended CACs for sovereign bonds issued under English-law.[29] Paragraph (e) of the recommended CACs provides that:

> "*Modifications*: Subject as provided in paragraph (d) (*Matters requiring unanimity*), any modification of any provision of these Conditions may be made if approved by an Extraordinary Resolution or a Written Resolution. In these Conditions, '*Extraordinary Resolution*' means a resolution passed at a meeting of Noteholders duly convened and held in accordance with the Fiscal Agency Agreement by a majority of at least:
>
> (i) in the case of a Reserved Matter, 75 per cent. of the *aggregate principal amount of the outstanding Notes;* or
> (ii) in the case of a matter other than a Reserved Matter, 66⅔ per cent. of the aggregate principal amount of the outstanding Notes which are represented at that meeting.
>
> Any Extraordinary Resolution duly passed at any such meeting shall be binding on *all the Noteholders,* whether present or not and whether they voted in favour or not, and all Couponholders."[30]

(3.12) As stated in the recommended CAC, the decision of a qualified majority binds "all the Noteholders" of the same bond series under such a collective

26 M. Weidemaier & M. Gulati, "How Markets Work: The Lawyer's Version", July 2011, pp. 5, 16-17. For a discussion of old English CACs, see A. Gelpem & M. Gulati, "Foreword: Of Lawyers, Leaders, and Returning Riddles in Sovereign Debt", in: A Modern Legal History of Sovereign Debt, Law and Contemporary Problems, Vol.73, No. 4, Fall 2010, at viii-ix.

27 IMF, *supra* note 25; M. Bradley & M. Gulati, *supra* note 25, pp. 6 & 10; M. Weidemaier & M. Gulati, "A People's History of Collective Action Clauses" (2014), available at http://scholarship.law.duke.edu/cgi/viewcontent.cgi?article=5387&context=faculty_scholarship (last visited 26 Feb 2014).

28 A. Haldane, A. Penalver, V. Saporta & H. S. Shin, "Optimal Collective Action Clause Thresholds", Bank of England Working Paper No. 249, 2005, pp. 7 & 9.

29 International Primary Market Association, "Standard Collective Action Clauses (CACs) for the Terms and Conditions of Sovereign Notes", (2004). The name has since been changed to the International Credit Market Association, available at https://www.icmagroup.org/ICMAGroup/files/3c/3cc80d90-da99-4562-8ef2- f604a8e5963e.PDF (last visited 26 Feb 2014).

30 *Ibid.*, pp.2-3.

action mechanism. To phrase it in another way, ordinary CACs bind non-participating bondholders only on a series-by-series basis.[31] Accordingly, the author argues that this collective action mechanism differs from the Greek Bondholder Act, in that the operation of the latter involves the voting rights of holders of "all eligible titles" and requires a qualified majority of "the aggregate principle amount outstanding of all eligible titles"[32] to trigger the collective action mechanism. In case of any doubt concerning the interpretation of the Greek Bondholder Act, the press release issued by the Greek Ministry of Finance unambiguously stated that the proposed amendment of bond terms will bind holders of all Greek-law bonds, "if at least two thirds by face amount of a quorum of these bonds, voting collectively without distinction by series, approve the proposed amendments."[33] It is clear from the term "collectively without distinction by series" that the collective action mechanism under the Act does not operate on a series-by-series basis.

3.3.2 Greek Bondholder Act = Aggregated CAC?

(3.13) In light of the fact that the term "aggregate principle amount" has been employed in Article 4 of the Greek Bondholder Act, it would not be unreasonable to assume that the Act is in fact an aggregated CAC, that is, a CAC with an aggregation clause.

(3.14) To date, four countries have included aggregation clauses in their sovereign bonds – Argentina, the Dominican Republic, Greece and Uruguay.[34] These aggregation clauses contain a two-tier voting system: (1) 75 (Greece) or 85 (Argentina, the Dominican Republic and Uruguay) percent of the aggregated outstanding principal of *all* series to be affected, and (2) 66⅔ percent of the outstanding principal of *each* individual series to be affected.[35] To give an example, the aggregated CAC contained in the Uruguay Prospectus Supplement- Offer to Exchange dated April 10, 2003 provides as follows:

> "If Uruguay proposes any reserve matter modification to the terms and conditions of the debt securities of two or more series, or to the indenture insofar as it affects the debt securities of two or more series, in either case as part of a single trans-

31 Lee Buchheit et al., "Sovereign Bonds and the Collective Will," 51 Emory L. J. 1317 (Fall 2002), p.22; C. Schmerler, "Restructuring Sovereign Debt", in: The Law of International Insolvencies and Debt Restructuring (2006), pp. 461-462.

32 Greek Bondholder Act Article 4, *supra* note 24.

33 Hellenic Republic Ministry of Finance, *supra* note 15.

34 IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", 26 April 2013, para. 40, available at http://www.imf.org/external/np/pp/eng/2013/042613.pdf (last visited 26 Feb 2014); Cleary Gottlieb Steen & Hamilton LLP, "Collective Action Clauses with Aggregation Mechanisms", 02/11/2011.

35 IMF, *supra* note 34.

action, Uruguay may elect to proceed pursuant to provisions of the indenture providing that such modifications may be made, and future compliance therewith may be waived, for each affected series if made with the consent of Uruguay and

- the holders of not less than 85% in *aggregate principal amount of the outstanding debt securities of all series affected by that modification (taken in aggregate),* and
- the holders of not less than 66⅔% in *aggregate principal amount of the outstanding debt securities of that series (taken individually).*"[36]

(3.15) More recently, the Treaty Establishing the European Stability Mechanism ("ESM") also forced the inclusion of CACs, as of 1 January 2013, in all euro-area government securities with maturity above one year.[37] The model CAC prepared by the EU Economic and Financial Committee Sub-Committee on EU Sovereign Debt Markets includes an aggregation feature – referred to as cross-series modification – that permits changes to bind more than one series of bonds.[38] Compared with the Uruguay aggregated CAC, the Eurozone model adopts a lower threshold (i.e. 75%) to calculate the affirmative vote of the aggregate principle amount of the outstanding debt securities of *all* the series that would be affected by the proposed modification.[39]

(3.16) What is exactly an aggregated CAC or a cross-series modification? The EU Committee on EU Sovereign Debt Markets explains that a cross-series modification can be understood as a CAC that works at the series level, in that the decision of a specified majority binds all holders of all affected series, "with the important further protection that holders of any individual series of affected bonds will not be bound by the decision of the group as a whole unless they also vote in favour of the proposed modification".[40] In other words, from a sovereign debtor's prospective, the cross-series modification clause has one

36 Cleary Gottlieb Steen & Hamilton LLP, *supra* note 34.

37 Article 12 (3) of the Treaty provides that "Collective action clauses shall be included in all new euro area government securities, with maturity above one year, from July 2013, in a standardised manner which ensures that their legal impact is identical." See Treaty establishing the European Stability Mechanism, available at http://ec.europa.eu/economy_finance/articles/financial_operations/2011-07-11-esm-treaty_en.htm (last visited 26 Feb 2014).

38 The model clause is available at http://europa.eu/efc/sub_committee/cac/index_en.htm (last viewed 13 Dec. 2012). See Cliffford Chance newsletter, "Euro area member states take collective action to facilitate sovereign debt restructuring", Dec. 2012, available at http://www.cliffordchance.com/publicationviews/publications/2012/12/euro_area_memberstates takecollectiveactiont.html (last visited 26 Feb 2014).

39 "Common Terms of Reference" of the Eurozone Model CAC (17/02/2012), para. 2.2, available at http://europa.eu/efc/sub_committee/pdf/cac_-_text_model_cac.pdf (last visited 26 Feb 2014).

40 EFC Sub-Committee on EU Sovereign Debt Markets, "Model Collective Action Clause Supplemental Explanatory Note", 26 March 2012, pp. 3-4, available at http://europa.eu/efc/sub_committee/pdf/supplemental_explanatory_note_on_the_model_cac_-_26_march_2012.pdf (last visited 26 Feb 2014).

key limitation – it still enables a creditor or a group of creditors to obtain a blocking position in a particular series.[41]

(3.17) By contrast, the Greek Bondholder Act does not permit a creditor or a group of creditors to obtain a blocking position in a particular series, because the voting process only takes place at the series level. To quote the terms of the Act, "[f]or the modification of the eligible titles, it is required the participation in the procedure (quorum) of at least one half (½) of the aggregate principle amount outstanding of all eligible titles that are specified in the relevant invitation ("participating principal amount") and a qualified majority in favour of the modification of at least two thirds (⅔) of the participating capital." Phrased in this fashion, clearly the Act does not envisage any voting to take place within *each* individual series. The collective action mechanism is activated simply when a qualified majority of the aggregate principle amount outstanding of all eligible titles is reached. This interpretation is confirmed by the language of the press release issued by the Greek Ministry of Finance, which provides that the proposed amendment of bond terms will bind holders of all Greek-law bonds, "if at least two thirds by face amount of a quorum of these bonds, voting collectively without distinction by series, approve the proposed amendments."[42] Thus, the author argues that the Greek Bondholder Act also differs from the aggregated CACs.

3.3.3 Greek Bondholder Act = Cram-down in Bankruptcy Law

(3.18) Having dismissed the assumptions that the Greek Bondholder Act resembles an ordinary CAC or aggregated CAC, the following paragraphs explore the similarity between the Greek Bondholder Act and the cram-down procedure in domestic bankruptcy law systems, for ease of reference, the law system of the US It should be stated at the outset that the cram-down procedures exist in US bankruptcy law designed for all kinds of debtors, including consumers, companies and municipalities. Among these debtors, the status of municipalities is most similar to that of States.[43] As a result, the most well-known bankruptcy law for municipalities – the US Code Chapter 9 on muni-

41 IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", *supra* note 34, para. 41.

42 Hellenic Republic Ministry of Finance, *supra* note 15.

43 A municipality's insolvency is determined on the basis of a cash-flow analysis, not budget deficiency analysis; a municipality is insolvent when it is unable to pay its debts as they become due. *In re Hamilton Creek Metropolitan District*, 143 F.3d 1381 (10th Cir. 1998); *In Re City of Bridgeport*, 129 B.R. 332 (Bankr. D. Conn, 1991).

cipality bankruptcy[44] – will be used as an example for our discussion on cram down procedures.

(3.19) Under Chapter 9 municipality bankruptcy, a restructuring plan is deemed to be accepted by *a* class of creditors if creditors holding at least two-thirds in amount and more than one-half in number of all claims in that class accept the plan.[45] With respect to all classes of creditors, a reorganization plan can be confirmed if *each* class of claims or interests "has accepted the plan" or "is not impaired under the plan".[46] In the event of the failure of an impaired class to accept the plan, the plan can still be confirmed under the cram-down procedure in Section 1129(b)(1):

> "the court, on request of the proponent of the plan, shall confirm the plan… if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan."[47]

(3.20) It appears from the above text that the purpose of the cram-down is to force an impaired class to accept a proposed plan. In the context of the Greek debt restructuring, does the Greek Bondholder Act force an impaired class to accept a proposed plan? To answer this question, closer attention should be paid to the wording of the Act, which provides for one voting procedure at the level of the "aggregate principle amount outstanding of all eligible titles". In other words, the Act enables a qualified majority of bond-

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44 The U.S. Bankruptcy Code defines a 'municipality' as a 'political subdivision or public agency or instrumentality of a state.' It includes cities and towns, villages, counties, taxing districts, municipal utilities, and school districts. A municipality may be a debtor in a Chapter 9 case if (a) it has been 'specifically authorized' to be a Chapter 9 debtor, b) is 'insolvent' and (c) has either (i) obtained majority approval of creditors in each class for the proposed plan of reorganization, or (ii) negotiated in 'good faith' with creditors and failed to obtain such a majority, or (iii) is unable to negotiate with creditors because such negotiations are 'impracticable.' See 11 U.S.C. §101(40), United States Courts: Chapter 9 Municipality Bankruptcy, available at http://www.uscourts.gov/FederalCourts/BankruptcyBasics/Chapter9.aspx (last visited 26 Feb 2014); Z. Clement et al., "Important Issues in a Chapter 9 Case for a Municipality", 24 October 2011, available at http://www.nortonrosefulbright.com/knowledge/publications/94035/important-issues-in-a-chapter-9-case-for-a-municipality (last visited 26 Feb 2014).

45 The U.S. Code Title 11 Section 943(b) sets out the conditions when the court shall confirm the plan, which include that the plan complies with the provisions of this title made applicable by Section 901. Section 901(a) explicitly makes Sections 1126(c) dealing with the bankruptcy of companies applicable for municipalities, which provides that a class of claims has accepted a plan if such plan has been accepted by creditors "that hold at least two-thirds in amount and more than one-half in number" of all allowed claims. See 11 U.S.C. §§943(b), 901(a) and 1126(c).

46 11 U.S.C. §1129(a)(8). It should be noted that Section 901(a) explicitly makes Section 1129(a)(8) dealing with the bankruptcy of companies applicable for municipalities.

47 11 U.S.C. §1129(b)(1). It should be noted that Section 901(a) explicitly makes Section 1129(b)(1) dealing with the bankruptcy of companies applicable for municipalities.

holders to bind all holders of the affected domestic debt to the restructured terms even where the needed majority of creditors for the restructuring would not be attained within a single bond issue.[48] Importantly, the Act eliminates the power of a creditor or a group of creditors to obtain a blocking position in an individual issuance.[49]

(3.21) However, the elimination of the power of a creditor to obtain a blocking position in an individual issuance does not necessarily resemble the craw-down procedure. As the victim of the cram-down procedure is an impaired class of creditors, the Act has to eliminate the power of an impaired class to be qualified as a cram down procedure. Thus, the key issue at stake concerns claim classification – whether claims of an individual issuance differ from that of other issuances so that they constitute a particular class by themselves?

(3.22) The UNCITRAL Legislative Guide on Insolvency Law provides some useful guidance on class classification. The purpose of classification of claims is to "satisfy the requirements to provide fair and equitable treatment to creditors, treating similarly situated claims in the same manner and ensuring that all creditors in a particular class are offered the same menu of terms by the reorganization plan".[50] Although the general rule is to put secured creditors in one class and unsecured creditors in another, the Legislative Guide mentions that ordinary unsecured creditors can be divided into "different classes based upon their varying economic interests."[51] In determining commonality of interest, the relevant criteria may include "the nature of debts giving rise to the claims".[52]

(3.23) To apply these criteria to the Greek debt restructuring, it can be argued that the nature of an individual issuance differs from that of other issuances with different maturities. Due to the fact that the exchange offer was extended by Greece in a pre-default context, all claims will not yet have become due and payable as a result of the operation of the acceleration clause in the event of default.[53] As a result, Greece's eligible debt instruments enjoy enormous

48 IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", *supra* note 34, para. 38.
49 *Ibid.*
50 See UNCITRAL Legislative Guide on Insolvency Law (2004), p. 218, available at http://www.uncitral.org/pdf/english/texts/insolven/05-80722_Ebook.pdf (last visited 26 Feb 2014).
51 *Ibid.*, p. 222.
52 *Ibid.*
53 Bonds issued in the international markets by emerging market sovereigns typically require a vote of 25% of the outstanding bonds in order to accelerate unmatured principal following an event of default. It should be pointed out that pre-default bond restructuring happens very often. Among the 13 debt restructurings announced between 2003 and 2013, 8 restructurings were conducted in a pre-default context. These 8 debt restructurings were announced

diversity, particularly with respect to residual maturities, ranging from almost zero to 45 years.[54] Logically speaking, the nature of bonds with short-term maturity and those with long-term maturity are totally different, because the former are legally entitled to get paid before the latter.

(3.24) As far as the outcome of the restructuring is concerned, due to different residual maturities involved, the same restructuring term extended to all bondholders implies large differences in the present value haircut across the existing bonds. According to Zettelmeyer and others, the present value haircut declines with maturity, with large haircuts at the short end (in excess of 75 per cent for bonds maturing within a year) and smaller haircuts at the long end (less than 50 per cent for old bonds coming due in 2025 and beyond).[55] Such large differences confirm that the nature of an individual issuance differs from that of other issuances with different maturities, although they are all ordinary unsecured claims. As a result of these differences, claims of an individual issuance constitute a particular class by themselves. The author therefore argues that what the Greek Bondholder Act introduced was not an ordinary CAC or aggregated CAC but something similar to cram-down procedures in bankruptcy law.

3.4 Safeguard Provision for Cram-down in US Municipality Bankruptcy Law

(3.25) Given that the Greek Bondholder Act resembles cram-down procedures in bankruptcy law, an analysis of the policy implication of the *Poštová* tribunal's jurisdiction over sovereign bonds would require a closer look at how cram-down procedures are regulated.

(3.26) A second reading of Section 1129(b)(1) reveals that it provides not only the cram-down procedure but also a safeguard provision to ensure that each impaired dissent class receives minimum protection. To quote the language of Section 1129(b)(1), the court shall confirm the plan under the cram down procedure "if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and

by Dominican Republic (2004), Grenada (2004), Belize (2006), Jamaica (2010), St. Kitts and Nevis (2011), Greece (2011), Belize (2012) and Jamaica (2013). See IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", *supra* note 34, p. 22; IMF, "The Restructuring of Sovereign Debt –Assessing the Benefits, Risks and Feasibility of Aggregating Claims", 3 September 2003, p. 5; L. Buchheit et al., *supra* note 31, p.10;

54 J. Zettelmeyer, C. Trebesch and M. Gulati, *supra* note 14, p. 16.

55 *Ibid.*

has not accepted, the plan."[56] In the view of the author, Section 1129(b)(1) provides minimum protection for each impaired dissent class from two distinctive aspects. It first addresses the interests of each impaired dissent class and other creditor classes by prohibiting unfair discrimination, and then maintains a balance between the interests of each impaired dissent class and that of the debtor with the fair and equitable treatment standard. The following paragraphs will discuss them in turn.

3.4.1 Prohibition of Unfair Discrimination

(3.27) Although Section 1129(b) does not provide a definition of unfair discrimination, the case law from US bankruptcy courts on this issue is quite straightforward, which indicates that the prohibition again unfair discrimination requires equal treatment of similarly situated creditors.[57] In *re Barney & Carey Co.*, the court stated, "the unfair discrimination language of section 1129(b)(1) prohibits a debtor from proposing unreasonably different treatment between classes of similar claims."[58] The court continued that "[t]he burden is on the Debtor to show that unequal treatment between classes having the same priority does not constitute unfair discrimination."[59] In re *Tucson Self-Storage, Inc.*, the court found that "[a] plan discriminates unfairly if it singles out the holder of some claim or interest for a particular treatment."[60] Similarly, the court in *re Johns-Manville Corp.* ruled that "a plan proponent may not segregate two similar claims or groups of claims into separate classes and provide disparate treatment for those classes."[61]

3.4.2 Fair and Equitable Standard

(3.28) As regards the fair and equitable standard, Section 1129(b)(2) sets out certain specified requirements for a plan to be fair and equitable but leaves

56 11 U.S.C. §§901(a), 1129(b)(1).
57 D. Kupetz, "Municipal Debt Adjustment Under the Bankruptcy Code", 27 Urb. Law. 531 (1995), p. 18, citing *In re Orfa Corp. of Philadelphia*, 129 B.R. 404, 416 (Bankr.E.D.Pa.1991) and *In re AOV Indus., Inc.*, 792 F.2d 1140, 1150 (D.C.Cir.1986).
58 *Ibid.*, citing In re Barney & Carey Co., 170 B.R. 17, 25 (Bankr.D.Mass.1994).
59 *Ibid.*
60 *Ibid.*, n. 292, citing *Oxford Life Ins. Co. v. Tucson Self-Storage, Inc.*, 166 B.R. 892, 898 (Bankr.9th Cir.1994).
61 *Ibid.*, citing *In re Johns-Manville Corp.*, 68 B.R. 618, 636 (Bankr.S.D.N.Y.1986), aff'd, 78 B.R. 407 (Bankr.S.D.N.Y.1987), aff'd, 843 F.2d 636 (2d Cir.1988).

the substance of the term "fair and equitable" open to interpretation.[62] In Chapter 11 cases involving the bankruptcy of corporates, the phrase "fair and equitable" has been interpreted to require that unsecured creditors be paid in full first before junior equity holders can be paid.[63] This interpretation is, however, not applicable in a Chapter 9 context, as a municipality does not have any equity holder. By contrast, US bankruptcy courts have construed that a Chapter 9 plan is fair and equitable if it is balanced and the debtor has taken reasonable steps to increase revenue and cut costs before proposing debt renegotiation.[64] In applying this standard, courts analyze whether the amount to be received by dissenting creditors under the plan is "all that they can reasonably expect in the circumstances."[65]

(3.29) When interpreting the meaning of "all that [dissenting creditors] can reasonably expect in the circumstances", some courts have required the debtor to exercise its taxing power to a greater extent in the facts of the case presented.[66] Other courts have held that it is not necessary that all taxes collected go to the payment of creditors and that taxes be increased where evidence indicates that this would not be feasible.[67] Indeed, while raising taxes could

62 Section 1129(b)(2)(A) provides that secured claims may be treated fairly and equitably if the plan, (a) allows the secured creditor to retain its lien and to receive cash payments over time which have a present value equal to the value of its collateral as of the effective date of the plan; (b) provides for a sale of the secured creditor's collateral at which it can credit bid or (c) provides the secured creditor with the indubitable equivalent of its claim, including, among other things, returning the creditor's collateral to it. Section 1129(b)(2)(B) provides that unsecured creditors who are not paid in full are still treated fairly and equitably under a plan as long as any claim or interest that is junior will not receive or retain under the plan or on account of such junior claim or interest any property. See 11 U.S.C. §1129(b)(2).

63 See *Case v. Los Angeles Lumber Products*, 308 U.S. 106 (1939).

64 B. Chandler & M. Kaufman, "Maybe Taxes Aren't So Certain: What is 'Fair and Equitable' in a Chapter 9 Plan?", American Bankruptcy Institute Journal, February 2013, p. 2, available at http://www.mckennalong.com/media/resource/1984_American%20Bankruptcy%20Institute%20Journal.pdf (last visited 26 Feb 2014).

65 See *Lorber v. Vista Irrigation Dist.*, 127 F.2d 628, 639 (9th Cir. 1942); *West Coast Life Insurance Company et al. v. Merced Irrigation District*, 114 F.2d 654 (9th Cir. 1940); *Moody v. James Irrigation District*, 114 F.2d 685 (9th Cir. 1940); *Bekins v. Lindsay-Strathmore Irrigation District*, 114 F.2d 680 (9th Cir. 1940), *Jordan v. Palo Verde Irrigation District*, 114 F.2d 691 (9th Cir. 1940).

66 In *Fano v. Newport Heights Irr. Dist.*, the court denied the proposed plan and stated that 'we are unable to find any reason why the tax rate should not have been increased sufficiently to meet the District's obligations or why it can be said that the plan is 'equitable' and 'fair' and for the 'best interest of the creditors' with no sufficient showing that the taxing power was inadequate to raise the taxes to pay them'. See *Fano v. Newport Heights Irr. Dist.*,114 F.2d 563 (9th Cir. 1940).

67 In *Lorber v. Vista Irr. Dist.*, the court analyzed the debtor's situation and found that '55 cents on the dollar was the maximum that the District could reasonably pay on outstanding bonds." See *Lorber v. Vista Irrigation Dist.*, 143 F.2d 282 (9th Cir. 1944). In *re Corcoran Hosp. Dist.*, the court 'looked at the insolvency of the debtor and whether the debtor could, in

help the municipality to pay back its debt, it might be detrimental to attract new residents and corporations and thus would adversely affect the municipality's long-term revenues.[68] The limited body of case law suggests that to what extent the debtor shall impose new or increased taxes should be determined on a case-by-case basis.[69] Besides raising taxes, other reasonable steps the debtor shall take to increase revenue and reduce costs include (1) checking existing contracts to look for inefficiencies; (2) negotiating modifications to collective-bargaining agreements and retiree benefits; (3) cutting labor costs; (4) selling or leasing municipal assets; (5) privatizing or outsourcing certain services; and (6) securing financial support.[70]

3.5 ICSID Arbitration as the Best Forum to Develop a Safeguard Provision for Cram-down

(3.30) An overview of the safeguard provision for cram-down procedures under the US municipality bankruptcy law tells us that the current legal regime of sovereign debt restructuring is seriously flawed with respect to creditor protection. In the absence of any bankruptcy rules for States, the author argues, ICSID arbitration could serve as the best forum to develop a safeguard provision for cram-downs employed in sovereign debt restructuring similar to those in the US municipality bankruptcy law. This section discusses, in turn, the possible safeguard principles in sovereign debt litigations and that under investment treaties.

3.5.1 Possible Safeguard Principles in Sovereign Debt Litigations

(3.31) Historically, since the doctrine of "absolute" sovereign immunity did not permit States be sued in foreign domestic courts without their express

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fact, raise taxes sufficient to pay the bondholders in full' and concluded that 'the debtor Hospital District could not raise taxes sufficient to pay more to Class 5'. See *In re Corcoran Hosp. Dist.*, 233 B.R. 449, 459-60 (Bankr. E.D. Cal. 1999). In *Newhouse v. Corcoran Irr. Dist.*, the court stated that '[t]he bankruptcy of a public entity, however, is very different from that of a private person or concern. The operative assets of an irrigation district and the value of the land of the District, of course, have their evidentiary value as to the amount of money the District can reasonably raise to meet its indebtedness.' See *Newhouse v. Corcoran Irr. Dist.*, 114 F. 2d 690 (9th Cir. 1940).

68 B. Chandler & M. Kaufman, *supra* note 64.

69 Main factors to take into account when deciding whether a debtor shall impose new or increased taxes include (1) the tax rates of neighboring municipalities; (2) the employment market; (3) the local population and the potential impact of increased tax burden; (4) prospects for attracting new business with increased tax burden; and (5) any new financial needs of the municipality. See *Ibid.*

70 *Ibid.*

consent, disappointed private lenders to foreign States had very few options other than to seek the help of their own governments, known as "diplomatic protection".[71] These governments have pressured the sovereign debtor into payment or settlement or brought the dispute to international courts and tribunals.[72] However, persuading governments to take up their nationals' claims has never been an easy undertaking, and its success depends largely on governments' economic and political objectives. Since the 1970s, many countries have adopted the doctrine of "restrictive" sovereign immunity on jurisdiction, which permits sovereign States to be sued for their private acts.[73] Consequently, bondholders are entitled to sue the sovereign debtor directly in foreign domestic courts.[74]

(3.32) Traditionally, sovereign debt claims in foreign domestic courts have been exclusively based on an allegation of the debtor's failure to perform the contract. Given that the contract terms in respect of performance are generally unambiguous, the dispute in such debt claims mainly concerns the issue of sovereign immunity, that is, to what extent the restrictive sovereign immunity principle applies. On most occasions, legal battles over sovereign immunity have been extremely challenging for creditors. First, such battles often last many years and most bondholders do not have the financial recourses to fight until the end. Second, even if creditors obtain a favorable judgment in the end, they are not yet winners until they are able to enforce it. Often attempts to enforce the judgment and attach property in the sovereign debtor's territory may face objections based on public policy, efforts to enforce it abroad may fail due to the sovereign's lack of attachable assets in foreign countries and the principle that certain assets located abroad cannot be attached due to their special characteristics (i.e. diplomatic missions, central bank reserves, military

71 L. Buchheit, "The Role of the Official Sector in Sovereign Debt Workouts", 6 Chi J Intl L 333, 2005, p. 335.

72 Examples are *French Company of Venezuelan Railroads Case* (1905); *Canavero Claim* (Italy v. Peru, PCA, 1912); *French Claims Against Peru* (PCA, 1921); *Payment of Various Serbian Loans Issued in France* (PCIJ, 1929); *Payment in Gold of Brazilian Federal Loans Contracted in France* (PCIJ, 1929); *Societe Commerciale De Belgique* (Belgium v. Greece, PCIJ, 1939); *Certain Norwegian Loans* (ICJ, France v. Norway, 1957). See generally M. Waibel, Sovereign Defaults Before International Courts and Tribunals, *supra* note 12, p. 22.

73 Examples include the Sovereign Immunities Acts of the United States. (1976), United Kingdom (1978), Singapore (1979), Pakistan (1981), South Africa (1981), Canada (1982), and Australia (1985). See generally H. Fox, The Law of State Immunity (2008, Oxford).

74 Schumacher recently conducted empirical research concerning sovereign debt litigation filed against debtor governments in the US and UK courts between 1976 and 2010. This research shows that 108 cases were filed in the US and the UK by foreign banks, bondholders and other commercial creditors during this period, and that these cases relate to 29 of the 180 sovereign debt restructurings with private creditors (16%). It further reveals that 27 out of 69 debtor governments have been sued. See Schumacher et al., "Sovereign Defaults in Court: The Rise of Creditor Litigation 1976-2010", p.8, available at http://dx.doi.org/10.2139/ssrn.2189997 (last visited 26 Feb 2014).

assets etc.).[75] Furthermore, the legal framework concerning the recognition and enforcement of foreign court judgments does not provide much help either. As of today, the *Convention of 1 February 1971 on the Recognition and Enforcement of Foreign Judgments in Civil and Commercial Matters* concluded under the framework of the Hague Conference on Private International Law only has five contracting States.[76]

(3.33) Over the past decade, various creditors in different jurisdictions have made attempts to circumvent the enforcement problem by arguing that, as a result of the *pari passu* clause, sovereign debtors are prevented from making payments to other creditors without paying the litigating creditors on a *pro rata* basis.[77] A *pari passu* clause is a standard clause included in public or private international unsecured debt obligations, which often provides that "[Country X] shall ensure that its obligations hereunder shall rank pari passu among themselves and with all of its other present and future unsecured and unsubordinated Public Debt."[78] In September 2000, a Brussels Court of Appeals issued a restraining order in *Elliott* prohibiting a fiscal agent and a payment settlement system from paying interest on Peru's Brady Plan Bonds.[79] In response to this decision, INC Belgian Law 4765 (C-2004/03482) was passed in November 2004 to prohibit attachment of cash accounts held with Belgium clearing systems.[80] Moving to the US courts, a New York trial

75 R. Olivares-Caminal, Legal Aspects of Sovereign Debt Restructuring (2009, Sweet & Maxwell), paras. 2-001, 2-002, 2-004.

76 The five contracting States are Albania, Cyprus, the Netherlands, Portugal and Kuwait. See HccH official website, status table, available at http://www.hcch.net/index_en.php?act=conventions.status&cid=78.

77 See *Elliott Assocs. LP*, unreported September 26, 2000, General Docket No. 2000/QR/92, Court of Appeal of Brussels, 8th Chamber; *Red Mountain Finance Inc v. Democratic Republic of Congo*, No. CV 00-0164 R (C.D. Cal. 29 May 2001); *Republique Du Nicaragua v. INC invs. LLC No.2003/KR/334*, p. 2 (Ct. App. Brussels, 9th Chamber, 2004); *Macrotenic International Corp v. Republic of Argentina and EM Ltd v. Republic of Argentina* (S.D.N.Y. January 12, 2004) (No.02 CV 5932 (TPG), No. 03 CV 2507 (TPG)); *NML Capital, Ltd. v. Republic of Argentina*, No. 12-105-(L) (2d Cir. 26 Oct. 2012). See generally M. Gulati and R. Scott, "The Three and a Half Minute Transaction: Boilerplate and the Limits of Contract Design" (October 5, 2011), Columbia Law and Economics Working Paper No. 407; R. Olivares-Caminal, Legal Aspects of Sovereign Debt Restructuring, *supra* note 75; L. Buchheit & J. Pam, "The Pari Passu Clause in Sovereign Debt Instruments", 53 Emory L.J. 913 (2004).

78 R. Olivares-Caminal, Legal Aspects of Sovereign Debt Restructuring, *supra* note 75, p. 84; Offering Memorandum of the Government of Belize dated December 18, 2006, for the exchange of US Dollar Bonds due 2029, p. 142.

79 M. Gulati and R. Scott, *supra* note 77, pp. 23-24, citing Elliott Assocs. LP, unreported September 26, 2000, General Docket No. 2000/QR/92, Court of Appeal of Brussels, 8th Chamber.

80 R. Olivares-Caminal, "The Pari Passu Interpretation in the Elliott Case: A Brilliant Strategy But An Awful (Mid-Long Term) Outcome", Hofstra Law Review, vol 40, no 39. p. 52 (2012), citing MONITEUR BELGE [M.B.] [Official Gazette of Belgium], Dec. 28, 2004, 85,854, http://www.ejustice.just.fgov.be/mopdf/2004/12/28_1.pdf.

court in January 2014 was asked to consider whether the *pari passu* clause in Argentina's bonds could not be used by judgment creditors as a legal basis to interfere with Argentina's payment of its other indebtedness.[81] The court did not answer the core question but issued a discovery order asking Argentina to divulge information about government property outside the country that is used for commercial purposes.[82] More recently, in October 2012, the United States Court of Appeals for the Second Circuit in *NML Capital Ltd. v. Republic of Argentina* affirmed the trial court's decision to issue injunctions designed to remedy Argentina's breach of the *pari passu* clause in certain bond indentures, on the grounds that Argentina had issued new debt pursuant to exchange offers in 2005 and 2010 and was making the required payments on this new debt, but had declared through legislation that it would make no payments to those still holding the old bonds.[83]

(3.34) Based on the foregoing, the author argues that it is unlikely that legal battles at domestic courts would lead to the creation of safeguard principles for cram-down in sovereign debt restructuring in line with those in municipality bankruptcy law. Having noted that the legal basis for sovereign debt litigations has mainly been the debtor's failure to perform the contract, the author contends that none of these court decisions would touch upon the notion of unfair discrimination and fair and equitable treatment. In respect of the *pari passu* clause, the author maintains that the meaning of this clause is highly controversial and it is uncertain that other courts will follow the *NML*

81 R. Olivares-Caminal,"To Rank Pari Passu or Not to Rank Pari Passu: That is The Question in Sovereign Bonds After the Latest Episode of the Argentine Saga", Law & Business Review of the Americas, vol 15, no 4, p. 753 (2009), citing *Macrotenic International Corp v. Republic of Argentina and EM Ltd v. Republic of Argentina* (S.D.N.Y. January 12, 2004) (No.02 CV 5932 (TPG), No. 03 CV 2507 (TPG)).

82 R. Olivares-Caminal, Legal Aspects of Sovereign Debt Restructuring, *supra* note 75, p. 90.

83 The Second Circuit affirmed the injunctions issued by the trial court that requires Argentina to make ratable payments to plaintiffs concurrent with or in advance of its payments to holders of old bonds, and asked the trial court to further clarify how the payment formula in the injunction will operate. The trial court clarified, in a subsequent order issued on 21 November 2012, that the payment formula in the injunction is intended to operate as follows: whenever Argentina pays any amount due under the terms of the exchange bonds, it must concurrently or in advance pay plaintiffs the same *percentage* of the amount due to them. See *NML Capital, Ltd. v. Republic of Argentina*, No. 12-105-(L) (2d Cir. 26 Oct. 2012); *NML Capital, Ltd. v. Republic of Argentina*, 08 Civ. 6978 (TPG), 09 Civ. 1707 (TPG), 09 Civ. 1708 (TPG) (S.D.N.Y., 21 Nov. 2012), available at http://www.shearman.com/argentine-sovereign-debt/ (last visited 26 Feb 2014). For a discussion of this case, see Global Law Intelligence Unit, Allen & Overy LL.P, "The pari passu clause and the Argentine case", 27 Dec. 2012; W. Weidemaier, "Sovereign Debt After NML v. Argentina", Capital Markets Law Journal, available at http://ssrn.com/abstract=2199655 (last visited 26 Feb 2014); R. Zamour, "NML v. Argentina and the Ratable Payment Interpretation of the Pari Passu Clause", Yale Journal of International Law, Vol. 38 (Spring 2013).

Capital decision.[84] In any event, the author argues that the *pari passu* clause only relates to the concept of equal treatment but not fair and equitable treatment.

(3.35) Furthermore, in the author's view, it is beyond doubt that the exercise of CACs changes the contractual obligations under the sovereign bond and prevents non-participating bondholders from bringing the contractual dispute to domestic courts. Notably, the US Court of Appeals for the Second Circuit explicitly stated in *NML Capital, Ltd. v. Republic of Argentina* that CACs "effectively eliminate the possibility of 'holdout' litigation" and "it is highly unlikely that in the future sovereigns will find themselves in Argentina's predicament" because CACs "have been included in 99% of the aggregate value of New York-law bonds issued since January 2005".[85]

3.5.2 Possible Safeguard Principles under Investment Treaties

(3.36) Since 2006, four groups of foreign bondholders have brought arbitrations under bilateral investment treaties at ICSID against sovereign debtors following the debt crises.[86] Recourse to ICSID arbitration was mainly motivated by the enforcement regime under the ICSID Convention, which requires its 147 member States to recognize and enforce an arbitral award as if it were a final judgment of a court in that State.[87] Under most investment treaties, foreign investors are entitled to initiate arbitration against the host country directly for alleged breaches of treaty obligations through arbitration clauses, which often include fair and equitable treatment principle, full protection and security, no expropriation without prompt, adequate and effective compensation, as well as national and most favored nation treatment principle.[88] This section analyses the fair and equitable treatment principle and argues that such a principle could serve as a safeguard provision for cram-down in sovereign debt restructuring. Before engaging in the discussion, it should be recalled that the safeguard provision for cram-down under the US municipality

84 See Global Law Intelligence Unit, Allen & Overy LL.P, "The pari passu clause and the Argentine case"; M. Wright, "The Pari Passu Clause in Sovereign Bond Contracts: Evolution or Intelligent Design?", 1 Hofstra L. Rev. 40 (2011); B. Remy Chabot & M. Gulati, "Santa Anna and His Black Eagle: The Origins of the Pari Passu", 18 Feb 2014, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2397929 (last visited 26 Feb 2014).

85 See *NML Capital, Ltd. v. Republic of Argentina*, No. 12-105-(L), *supra* note 17, p. 27.

86 *Abaclat and others v. Argentine Republic*, *Giovanni Alemanni and others v. Argentine Republic*, *Giordano Alpi and others v. Argentine Republic*, and *Poštová banka, a.s. and ISTROKAPITAL SE v. Hellenic Republic*.

87 ICSID Convention Art. 54(1), available at https://icsid.worldbank.org/ICSID/ICSID/RulesMain.jsp (last visited 26 Feb 2014).

88 N. Blackaby et al., "Chapter 8. Arbitration Under Investment Treaties", in: Redfern and Hunter on International Arbitration, 5th ed, 2009, paras. 8.09, 8.58-8.112.

bankruptcy law provides that the plan shall not "discriminate unfairly" and shall be "fair and equitable" with respect to each impaired dissent class.

3.5.2.1 Overview of the FET Principle

(3.37) The fair and equitable treatment principle is a well-established clause in the vast majority of investment agreements, and is often drafted in three ways: (1) combined with a reference to general international law, (2) combined with a reference to customary international law, and (3) combined with other investment guarantees, for instance, the guarantee of protection and security and the obligations of most-favored-nation and national treatment.[89] According to some commentators, the issue of whether the FET is included in a separate clause or combined with other investment guarantees is not a substantive question but a stylistic one.[90] When the FET is combined with a reference to either general international law or customary international law, it generally provides that each contracting party shall accord to investments of investors of another party treatment in accordance with [international law][customary international law], including fair and equitable treatment and full protection and security.[91]

(3.38) It is worth noting that a long-standing doctrinal debate exists with respect to the FET principle. Some argue that the FET is limited to the international minimum standard of customary international law, on the basis that the formulation of such a principle is vague and indeterminate and equating it with the international minimum standard could avoid the difficulties in addressing this norm.[92] They refer to the writings and decisions on international minimum standard to argue that there exists an established and well-known body of legal principles in customary international law.[93] On the contrary, other commentators suggest that the international minimum standard is as indeterminate as the FET principle.[94] They note that if the two concepts were intended to be interchangeable, states would have specified this expressly in their investment agreements; instead, the combination of the FET principle with a reference to international law indicates that international law only plays a complementary role.[95] Importantly, in the context of NAFTA, on 31 July 2001

89 R. Klager, "Fair and Equitable Treatment" in International Investment Law (Cambridge, 2011), pp.14-20.
90 *Ibid.*, p.17.
91 *Ibid.*, pp.17 & 19.
92 G. Sacerdoti, Bilateral Treaties and Multilateral Instruments on Investment Protection, RdC 269 (1997), p. 341; R. Klager, *supra* note 89, p. 56.
93 *Ibid.*
94 *Ibid.*, p. 58.
95 UNCTAD, "Fair and Equitable Treatment", UNCTAD/ITE/IIT/11 (Vol. III) (1999), p.13; R. Klager, *supra* note 89, p. 59.

the NAFTA Free Trade Commission issued a note of interpretation, which shall be binding on arbitral tribunals and provides that the concept of FET does not go beyond the customary international law minimum standard.[96]

(3.39) As far as case law is concerned, ICSID tribunals have adopted two main approaches dealing with the relation between FET and the international minimum standard in customary international law.[97] The first approach addresses FET as being equated with the minimum standard of treatment and was for example adopted by the *CMS* tribunal.[98] The second approach views FET as an autonomous concept, which is considered as higher standards than required by international law and more protective of investors' rights.[99] Between these two approaches, some tribunals chose not to decide on this issue. For instance, the *BG v. Argentina* tribunal stated that Argentina's actions fall below the minimum standard and it is consequently not necessary to examine the standard of protection under the Argentine-UK BIT.[100]

3.5.2.2 Interpretation of the FET Principle

(3.40) Over the past decade, investment treaty tribunals have struggled unsuccessfully to define the obligation of the FET principle included in a vast majority of over 2,600 bilateral investment treaties.[101] Recent case law indicates that most tribunals find it unnecessary to engage in an extensive discussion of the definition of the FET standard, and only analyze the meaning of FET when it is applied to a set of specific facts. For instance, the tribunal in *Swisslion v. Macedonia* did not provide a precise definition of the FET standard and limited itself to subscribe "the view expressed by certain tribunals that the standard basically ensures that the foreign investor is not unjustly treated, with due regard to all surrounding circumstances, and that it is a means to guarantee justice to foreign investors."[102]

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96 R. Klager, *supra* note 89, pp. 70-71.

97 *El Paso Energy International Company v. Argentina* (ICSID Case No. ARB/03/15), Award of 31 October 2011, para. 331; *Impregilo S.p.A. v. Argentine Republic* (ICSID Case No. ARB/07/17), Award of 21 June 2011, paras. 286-288.

98 *GMS Gas Transportation Company v. Argentina* (ICSID Case No. ARB/01/8), Award of 12 May 2005, para. 284; *SAUR International SA v. Republic of Argentina* (ICSID Case No. ARB/04/4), Decision on Jurisdiction and Liability, paras. 491-494.

99 *Azurix Corp. v. The Argentine Republic* (ICSID Case No. ARB/01/12), Award of 14 July 2006, para. 361; *Deutsche Bank v. Democratic Socialist Republic of Sri Lanka* (ICSID Case No. ARB/09/2), Award of 31 October 2012, paras. 418-419.

100 *BG Group Plc v. Argentina* (UNCITRAL), Award of 24 December 2007, para. 291.

101 K. J. Vandevelde, "A Unified Theory of Fair and Equitable Treatment", New York University Journal of International Law and Politics (JILP), Vol. 43, No. 1, p. 43, 2010, p. 44.

102 *Swisslion DOO Skopje v. The Former Yugoslav Republic of Macedonia* (ICSID Case No. ARB/09/16), Award of July 6, 2012, para. 273, citing *PSEG Global, The North American Coal Corporation, and Konya Ingin Electrik ve Ticaret Sirketi v. Republic of Turkey* (ICSID Case No. ARB/02/5),

(3.41) Among those tribunals that made an attempt to define the FET standard, the tribunal in *Deutsche Bank v. Sri Lanka* confirmed the non-exhaustive definition of the FET standard offered by the *Waste Management* tribunal and listed a few components of the FET definition:

- "protection of legitimate and reasonable expectations which have been relied upon by the investor to make the investment;
- good faith conduct although bad faith on the part of the State is not required for its violation;
- conduct that is transparent, consistent and not discriminatory, that is, not based on unjustifiable distinctions or arbitrary;
- conduct that does not offend judicial propriety, that complies with due process and the right to be heard."[103]

(3.42) In this connection the author submits that while the maximum scope of the FET principle remains unclear, its minimum reach seems rather clear-cut. The sub-sections below analyze two notions covered by the FET standard that are similar to the safeguard provision under municipality bankruptcy law: (a) prohibition of unfair discrimination, and (b) legitimate expectations and the obligation of proportionality.

a. Prohibition of Unfair Discrimination

(3.43) The most relevant case law on unfair discrimination is *Saluka Investment BV v. Czech Republic*, which concerned the gradual privatization of the Czech banking sector.[104] In this case, the IPB bank that had been fully privatized could not participate in a government assistance program and subsequently collapsed, while three still mainly stated-owned banks obtained assistance from that program.[105] In explaining the meaning of FET and non-discrimination, the tribunal stated "any differential treatment of a foreign investor must not be based on unreasonable distinctions and demands, and must be justified by showing that it bears a reasonable relationship to rational policies not motivated by a preference for other investments over the foreign-owned investment."[106] The tribunal further developed a test for the determination of discriminatory conduct, which provides that a conduct is considered as dis-

Award of 19 January 2007, para. 239; *El Paso Energy International Company v. The Argentine Republic* (ICSID Case No ARB/03/15), Award of 31 October 2011, para. 373.

103 *Deutsche Bank v. Democratic Socialist Republic of Sri Lanka* (ICSID Case No. ARB/09/2), Award of 31 October 2012, para. 420; *Waste Management, Inc. v. United Mexican States* (ICSID Case No. ARB(AF)/00/3), Award of 30 April 2004, para. 98.

104 *Saluka Investment BV v. Czech Republic* (UNCITRAL), Partial Award of 17 March 2006.

105 R. Klager, *supra* note 89, p. 193.

106 Saluka Investment BV v. Czech Republic, *supra* note 104, para. 307.

criminatory if similar cases are treated differently and without reasonable justification.[107]

b. Legitimate Expectations and the Obligation of Proportionality

(3.44) Many tribunals have dealt with the concept of legitimate expectations in the context of the FET principle. For instance, in *Tecmed v. Mexico*, the tribunal stated that the FET principle requires contracting States to "provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment."[108] In explaining what are the basic expectations, the *Tecmed* tribunal continued that the host State is expected to "act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations."[109] Similarly, the tribunal in *Saluka v. Czech Republic* also mentioned that a foreign investor may "properly expect that the [Government] implements its policies bona fide by conduct that is, as far as it affects the investor's investment, reasonably justifiable by public policies and that such conduct does not violate the requirements of consistency, transparency, even-handedness and non-discrimination."[110]

(3.45) In the recent years, some tribunals have rejected a broad interpretation of the concept of legitimate expectations. For instance, the tribunal in *El Paso Energy v. Argentina* stated that the legitimate expectations are not solely the subjective expectations of investors but objective expectations under particular circumstances and with due regard to the rights of the State.[111] Importantly, several tribunals expressly associated the notion of legitimate expectations with "a promise of the administration on which the Claimants rely to assert a right that needs to be observed".[112] More recently, the tribunal in *Ulysseas v. Ecuador* also quoted with approval the holding of the tribunal in *EDF v. Romania* according to which, "[e]xcept where specific promises or representations are made by the State to the investor, the latter may not rely on a bilateral

107 *Ibid.*, para. 313.

108 *Técnicas Medioambientales Tecmed, S.A. v. United Mexican States* (ICSID Case No. ARB (AF)/00/2), Award of 29 May 2003, para. 154.

109 *Ibid.*

110 *Saluka Investments B.V. v. Czech Republic*, *supra* note 104, para. 307.

111 *El Paso Energy International Company v. Argentina*, *supra* note 97, para. 358.

112 P*SEG Global, Inc., The North American Coal Corporation, and Konya Ingin Electrik Üretim ve Ticaret Limited Sirketi v. Republic of Turkey*, *supra* note 102, paras. 239-241; *Metalpar S.A. and Buen Aire S.A. v. The Argentine Republic* (ICSID Case No. ARB/03/5), Award on the Merits of 6 June 2008, para. 183.

investment treaty as a kind of insurance policy against the risk of any changes in the host State's legal and economic framework".[113] Similarly, the tribunal in *Toto v. Lebanon* noted that, in the absence of a stabilization clause or similar commitment, changes in the regulatory framework would be considered as violation of the FET principle "only in case of a drastic or discriminatory change in the essential features of the transaction."[114]

(3.46) On the other hand, there are also several tribunals that found – "[w]hile specific assurances given by the host State may reinforce the investor's expectations, such an assurance is not always indispensable".[115] In clarifying this view, the *Electrabel v. Hungary* tribunal noted that:

> "While the investor is promised protection against unfair changes, it is well-established that that the host State is entitled to maintain a reasonable degree of regulatory flexibility to respond to changing circumstances in the public interest. Consequently, the requirement of fairness must not be understood as the immutability of the legal framework, but as implying that subsequent changes should be made fairly, consistently and predictably, taking into account the circumstances of the investment."[116]

(3.47) More importantly, the FET principle has on several occasions been interpreted to import an obligation of proportionality. In *Tecmed v. Mexico*, the tribunal relied on case law from the European Court of Human Rights and stated that "[t]here must be a reasonable relationship of proportionality between the charge or weight imposed to the foreign investor and the aim sought to be realized by any expropriatory measure."[117] The tribunal in *Azurix v. Argentina* endorsed the reliance in *Tecmed* on case law from the European Court of Human Rights, and emphasized the need for proportionality between the means employed and the aim.[118]

113 *Ulysseas, Inc. v. The Republic of Ecuador* (UNCITRAL), Final Award, 12 June 2012, para. 249 quoting *EDF International S.A., SAUR International S.A. and León Participaciones Argentinas S.A. v. Argentine Republic* (ICSID Case No. ARB/03/23), Award of 11 June 2012, para 217.

114 *Toto Costruzioni Generali S.p.A. v. The Republic of Lebanon* (ICSID Case No. ARB/07/12), Award of 7 June 2012, para. 244.

115 *Electrabel S.A. v. Republic of Hungary* (ICSID Case No. ARB/07/19), Decision on Jurisdiction, Applicable Law and Liability dated 30 November 2012, para. 7.78, citing *MTD v Chile* (ICSID Case No. ARB/01/7), Award of 25 May 2004; *GAMI Investments v Mexico* (UNCITRAL), Final Award of 15 November 2004; and *SD Myers v Canada* (UNCITRAL), Second Partial Award of 21 October 2002.

116 *Electrabel S.A. v. Republic of Hungary*, *supra* note 115, para. 7.77.

117 *Técnicas Medioambientales Tecmed, S.A. v. United Mexican States*, *supra* note 108, para. 122. In support of this proposition, the tribunal cited several decisions of the European Court of Human Rights: In the case of *Mellacher and Others v. Austria*, Judgment of December 19, 1989, 48, p.24; In the case of *Pressos Compañía Naviera and Others v. Belgium*, Judgment of November 20, 1995, 38, p. 19.

118 Azurix Corp. v. The Argentine Republic, *supra* note 99, para. 311.

(3.48) More recently, in *Occidental v. Ecuador*, the tribunal also interpreted the FET principle as requiring an obligation of proportionality. Having noted that "the overriding principle of proportionality requires that any such administrative goal must be balanced against the Claimants' own interests and against the true nature and effect of the conduct being censured", the tribunal found that the price paid by the claimants was out of proportion to the wrongdoing.[119]

b. Necessity Defense

(3.49) In nearly all investment arbitrations brought by foreign investors against Argentina after the 1999-2001 debt crisis, Argentina has invoked the defense that it should be excused from liability for damages to foreign investments, including a FET breach, on the basis of the state of necessity during the crisis. This necessity defense was raised under both bilateral investment treaties[120] and customary international law.[121]

(3.50) Up until now, these tribunals have interpreted the necessity defense claimed by Argentina in a very different manner, which makes it difficult to draw a meaningful conclusion. One good example to illustrate such difficulty is the four ICSID cases concerning investments in the Argentina's gas industry (i.e. CMS, LG & E, Enron, and Sempra).[122] The facts giving rise to these four

119 *Occidental Petroleum Corporation and Occidental Exploration and Production Company v. The Republic of Ecuador* (ICSID Case No. ARB/06/11), Award of 5 October 2012, para. 450.

120 For example, Article XI of the Argentina-U.S. Bilateral Investment Treaty provides that: "The 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". See Article XI of the Argentina-U.S. BIT, available at http://unctad.org/sections/dite/iia/docs/bits/argentina_us.pdf (last visited 26 Feb 2014).

121 Article 25 of the International Law Commission's Draft Articles on Responsibility of States for Internationally Wrongful Acts defines the customary international law defense of necessity as follows:
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.

122 *CMS Gas Transmission Company v. The Republic of Argentina* (ICSID Case No. ARB/01/8); *LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc .v. Argentine Republic* (ICSID Case No. ARB/02/1); *Enron Creditors Recovery Corp. v. Argentine Republic* (ICSID

disputes were practically identical.[123] In the early 1990s, Argentina adopted a regulatory framework for the gas sector containing specific guarantees to attract capital aboard, which included guarantees that tariffs would be calculated in US dollars and converted into pesos for billing purposes, and would not be subject to freezing or price controls without compensation.[124] While three of these tribunals rejected Argentina's necessity defense, the fourth tribunal (i.e. LG & E) found in favor of Argentina.[125] Further complicating matters, two of the three decisions against Argentina (i.e. Enron, and Sempra) were subsequently annulled with respect to the issue of necessity defense.[126] Although the CMS decision was not annulled, the annulment committee recognized several "errors of law" in the part of the award on the necessity defense.[127] It is worth mentioning that ICSID awards may be annulled only in limited situations, such as manifest excess of powers or failure to state reasons on which it based its decision.[128] Overall, these original awards and annulment decisions differed as to the interpretation of the necessity defense both under the Argentina-United States bilateral investment treaty and customary international law.

(3.51) More recently, in *EDF et al. v. Argentina*, the tribunal stated that "[n]ecessity must be construed strictly and objectively, not as an easy escape

Case No. ARB/01/3); and *Sempra Energy Int'l v. Argentine Republic* (ICSID Case No. ARB/02/16).

123 E. A. Martinez, "Understanding the Debate over Necessity: Unanswered Questions and Future Implications of Annulments in the Argentine Gas Cases", Duke Journal of Comparatives & International Law, Vol. 23:149, p. 152.

124 *Enron Corp. and Ponderosa Assets LP v. Argentina* (ICSID Case No. ARB/01/3), Award of 22 May 2007, para. 264; R. Klager, *supra* note 89, p. 172.

125 *CMS Gas Transmission Company v. The Republic of Argentina* (ICSID Case No. ARB/01/8), Award of 12 May 2005, para. 331; *Enron Corp. and Ponderosa Assets LP v. Argentina*, *supra* note 124, para. 313; *Sempra Energy Int'l v. Argentine Republic* (ICSID Case No. ARB/02/16), Award of 28 September 2007, para. 355; and *LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc .v. Argentine Republic* (ICSID Case No. ARB/02/1), Decision on Liability of 3 Oct 2006, paras. 239-240, 258-259.

126 *Sempra Energy Int'l v. Argentine Republic*, Decision on the Argentine Republic's Application for Annulment of the Award, paras. 222-23 (June 29, 2010); *Enron Creditors Recovery Corp. v. Argentine Republic*, Decision on the Application for Annulment of the Argentine Republic, para. 395 (July 30, 2010).

127 *CMS Gas Transmission Company v. The Republic of Argentina*, Decision of the Ad Hoc Committee on the Application for Annulment of the Argentine Republic dated 25 September 2007, para. 158-159.

128 Under Article 52 of the ICSID Convention, each Party may request annulment of an award on one or more of the following grounds: "(a) that the Tribunal was not properly constituted; (b) that the Tribunal has manifestly exceeded its powers; (c) that there was corruption on the part of a member of the Tribunal; (d) that there has been a serious departure from a fundamental rule of procedure; or (e) that the award has failed to state the reasons on which it is based." See *supra* note 87.

hatch for host states wishing to avoid treaty obligations which prove difficult."[129] In *Continental Casualty Company v. Argentina*, the tribunal rejected the defense of necessity in respect of the restructuring of certain treasury bills and named three factors that influenced its decision. The tribunal pointed out that the debt restructuring was offered at late date when Argentina's financial situation was moving towards normality.[130] It also considered the discounted value of the debt that Argentina unilaterally offered to recognize and the condition that any other rights, including the protection of BIT, would be waived.[131]

3.5.2.3 Safeguard Provision for Cram-down in the Sovereign Debt Restructuring

(3.52) In the context of sovereign debt, States often borrow from one or more of the following sources: commercial banks, bondholders, governments and multilateral institutions such as the IMF and World Bank.[132] At present, there is no international insolvency regime governing sovereign debt crisis, and sovereign debt defaults are dealt with using an *ad hoc*, individual case-by-case approach. In practice, in order to avoid an eternal default, the sovereign debtor is compelled to seek debt relief from creditors before or shortly after the default, via an extension of maturity, and/or a reduction of the value of the claim. Such relief is obtained by renegotiating the relevant debt instruments with individual creditors, which is commonly referred to by the term "debt restructuring".

(3.53) Renegotiations with multilateral creditors are often conducted in this *ad hoc* manner. Renegotiations with bilateral creditors who are members of the Paris Club are conducted through the Club's processes. The Paris Club is an informal group of official creditors with 19 permanent members and a small secretariat in Paris.[133] Countries that are not members of the Paris Club renegotiate with the sovereign debtor on an *ad hoc* basis. Renegotiations with commercial banks are either purely *ad hoc* or conducted through the London

129 *EDF International S.A., SAUR International S.A. and León Participaciones Argentinas S.A. v. Argentine Republic*, *supra* note 113, para. 1171.
130 *Continental Casualty Company v. Argentina* (ICSID Case No. ARB/03/9), Award of 5 Sep 2008, para. 221.
131 *Ibid.*
132 A. Gelpern and M. Gulati, "Public Symbol in Private Contract: a Case Study", (2006) 84 Wash. U. L. Rev. 1627, pp. 1632-1633; L. Rieffel, "The Bank Advisory Committee Process", Chapter 6 in Restructuring Sovereign Debt: The Case for Ad Hoc Machinery (2003, Brookings), p. 96.
133 Paris Club official website, available at http://www.clubdeparis.org/sections/composition/membres-permanents-et/membres-permanents, (last visited 26 Feb 2014). See generally E. Cosio-Pascal, "The Emerging of a Multilateral Forum for Debt Restructuring: The Paris Club", UNCTAD/OSG/DP/2008/7, Discussion Papers No. 192, available at http://unctad.org/en/Docs/osgdp20087_en.pdf (last visited 26 Feb 2014).

Club, an informal group of commercial banks with no fixed membership and no secretariat.[134] Renegotiations with bondholders are conducted through exchange offers prepared by the sovereign debtor. Occasionally bondholder committees are formed on an *ad hoc* basis to facilitate the process.[135]

(3.54) Under the current legal framework, one possible situation where the issue of unfair discrimination could arise is when similarly situated creditors are treated differently. For instance, Greece excluded the bond holdings of the Europe Central Bank and other central banks from restructuring by swapping them into a new series with identical payment terms and maturity dates right before the publication of the exchange offer.[136] As mentioned earlier in this Paper, municipal debtors in the US enjoy the safeguard protection concerning unfair discrimination as a result of cram-downs under section 1129(b)(1), which has been interpreted by US bankruptcy courts as prohibiting "a debtor from proposing unreasonably different treatment between classes of similar claims."[137] The author argues that a similar safeguard principle could be developed in the sovereign debt context at ICSID tribunals. Like the *Saluka* tribunal, the *Poštová* tribunal and other future ICSID tribunals may be asked to determine whether "similar cases are treated differently and without reasonable justification".[138] More specifically, whether the ECB and other holders of the same series of bonds are similarly situated creditors? Whether there are reasonable justifications for treating the ECB differently?

(3.55) As regards the principles of legitimate expectations and proportionality, non-participating bondholders could possibly argue that the exchange offer frustrates their legitimate expectations and is not proportionate to the aim sought to be realized by the debt restructuring. In the case of Greek debt restructuring, bondholders were offered with a package of new securities with face values equal to 31.5% and 15% of the face amount of the old bonds.[139] As discussed above, if U.S bankruptcy courts were faced with a similar situ-

134 L. Rieffel, "The Bank Advisory Committee Process", *supra* note 9, p. 103.

135 For a discussion of the use of creditors' committees in the Congo debt restructuring, see M. Richards, "The Republic of Congo's Debt Restructuring: Are Sovereign Creditors Getting Their Voice Back?", (2010) 73 Law & Contemp. Probs 273-299. Creditors' committees were also organized in the Greek debt restructuring, see J. Zettelmeyer, C. Trebesch and M. Gulati, *supra* note 14.

136 As part of this swap arrangement, the ECB committed to return any profits made through its Greek government bond holdings to its shareholders. Hence, Greece received virtually no debt relief on these bonds, both because the bulk of the ECB's Greek bond holdings were bought during 2010 at relatively small discounts, and because of its small share in the ECB (about 2 per cent). See J. Zettelmeyer, C. Trebesch and M. Gulati, *supra* note 14, p. 5.

137 D. Kupetz, *supra* note 57, citing *In re Barney & Carey Co.*, 170 B.R. 17, 25 (Bankr.D.Mass.1994).

138 *Investment BV v. Czech Republic*, *supra* note 104, para. 313.

139 Hellenic Republic Ministry of Finance, *supra* note 15.

ation of municipalities, they would analyze whether the amount to be received by non-participating bondholders under the plan is "all that they can reasonably expect in the circumstances."[140] In the author's view, a similar safeguard principle could be developed in the sovereign debt context at ICSID tribunals. Like the tribunals in *Tecmed v. Mexico*, *Azurix v. Argentina*, and *Occidental v. Ecuador*, the *Poštová* tribunal and other future ICSID tribunals may be asked to determine whether there is "a reasonable relationship of proportionality between the charge or weight imposed to the foreign investor and the aim sought to be realized by any expropriatory measure."[141] These tribunals may also have to rule on whether the debt restructuring could be justified by a necessity defense. Notably, the *Continental Casualty* tribunal rejected the necessity defense in respect of the restructuring of certain treasury bills, noting, among others, that the debt restructuring was offered at late date when Argentina's financial situation was moving towards normality.[142]

(3.56) As a result, the author argues that in the absence of any bankruptcy rules for States, ICSID arbitration could serve as the best forum to develop a safeguard provision for cram-downs employed in sovereign debt restructuring similar to those in the US municipality bankruptcy law.

3.6 Concluding Remarks

(3.57) In light of the Greek debt restructuring in 2012 as well as ongoing litigations brought by Argentine bondholders, the IMF recently revisited sovereign debt restructuring and put forward potential reform ideas.[143] Notably, the IMF praised the effectiveness of the Greek Bondholder Act in facilitating sovereign debt restructuring and suggested that "a more robust form of aggregation clause" similar to the Greek Act should be designed and intro-

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140 *Lorber v. Vista Irrigation Dist.*, 127 F.2d 628, 639 (9th Cir. 1942); *West Coast Life Insurance Company et al. v. Merced Irrigation District*, 114 F.2d 654 (9th Cir. 1940); *Moody v. James Irrigation District*, 114 F.2d 685 (9th Cir. 1940); *Bekins v. Lindsay-Strathmore Irrigation District*, 114 F.2d 680 (9th Cir. 1940), *Jordan v. Palo Verde Irrigation District*, 114 F.2d 691 (9th Cir. 1940).

141 *Técnicas Medioambientales Tecmed, S.A. v. United Mexican States*, *supra* note 108, para. 122.

142 *Continental Casualty Company v. Argentina*, *supra* note 103, para. 221.

143 IMF Public Information Notice (PIN) No. 13/61, May 23, 2013, available at http://www.imf.org/external/np/sec/pn/2013/pn1361.htm (last visited 26 Feb 2014); IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", supra note 34. For a discussion of the old reform proposal, see S. Hagan, "Designing a Legal Framework to Restructure Sovereign Debt", 36 Geo. J. Int'l L. 299 (2005); IMF, "The Design of the Sovereign Debt Restructuring Mechanism-Further Considerations", prepared by the Legal and Policy Department and Review Departments (Nov. 2002).

duced into international sovereign bonds.[144] Before that reform idea is materialized, the author argues, more attention should be paid to the policy implication of the *Poštová* tribunal's jurisdiction over sovereign bonds to ensure that non-participating bondholders would receive minimum protection in the context of cram-downs. The author reiterates that, in the absence of any bankruptcy rules for States, ICSID arbitration could serve as the best forum to develop a safeguard provision for cram-downs employed in sovereign debt restructuring similar to those in the US municipality bankruptcy law.

(3.58) Last but not least, the author maintains that ICSID tribunals should be entrusted to exercise their discretion and determine complex and delicate issues, such as whether the amount received by non-participating bondholders is all that they can reasonably expect in the circumstances or is proportionate to the aim sought to be realized by the debt restructuring. In this connection, it is worth emphasizing that one of the often-cited advantages of arbitration is the potential for choosing arbitrators with experience and expertise relevant to the dispute. As arbitration is merely a dispute resolution mechanism, it would be wrong to suggest that ICSID tribunals lack the expertise to play the role of a bankruptcy court.[145] In practice, the parties to a dispute can appoint whomever they want as arbitrator and they certainly can choose someone with sovereign debt or bankruptcy law background. Arguably, an increase in ICSID cases involving sovereign bonds would allow the development of legal principles for sovereign insolvency.[146] After all, a legal framework for sovereign insolvency can only arise if it can be built over time.[147]

144 IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", *supra* note 34, paras. 38 & 42.

145 M. Waibel, Sovereign Defaults Before International Courts and Tribunals, *supra* note 12, p. 323.

146 E. Norton, *supra* note 12, at 8.

147 *Ibid.*

4 New IMF Initiative Revives Old Inter-creditor Issues[1]

4.1 Introduction

(4.1) The essence of every kind of insolvency law is to find a balance between two conflicting interests – the desire of the debtor to alleviate the burden of indebtedness and the wish of creditors to recover as large portion of their claims as possible. In order to strike a right balance, insolvency law addresses not only debtor-creditor relationships, but also inter-creditor issues. Then why there is no insolvency law for States? Is it because States rarely encounter payment problems? The answer is certainly no. An overview of the occurrences of sovereign debt restructurings since 1950 reveals that over 600 debt restructurings have been conducted by sovereign debtors with respect to claims held by different types of creditors.[2] Despite of the significant number of debt restructuring, the number of litigation filed against sovereign debtors is still quite limited,[3] due to sovereign immunity against execution. In the absence of a creditor run to the courthouse, the need for an insolvency law for States seems less urgent. Nevertheless, there exists the need to achieve a balance

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1 This chapter has been published in *Tijdschrift voor Insolventierecht* Vol. 19, No. 5: 177- 186 (2013). The author is very grateful to Professor Bob Wessels for his helpful comments on an earlier draft.

2 For instance, the following countries have restructured their debts in the past decade: Argentina (2003), Dominican Republic (2004), Grenada (2004), Belize (2006), Ecuador (2009), Seychelles (2009), Jamaica (2010), Argentina (2010), St. Kitts and Nevis (2011), Greece (2011), Belize (2012) and Jamaica (2013). See IMF, Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework, April 26, 2013, at 22; U. Das, M. Papaioannou and C. Trebesch, "Sovereign Debt Restructurings 1950–2010: Literature Survey, Data, and Stylized Facts", (2012) IMF WP/12/203, at 30.

3 Schumacher recently conducted empirical research concerning sovereign debt litigation filed against debtor governments in the US and UK courts between 1976 and 2010. This research shows that only 108 cases were filed in the US and the UK by foreign banks, bondholders and other commercial creditors during this period, and that these cases only relate to 29 of the 180 sovereign debt restructurings with private creditors (16%). It further reveals that only 27 out of 69 debtor governments have been sued. See Schumacher et al., "Sovereign Defaults in Court: The Rise of Creditor Litigation 1976-2010", available at http://dx.doi.org/10.2139/ssrn.2189997 (last viewed 11 Mar. 2013). For a few examples of sovereign debt litigations, see O. Armas & T. Hall, "Debt restructuring cases against sovereigns and the US Foreign Sovereign Immunities Act", in: Sovereign Debt and Debt Restructuring, E. Bruno (eds.), pp. 51-78 (2013).

between different conflicting interests, as long as the debtor's limited pool of assets is insufficient to repay everyone.

(4.2) In 2001, the International Monetary Fund ("IMF") made an attempt to strike a balance between different conflicting interests in the sovereign debt context by introducing a treaty-based framework to restructure sovereign debt –the Sovereign Debt Restructuring Mechanism ("SDRM"). The SDRM idea was eventually abandoned due to a lack of sufficient support from the IMF member States. More recently, the IMF revisited sovereign debt restructuring and discussed various reform ideas in late May 2013. The IMF's revisit was mainly triggered by lessons from the Greek debt restructuring and Argentine bondholder litigation.

(4.3) This paper analyses the treatment of inter-creditor issues in the IMF's revisit. Part II provides an introduction to inter-creditor issues in sovereign debt restructuring. Part III begins with an overview of the SDRM and the new IMF initiative, and then moves on to explore issues concerning inter-creditor relations in the new initiative. It focuses on inter-creditor concerns in the context of the enhanced aggregated Collective Action Clauses ("CACs") as well as official sector involvement discussed in the new initiative. It proposes solutions to address those inter-creditor concerns. Part IV concludes this paper.

4.2 Inter-creditor Issues in Sovereign Debt Restructuring

4.2.1 The Context

(4.4) The current practice of sovereign lending and borrowing is unprecedented. For two centuries, sovereign debtors borrowed from one or more, but not all, of the following sources: commercial banks, bondholders, governments and multilateral institutions. It was not until the early 1990s that all four types of creditors began to play an active role in the sovereign debt market.[4] While

4 Following the first issuance of international bonds by Barings in 1817, bonds were the primary means of international long-term lending to States for more than 100 years until the 1930s. Bank lending was often limited to the form of short-term trade financing or interbank credit lines. The Great Depression in the 1930s shut down the bond market. At that time, States began to lend money to one another through loans, grants, and export credits. Since 1944, the IMF, World Bank and many regional development banks have been established to achieve international economic cooperation, and joining the sovereign debt creditor group. Also after the Second World War, long-term borrowing from commercial banks to sovereign States began to grow rapidly, and peaked in the 1970s. A wave of bank loan defaults in the 1980s triggered a new debt crisis, and in the early 1990s, banks agreed to exchange bad loans for Brady bonds. As a result, bond finance, largely dormant for more than sixty years, has again dominated foreign sovereign borrowing. See A. Gelpern and M. Gulati, "Public Symbol in Private Contract: a Case Study", (2006) 84 Wash. U. L. Rev.

commercial banks and bondholders form the "private sector" creditor group, the "official sector" creditor group is composed of governments ("bilateral creditors") and multilateral institutions such as the IMF, the World Bank and other regional banks (collectively, "multilateral creditors").

(4.5) With debt comes the possibility of default, and sovereigns are no exception to this axiom. At present, there is no international insolvency regime governing sovereign debt defaults, comprised of rules designed to cope with the scenario in which creditors cannot be fully satisfied. Instead, sovereign debt defaults are dealt with using an *ad hoc*, individual case-by-case approach in which most rules are invented along the way. In practice, in order to avoid an eternal default, the sovereign debtor is compelled to seek debt relief from creditors before or shortly after the default, via an extension of maturity, and/or a reduction of the value of the claim. Such relief is obtained by renegotiating the relevant debt instruments with different creditors separately.

(4.6) Renegotiations with multilateral creditors are often conducted in an *ad hoc* manner. Renegotiations with bilateral creditors who are members of the Paris Club are conducted through the Club's processes. The Paris Club is an informal group of official creditors with 19 permanent members and a small secretariat in Paris.[5] Countries that are not members of the Paris Club renegotiate with the sovereign debtor on an *ad hoc* basis. Renegotiations with commercial banks are either purely *ad hoc* or conducted through the London Club, an informal group of commercial banks with no fixed membership and no secretariat.[6] Renegotiations with bondholders are conducted through exchange offers prepared by the sovereign debtor. Occasionally bondholder committees are formed on an *ad hoc* basis to facilitate the process.[7]

(4.7) When a sovereign debtor is financially sound, renegotiation is only a matter between the debtor and a particular creditor. The creditor does not need to know the identities of other creditors. However, the situation changes

1627, at 1632-1633; L. Rieffel, "The Bank Advisory Committee Process", Chapter 6 in Restructuring Sovereign Debt: The Case for Ad Hoc Machinery (2003, Brookings), at 96.

5 Paris Club official website, available at http://www.clubdeparis.org/sections/composition/membres-permanents-et/membres-permanents, (last viewed 13 Dec. 2012). See generally E. Cosio-Pascal, "The Emerging of a Multilateral Forum for Debt Restructuring: The Paris Club", UNCTAD/OSG/DP/2008/7, Discussion Papers No. 192, available at http://unctad.org/en/Docs/osgdp20087_en.pdf (last viewed 7 Jan. 2013).

6 L. Rieffel, "The Bank Advisory Committee Process", *supra* note 9, at 103.

7 For a discussion of the use of creditors' committees in the Congo debt restructuring, see M. Richards, "The Republic of Congo's Debt Restructuring: Are Sovereign Creditors Getting Their Voice Back?", (2010) 73 Law & Contemp. Probs 273-299. Creditors' committees were also organized in the Greek debt restructuring, see J. Zettelmeyer, C. Trebesch and M. Gulati, "The Greek Debt Exchange: An Autopsy" (2012), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2144932 (last viewed 13 Dec. 2012).

when a sovereign debtor encounters serious financial distress and does not have enough money to repay everyone. Under such circumstances, creditors face the reality that sovereign lending activities are not risk-free and that they may have to take a loss. It is often said that, in the time of crisis, creditors should make "contribution" to help the debtor recover.[8] Given that the total amount of contribution needed by the debtor to recover from the crisis is certain, the fact that a particular creditor makes a lesser contribution means that other creditors must make a larger one. Therefore, as soon as the news of the debtor's financial distress spreads, creditors immediately want to find out who the other creditors are, whether they would be willing to make contributions and how large these might be. This change of attitude towards other creditors caused by a conflict of interest is referred to as "inter-creditor issues".

4.2.2 The Status Quo of Inter-creditor Issues

4.2.2.1 Treatment Within the Same Group

(4.8) As far as the public sector is concerned, multilateral and bilateral creditors enjoy different treatment within their respective groups. Negotiations with multilateral creditors are conducted on an *ad hoc* and individual basis. Each multilateral creditor is responsible for its own negotiation process with the debtor and has no influence over other multilateral creditors' negotiation processes. Bilateral creditors within the Paris Club support the principle of equal treatment within the Club. All Paris Club decisions are taken based on consensus, in the form of so-called "Agreed Minutes". Although the Agreed Minutes are not binding, they provide guidance to future bilateral negotiations that result in changes to the debt contracts.[9] In practice, driven by a mutual interest in avoiding disproportionate repayment of loans, all Paris Club members fully respect the commitments made through the Agreed Minutes.[10] However, such a principle does not apply to bilateral creditors outside the Paris Club, such as China, who are responsible for their own negotiations.

(4.9) In the private sector, commercial banks and bondholders all enjoy equal treatment within their groups but to a different extent. Commercial banks have employed the "mandatory repayment clause", which requires pro rata payments to all lenders in the event of a prepayment to any lender.[11] This clause

8 L. Buchheit, "The Search for Intercreditor Parity", 8 L. & Bus. Rev. Am. 73 (2002), at 76.
9 E. Cosio-Pascal, *supra* note 10, at 12.
10 *Ibid.*, at 13.
11 M. Wright, "The Pari Passu Clause in Sovereign Bond Contracts: Evolution or Intelligent Design?", 1 Hofstra L. Rev. 40 (2011), at 5; L. Buchheit, *supra* note 8, at 76.

excludes certain categories of claims, such as IMF debt, trade debt, foreign exchange contract obligations, interest and other agreed categories.[12] In addition, certain bank syndications also contain the "pro rata sharing clause", which provides that any bank receiving a greater proportion of its share must pay the excess to the agent bank who then redistributes to all banks on a pro rata basis.[13] The purpose of this clause is to share individual receipts, such as receipts by set-off, proceeds of litigation, individual guarantees or direct payments by the debtor.[14] Private bondholders have over the years expanded the use of the "*pari passu* clause" in the bond contracts, which provides, in part, that the bonds of that particular issue shall rank equally among themselves.[15]

4.2.2.2 Treatment Among Different Groups

a. Contractual Provisions

(4.10) Two types of contractual provisions in sovereign debt instruments address issues concerning treatment among different creditor groups: the "negative pledge clause" and the "*pari passu* clause". The "negative pledge clause" restricts the sovereign debtor's ability to grant security interests in its property to secure other creditors. The clause provides that if the debtor issues new debt and grants new creditors a security interest in the debtor's assets, the debtor has to grant old creditors an equivalent security interest.[16] While such a clause appears in both bank loan agreements and bond contracts, in the case of bonds the negative pledge generally only applies to security for bonds and other debt that is capable of being listed or traded on a market.[17]

(4.11) Besides ensuring the equal ranking of all bonds of that particular issue, the "*pari passu* clause" in most bond contracts also provides, in its second part, that the debtor's payment obligation under that particular issue shall rank equally with all other existing and future unsubordinated and unsecured

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12 P. Wood, "Sovereign insolvency: the bankruptcy ladder of priorities and the pari passu clause", Tijdschrift voor Financieel Recht (Mar. 2012), at 69.

13 *Ibid.*

14 *Ibid.*

15 The usage of *pari passu* clauses in unsecured bonds issued from 1960 to 2011 is recorded as follows: 123/144 (1960-1979), 429/464 (1980-1999), and 684/691 (2000-2011). See M. Gulati and R. Scott, The Three and a Half Minute Transaction: Boilerplate and the Limits of Contract Design (2012, Chicago), Appendix 7.

16 *Ibid.*, at 34. M. Wright, *supra* note 31, at 6.

17 One limitation of the negative pledge clause is that it does not catch various forms of quasi-security or title finance which, although not security in legal form, may be security in substance. P. Wood, *supra* note 12, at 69-70.

external indebtedness.[18] On many occasions, the *pari passu* treatment in bond contracts is further limited to other bonds and tradable debt instruments.[19] Over the past decade, the *pari passu* clause has become a litigation tool for bondholders who refused to accept the exchange offer, and the meaning of this clause has always remained controversial.[20] A narrow interpretation of this clause holds that all claims legally rank equally; in contrast, a wider interpretation suggests that the debtor must pay all its creditors ratably.[21]

(4.12) Despite Argentine bondholders' victory in the recent *NML Capital Ltd.* v. Argentina decision[22] which finds Argentina in breach of the *pari passu* clause, the meaning of this clause is far from being settled. It is not clear whether the US court in *NML Capital Ltd.* chose the narrow or the wider interpretation because it held that a combination of Argentina's actions breached the clause.[23] Furthermore, the court left the issue of whether payments to multilateral creditors would breach the *pari passu* clause entirely open, simply noting that the plaintiffs had not argued that preferential payments to the IMF made by Argentina could similarly entitle the plaintiffs to ratable payments.[24] Nevertheless, what is clear is that the history of the *pari passu* clause indicates that its introduction was intended, at least in part, as a tool for preserving inter-creditor equity and fairness in negotiations.[25]

b. Creditor Policies

(4.13) In the 1980s, commercial banks routinely imposed conditions for the restructuring of their loans, which involved a corresponding restructuring of

18 Wood lists a few examples of the pari passu clause in sovereign bonds, e.g. Pakistan (15 November 1999), Ecuador (27 July 2000), Ukraine (8 February 2001), Russian (25 February 2004), Argentina (10 January 2005), and Dominican Republic (20 April 2005). *Ibid*., at 66-67.

19 Global Law Intelligence Unit, Allen & Overy LL.P, "The pari passu clause and the Argentine case" (27 Dec. 2012), at 7.

20 For a discussion of relevant case law, see P. Wood, *supra* note 12, at 65-66; M. Gulati and R. Scott, *supra* note 15, at 20-26.

21 Global Law Intelligence Unit, Allen & Overy LL.P, *supra* note 19, at 8.

22 See *NML Capital, Ltd. v. Republic of Argentina,* No. 12-105-(L) (2d Cir. 26 Oct. 2012); *NML Capital, Ltd. v. Republic of Argentina*, 08 Civ. 6978 (TPG), 09 Civ. 1707 (TPG), 09 Civ. 1708 (TPG) (S.D.N.Y., 21 Nov. 2012). Both decisions are available at http://www.shearman.com/argentine-sovereign-debt/ (last viewed 20 Jun. 2013).

23 Those actions included executive-declared moratoriums on payments on the old bonds which had been renewed each year, the fact that Argentina had not made a single payment on the old bonds for six years while timely servicing the new bonds, that Argentina enacted the Lock Law and that Argentina had stated in the prospectuses for the new bonds that it had no intention of making any payments on the old bonds and classified the old bonds as a separate category from the new bonds in its SEC filings. *Ibid*., at 11.

24 *NML Capital, Ltd. v. Republic of Argentina,* No. 12-105-(L) (2d Cir. 26 Oct. 2012), at 21; Global Law Intelligence Unit, Allen & Overy LL.P, *supra* note 19, at 12.

25 M. Wright, *supra* note 31, at 4.

the Paris Club debt.[26] Paris Club members have actively advocated that a sovereign debtor may not accept less debt relief from its non-Paris Club creditors than the amount agreed with the Paris Club. This is referred to as the comparability of treatment principle.[27] The principle, in essence, forbids other creditors from making a lesser contribution than Paris Club creditors – although the Club considers certain mitigating factors to justify a deviation from the principle.[28] A controversial issue arises with respect to the willingness of Paris Club members to contribute proportionally when other creditor groups make larger contributions.[29] However, it is worth noting that the Paris Club considers on a case-by-case basis whether mitigating factors exist to justify a deviation from the comparability of treatment principle in respect of a particular creditor or debt instrument – although no explanation is provided as to what the "mitigating" factors entail.[30]

4.3 The IMF Reform Initiatives

4.3.1 An Overview

4.3.1.1 SDRM

(4.14) From November 2001 through April 2003, the IMF proposed a reform to the contemporary international financial architecture by introducing a treaty-based framework to restructure sovereign debt –the Sovereign Debt Restructuring Mechanism.[31] The SDRM is designed for private sector claims, with the possibility of including bilateral official claims as a separate class.[32] The key feature of the SDRM is a majority voting system, which binds all creditors to a restructuring agreement that has been accepted by a qualified majority.[33]

26 L. Buchheit, *supra* note 8, at 78.
27 Non-Paris Club creditors include all external creditors except multilateral creditors. The Paris Club explains that non-Paris Club official bilateral creditors grant loans generally similar to those provided by Paris Club creditors. Consequently, non-Paris Club official bilateral creditors often restructure on terms very similar to those agreed with the Paris Club. These creditors may also participate in Paris Club treatments and, under these circumstances, apply exactly the same treatment as that applied by Paris Club creditors. See Paris Club official website, *supra* note 10.
28 *Ibid.*
29 L. Buchheit, *supra* note 8, at 76.
30 See Paris Club official website, *supra* note 10; L. Rieffel, "What Is Broken? What Fixes Make Sense?", Chapter 12 in Restructuring Sovereign Debt: The Case for Ad Hoc Machinery (2003, Brookings), at 282.
31 S. Hagan, "Designing a Legal Framework to Restructure Sovereign Debt", 36 Geo. J. Int'l L. 299 (2005), at 300-301.
32 IMF, "The Design of the Sovereign Debt Restructuring Mechanism-Further Considerations", November 27, 2002, at 23-25.
33 *Ibid*, at 5.

The other elements of the SDRM include stay on enforcement,[34] priority financing[35] and dispute resolution forum.[36] It is worth noting that the SDRM does not directly address inter-creditor concerns as it would identify the range of claims that could be potentially restructured under the mechanism, but leave to the debtor to decide which subset of eligible claims would need to be restructured in a particular case.[37]

(4.15) Whereas this proposal was eventually shelved due to a lack of sufficient support from the IMF member States,[38] the idea of a majority voting system survived. Collective Action Clauses, a contractual approach to implementing a majority voting system, gained broad support from market participants and sovereign debtors.[39] However, CACs still cannot replace the SDRM in this

34 The SDRM introduces the "hotchpot" rule to provide a disincentive for litigation. This rule provides that any creditor that had managed to partially satisfy its claim through judicial enforcement after activation but prior to the restructuring agreement would automatically have the value of its residual claim reduced under the restructuring agreement in a manner that ensures that all of the benefits of its enforcement and collection have been neutralized. *Ibid.*, at 35.

35 The SDRM provides that a specified amount of financing or financing transaction would be excluded from the restructuring if such exclusion is supported by a qualified majority of eligible creditors. *Ibid.*, at 47.

36 The SDRM would establish, through an amendment of the IMF Articles of Agreement, a dispute resolution forum – Sovereign Debt Dispute Resolution Forum ("SDDRF"). The SDDRF would perform administrative functions such as notification to creditors, registration of claims and administration of the voting process. When resolving disputes, the SDDRF would apply the relevant national law for substantive issues, for example an interpretation of the validity of a claim, and apply its own law for procedural issues, for example claims of undue influence on certain creditors or abuse of the voting process. *Ibid.*, at 67-68.

37 *Ibid.*, at 13.

38 An amendment of the IMF's Articles of Agreement needs the approval of three-fifths of member States, holding eighty-five percent of the total voting power. See Articles of Agreement of the International Monetary Fund, as amended, art. XXVIII(a), available *at* http:// www.imf.org/external/pubs/ft/aa/aa28.htm (last viewed 11 Mar. 2013).

39 In fact, CACs in bonds governed by English law began to appear in 1980s. What the SDRM initiative encouraged was the inclusion of such clauses in bonds governed by New York law and others. Countries such as Mexico, Brazil, Belize, Guatemala, Venezuela, Uruguay were among the first group to include CACs in their New York law bonds. More recently, the Treaty Establishing the European Stability Mechanism ("ESM") also forces the inclusion of CACs, as of 1 January 2013, in all euro-area government securities with maturity above one year. In addition, the model CAC prepared includes an aggregation feature – referred to as cross-series modification – that permits changes to bind more than one series of bonds. See generally Clifford Chance newsletter, "Euro area member states take collective action to facilitate sovereign debt restructuring", Dec. 2012, available at http://www.cliffordchance.com/publicationviews/publications/2012/12/euro_area_memberstatestakecollectiveactiont.html (last viewed 7 Jan. 2013); M. Bradley & M. Gulati, "Collective Action Clauses for the Eurozone: An Empirical Analysis" (Oct. 2011), available at http://ssrn.com/abstract=1948534 (last viewed 11 Mar. 2013); R. Quarles, "Herding cats: collective-action clauses in sovereign debt the genesis of the project to change market practice in 2001 through 2003", Law & Contemp. Probs (Sept. 2010); J. Drage & C. Hovaguimian, "Collective Action Clauses (CACS): an analysis of provisions included in recent sovereign bond issues" (Nov. 2004).

respect. Unlike the SDRM that contemplated aggregated voting across all debt instruments, the voting under CACs is conducted on a series by series basis.[40]

4.3.1.2 New IMF Initiative

(4.16) On May 20, 2013, the IMF Executive Board of Directors revisited sovereign debt restructuring and discussed potential reform ideas presented in a staff paper on "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework".[41] The staff paper was prepared in response to recent debt restructurings, including the largest restructuring in history in Greece, as well as ongoing litigations brought by Argentine bondholders.[42] The staff paper begins with an overview of the IMF's legal and policy framework for sovereign debt restructuring, which covers issues concerning debt sustainability, market access, financing assurances, arrears, private sector involvement, official sector involvement and the use of legal instruments.[43] The paper then reviews how this framework has been applied in the context of fund-supported programs, and describes recent initiatives in various fora aimed at promoting orderly sovereign debt restructuring.[44] In the end, the paper does not provide concrete reform proposals, but identifies four issues to be studied further through follow-up staff papers.[45]

(4.17) The first issue relates to the staff's observation that debt restructurings have often been too little and too late, thus failing to re-establish debt sustainability and market access in a durable way.[46] Most Directors saw merit in exploring options to make restructurings more timely and effective, where debt is unsustainable and the extent of feasible economic adjustment and available new financing cannot restore viability.[47] Some Directors suggested an in-depth study of the implication of debt restructurings in current unions and noted the close economic and financial relationship among union members and potential contagion risks.[48]

40 IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", April 26, 2013, at 14, available at http://www.imf.org/external/np/pp/eng/2013/042613.pdf (last viewed 20 Jun. 2013).
41 IMF Public Information Notice (PIN) No. 13/61, May 23, 2013, available at http://www.imf.org/external/np/sec/pn/2013/pn1361.htm (last viewed 20 Jun. 2013).
42 *Ibid.*
43 *Ibid.*
44 *Ibid.*
45 *Ibid.*
46 IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", *supra* note 40, at 7.
47 IMF PIN No. 13/61, *supra* note 143.
48 *Ibid.*

(4.18) The second issue concerns the collective action problems in sovereign debt restructurings, especially in pre-default contexts.[49] All Directors agreed on the need to strengthen the existing contractual framework to make it more effective in overcoming these problems.[50] They supported the view in the paper that, in the context of CACs, consideration should be given to "a more robust form of aggregation clause".[51]

(4.19) The third issue touches upon the growing role and changing composition of official lending that call for a clearer framework for official sector involvement.[52] Having noted that the lack of a specific standard for securing program financing commitments from non-Paris Club lenders may lead to uneven practices and create safeguard risks for the IMF, most Directors saw merit in clarifying the current framework to ensure a more consistent, evenhanded and transparent approach.[53] A number of Directors supported the view in the staff paper that the membership of the Paris Club should be extended.[54]

(4.20) The final issue is associated with the IMF's lending into arrears (LIA) policy that the collaborative, good faith approach should be adopted to resolve external private arrears.[55] All Directors agreed to the need for a review of this policy in light of the recent experience and increased complexity of the creditor base, in particular with respect to how a member's adherence of the underlying guiding principles of the good faith criterion should be assessed.[56]

4.3.1.3 Preliminary Observations

(4.21) The new initiative shares the majority voting system that aggregates voting across different debt instruments with the earlier SDRM proposal, but differs in a way that it is, unlike the SDRM, applicable only to international sovereign bonds. Notably, the new initiative does not have the ambition of achieving a statutory reform as the SDRM, and merely focuses on options to strengthen the current contractual framework. The new initiative also drops ideas concerning stay on enforcement, priority financing and dispute resolution

49 IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", *supra* note 40, at 7.
50 IMF PIN No. 13/61, *supra* note 143.
51 *Ibid.*
52 IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", *supra* note 40, at 7.
53 IMF PIN No. 13/61, *supra* note 143.
54 *Ibid.*
55 IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", *supra* note 40, at 7.
56 IMF PIN No. 13/61, *supra* note 143.

in the SDRM, partly because these ideas can only be implemented through a statutory change.

(4.22) However, this does not mean that the new initiative is just a weak and more limited version of the SDRM. Importantly, the new initiative touches upon the inter-creditor concerns in the context of official lending, and thus brings the sensitive issue of inter-creditor relations to the reform stage. The following paragraphs address various inter-creditor issues in the context of enhanced aggregated CACs and official sector involvement.

4.3.2 Enhanced aggregated CACs

(4.23) As explained above, the second issue raised in the staff paper concerns the collective action problems in sovereign debt restructuring, especially in pre-default contexts. The paper suggests that there is merit in designing a more robust form of aggregated Collective Action Clauses for international sovereign bonds. The IMF Executive Board of Directors supported this suggestion.

4.3.2.1 The New Initiative Proposal

(4.24) According to the paper, the recent Greek debt restructuring and the *NML.Capital v. Argentina* case[57] call for a more robust form of aggregation clause. In the Greek restructuring, only 17 out of the 36 bonds governed by English law were successfully restructured using CACs.[58] The paper explains that a creditor or a group of creditors could obtain a blocking position in one or more series to prevent the operation of CACs in that series, as CACs only bind holders on an issue-by-issue basis.[59] By contrast, the paper stresses that all Greek bonds governed by Greek law were restructured pursuant to the new legislation.[60] The new legislation allows a qualified majority of bondholders to bind all holders of the affected domestic debt to the restructured terms.[61] The key difference between this legislation and CACs is that it aggre-

57 See *NML Capital, Ltd. v. Republic of Argentina,* No. 12-105-(L) and *NML Capital, Ltd. v. Republic of Argentina*, 08 Civ. 6978 (TPG), 09 Civ. 1707 (TPG), 09 Civ. 1708 (TPG), *supra* note 22. For a discussion of this case, see Global Law Intelligence Unit, Allen & Overy LL.P, "The pari passu clause and the Argentine case", 27 Dec. 2012; W. Weidemaier, "Sovereign Debt After NML v. Argentina", Capital Markets Law Journal (forthcoming), available at http://ssrn.com/abstract=2199655 (last viewed 10 Mar. 2013); E. Bruno, "Argentina: effects of the pari passu clause on future sovereign debt restructurings", in: Sovereign Debt and Debt Restructuring, E. Bruno (eds.), pp. 209-225 (2013).

58 IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", *supra* note 40, at 28.

59 *Ibid*.

60 *Ibid*., at 29.

61 *Ibid.*

gated claims across all of the affected domestic debt, thereby eliminating the power of a creditor or a group of creditors to obtain a blocking position in an individual issuance.[62]

(4.25) The paper then describes the recent development in a long litigation initiated by holdout creditors against Argentina following the 2001 default, i.e. the *NML. Capital v. Argentina* case. In that case, the holdout creditors requested the payment on the full amount of the defaulted bonds issued before 2001 and not tendered in the 2005 and 2010 debt restructuring.[63] The Second Circuit Court of Appeals in New York has upheld the District Court's interpretation of the *pari passu* clause contained in the defaulted bonds that would require ratable payments to creditors who accepted the restructuring offer and holdout creditors.[64] The District Court issued an injunction order that would prohibit Argentina from making payments on its restructured debt unless it pays in full the principal and interest owed on the original unstructured debt.[65] This order has been suspended by the Second Circuit Court pending its assessment of the payment formula and the coverage of the third parties subject to the order.[66] The paper argues that this decision is likely to give holdout creditors greater leverage and make future restructuring more difficult, because it allows holdouts to interrupt the flow of payments to restructured creditors and offers them a mechanism to recover outside a voluntary debt restructuring.[67]

(4.26) In light of the foregoing, the paper advocates for the aggregated voting in CACs in new bond issuances. The paper notes that only four countries have included aggregation clauses in their sovereign bonds to date – Argentina, the Dominican Republic, Greece and Uruguay.[68] These aggregation clauses contain a two-tier voting system: (1) 75 (Greece) or 85 (Argentina, the Dominican Republic and Uruguay) percent of the aggregated outstanding principal of all series to be affected, and (2) 66⅔ percent of the outstanding principal of each individual series to be affected.[69] According to the paper, the two-tier aggregation clauses have limitations. For instance, it still enables a creditor or a group of creditors to obtain a blocking position in a particular issue.[70] In order to address this limitation, the paper suggests that the two-tier voting thresholds in the existing aggregation clauses could be replaced with one-tier

62 *Ibid.*
63 *Ibid.*, at 30.
64 *Ibid.*
65 *Ibid.*
66 *Ibid.*
67 *Ibid.*, at 31.
68 *Ibid.*, at 29.
69 *Ibid.*
70 *Ibid.*

voting threshold, which disallows blocking minorities in single bond series.[71] In this respect, the paper admits that aggregating claims with different maturities associated with different economic interests through the one-tier clause may give rise to inter-creditor equity concerns, especially in pre-default restructurings.[72]

4.3.2.2 The Potential Risk of One-tier Aggregation

(4.27) As mentioned in an earlier IMF paper, inter-creditor equity concerns associated with aggregation may arise where a majority of creditors that hold a certain type of claims impose an agreement on a minority of creditors with very different claims, including different seniority or maturity.[73] In the context of sovereign bonds, the issue of different maturity is more relevant because nearly all bonds are unsecured and many recent debt restructurings were conducted prior to default. Among the 13 debt restructurings announced between 2003 and 2013, 8 restructurings were conducted in a pre-default context,[74] in which all claims will not yet have become due and payable as a result of acceleration.[75]

(4.28) In these circumstances, an one-tier aggregation clause that disallows blocking minorities in single bond series may present the risk of discriminating minorities with different maturities by empowering majorities to impose an agreement on minorities. For instance, creditors holding long-term maturity bonds may impose an unfavorable treatment on creditors with short-term maturity bonds. Unlike two-tier aggregation clause, one-tier clause leaves no room for short-term maturity creditors to disagree and stay outside restructuring. This problem is solved in the post-default context, because all claims will be accelerated and considered to have same maturity, i.e., all due and payable.[76] Therefore, the previous IMF paper suggested "a minimum threshold of support from each bond issuance would no longer be needed" in circumstances "where all bond issuances have been accelerated".[77] It also referred to the pre-pack arrangements in the non-sovereign context, where unsecured creditors with different maturities are generally willing to treat their claims

71 *Ibid.*, at 30.
72 *Ibid.*
73 IMF, "The Restructuring of Sovereign Debt –Assessing the Benefits, Risks and Feasibility of Aggregating Claims", September 3, 2003, at 5.
74 These 8 debt restructurings were announced by Dominican Republic (2004), Grenada (2004), Belize (2006), Jamaica (2010), St. Kitts and Nevis (2011), Greece (2011), Belize (2012) and Jamaica (2013). See IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", *supra* note 40, at 22.
75 IMF, "The Restructuring of Sovereign Debt –Assessing the Benefits, Risks and Feasibility of Aggregating Claims", *supra* note 73, at 5.
76 *Ibid.*, at 27.
77 *Ibid.*, at 22.

as accelerated for voting purposes and to receive the same treatment as others, because they fear that failure to agree to a restructuring plan will result in general default and insolvency and they would receive less as a result.[78] Although the new IMF initiative does not clarify the claim acceleration issue, it is implied from the one-tier aggregation proposal that all claims will be accelerated for voting purposes in the context of one-tier aggregated CACs. Then the next question becomes whether the acceleration of all sovereign debt claims is appropriate.

(4.29) I submit that the pre-pack example in the non-sovereign context is not applicable to sovereign debtors due to the alive feature of the pool of sovereign assets and the non-liquitable feature of sovereign debtors. Unlike in the pre-pack scenario, unsecured creditors holding sovereign bonds may have less incentive to voluntarily agree on the acceleration of their claims, simply because the likelihood of a general default and insolvency in the sovereign debt context is comparatively small. Given that sovereign debtors can raise revenue through taxation, the pool of assets, although limited, is not still but alive. In addition, States can never be liquidated, thus rendering sovereign debt crisis merely temporary. When the debt crisis is over in a few years, the sovereign debtor will again be able to repay everyone. In that case, why would creditors holding claims with long-term maturities agree to accelerate their claims and to receive restructuring terms less than the full amount of the claim value? Notably, accelerating all claims for voting purposes in the context of one-tier aggregated CACs carries the potential risk of discriminating against creditors holding claims with long-term maturities.

4.3.2.3 A Proposed Solution to Minimize the Potential Risk

(4.30) One solution to minimize the potential risk of discriminating against long-term creditors through claim acceleration is to leave them out and only to accelerate those claims that would become due and payable before the end of the temporary crisis period. Given that the task of specifying the temporary crisis period is extremely complex, if not impossible, a practical approach would be to allow sovereign debtors to determine their anticipated date of recovery from the crisis, after considering the debt sustainability analysis provided by the IMF. This approach will not be problematic, as the line to be drawn intends to solve inter-creditor equity concerns, but not to make the restructuring process necessarily easier for sovereign debtors.

(4.31) But would the line to be drawn make debt restructurings more difficult for sovereign debtors? In other words, would sovereign debtors receive less debt relief if long-term claims were left out in restructurings? In this respect,

78 *Ibid.*, at 27.

it is worth mentioning that the general presumption is that including all debt claims permits the broadest possible relief to the debtor, which is also the legislative reason for the automatic acceleration principle under US bankruptcy law.[79] However, this presumption does not hold in the context of sovereign debt restructuring. In the recent successful Greek restructuring, all creditors holding claims with maturities between 0 (20 March 2012) to 45 years (25 July 2057) were offered the same deal, which provides that the latest repayment date is 2042.[80] As a result, bonds maturing in 2057 will now be paid in 2042, before they become due; the present value haircut implicit in the restructuring for these bonds was -26.5.[81] This negative figure indicates that the inclusion of all claims in debt restructurings does not necessarily contribute to the broadest possible relief for sovereign debtors.

(4.32) Finally, when drawing the line, sovereign debtors may face objections from various creditors as to where the line should be. Such objections are inevitable as the line touches upon inter-creditor equity concerns and all creditors would want to protect their own interest in light of conflicts. Therefore, the line should be drawn only by the debtor, after taking into account the IMF's debt sustainability analysis. Obviously, it is possible, or even likely, that the line drawn by the debtor does not depict the actual crisis period given the difficulties involved in calculating the exact duration of a crisis. However, this would not be problematic because the purpose of the line is to address inter-creditor concerns, but not to resolve the debt crisis. The resolution of debt crisis mainly relates to issues other than inter-creditor concerns, such as the amount of debt relief and the level of growth. Nevertheless, the resolution of inter-creditor issues may increase the total amount of debt relief by encouraging more creditors to participate in the restructuring, on the ground that it ensures that debt relief is obtained from various creditors in a fair manner.

(4.33) As a result, I would argue that creditors holding claims with long-term maturities should be excluded from the restructuring process if one-tier aggregated CACs are implemented in new sovereign bonds.

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79 The automatic acceleration principle is to be found in 11 U.S.C. § 101, which defines claim as "right to payment, whether or not such right is […] matured, unmatured […]". The legislative reason mentioned in 11 U.S.C.A. § 101 provides that such a broad definition "permits the broadest possible relief in the bankruptcy court".

80 All creditors were offered (i) One and two year notes issued by the European Financial Stability Facility ("EFSF"), amounting to 15 per cent of the old debt's face value; (ii) 20 new government bonds maturing between 2023 and 2042, amounting to 31.5 per cent of the old debt's face value, with annual coupons between 2 and 4.3 per cent; (iii) A GDP-linked security which could provide an extra payment stream of up to one percentage point of the face value of the outstanding new bonds if GDP exceeds a specified target path (roughly in line with the IMF's medium and long term growth projections for Greece). See J. Zettelmeyer, C. Trebesch and M. Gulati, *supra* note 12, at 6.

81 *Ibid*., at 17.

4.3.3 Official Sector Involvement

4.3.3.1 The new Initiative Proposal

a. Ranking Among Official Bilateral Creditors

(4.34) The staff paper acknowledges the growing role and changing composition of official lending, and calls for the clarification of the framework for official sector involvement.[82] The paper describes the IMF's lending into arrears (LIA) policy and explains the policy of non-toleration of arrears to official creditors, which requires the elimination of existing arrears and the non-accumulation of new arrears with respect to official creditors during the Fund-supported program period.[83] The paper notes that arrears to Paris Club official bilateral creditors covered by the Paris Club Agreed Minutes are deemed eliminated for the purposes of Fund-supported programs when financing assurances are received from Paris Club before the approval of a debtor's request for IMF financing.[84] However, if a Paris Club Agreed Minute does not exist, the paper continues that tacit approval of each official bilateral creditor of the debtor is needed, and describes the uneven practices across country cases (i.e. Poland, Egypt, Iraq, Seychelles and Greece).[85]

(4.35) In light of the growing number of non-Paris Club bilateral creditors, the paper points out the risk that under the current LIA policy the IMF could not lend to a member in need if one or more official bilateral creditors choose to holdout.[86] The paper suggests that the IMF may change its current LIA policy and no longer insists on the elimination of official bilateral arrears as a precondition for Fund-supported programs.[87] It adds that the issue how debt relief could be provided by non-Paris Club official lenders should be clarified.[88] Alternatively, the paper proposes that the Paris Club could extend its membership to all major lenders.[89]

b. Ranking Among Different Creditor Groups

(4.36) Among others, the staff paper summarizes the non-binding Principles for best practice in debtor-creditor relations prepared by the Institute of Inter-

82 IMF, "Sovereign Debt Restructuring – Recent Developments and Implications for the Fund's Legal and Policy Framework", *supra* note 40, at 33.
83 *Ibid*., at 48.
84 *Ibid*., at 49.
85 *Ibid*., at 34-35.
86 *Ibid*., at 35.
87 *Ibid.*
88 *Ibid.*
89 *Ibid.*

national Finance ("IIF") and the Addendum to the Principles adopted in October 2012. With respect to inter-creditor equity, the paper notes that the IIF Addendum proposes the fair and comparable treatment of all creditors, and forbids the exclusion of any creditor *ex ante* from participating in a sovereign debt restructuring.[90] According to the IIF Addendum, any exception to the inclusion of certain creditors should be discussed and agreed by all creditors.[91]

(4.37) The staff paper maintains that the IMF cannot endorse the IIF Principles, because it is of the view that "the design of the debt restructuring strategy should be left to the negotiations between creditors and the debtor".[92] Although the paper agrees with the need to ensure adequate fairness of treatment among creditors, it states that the purpose of doing so is to "secure high rates of participation".[93] It also notes that in some cases creditors "may accept" different treatment in order to "better fit with individual creditor preferences" or to "help limit the extent of economic dislocation, maintain market access, and preserve financial stability."[94] The Executive Board of Directors agreed with the view expressed in the staff paper at its May 20, 2013 meeting, noting that the IIF Principles are not fully consistent with IMF policies.[95]

4.3.3.2 The Unreasonableness of the New Initiative Approach

(4.38) In my view, the IMF's position on inter-creditor issues is self-contradictory. On the one hand, the IMF maintains that the debtor and creditors should have the freedom to negotiate the debt restructuring strategy, thereby assuming that debt negotiation is a matter that concerns only the debtor and creditor(s) in the negotiation, but not other creditors outside the negotiation. On the other hand, as discussed in the section above, the IMF is worried about the growing number of creditors that are non-Paris Club members as well as the uneven debt negotiation practices across country cases, which indicates its concern for inter-creditor equity.[96]

(4.39) In this respect, the IMF could probably argue that its concern for inter-creditor relations between different official bilateral creditors is only limited to discussions regarding its LIA policy. Under the current policy, the elimina-

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90 *Ibid.*, at 40.
91 *Ibid.*, at 40-41.
92 *Ibid.*, at 41.
93 *Ibid.*
94 *Ibid.*
95 IMF PIN No. 13/61, *supra* note 143.
96 IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", *supra* note 40, at 34-35.

tion of official bilateral arrears constitutes a precondition for Fund-supported programs.[97] Therefore, the IMF could not lend to a member in need if one or more official bilateral creditors choose to holdout.[98] As a result, the existence of any holdout official bilateral creditors would affect the operation of the IMF's LIA policy. If that is the case, this problem could easily be solved through an amendment of the current policy. Indeed, the staff paper does suggest the amendment of its policy in this context.[99] However, together with the amendment suggestion, the staff paper also calls for the clarification of "the modality through which assurance of debt relief are provided by (non-Paris Club) official lenders".[100] Notably, the fact that the IMF wants to know the practice of non-Paris Club lenders in this respect makes a powerful case for the recognition of inter-creditor concerns by the IMF. This clearly contradicts with the IMF's position that "the design of the debt restructuring strategy should be left to the negotiations between creditors and the debtor" when it disagrees with the IIF's Principle addressing inter-creditor issues.

(4.40) To further support its position that creditors and the debtor should negotiate the debt restructuring strategy themselves, the staff paper notes that in some cases creditors "may accept" different treatment in order to "better fit with individual creditor preferences" or to "help limit the extent of economic dislocation, maintain market access, and preserve financial stability." It is worth emphasizing that the word "may" is used, as creditors have the freedom to choose whether or not to accept different treatment under certain circumstances. This resembles the voluntary subordination concept under national bankruptcy law for non-State debtors. The author argues that the fact that certain creditors may voluntarily agree to accept different treatment on some occasions in no means supports the position that rules on inter-creditor issues are not worth developing. What about those creditors who may not voluntarily agree to different treatment? How should they be treated?

(4.41) Additionally, it appears from the staff paper that the IMF speaks only from the debtor's perspective. In response to the IIF's Principle on fair treatment of all creditors, the staff paper does not discuss principles regarding the treatment of creditors but merely states that adequate fairness principle should be sought in order to "secure high rates of participation". Needless to say, high participation rate is a concern solely for the sovereign debtor. Given that this approach does not consider creditors' rights at all, it is extremely unbalanced and unreasonable.

97 *Ibid.*, at 35.
98 *Ibid.*
99 *Ibid.*
100 *Ibid.*

4.3.3.3 Towards a 'Realistic' Ranking Order Between Official and Private Creditors

(4.42) It should be stated at the outset that the IMF's problematic position on inter-creditor issues is understandable. To begin with, as a multilateral lender itself, the IMF's interest conflicts with other official and private lenders. This conflict of interests is demonstrated by the fact that, in the absence of any legally binding principles on the ranking order, the IMF has been insisting on a preferred creditor status for decades. Even at the May 20 meeting, the Executive Board emphasized the "importance of preserving the Fund's preferred creditor status".[101] More importantly, as an international organization, the decision makers at the IMF are its Member States, which are bilateral official lenders themselves. Bilateral official lenders' interest also conflicts with private lenders. This double-conflict explains why the IMF tries to avoid any discussion of future rules on a ranking order among all creditors. Logically, rules on this issue, regardless of its design, are likely to bring predictability and certainly to the current regime and at the same time take away the flexibility official creditors presently enjoy.

(4.43) When designing a ranking order between official creditors and private creditors, attention should be paid to the nature of official claims, including multilateral and bilateral. While private creditors lend merely for profit, multilateral and bilateral creditor lend for a wide variety of purposes in addition to making a profit. For example, multilateral lending relates to information provision in terms of monitoring government policies in recipient countries and the exercise of conditionality aimed at changing governmental policies.[102] Similarly, bilateral creditors often extended to advance political and social objectives, such as ensuring that domestic exporters are not disadvantaged by financial support offered by other governments, or sharing the costs of building infrastructure projects that can help the debtor achieve higher rates of economic growth.[103] As it is impossible to weigh political considerations, the differences between official creditors and private creditors are simply non-comparable. This non-comparability calls for the separate treatment of these claims. Notably, separate treatment does not necessarily violate the

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101 IMF PIN No. 13/61, supra note 143.

102 D. Rodrik, "Why is There Multilateral Lending?", NBER Working Paper No. 5160 (June 1995), at 2. Crippa discusses the human right issues involved in projects financed by multilateral development banks. See L. Crippa, "Multilateral Development Banks and the Human Right Responsibility", 3 Am. U. Int'l L. Rev. 25 (2010): 531-577.

103 L. Rieffel, "What Is Broken? What Fixes Make Sense?", *supra* note 49. It is worth noting that China as a major bilateral lender to developing countries has a different approach towards bilateral lending. For example, Chinese loans generally do not require any change of national economic policies. See M. Mattlin & M. Nojonen, "Conditionality in Chinese bilateral lending", BOFIT Discussion Papers (14/2011); E. Downs, "INSIDE CHINA INC.: China Development Banks' Cross-border Energy Deals", The John L. Thornton China Center at Brookings (2011).

equitable treatment principle in national bankruptcy law, which basically ensures the fair treatment of creditors with similar legal rights so that assets are distributed according to the creditors' ranking.[104] All creditors do not need to be treated equally, but "in a manner that reflects the different bargains they have struck with the debtor".[105]

(4.44) How to solve inter-creditor equity concerns when these claims are treated separately? A realistic approach would be to impose a general rule that does not specify details of separate treatment, but simply requires all creditors to take a loss in order to contribute to the recovery of debt crisis. The obligation of all creditors to take a loss reflects the common understanding that all participants in lending and borrowing activities shall, in principle, share the risk of insolvency. This rule is not likely to encounter great difficulties when it comes to implementation, because, in practice, both bilateral creditors and private creditors have on numerous occasions been willing to renegotiate with the debtor.[106]

4.4 Conclusion

(4.45) This paper welcomes the new IMF initiative and explores issues concerning inter-creditor relations in the initiative. First, it argues that accelerating all claims for voting purposes in the context of one-tier aggregated CACs carries the potential risk of discriminating against creditors holding claims with long-term maturities, due to the alive feature of the pool of sovereign assets and the non-liquitable feature of sovereign debtors. In order to minimize the potential risk, it suggests that not all claims should be accelerated, but only those that would become due and payable before the end of the temporary crisis period. Practically speaking, the crisis period should be determined by sovereign debtors after taking into account the IMF debt sustainability analysis.

(4.46) Second, this paper maintains that the IMF's position on inter-creditor issues is self-contradictory. On the one hand, the IMF maintains that the debtor and creditors should have the freedom to negotiate the debt restructuring strategy, thereby assuming that debt negotiation is a matter that concerns only the debtor and creditor(s) in the negotiation, but not other creditors outside the negotiation. On the other hand, the IMF is worried about the growing

104 UNCITRAL Legislative Guide on Insolvency Law (2004), available at http://www.uncitral.org/pdf/english/texts/insolven/05-80722_Ebook.pdf (last viewed 11 Mar. 2013), at 11.
105 *Ibid.*
106 From 1950 to 2010, there were 447 restructurings conducted with the Paris Club and 186 restructuring conducted with private creditors. See U. Das, M. Papaioannou and C. Trebesch, "Sovereign Debt Restructurings 1950–2010: Literature Survey, Data, and Stylized Facts", *supra* note 2, at 30-31.

number of creditors that are non-Paris Club members as well as the uneven debt negotiation practices across country cases, which indicates its concern for inter-creditor equity. This paper explains that the IMF's self-contradictory position is caused by its conflict of interest, and suggests that rules regarding the ranking between official creditors and private creditors should be developed in a realistic way. It advocates for the separate treatment of official and private creditors as well as a general rule that does not specify details of separate treatment, but simply requires all creditors to take a loss in order to contribute to the recovery of debt crisis.

5 The Missing Element of a Single Limb Voting Procedure

Fair and Equitable Treatment Standard in Sovereign Debt Restructuring[1]

5.1 Introduction

(5.1) On 6 October 2014, the Executive Board of the International Monetary Fund ("IMF") approved the staff paper on "Strengthening the Contractual Framework to Address Collective Action Problems in Sovereign Debt Restructuring".[2] The staff paper suggests a few contractual reforms designed to tackle collective action problems so as to achieve orderly sovereign debt restructurings.[3] Among other things, the paper advocates in favor of a single Collective Action Clause ("CAC") with a menu of voting procedures, including (1) a series-by-series voting procedure, (2) a two-limb aggregated voting procedure, and (3) a single-limb voting procedure with the possibility for "sub-aggregation".[4] Given that the CAC's function is to enable a qualified majority of bondholders to bind all holders of the same series to an amendment of the bond terms, different voting procedures permit different levels of influence that minority bondholders could potentially exercise over the restructuring process. Under options (1) and (2), for example, a creditor or a group of creditors could obtain a blocking position in a particular series and effectively prevent the operation of CAC in that series. By contrast, a single-limb voting procedure in option (3) will enable contract terms to be amended on the basis of a single vote across all affected instruments, thereby limiting the ability of holdout creditors to undermine the restructuring process.[5] To ensure inter-creditor equity, the paper suggests that in a single-limb voting procedure all affected bondholders should be offered "the same instrument or an identical menu of instruments".[6]

1 This chapter has been accepted for publication in R. Hoffmann (eds.), International Investment Law and the Global Financial Architecture, Elgar Publishing 2015. The author is very grateful to Professor Bob Wessels for his helpful comments on an earlier draft.
2 IMF Press Release No.14/459 dated 6 October 2014 <http://www.imf.org/external/np/sec/pr/2014/pr14459.htm> accessed 18 October 2014.
3 IMF, 'Strengthening the Contractual Framework to Address Collective Action Problems in Sovereign Debt Restructuring' (2014) <http://www.imf.org/external/pp/longres.aspx?id=4911> accessed 18 October 2014.
4 *Ibid.*, p. 22.
5 *Ibid.*, p. 20.
6 *Ibid.*, 21.

(5.2) As explained in the staff paper, the success of the newly adopted Greek Bondholder Act in the 2012 debt restructuring prompted the introduction of the single-limb voting procedure.[7] In February 2012, Greece announced a plan to restructure over € 200 billion in privately held Greek bonds.[8] Among all targeted bonds, nearly 91% of the sovereign bonds had been issued under the Greek law.[9] While the English-law bonds contain CACs, the Greek-law bonds do not.[10] On 23 February 2012, the Greek legislature introduced a collective action procedure by passing the Greek Bondholder Act (4050/12), under which the proposed amendment of bond terms will bind holders of all Greek-law bonds, "if at least two thirds by face amount of a quorum of these bonds, voting collectively without distinction by series, approve the proposed amendments."[11] It further provides that "[o]ne half by face amount of all the Republic's bonds subject to the collective action procedure will constitute a quorum for these purposes."[12] In essence, what the Greek Bondholder Act introduced is a single-limb voting procedure, as it allows for "voting collectively without distinction by series". In the end, 146.2 billion out of the € 177.3 billion Greek-law bonds had accepted the exchange offer.[13] Thus, the quorum and voting thresholds for amending the Greek-law bonds under the Act were easily met. Through the implementation of the Act, the proposed amendment became binding on all holders of Greek-law bonds.[14] Following the restructuring, dissenting bondholders *Poštová* Banka A.S. (a Slovak entity) and its shareholder Istrokapital S.E. (a Cypriot entity) commenced arbitration against Greece in May 2013 before the International Centre for Settlement of Investment Disputes

7 *Ibid*., 19.
8 The restructuring offer was directed at the holders of all sovereign bonds issued prior to 2012 (total face value of _195.7 billion) and 36 sovereign-guaranteed bonds issued by public enterprises (total face value of just under _10 billion). The holders of these bonds were offered a swap of their old bonds with a package of new ones comprised of (1) English-law bonds maturing between 2023 and 2042 with a face value equal to 31.5% of the face amount of the old bonds, (2) English-law EFSF (European Financial Stability Facility) notes with a maturity date of one or two year from the date of closure of the restructuring with a face value equal to 15% of the face amount of the old bonds, and (3) detachable GDP-linked securities issued under English law having a notional amount equal to the face amount of each holder's new bonds. See Jeromin Zettelmeyer, Christoph Trebesch and Mitu Gulati, 'The Greek Debt Exchange: An Autopsy', Peterson Institute for International Economics Working Paper No. 2013-13-8, 5 <http://ssrn.com/abstract=2144932> accessed 10 October 2014; Hellenic Republic Ministry of Finance, Press Release dated 24 February 2012 <http://www.minfin.gr/portal/en/resource/contentObject/contentTypes/announcementObject> accessed 2 October 2014.
9 JerominZettelmeyer, Christoph Trebesch and Mitu Gulati, *supra* note 8.
10 *Ibid*., pp.6-7.
11 Hellenic Republic Ministry of Finance, *supra* note 8.
12 *Ibid.*
13 Hellenic Republic Ministry of Finance, Press Release dated 9 March 2012 <http://www.minfin.gr/portal/en/resource/contentObject/contentTypes/announcementObject> accessed 2 October 2014.
14 *Ibid.*

("ICSID"), pursuant to the bilateral investment treaties concluded between Greece and Slovakia as well as Greece and Cyprus.[15] This arbitration is currently pending.[16]

(5.3) This article explores the missing element in a single-limb voting procedure. It is structured as follows: Part II analyses the nature of a single-limb voting procedure and finds that it resembles cram-down procedures in bankruptcy law; Part III describes the safeguard provision for cram-down procedures in bankruptcy law, which includes the prohibition of unfair discrimination and the fair and equitable treatment principle; and Part IV discusses the similarities between the safeguard provision for cram-down procedures in bankruptcy law and the fair and equitable treatment principle under investment treaties, and argues that investment arbitration could serve as an appropriate forum to develop a safeguard provision for a single-limb voting procedure in the context of sovereign debt restructuring. Part V presents the conclusion.

5.2 CAC With a Single-limb Voting Procedure

(5.4) This section analyses the nature of a single-limb voting procedure. Is it the same procedure as contained in traditional aggregated CACs or something else?

5.2.1 Traditional Aggregated CACs

(5.5) As explained above, CACs enable a qualified majority of bondholders to bind all holders of the same bond issuance to a change of the contract terms, including the maturity date as well as the amount of interest and principal.[17]

15 *Poštová banka, a.s. and ISTROKAPITAL SE v. Hellenic Republic* (ICSID Case No. ARB/13/8) <https://icsid.worldbank.org/ICSID/FrontServlet?requestType=GenCaseDtlsRH&actionVal=ListPendin> accessed 18 October 2014.

16 *Ibid*.

17 Strictly speaking, the term CACs include two types of clauses: (1) "majority restructuring" provisions, which enable a qualified majority of bondholders to bind all holders to the same bond issuance to the financial terms of a restructuring; and (2) "majority enforcement" provisions, which allows a qualified majority of bondholders to limit the ability of a minority bondholders to enforce their rights following a default. The former type, "majority restructuring" provisions, is most frequently employed in practice. See IMF, 'Collective Action Clauses in Sovereign Bond Contracts –Encouraging Greater Use' (Prepared by the Policy Development and Review, International Capital Markets and Legal Departments) (2002) <http://www.imf.org/external/np/psi/2002/eng/060602a.htm> accessed 30 September 2014. The typical threshold for a qualified majority is 75%. See Michael Bradley & Mitu

They began to appear in bonds governed by English law in the 1980s.[18] In the wake of the Mexican crisis in 1995 and the Argentine debt default in 2001, the IMF began pushing for the adoption of CACs in sovereign bonds governed by New York law to facilitate the restructuring of sovereign bonds held by numerous and largely anonymous creditors.[19] Countries such as Mexico, Brazil, Belize, Guatemala, Venezuela, Uruguay were among the first group to include CAC in their New York law bonds.[20] One limitation of these CACs is that they bind non-participating bondholders only on a series-by-series basis.[21]

(5.6) In recent years, CACs with aggregation features appeared in the sovereign bond market. So far, four countries have included aggregation clauses in their sovereign bonds – Argentina, the Dominican Republic, Greece and Uruguay.[22] These aggregation clauses contain a two-limb voting system: (1) 75 (Greece) or 85 (Argentina, the Dominican Republic and Uruguay) percent of the aggregated outstanding principal of *all* series to be affected, and (2) 66⅔ percent of the outstanding principal of *each* individual series to be affected.[23] To give an example, the aggregated CAC contained in the Uruguay Prospectus Supplement- Offer to Exchange dated April 10, 2003 provides as follows:

> "If Uruguay proposes any reserve matter modification to the terms and conditions of the debt securities of two or more series, or to the indenture insofar as it affects the debt securities of two or more series, in either case as part of a single transaction, Uruguay may elect to proceed pursuant to provisions of the indenture providing that such modifications may be made, and future compliance therewith may be waived, for each affected series if made with the consent of Uruguay and

Gulati, 'Collective Action Clauses for the Eurozone: An Empirical Analysis' (2013) 5 <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1948534> accessed 2 October 2014.

18 Mark Weidemaier & Mitu Gulati, 'How Markets Work: The Lawyer's Version' in Bettina Lange, Dania Thomas , Austin Sarat (eds.), *Studies in Law, Politics, and Society (*Emerald Group Publishing 2013),107 – 133. For a discussion of old English CACs, see Anna Gelpem & Mitu Gulati, 'A Modern Legal History of Sovereign Debt', Law and Contemporary Problems (2010) Vol.73, No. 4, viii-ix.

19 IMF, *supra* note 25; Michael Bradley & Mitu Gulati, *supra* note 25, 6 & 10; Mark Weidemaier & Mitu Gulati, 'A People's History of Collective Action Clauses' (2014) <http://scholarship.law.duke.edu/cgi/viewcontent.cgi?article=5387&context=faculty_scholarship> accessed 10 October 2014.

20 Andrew Haldane et al., 'Optimal Collective Action Clause Thresholds', Bank of England Working Paper No. 249 (2005), 7 & 9.

21 Lee Buchheit et al., 'Sovereign Bonds and the Collective Will', 51 Emory L. J. 1317 (Fall 2002); Charles Schmerler, 'Restructuring Sovereign Debt' in *The Law of International Insolvencies and Debt Restructuring* (OUP 2006), 461-462.

22 IMF, 'Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework' (2013) para 40 <http://www.imf.org/external/np/pp/eng/2013/042613.pdf> accessed 10 October 2014.

23 *Ibid.*

- the holders of not less than 85% in *aggregate principal amount of the outstanding debt securities of all series affected by that modification (taken in aggregate),* and
- the holders of not less than 66⅔% in *aggregate principal amount of the outstanding debt securities of that series (taken individually).*"[24]

(5.7) More recently, the Treaty Establishing the European Stability Mechanism ("ESM") also forced the inclusion of CACs, as of 1 January 2013, in all euro-area government securities with maturity above one year.[25] The model CAC prepared by the EU Economic and Financial Committee Sub-Committee on EU Sovereign Debt Markets includes an aggregation feature – referred to as cross-series modification – that permits changes to bind more than one series of bonds.[26] Compared with the Uruguay aggregated CAC, the Eurozone model adopts a lower threshold (i.e. 75%) to calculate the affirmative vote of the aggregate principle amount of the outstanding debt securities of *all* the series that would be affected by the proposed modification.[27]

(5.8) What is the nature of aggregated CACs or CACs with a cross-series modification? The EU Committee on EU Sovereign Debt Markets explains that a cross-series modification can be understood as a CAC that works at the series level, in that the decision of a specified majority binds all holders of all affected series, "with the important further protection that holders of any individual series of affected bonds will not be bound by the decision of the group as a whole unless they also vote in favour of the proposed modification".[28] In other words, from a sovereign debtor's prospective, the cross-series modification clause has one key limitation – it still enables a creditor or a group of creditors to obtain a blocking position in a particular series.[29]

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24 Cleary Gottlieb Steen & Hamilton LLP, 'Collective Action Clauses with Aggregation Mechanisms', 02/11/2011 <http://scholarship.law.duke.edu/cgi/viewcontent.cgi?article=3004&context=faculty_scholarship> accessed 10 October 2014.

25 Article 12 (3) of the Treaty provides that "Collective action clauses shall be included in all new euro area government securities, with maturity above one year, from July 2013, in a standardised manner which ensures that their legal impact is identical." See Treaty establishing the European Stability Mechanism <http://ec.europa.eu/economy_finance/articles/financial_operations/2011-07-11-esm-treaty_en.htm> accessed 10 October 2014.

26 The model clause is available at <http://europa.eu/efc/sub_committee/cac/index_en.htm> accessed 30 September 2014. See Cliffford Chance newsletter, 'Euro area member states take collective action to facilitate sovereign debt restructuring' (2012) <http://www.cliffordchance.com/publicationviews/publications/2012/12/euro_area_memberstatestakecollectiveactiont.html> accessed 10 October 2014.

27 "Common Terms of Reference" of the Eurozone Model CAC (17/02/2012) para 2.2 <http://europa.eu/efc/sub_committee/pdf/cac_-_text_model_cac.pdf> accessed 10 October 2014.

28 EFC Sub-Committee on EU Sovereign Debt Markets, 'Model Collective Action Clause Supplemental Explanatory Note' (2012) 3-4, available at <http://europa.eu/efc/sub_committee/pdf/supplemental_explanatory_note_on_the_model_cac_-_26_march_2012.pdf> accessed 10 October 2014.

29 IMF, "Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework", *supra* note 34, para 41.

(5.9) By contrast, a single-limb voting procedure "requires only a single vote calculated on an aggregated basis across all affected bond series."[30] As a result, a single-limb voting procedure "removes the possibility of obtaining a controlling position within a particular issuance to block the restructuring of that issuance."[31] Thus, the author argues that a single-limb voting procedure differs from the voting procedure contained in traditional aggregated CACs.

5.2.2 Cram-down in Bankruptcy Law

(5.10) Having dismissed the assumption that the CAC with a single-limb voting procedure is a form of traditional aggregated CACs, this section explores the similarity between a single-limb voting procedure and cram-down procedures in domestic bankruptcy law systems, for ease of reference, the law system of the US It should be stated at the outset that cram-down procedures exist in US bankruptcy law for all kinds of debtors, including consumers, companies and municipalities. Among these debtors, the status of municipalities is most similar to that of States.[32] As a result, the bankruptcy law for municipalities – the US Code Chapter 9 on municipality bankruptcy[33] – will be used as an example for our discussion on cram down procedures.

(5.11) Under Chapter 9 municipality bankruptcy, a restructuring plan is deemed to be accepted by *a* class of creditors if creditors holding at least two-thirds in amount and more than one-half in number of all claims in that class

30 IMF, "Strengthening the Contractual Framework to Address Collective Action Problems in Sovereign Debt Restructuring", *supra* note 3, 20.

31 *Ibid.*

32 A municipality's insolvency is determined on the basis of a cash-flow analysis, not budget deficiency analysis; a municipality is insolvent when it is unable to pay its debts as they become due. *In re Hamilton Creek Metropolitan District*, 143 F.3d 1381 (10th Cir. 1998); *In Re City of Bridgeport*, 129 B.R. 332 (Bankr. D. Conn, 1991).

33 The U.S. Bankruptcy Code defines a "municipality" as a "political subdivision or public agency or instrumentality of a state". It includes cities and towns, villages, counties, taxing districts, municipal utilities, and school districts. A municipality may be a debtor in a Chapter 9 case if (a) it has been "specifically authorized" to be a Chapter 9 debtor, b) is "insolvent" and (c) has either (i) obtained majority approval of creditors in each class for the proposed plan of reorganization, or (ii) negotiated in "good faith" with creditors and failed to obtain such a majority, or (iii) is unable to negotiate with creditors because such negotiations are "impracticable". See 11 U.S.C. §101(40), United States Courts: Chapter 9 Municipality Bankruptcy <http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/Chapter9.aspx> accessed 10 October 2014; Zack Clement et al., 'Important Issues in a Chapter 9 Case for a Municipality', 24 October 2011 <http://www.nortonrosefulbright.com/knowledge/publications/94035/important-issues-in-a-chapter-9-case-for-a-municipality> accessed 10 October 2014.

accept the plan.[34] With respect to all classes of creditors, a reorganization plan can be confirmed if *each* class of claims or interests "has accepted the plan" or "is not impaired under the plan".[35] In the event of the failure of an impaired class to accept the plan, the plan can still be confirmed under the cram-down procedure in Section 1129(b)(1):

> "the court, on request of the proponent of the plan, shall confirm the plan… if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan."[36]

(5.12) It appears from the above text that the purpose of the cram-down procedure is to force an impaired class to accept a proposed plan. Although as explained earlier a single-limb voting procedure eliminates the power of a creditor or a group of creditors to obtain a blocking position in an individual issuance, the elimination of such power does not necessarily resemble the craw-down procedure. Because the victim of the cram-down procedure is an impaired class of creditors, a single-limb voting procedure has to eliminate the power of an impaired class to be qualified as a cram down procedure. Hence, the key issue at stake concerns claim classification – whether claims of an individual issuance differ from that of other issuances so that it constitutes a particular class by themselves?

(5.13) The UNCITRAL Legislative Guide on Insolvency Law provides some useful guidance on class classification. The purpose of classification of claims is to "satisfy the requirements to provide fair and equitable treatment to creditors, treating similarly situated claims in the same manner and ensuring that all creditors in a particular class are offered the same menu of terms by the reorganization plan".[37] Although the general rule is to put secured creditors in one class and unsecured creditors in another, the Legislative Guide mentions that ordinary unsecured creditors can be divided into "different

34 The U.S. Code Title 11 Section 943(b) sets out the conditions when the court shall confirm the plan, which include that the plan complies with the provisions of this title made applicable by Section 901. Section 901(a) explicitly makes Sections 1126(c) dealing with the bankruptcy of companies applicable for municipalities, which provides that a class of claims has accepted a plan if such plan has been accepted by creditors "that hold at least two-thirds in amount and more than one-half in number" of all allowed claims. See 11 U.S.C. §§943(b), 901(a) and 1126(c).

35 11 U.S.C. §1129(a)(8). It should be noted that Section 901(a) explicitly makes Section 1129(a)(8) dealing with the bankruptcy of companies applicable for municipalities.

36 11 U.S.C. §1129(b)(1). It should be noted that Section 901(a) explicitly makes Section 1129(b)(1) dealing with the bankruptcy of companies applicable for municipalities.

37 See UNCITRAL Legislative Guide on Insolvency Law (2004) 218 <http://www.uncitral.org/pdf/english/texts/insolven/05-80722_Ebook.pdf> accessed 10 October 2014.

classes based upon their varying economic interests."[38] In determining commonality of interest, the relevant criteria may include "the nature of debts giving rise to the claims".[39]

(5.14) To take the Greek debt restructuring as an example, it can be argued that the nature of an individual issuance differs from that of other issuances with different maturities. Due to the fact that the exchange offer was extended by Greece in a pre-default context, all claims will not yet have become due and payable as a result of the operation of the acceleration clause in the event of default.[40] As a result, Greece's eligible debt instruments enjoy enormous diversity, particularly with respect to residual maturities, ranging from almost zero to 45 years.[41] Logically speaking, the nature of bonds with short-term maturity and those with long-term maturity are totally different, because the former are legally entitled to get paid before the latter.

(5.15) As far as the outcome of the restructuring is concerned, due to different residual maturities involved, the same restructuring term extended to all bondholders implies large differences in the present value haircut across the existing bonds. According to Zettelmeyer and others, the present value haircut declines with maturity, with large haircuts at the short end (in excess of 75 per cent for bonds maturing within a year) and smaller haircuts at the long end (less than 50 per cent for old bonds coming due in 2025 and beyond).[42] Such large differences confirm that the nature of an individual issuance differs from that of other issuances with different maturities, although they are all ordinary unsecured claims. As a result of these differences, claims of an individual issuance constitute a particular class by themselves. The author therefore argues that a single-limb voting procedure does resemble the cram-down procedure in the US municipality bankruptcy law.

38 *Ibid.*, 222.
39 *Ibid.*
40 Bonds issued in the international markets by emerging market sovereigns typically require a vote of 25% of the outstanding bonds in order to accelerate unmatured principal following an event of default. It should be pointed out that pre-default bond restructuring happens very often. Among the 13 debt restructurings announced between 2003 and 2013, 8 restructurings were conducted in a pre-default context. These 8 debt restructurings were announced by Dominican Republic (2004), Grenada (2004), Belize (2006), Jamaica (2010), St. Kitts and Nevis (2011), Greece (2011), Belize (2012) and Jamaica (2013). See IMF, 'Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework', *supra* note 34, 22; IMF, 'The Restructuring of Sovereign Debt –Assessing the Benefits, Risks and Feasibility of Aggregating Claims' (2003) 5 <https://www.imf.org/external/np/pdr/sdrm/2003/090303.htm> accessed 19 October 2014; Lee Buchheit et al., *supra* note 31, 10.
41 Jeromin Zettelmeyer, Christoph Trebesch and Mitu Gulati, *supra* note 8, 16.
42 *Ibid.*

5.3 Safeguard Provision for Cram-down in US Municipality Bankruptcy Law

(5.16) Given that a single-limb voting procedure resembles the cram-down procedure in the US municipality bankruptcy law, an analysis of this voting procedure would require a closer look at how cram-down procedures work. A second reading of Section 1129(b)(1) (applicable as a result of Section 901(a)) reveals that it provides not only the cram-down mechanism but also a safeguard provision to ensure that each impaired dissent class receives minimum protection. To quote the language of Section 1129(b)(1), the court shall confirm the plan under the cram down procedure "if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan."[43] In the view of the author, Section 1129(b)(1) provides minimum protection for each impaired dissent class from two distinctive aspects. It first addresses the interests of each impaired dissent class and other creditor classes by prohibiting unfair discrimination, and then maintains a balance between the interests of each impaired dissent class and that of the debtor with the fair and equitable treatment standard. The following paragraphs will discuss them in turn.

5.3.1 Prohibition of Unfair Discrimination

(5.17) Although Section 1129(b) does not provide a definition of unfair discrimination, the case law from US bankruptcy courts on this issue is quite straightforward, which indicates that the prohibition against unfair discrimination requires equal treatment of similarly situated creditors.[44] In *re Barney & Carey Co.*, the court stated, "the unfair discrimination language of section 1129(b)(1) prohibits a debtor from proposing unreasonably different treatment between classes of similar claims."[45] The court continued that "[t]he burden is on the Debtor to show that unequal treatment between classes having the same priority does not constitute unfair discrimination."[46] In re *Tucson Self-Storage, Inc.*, the court found that "[a] plan discriminates unfairly if it singles out the holder of some claim or interest for a particular treatment."[47] Similarly, the court in *re Johns-Manville Corp.* ruled that "a plan proponent may not

43 11 U.S.C. §§1129(b)(1). It should be noted that Section 901(a) explicitly makes Section 1129(a)(8) dealing with the bankruptcy of companies applicable for municipalities.

44 David Kupetz, 'Municipal Debt Adjustment Under the Bankruptcy Code' (1995) 27 Urb. Law. 531, 595, citing *In re Orfa Corp. of Philadelphia*, 129 B.R. 404, 416 (Bankr.E.D.Pa.1991) and *In re AOV Indus., Inc.*, 792 F.2d 1140, 1150 (D.C.Cir.1986).

45 *Ibid.*, citing In re Barney & Carey Co., 170 B.R. 17, 25 (Bankr.D.Mass.1994).

46 *Ibid.*

47 *Ibid.*, n. 292, citing *Oxford Life Ins. Co. v. Tucson Self-Storage, Inc.*, 166 B.R. 892, 898 (Bankr.9th Cir.1994).

segregate two similar claims or groups of claims into separate classes and provide disparate treatment for those classes."[48]

5.3.2 Fair and Equitable Standard

(5.18) As regards the fair and equitable standard, Section 1129(b)(2) sets out certain specified requirements for a plan to be fair and equitable but leaves the substance of the term "fair and equitable" open to interpretation.[49] In Chapter 11 cases involving the bankruptcy of corporates, the phrase "fair and equitable" has been interpreted to require that unsecured creditors be paid in full first before junior equity holders can be paid.[50] This interpretation is, however, not applicable in a Chapter 9 context, as a municipality does not have any equity holder. By contrast, US bankruptcy courts have construed that a Chapter 9 plan is fair and equitable if it is balanced and the debtor has taken reasonable steps to increase revenue and cut costs before proposing debt renegotiation.[51] In applying this standard, courts analyze whether the amount to be received by dissenting creditors under the plan is "all that they can reasonably expect in the circumstances."[52]

(5.19) When interpreting the meaning of "all that [dissenting creditors] can reasonably expect in the circumstances", some courts have required the debtor to exercise its taxing power to a greater extent in the facts of the case pres-

48 *Ibid.*, citing *In re Johns-Manville Corp.*, 68 B.R. 618, 636 (Bankr.S.D.N.Y.1986), aff'd, 78 B.R. 407 (Bankr.S.D.N.Y.1987), aff'd, 843 F.2d 636 (2d Cir.1988).

49 Section 1129(b)(2)(A) provides that secured claims may be treated fairly and equitably if the plan, (a) allows the secured creditor to retain its lien and to receive cash payments over time which have a present value equal to the value of its collateral as of the effective date of the plan; (b) provides for a sale of the secured creditor's collateral at which it can credit bid or (c) provides the secured creditor with the indubitable equivalent of its claim, including, among other things, returning the creditor's collateral to it. Section 1129(b)(2)(B) provides that unsecured creditors who are not paid in full are still treated fairly and equitably under a plan as long as any claim or interest that is junior will not receive or retain under the plan or on account of such junior claim or interest any property. See 11 U.S.C. §1129(b)(2).

50 See *Case v. Los Angeles Lumber Products*, 308 U.S. 106 (1939).

51 B. Summer Chandler & Mark Kaufman, 'Maybe Taxes Aren't So Certain: What is "Fair and Equitable" in a Chapter 9 Plan?' (2013) American Bankruptcy Institute Journal, 2, <http://www.mckennalong.com/media/resource/1984_American%20Bankruptcy%20Institute%20Journal.pdf> accessed 26 September 2014.

52 See *Lorber v. Vista Irrigation Dist.*, 127 F.2d 628, 639 (9th Cir. 1942); *West Coast Life Insurance Company et al. v. Merced Irrigation District*, 114 F.2d 654 (9th Cir. 1940); *Moody v. James Irrigation District*, 114 F.2d 685 (9th Cir. 1940); *Bekins v. Lindsay-Strathmore Irrigation District*, 114 F.2d 680 (9th Cir. 1940), *Jordan v. Palo Verde Irrigation District*, 114 F.2d 691 (9th Cir. 1940).

ented.[53] Other courts have held that it is not necessary that all taxes collected go to the payment of creditors and that taxes be increased where evidence indicates that this would not be feasible.[54] Indeed, while raising taxes could help the municipality to pay back its debt, it might be detrimental to attract new residents and corporations and thus would adversely affect the municipality's long-term revenues.[55] The limited body of case law suggests that to what extent the debtor shall impose new or increased taxes should be determined on a case-by-case basis.[56] Besides raising taxes, other reasonable steps the debtor shall take to increase revenue and reduce costs include (1) checking existing contracts to look for inefficiencies; (2) negotiating modifications to collective-bargaining agreements and retiree benefits; (3) cutting labor costs; (4) selling or leasing municipal assets; (5) privatizing or outsourcing certain services; and (6) securing financial support.[57]

5.4 Investment Arbitration as an Appropriate Forum to Develop a Safeguard Provision for the Single-limb Voting Procedure

(5.20) An overview of the safeguard provision for the cram-down procedure under the US municipality bankruptcy law tells us that the current legal regime of sovereign debt restructuring is seriously flawed with respect to creditor protection. In the absence of any bankruptcy rules for States, the author argues,

53 In *Fano v. Newport Heights Irr. Dist.*, the court denied the proposed plan and stated that "we are unable to find any reason why the tax rate should not have been increased sufficiently to meet the District's obligations or why it can be said that the plan is 'equitable' and 'fair' and for the 'best interest of the creditors' with no sufficient showing that the taxing power was inadequate to raise the taxes to pay them". See *Fano v. Newport Heights Irr. Dist.*, 114 F.2d 563 (9th Cir. 1940).

54 In *Lorber v. Vista Irr. Dist.*, the court analyzed the debtor's situation and found that "55 cents on the dollar was the maximum that the District could reasonably pay on outstanding bonds". See *Lorber v. Vista Irrigation Dist.*, 143 F.2d 282 (9th Cir. 1944). In *re Corcoran Hosp. Dist.*, the court "looked at the insolvency of the debtor and whether the debtor could, in fact, raise taxes sufficient to pay the bondholders in full" and concluded that "the debtor Hospital District could not raise taxes sufficient to pay more to Class 5". See *In re Corcoran Hosp. Dist.*, 233 B.R. 449, 459-60 (Bankr. E.D. Cal. 1999). In *Newhouse v. Corcoran Irr. Dist.*, the court stated that "[t]he bankruptcy of a public entity, however, is very different from that of a private person or concern. The operative assets of an irrigation district and the value of the land of the District, of course, have their evidentiary value as to the amount of money the District can reasonably raise to meet its indebtedness". See *Newhouse v. Corcoran Irr. Dist.*, 114 F. 2d 690 (9th Cir. 1940).

55 B. Summer Chandler & Mark Kaufman, *supra* note 64.

56 Main factors to take into account when deciding whether a debtor shall impose new or increased taxes include (1) the tax rates of neighboring municipalities; (2) the employment market; (3) the local population and the potential impact of increased tax burden; (4) prospects for attracting new business with increased tax burden; and (5) any new financial needs of the municipality. See *Ibid.*

57 *Ibid.*

investment arbitration could serve as an appropriate forum to develop a safeguard provision for the single-limb voting procedure employed in sovereign debt restructuring similar to those in the US municipality bankruptcy law. Notably, since 2006 four groups of foreign bondholders have brought arbitrations under bilateral investment treaties at ICSID against sovereign debtors following the debt crises.[58] Under most investment treaties, foreign investors are entitled to initiate arbitration against the host country directly for alleged breaches of treaty obligations through arbitration clauses, which often include fair and equitable treatment principle, full protection and security, no expropriation without prompt, adequate and effective compensation, as well as national and most favored nation treatment principle.[59] This section analyses the fair and equitable treatment principle ("FET") and argues that such a principle could serve as a safeguard provision for the single-limb voting procedure in sovereign debt restructuring. Before engaging in the discussion, it should be recalled that the safeguard provision for cram-down under the US municipality bankruptcy law provides that the plan shall not "discriminate unfairly" and shall be "fair and equitable" with respect to each impaired dissent class.

5.4.1 Overview of the FET Principle

(5.21) The fair and equitable treatment principle is a well-established clause in the vast majority of investment agreements, and is often drafted in three ways: (1) combined with a reference to general international law, (2) combined with a reference to customary international law, and (3) combined with other investment guarantees, for instance, the guarantee of protection and security and the obligations of most-favored-nation and national treatment.[60] According to some commentators, the issue of whether the FET is included in a separate clause or combined with other investment guarantees is not a substantive question but a stylistic one.[61] When the FET is combined with a reference to either general international law or customary international law, it generally provides that each contracting party shall accord to investments of investors of another party treatment in accordance with [international law][customary international law], including fair and equitable treatment and full protection and security.[62]

58 *Abaclat and others v. Argentine Republic*, *Giovanni Alemanni and others v. Argentine Republic*, *Giordano Alpi and others v. Argentine Republic*, and *Poštová banka, a.s. and ISTROKAPITAL SE v. Hellenic Republic*.

59 Nigel Blackaby et al., 'Chapter 8. Arbitration Under Investment Treaties' in *Redfern and Hunter on International Arbitration* (5th edn, OUP 2009), paras 8.09, 8.58-8.112.

60 Roland Klager, *'Fair and Equitable Treatment' in International Investment Law* (Cambridge 2013) 14-20.

61 *Ibid.*, 17.

62 *Ibid.*, 17 & 19.

(5.22) It is worth noting that a long-standing doctrinal debate exists with respect to the FET principle. Some argue that the FET is limited to the international minimum standard of customary international law, on the basis that the formulation of such a principle is vague and indeterminate and equating it with the international minimum standard could avoid the difficulties in addressing this norm.[63] They refer to the writings and decisions on international minimum standard to argue that there exists an established and well-known body of legal principles in customary international law.[64] On the contrary, other commentators suggest that the international minimum standard is as indeterminate as the FET principle.[65] They note that if the two concepts were intended to be interchangeable, states would have specified this expressly in their investment agreements; instead, the combination of the FET principle with a reference to international law indicates that international law only plays a complementary role.[66] Importantly, in the context of NAFTA, on 31 July 2001 the NAFTA Free Trade Commission issued a note of interpretation, which shall be binding on arbitral tribunals and provides that the concept of FET does not go beyond the customary international law minimum standard.[67]

(5.23) As far as case law is concerned, ICSID tribunals have adopted two main approaches dealing with the relation between FET and the international minimum standard in customary international law.[68] The first approach addresses FET as being equated with the minimum standard of treatment and was for example adopted by the *CMS* tribunal.[69] The second approach views FET as an autonomous concept, which is considered as higher standards than required by international law and more protective of investors' rights.[70] Between these two approaches, some tribunals chose not to decide on this issue. For instance, the *BG v. Argentina* tribunal stated that Argentina's actions fall below the

63 Giorgio Sacerdoti, *Bilateral Treaties and Multilateral Instruments on Investment Protection*, Recueil des Cours 269 (1997) 341; Roland Klager, *supra* note 89, 56.

64 Roland Klager, *supra* note 89, 56.

65 *Ibid.*, 58.

66 UNCTAD, 'Fair and Equitable Treatment', UNCTAD/ITE/IIT/11 (Vol. III) (1999)13 <http://unctad.org/en/docs/psiteiitd11v3.en.pdf> accessed 10 October 2014; Roland Klager, *supra* note 89, 59.

67 Roland Klager, *supra* note 89, 70-71.

68 *El Paso Energy International Company v. Argentina* (ICSID Case No. ARB/03/15), Award of 31 October 2011, para 331; *Impregilo S.p.A. v. Argentine Republic* (ICSID Case No. ARB/07/17), Award of 21 June 2011, paras 286-288.

69 *GMS Gas Transportation Company v. Argentina* (ICSID Case No. ARB/01/8), Award of 12 May 2005, para 284; *SAUR International SA v. Republic of Argentina* (ICSID Case No. ARB/04/4), Decision on Jurisdiction and Liability, paras 491-494.

70 *Azurix Corp. v. The Argentine Republic* (ICSID Case No. ARB/01/12), Award of 14 July 2006, para 361; *Deutsche Bank v. Democratic Socialist Republic of Sri Lanka* (ICSID Case No. ARB/09/2), Award of 31 October 2012, paras 418-419.

minimum standard and it is consequently not necessary to examine the standard of protection under the Argentine-UK BIT.[71]

5.4.2 Interpretation of the FET Principle

(5.24) Over the past decade, investment treaty tribunals have struggled unsuccessfully to define the obligation of the FET principle included in a vast majority of over 2,600 bilateral investment treaties.[72] Recent case law indicates that most tribunals find it unnecessary to engage in an extensive discussion of the definition of the FET standard, and only analyze the meaning of FET when it is applied to a set of specific facts. For instance, the tribunal in *Swisslion v. Macedonia* did not provide a precise definition of the FET standard and limited itself to subscribe "the view expressed by certain tribunals that the standard basically ensures that the foreign investor is not unjustly treated, with due regard to all surrounding circumstances, and that it is a means to guarantee justice to foreign investors."[73]

(5.25) Among those tribunals that made an attempt to define the FET standard, the tribunal in *Deutsche Bank v. Sri Lanka* confirmed the non-exhaustive definition of the FET standard offered by the *Waste Management* tribunal and listed a few components of the FET definition:

"- protection of legitimate and reasonable expectations which have been elied upon by the investor to make the investment;
- good faith conduct although bad faith on the part of the State is not equired for its violation;
- conduct that is transparent, consistent and not discriminatory, that is, not based on unjustifiable distinctions or arbitrary;
- conduct that does not offend judicial propriety, that complies with due process and the right to be heard."[74]

(5.26) In this connection the author submits that while the maximum scope of the FET principle remains unclear, its minimum reach seems rather clear-cut.

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71 *BG Group Plc v. Argentina* (UNCITRAL), Award of 24 December 2007, para 291.

72 Kenneth J. Vandevelde, 'A Unified Theory of Fair and Equitable Treatment' (2010) Journal of International Law and Politics, Vol. 43, 43, 44.

73 *Swisslion DOO Skopje v. The Former Yugoslav Republic of Macedonia* (ICSID Case No. ARB/09/16), Award of July 6, 2012, para 273, citing *PSEG Global, The North American Coal Corporation, and Konya Ingin Electrik ve Ticaret Sirketi v. Republic of Turkey* (ICSID Case No. ARB/02/5), Award of 19 January 2007, para 239; *El Paso Energy International Company v. The Argentine Republic*, *supra* note 97, para 373.

74 *Deutsche Bank v. Democratic Socialist Republic of Sri Lanka* (ICSID Case No. ARB/09/2), Award of 31 October 2012, para 420; *Waste Management, Inc. v. United Mexican States* (ICSID Case No. ARB(AF)/00/3), Award of 30 April 2004, para 98.

The sub-sections below analyze two notions covered by the FET standard that are similar to the safeguard provision under municipality bankruptcy law: (a) prohibition of unfair discrimination, and (b) legitimate expectations and the obligation of proportionality.

5.4.2.1 Prohibition of Unfair Discrimination

(5.27) The most relevant case law on unfair discrimination is *Saluka Investment BV v. Czech Republic*, which concerned the gradual privatization of the Czech banking sector.[75] In this case, the IPB bank that had been fully privatized could not participate in a government assistance program and subsequently collapsed, while three still mainly stated-owned banks obtained assistance from that program.[76] In explaining the meaning of FET and non-discrimination, the tribunal stated "any differential treatment of a foreign investor must not be based on unreasonable distinctions and demands, and must be justified by showing that it bears a reasonable relationship to rational policies not motivated by a preference for other investments over the foreign-owned investment."[77] The tribunal further developed a test for the determination of discriminatory conduct, which provides that a conduct is considered as discriminatory if similar cases are treated differently and without reasonable justification.[78]

5.4.2.2 Legitimate Expectations and the Obligation of Proportionality

(5.28) Many tribunals have dealt with the concept of legitimate expectations in the context of the FET principle. For instance, in *Tecmed v. Mexico,* the tribunal stated that the FET principle requires contracting States to "provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment."[79] In explaining what are the basic expectations, the *Tecmed* tribunal continued that the host State is expected to "act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations."[80] Similarly, the tribunal in *Saluka v. Czech Republic* also mentioned that a foreign investor may "properly expect that the

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75 *Saluka Investment BV v. Czech Republic* (UNCITRAL), Partial Award of 17 March 2006.
76 Roland Klager, *supra* note 89, 193.
77 Saluka Investment BV v. Czech Republic, *supra* note 104, para 307.
78 *Ibid.*, para 313.
79 *Técnicas Medioambientales Tecmed, S.A. v. United Mexican States* (ICSID Case No. ARB (AF)/00/2), Award of 29 May 2003, para 154.
80 *Ibid.*

[Government] implements its policies bona fide by conduct that is, as far as it affects the investor's investment, reasonably justifiable by public policies and that such conduct does not violate the requirements of consistency, transparency, even-handedness and non-discrimination."[81]

(5.29) In recent years, some tribunals have rejected a broad interpretation of the concept of legitimate expectations. For instance, the tribunal in *El Paso Energy v. Argentina* stated that the legitimate expectations are not solely the subjective expectations of investors but objective expectations under particular circumstances and with due regard to the rights of the State.[82] Importantly, several tribunals expressly associated the notion of legitimate expectations with "a promise of the administration on which the Claimants rely to assert a right that needs to be observed".[83] More recently, the tribunal in *Ulysseas v. Ecuador* also quoted with approval the holding of the tribunal in *EDF v. Romania* according to which, "[e]xcept where specific promises or representations are made by the State to the investor, the latter may not rely on a bilateral investment treaty as a kind of insurance policy against the risk of any changes in the host State's legal and economic framework."[84] Similarly, the tribunal in *Toto v. Lebanon* noted that, in the absence of a stabilization clause or similar commitment, changes in the regulatory framework would be considered as violation of the FET principle "only in case of a drastic or discriminatory change in the essential features of the transaction."[85]

(5.30) On the other hand, there are also several tribunals that found – "[w]hile specific assurances given by the host State may reinforce the investor's expectations, such an assurance is not always indispensable".[86] In clarifying this view, the *Electrabel v. Hungary* tribunal noted that:

81 *Saluka Investments B.V. v. Czech Republic*, *supra* note 104, para 307.
82 *El Paso Energy International Company v. Argentina*, *supra* note 97, para 358.
83 P*SEG Global, Inc., The North American Coal Corporation, and Konya Ingin Electrik Üretim ve Ticaret Limited Sirketi v. Republic of Turkey*, *supra* note 102, paras 239-241; *Metalpar S.A. and Buen Aire S.A. v. The Argentine Republic* (ICSID Case No. ARB/03/5), Award on the Merits of 6 June 2008, para 183.
84 *Ulysseas, Inc. v. The Republic of Ecuador* (UNCITRAL), Final Award, 12 June 2012, para 249 quoting *EDF International S.A., SAUR International S.A. and León Participaciones Argentinas S.A. v. Argentine Republic* (ICSID Case No. ARB/03/23), Award of 11 June 2012, para 217.
85 *Toto Costruzioni Generali S.p.A. v. The Republic of Lebanon* (ICSID Case No. ARB/07/12), Award of 7 June 2012, para 244.
86 *Electrabel S.A. v. Republic of Hungary* (ICSID Case No. ARB/07/19), Decision on Jurisdiction, Applicable Law and Liability dated 30 November 2012, para 7.78, citing *MTD v Chile* (ICSID Case No. ARB/01/7), Award of 25 May 2004; *GAMI Investments v Mexico* (UNCITRAL), Final Award of 15 November 2004; and *SD Myers v Canada* (UNCITRAL), Second Partial Award of 21 October 2002.

> "While the investor is promised protection against unfair changes, it is well-established that that the host State is entitled to maintain a reasonable degree of regulatory flexibility to respond to changing circumstances in the public interest. Consequently, the requirement of fairness must not be understood as the immutability of the legal framework, but as implying that subsequent changes should be made fairly, consistently and predictably, taking into account the circumstances of the investment."[87]

(5.31) More importantly, the FET principle has on several occasions been interpreted to import an obligation of proportionality. In *Tecmed v. Mexico*, the tribunal relied on case law from the European Court of Human Rights and stated that "[t]here must be a reasonable relationship of proportionality between the charge or weight imposed to the foreign investor and the aim sought to be realized by any expropriatory measure."[88] The tribunal in *Azurix v. Argentina* endorsed the reliance in *Tecmed* on case law from the European Court of Human Rights, and emphasized the need for proportionality between the means employed and the aim.[89]

(5.32) More recently, in *Occidental v. Ecuador*, the tribunal also interpreted the FET principle as requiring an obligation of proportionality. Having noted that "the overriding principle of proportionality requires that any such administrative goal must be balanced against the Claimants' own interests and against the true nature and effect of the conduct being censured", the tribunal found that the price paid by the claimants was out of proportion to the wrongdoing.[90]

5.4.3 Safeguard Provision for a Single-limb Voting Procedure in Sovereign Debt Restructuring

(5.33) In the context of sovereign debt, States often borrow from one or more of the following sources: commercial banks, bondholders, governments and multilateral institutions such as the IMF and World Bank.[91] At present, there

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87 *Electrabel S.A. v. Republic of Hungary*, *supra* note 115, para 7.77.

88 *Técnicas Medioambientales Tecmed, S.A. v. United Mexican States*, *supra* note 108, para. 122. In support of this proposition, the tribunal cited several decisions of the European Court of Human Rights: In the case of *Mellacher and Others v. Austria*, Judgment of December 19, 1989, 48, p.24; In the case of *Pressos Compañía Naviera and Others v. Belgium*, Judgment of November 20, 1995, 38, p. 19.

89 *Azurix Corp. v. The Argentine Republic*, *supra* note 99, para 311.

90 *Occidental Petroleum Corporation and Occidental Exploration and Production Company v. The Republic of Ecuador* (ICSID Case No. ARB/06/11), Award of 5 October 2012, para 450.

91 Anna Gelpern & Mitu Gulati, 'Public Symbol in Private Contract: a Case Study' (2006) 84 Wash. U. L. Rev. 1627, 1632-1633; Lex Rieffel, Chapter 6 'The Bank Advisory Committee Process', in *Restructuring Sovereign Debt: The Case for Ad Hoc Machinery* (Brookings 2003),

is no international insolvency regime governing sovereign debt crisis, and sovereign debt defaults are dealt with using an *ad hoc*, individual case-by-case approach. In practice, in order to avoid an eternal default, the sovereign debtor is compelled to seek debt relief from creditors before or shortly after the default, via an extension of maturity, and/or a reduction of the value of the claim. Such relief is obtained by renegotiating the relevant debt instruments with individual creditors, which is commonly referred to by the term "debt restructuring".

(5.34) Renegotiations with multilateral creditors are often conducted in this *ad hoc* manner. Renegotiations with bilateral creditors who are members of the Paris Club are conducted through the Club's processes. The Paris Club is an informal group of official creditors with 19 permanent members and a small secretariat in Paris.[92] Countries that are not members of the Paris Club renegotiate with the sovereign debtor on an *ad hoc* basis. Renegotiations with commercial banks are either purely *ad hoc* or conducted through the London Club, an informal group of commercial banks with no fixed membership and no secretariat.[93] Renegotiations with bondholders are conducted through exchange offers prepared by the sovereign debtor. Occasionally bondholder committees are formed on an *ad hoc* basis to facilitate the process.[94]

(5.35) Under the current legal framework, one possible situation where the issue of unfair discrimination could arise is when similarly situated creditors are treated differently. For instance, Greece excluded the bond holdings of the Europe Central Bank and other central banks from restructuring by swapping them into a new series with identical payment terms and maturity dates right before the publication of the exchange offer.[95] As mentioned earlier, municipal debtors in the US enjoy the safeguard protection concerning

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92 Paris Club official website <http://www.clubdeparis.org/sections/composition/membres-permanents-et/membres-permanents> assessed 10 October 2014. See generally Enrique Cosio-Pascal, 'The Emerging of a Multilateral Forum for Debt Restructuring: The Paris Club', UNCTAD/OSG/DP/2008/7, Discussion Papers No. 192 <http://unctad.org/en/Docs/osgdp20087_en.pdf> assessed 10 October 2014.

93 Lex Rieffel, 'The Bank Advisory Committee Process', *supra* note 9, 103.

94 For a discussion of the use of creditors' committees in the Congo debt restructuring, see Mark Richards, 'The Republic of Congo's Debt Restructuring: Are Sovereign Creditors Getting Their Voice Back?', (2010) 73 Law & Contemp. Probs 273-299. Creditors' committees were also organized in the Greek debt restructuring, see Jeromin Zettelmeyer, Christoph Trebesch and Mitu Gulati, *supra* note 8.

95 As part of this swap arrangement, the ECB committed to return any profits made through its Greek government bond holdings to its shareholders. Hence, Greece received virtually no debt relief on these bonds, both because the bulk of the ECB's Greek bond holdings were bought during 2010 at relatively small discounts, and because of its small share in the ECB (about 2 per cent). See Jeromin Zettelmeyer, Christoph Trebesch and Mitu Gulati, *supra* note 8, 5.

unfair discrimination as a result of cram-downs under section 1129(b)(1), which has been interpreted by US bankruptcy courts as prohibiting "a debtor from proposing unreasonably different treatment between classes of similar claims."[96] The author argues that a similar safeguard principle could be developed in the sovereign debt context at investment treaty tribunals. Like the *Saluka* tribunal, the *Poštová* tribunal and other future investment treaty tribunals may be asked to determine whether "similar cases are treated differently and without reasonable justification".[97] More specifically, whether the ECB and other holders of the same series of bonds are similarly situated creditors? Whether there are reasonable justifications for treating the ECB differently?

(5.36) As regards the principles of legitimate expectations and proportionality, non-participating bondholders could possibly argue that the exchange offer frustrates their legitimate expectations and is not proportionate to the aim sought to be realized by the debt restructuring. In the case of Greek debt restructuring, bondholders were offered with a package of new securities with face values equal to 31.5% and 15% of the face amount of the old bonds.[98] As discussed above, if U.S bankruptcy courts were faced with a similar situation of municipalities, they would analyze whether the amount to be received by non-participating bondholders under the plan is "all that they can reasonably expect in the circumstances."[99] In the author's view, a similar safeguard principle could be developed in the sovereign debt context at investment treaty tribunals. Like the tribunals in *Tecmed v. Mexico*, *Azurix v. Argentina*, and *Occidental v. Ecuador*, the *Poštová* tribunal and other future investment treaty tribunals may be asked to determine whether there is "a reasonable relationship of proportionality between the charge or weight imposed to the foreign investor and the aim sought to be realized by any expropriatory measure."[100]

(5.37) In light of the foregoing, the author maintains that in the absence of any bankruptcy rules for States, investment treaty arbitration could serve as an appropriate forum to develop a safeguard provision for the single-limb voting procedure employed in sovereign debt restructuring similar to those in the US municipality bankruptcy law. In developing such a safeguard pro-

96 David Kupetz, *supra* note 57, citing *In re Barney & Carey Co.*, 170 B.R. 17, 25 (Bankr.D.Mass. 1994).
97 *Saluka Investment BV v. Czech Republic*, *supra* note 104, para. 313.
98 Hellenic Republic Ministry of Finance, *supra* note 8.
99 *Lorber v. Vista Irrigation Dist.*, 127 F.2d 628, 639 (9th Cir. 1942); *West Coast Life Insurance Company et al. v. Merced Irrigation District*, 114 F.2d 654 (9th Cir. 1940); *Moody v. James Irrigation District*, 114 F.2d 685 (9th Cir. 1940); *Bekins v. Lindsay-Strathmore Irrigation District*, 114 F.2d 680 (9th Cir. 1940), *Jordan v. Palo Verde Irrigation District*, 114 F.2d 691 (9th Cir. 1940).
100 *Técnicas Medioambientales Tecmed, S.A. v. United Mexican States*, *supra* note 108, para. 122.

vision, the investment treaty tribunals could take into consideration the Principles on Responsible Sovereign Lending and Borrowing developed in the context of the United Nations Conference on Trade and Development ("UNCTAD Principles"). It is worth noting that the dissenting arbitrator in *Ambiente Ufficio S.p.A. and others v. Argentine Republic* has referred to the UNCTAD Principles as relevant law.[101] Although these Principles do not specify the fair and equitable treatment standard in the sovereign debt context as such, they could still provide some useful guidance for the development of this standard.

5.5 Concluding Remarks

(5.38) Since spring 2013, the IMF began its revisit of reform ideas for sovereign debt restructuring.[102] Importantly, the IMF praised the effectiveness of the Greek Bondholder Act in facilitating sovereign debt restructuring, and subsequently introduced the concept of a single-limb voting procedure.[103] As explained in this article, the single-limb voting procedure will enable contract terms to be amended on the basis of a single vote across all affected instruments, thereby disallowing a creditor or a group of creditors to obtain a blocking position in a particular series. In the view of the author, the single-limb voting procedure resembles the cram-down procedure in the US municipality bankruptcy law, with the exception of one missing element. Whereas the cram-down procedure contains a safeguard provision that ensures minimum protection for each impaired dissent creditor class through the prohibition of unfair discrimination and fair and equitable treatment principle, the single-limb voting procedure is silent about creditor protection in this context. In searching for a safeguard provision for the single-limb voting procedure, the author discovers the similarities between the safeguard pro-

101 Juan Pablo Bohoslavsky, Yuefen Li and Marie Sudreau, 'Emerging customary international law in sovereign debt governance?', Capital Markets Law Journal, Vol. 9, No.1, 55, 65 <http://cmlj.oxfordjournals.org/content/9/1/55.full.pdf+html> accessed 10 October 2014, citing *Ambiente Ufficio S.p.A. and others v. Argentine Republic*, dissenting opinion of Santiago Torres Bernardes, 2 May 2013 <http://www.italaw.com/cases/documents/2058> accessed 10 October 2014.

102 IMF Press Release No.14/459 dated 6 October 2014, *supra* note 2; IMF Public Information Notice (PIN) No. 13/61 dated 23 May 2013 <http://www.imf.org/external/np/sec/pn/2013/pn1361.htm> accessed 10 October 2014. For a discussion of the old reform proposal, see Sean Hagan, 'Designing a Legal Framework to Restructure Sovereign Debt' (2005) 36 Geo. J. Int'l L. 299; IMF, 'The Design of the Sovereign Debt Restructuring Mechanism-Further Considerations', prepared by the Legal and Policy Department and Review Departments (Nov. 2002) <https://www.imf.org/external/np/pdr/sdrm/2002/112702.htm> accessed 10 October 2014.

103 IMF, 'Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework', *supra* note 34, paras 38 & 42; IMF, 'Strengthening the Contractual Framework to Address Collective Action Problems in Sovereign Debt Restructuring', *supra* note 3, 20.

vision for cram-down procedures and the fair and equitable treatment principle under investment treaties, and argues that investment arbitration could serve as an appropriate forum to develop a safeguard provision for the single-limb voting procedure.

(5.39) According to the author, investment treaty tribunals should be trusted to exercise their discretion and determine complex and delicate issues, such as whether the amount received by non-participating bondholders is all that they can reasonably expect in the circumstances or is proportionate to the aim sought to be realized by the debt restructuring. In this connection, it is worth emphasizing that one of the often-cited advantages of arbitration is the potential for choosing arbitrators with experience and expertise relevant to the dispute. As arbitration is merely a dispute resolution mechanism, it would be wrong to suggest that investment treaty tribunals lack the expertise to play the role of a bankruptcy court.[104] In practice, the parties to a dispute can appoint whomever they want as arbitrator and they certainly can choose someone with sovereign debt or bankruptcy law background.

(5.40) One key limitation for investment treaty tribunals to safeguard dissent creditors' interest lies in the fact that not all sovereign debt claims can be brought to investment treaty tribunals. A mere breach of the debt contract by a sovereign State differs from a breach of investment treaty obligations, as the former situation does not automatically trigger State responsibility.[105] It is worth mentioning that a State's debt contract is not a treaty itself and cannot involve State responsibility as an international obligation. The claim of breach of contract will be determined in accordance with the applicable municipal law.[106] Nevertheless, breach of a sovereign debt contract not governed by international law may entail state responsibility when there is a separate breach of a treaty obligation or a customary international law obligation governing the treatment of a foreigner and foreign property. To put it differently, while a mere breach by a state of a contract with foreign investors does not violate international law, a sovereign act of a State contrary to such a contract may do so.[107] Hence, arguably claims concerning the enactment of the Greek Bondholder Act may be brought before investment treaty tribunals, but not claims arising out of the contractual operation of CACs with

104 Michael Waibel, *Sovereign Defaults Before International Courts and Tribunals* (Cambridge 2013), 323.

105 Monique Sasson, 'Chapter 6: Contract versus Treaty Claims' in *Substantive Law in Investment Treaty Arbitration: The Unsettled Relationship between International Law and Municipal Law* (Kluwer 2010), 150; Ian Brownlie, *Principles of Public International Law* (Oxford 2008), 546–547.

106 Ian Brownlie, *supra* note 105, 549.

107 Andrew Newcombe & Lluís Paradell, 'Chapter 9 – Observance of Undertakings' in *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer Law International 2009), 438-439.

a single-limb voting procedure in sovereign bonds. Precisely because not all sovereign debt claims can be filed before investment treaty tribunals, investment arbitration could serve as an appropriate forum to develop a safeguard provision for the single-limb voting procedure but not as an appropriate forum to apply the safeguard provision once developed. The search for an appropriate forum to apply the safeguard provision constitutes an entirely different issue and merits careful consideration and discussion elsewhere.

6 Settlement of Sovereign Debt Disputes

The Present State of Law and Perspectives of Further Development

6.1 Introduction

(6.1) On September 9, 2014, the United Nations General Assembly took a big step forward and adopted a resolution entitled "Towards the establishment of a multilateral legal framework for sovereign debt restructuring processes", with 124 votes in favour, 11 votes against and 41 abstentions.[1] Prepared by Bolivia on behalf of the Group of 77 and China, the resolution stresses the importance of a timely, effective, comprehensive and durable solution for developing countries in order to promote economic growth and development in an inclusive manner.[2] More importantly, the resolution decides to "elaborate and adopt through a process of intergovernmental negotiations, as a matter of priority during its sixty-ninth session, a multilateral legal framework for sovereign debt restructuring processes with a view, inter alia, to increasing the efficiency, stability and predictability of the international financial system and achieving sustained, inclusive and equitable economic growth and sustainable development, in accordance with national circumstances and priorities".[3] It also decides to "define the modalities for the intergovernmental negotiations and the adoption of the text of the multilateral legal framework at the main part of its sixty-ninth session, before the end of 2014".[4]

(6.2) The adoption of this resolution was prompted by the so-called "trial of the century" in sovereign debt restructuring – *NML Capital Ltd. v. Republic of Argentina.* In October 2012, the US Court of Appeals for the Second Circuit affirmed the injunction issued by Judge Thomas Griesa from the US District Court for the Southern District of New York to remedy Argentina's breach of the *pari passu* clause, which provides that the debtor's payment obligation under that particular bond series shall rank equally with all other existing and

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1 UN General Assembly Press Release dated 9 September 2014 on "Resolution on Sovereign Debt Restructuring Adopted by General Assembly Establishes Multilateral Framework for Countries to Emerge from Financial Commitments", available at http://www.un.org/News/Press/docs/2014/ga11542.doc.htm (last visited 1 Aug 2015).

2 UN Document A/68/L.57/Rev.1, available at http://www.un.org/ga/search/view_doc.asp?symbol=a/68/l.57/rev.1 (last visited 1 Aug 2015).

3 *Ibid.*, p. 4.

4 *Ibid.*

future unsubordinated and unsecured external indebtedness.[5] In its operative part, this injunction forbids Argentina to pay exchange bondholders any amount due under the terms of the exchange bonds without concurrently or in advance paying plaintiffs the same percentage of the amount due to them.[6] This formula means that, if Argentina pays exchange bondholders the full amount due under the exchange bonds, it will have to pay holdouts in full in respect of the terms of the original bonds. Argentina strongly contested this payment method and subsequently filed an appeal to the US Supreme Court. On 16 June 2014, the Supreme Court announced that it refuses to hear Argentina's appeal.[7]

(6.3) On 7 August 2014, Argentina sought to institute proceedings against the US before the International Court of Justice ("ICJ"), arguing that the US "has committed violations of Argentine sovereignty and immunities and other related violations as a result of judicial decisions adopted by US tribunals concerning the restructuring of the Argentine public debt".[8] On the same day, the ICJ transmitted Argentina's application to the US government and announced that no action will be taken in the proceedings unless and until the US consents to its jurisdiction in the case.[9] Within a day, the US State Department replied negatively.[10] Following this failed attempt, Argentina shifted its attention to the UN General Assembly and stated publicly that the time has become ripe to create a legal framework for sovereign debt restructuring that respects creditors while allowing debtors to recover from debt crisis safely.[11]

(6.4) Through analyzing the existing dispute settlement mechanisms for sovereign debt restructuring, this paper shares Argentina's view that the time has become ripe to create a legal framework for sovereign debt restructuring and welcomes the newly adopted resolution. It is structured as follows: Part II provides an overview of sovereign lending and borrowing and then explains the categories of sovereign debt disputes. Part III describes the *status quo* of

5 *NML Capital, Ltd. v. Republic of Argentina*, No. 12-105-(L) (2d Cir. 26 Oct. 2012).
6 *NML Capital, Ltd. v. Republic of Argentina*, 08 Civ. 6978 (TPG), 09 Civ. 1707 (TPG), 09 Civ. 1708 (TPG) (S.D.N.Y., 21 Nov. 2012).
7 Order List, Certiorari- Summary Disposition of 16 June 2014, available at http://www.supremecourt.gov/orders/courtorders/061614zor_2b8e.pdf (last visited 1 Aug 2015).
8 International Court of Justice Press Release dated 7 August 2014, available at http://www.icj-cij.org/presscom/files/4/18354.pdf (last visited 1 Aug 2015).
9 *Ibid.*
10 News item, "US refuses to recognize UN court jurisdiction on Argentina's debt", available at http://rt.com/news/179228-argentina-us-un-debt/ (last visited 1 Aug 2015).
11 UN General Assembly Press Release dated 9 September 2014 on "Resolution on Sovereign Debt Restructuring Adopted by General Assembly Establishes Multilateral Framework for Countries to Emerge from Financial Commitments", available at http://www.un.org/News/Press/docs/2014/ga11542.doc.htm (last visited 1 Aug 2015).

the settlement of sovereign debt disputes, including disputes brought under dispute resolution clauses in debt instruments as well as those initiated pursuant to arbitration clauses under investment treaties. Part IV focuses on the problems with the *status quo* and identifies problems in connection with both domestic courts and investment treaty tribunals. Part V discusses the perspective of further development and assesses the desirability and feasibility of mediation, arbitration and adjudication to solve future sovereign debt disputes. Part VI concludes this paper.

6.2 Origin of Sovereign Debt Disputes

(6.5) The typical lenders to sovereign States include multilateral creditors, such as the International Monetary Fund, the World Bank, and regional development banks; bilateral creditors comprised of other sovereign States or State entities; and private creditors, such as commercial banks and bondholders. While commercial banks and bondholders lend for profit, bilateral creditors and multilateral creditors do not. Bilateral creditors often extend credit to advance political and social objectives, such as ensuring that domestic exporters are not disadvantaged by financial support offered by other governments, or sharing the costs of building infrastructure projects that can help the debtor achieve higher rates of economic growth.[12] Multilateral creditors frequently lend for the purpose of information provision in terms of monitoring government policies in recipient countries and the exercise of conditionality aimed at changing governmental policies.[13]

(6.6) At present, there is no international insolvency regime governing sovereign debt defaults. In order to avoid an eternal default, the sovereign debtor is compelled to seek debt relief from creditors before or shortly after the eve of default, via an extension of maturity, and/or a reduction of the value of the claim. Such relief is obtained by renegotiating the relevant debt instruments with individual creditors. Renegotiations with multilateral institutions

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12 L. Rieffel, "What Is Broken? What Fixes Make Sense?", Chapter 12 in Restructuring Sovereign Debt: The Case for Ad Hoc Machinery (2003, Brookings), p. 282. It is worth noting that China as a major bilateral lender to developing countries has a different approach towards bilateral lending. For example, Chinese loans generally do not require any change of national economic policies. See M. Mattlin & M. Nojonen, "Conditionality in Chinese bilateral lending", BOFIT Discussion Papers (14/2011); E. Downs, "INSIDE CHINA INC.: China Development Banks' Cross-border Energy Deals", The John L. Thornton China Center at Brookings (2011).

13 D. Rodrik, "Why is There Multilateral Lending?", NBER Working Paper No. 5160 (June 1995), p. 2. Crippa discusses the human right issues involved in projects financed by multilateral development banks. See L. Crippa, "Multilateral Development Banks and the Human Right Responsibility", 3 Am. U. Int'l L. Rev. 25 (2010): 531-577.

are often conducted in an *ad hoc* manner. Renegotiations with governments who are members of the Paris Club are conducted through the Club's processes. The Paris Club is an informal group of official creditors with 19 permanent members and a small secretariat in Paris.[14] Countries that are not members of the Paris Club renegotiate with the sovereign debtor on an *ad hoc* basis. Renegotiations with commercial banks are either purely *ad hoc* or conducted through the London Club, an informal group of commercial banks with no fixed membership and no secretariat.[15] Renegotiations with bondholders are conducted through exchange offers prepared by the sovereign debtor. Occasionally bondholder committees are formed on an *ad hoc* basis to facilitate the process.[16]

(6.7) In practice, disputes between the sovereign debtor and its creditors may arise from different kinds of obligations provided in loan agreements or bond contracts. The most commonly known obligation for the debtor is the repayment of debt. For instance, bond contracts generally provide that the bond issuer is pledged for the due and punctual payment of principal of, and interest on, the bonds.[17] Other obligations may include the *pari passu* clause, mandatory repayment clause, pro rata sharing clause, and negative pledge clause. The *pari passu* clause is often found in bond contracts and provides that the bonds of that particular issue shall rank equally among themselves, and that the debtor's payment obligation under that particular issue shall rank equally with all other existing and future unsubordinated and unsecured external indebtedness.[18] The mandatory repayment clause and

14 Paris Club official website, available at http://www.clubdeparis.org/sections/composition/membres-permanents-et/membres-permanents, (last visited 1 Aug 2015). See generally E. Cosio-Pascal, "The Emerging of a Multilateral Forum for Debt Restructuring: The Paris Club", UNCTAD/OSG/DP/2008/7, Discussion Papers No. 192, available at http://unctad.org/en/Docs/osgdp20087_en.pdf (last visited 1 Aug 2015).

15 L. Rieffel, "The Bank Advisory Committee Process", Chapter 6 in Restructuring Sovereign Debt: The Case for Ad Hoc Machinery (2003, Brookings), p. 103.

16 For a discussion of the use of creditors' committees in the Congo debt restructuring, see M. Richards, "The Republic of Congo's Debt Restructuring: Are Sovereign Creditors Getting Their Voice Back?", (2010) 73 Law & Contemp. Probs 273-299. Creditors' committees were also organized in the Greek debt restructuring, see J. Zettelmeyer, C. Trebesch and M. Gulati, "The Greek Debt Exchange: An Autopsy", Economic Policy, Vol. 28, Issue 75, pp. 513-563 (July 2013).

17 The Republic of Lithuania _100,000,000 Floating Rate Amortising Notes due 2021, Offering Circular dated 12 March 2009 (on file with the author).

18 The usage of *pari passu* clauses in unsecured bonds issued from 1960 to 2011 is recorded as follows: 123/144 (1960-1979), 429/464 (1980-1999), and 684/691 (2000-2011). See M. Gulati and R. Scott, The Three and a Half Minute Transaction: Boilerplate and the Limits of Contract Design (2012, Chicago), Appendix 7. Wood lists a few examples of the pari passu clause in sovereign bonds, e.g. Pakistan (15 November 1999), Ecuador (27 July 2000), Ukraine (8 February 2001), Russian (25 February 2004), Argentina (10 January 2005), and Dominican

pro rata sharing clause often appear in bank syndications. The mandatory repayment clause requires pro rata payments to all lenders in the event of a prepayment to any lender.[19] The pro rata sharing clause states that any bank receiving a greater proportion of its share must pay the excess to the agent bank who then redistributes to all banks on a pro rata basis.[20] Finally, the negative pledge clause appears in nearly all kinds of sovereign debt instruments. Such a clause restricts the sovereign debtor's ability to grant security interests in its property to secure other creditor by providing that if the debtor issues new debt and grants new creditors a security interest in the debtor's assets, the debtor has to grant old creditors an equivalent security interest.[21]

6.3 Settlement of Sovereign Debt Disputes: Status Quo

6.3.1 Dispute Resolution Clauses in Debt Instruments

6.3.1.1 Overview

(6.8) Different types of dispute resolution clauses exist in different kinds of sovereign debt instruments. With respect to loan agreements between the sovereign debtor and multilateral creditors, arbitration is the preferred dispute resolution mechanism. Arbitration clauses are included in the general conditions of the loan agreements offered by the International Bank for Reconstruction and Development,[22] the Inter-American Development Bank,[23] the African Development Bank,[24] the Asian Development Bank,[25] the Caribbean

Republic (20 April 2005). P. Wood, "Sovereign insolvency: the bankruptcy ladder of priorities and the pari passu clause", Tijdschrift voor Financieel Recht (Mar. 2012), pp. 66-67.

19 M. Wright, "The Pari Passu Clause in Sovereign Bond Contracts: Evolution or Intelligent Design?", 1 Hofstra L. Rev. 40 (2011), p. 5; L. Buchheit, "The Search for Intercreditor Parity", 8 L. & Bus. Rev. Am. 73 (2002), p. 76.

20 P. Wood, "Sovereign insolvency: the bankruptcy ladder of priorities and the pari passu clause", Tijdschrift voor Financieel Recht (Mar. 2012), p. 69.

21 M. Gulati and R. Scott, The Three and a Half Minute Transaction: Boilerplate and the Limits of Contract Design (2012, Chicago), p. 34. M. Wright, "The Pari Passu Clause in Sovereign Bond Contracts: Evolution or Intelligent Design?", 1 Hofstra L. Rev. 40 (2011), p. 6.

22 *See* Section 8.04 ("*Arbitration*") of the General Conditions for Loans of the International Bank for Reconstruction and Development.

23 *See* Chapter VIII ("*Arbitration Procedure*") of the General Conditions of Inter-American Development Bank.

24 *See* Section 10.04 ("*Settlement of Disputes*") of the General Conditions Applicable to the African Development Bank Loan Agreements and Guarantee Agreements (Sovereign Entities).

25 *See* Section 11.04 ("*Arbitration*") of the Ordinary Operations Loan Regulations of the Asian Development Bank.

Development Bank,[26] the International Fund for Agricultural Development,[27] and the OPEC Fund for International Development.[28] In terms of bilateral loans between one State and another, often in the form of official development assistance, it is difficult to name the most commonly used dispute resolution method, as most loan agreements are often negotiated individually, with terms that remain confidential. Moving to commercial bank loans, domestic courts are the popular dispute resolution fora due to the negative attitudes toward arbitration on the part of commercial banks.[29] Similar to commercial bank loans, sovereign bonds generally provide that the parties shall resort to domestic courts to settle their disputes. Nevertheless, sovereign bonds issued by a number of countries expressly permit bondholders to bring claims in arbitration.[30]

(6.9) Despite the widespread inclusion of arbitration clauses in multilateral loans, however, no evidence exists to date of an arbitration clause in a development bank loan agreement being utilized. Instead, the terms of development bank loans are simply renegotiated if and when difficulties with respect to repayment arise. The absence of resort to arbitration in this area can perhaps be explained by the close relationship that develops between the development institution and its borrower, and by the leverage that the development institution holds.[31] In the context of commercial bank loans and sovereign bonds, numerous creditors have initiated legal proceedings against sovereign debtors in domestic courts all over the world, in particular New York and London.[32]

26 *See* Article XIII ("*Arbitration*") of the General Provisions Applicable to Loan Agreements with Borrower Only of the Caribbean Development Bank.

27 *See* Section 14.04 ("*Arbitration*") of the General Conditions for Agricultural Development Financing.

28 *See* Article 9.03 ("*Negotiation/Arbitration*") of the General Conditions Applicable to Public Sector Loan Agreements.

29 G. Affaki, "A Banker's Approach to Arbitration", in: K. Gabrielle & F. Viviane (eds.), Arbitration in Banking and Financial Matters 68 (2003).

30 Bonds issued by Brazil, El Salvador, Estonia, Georgia, Poland, the Slovak Republic and Ukraine have all included arbitration clauses, although in the case of the Eastern European issuers, arbitration was provided as an option alongside the jurisdiction of the English courts, to be invoked at the bondholder's discretion. M. Weidemaier, Disputing Boilerplate, 82 Temp. L. Rev. 1 (spring 2009).

31 K. Cross, Arbitration as a Means of Resolving Sovereign Debt Disputes, 17(3) Am. Rev. of Int'l Arb. 335, fn. 26 (2006).

32 Schumacher recently conducted empirical research concerning sovereign debt litigation filed against debtor governments in the US and UK courts between 1976 and 2010. This research shows that 108 cases were filed in the US and the UK by foreign banks, bondholders and other commercial creditors during this period, and that these cases relate to 29 of the 180 sovereign debt restructurings with private creditors (16%). It further reveals that 27 out of 69 debtor governments have been sued. See J. Schumacher et al., "Sovereign Defaults in Court: The Rise of Creditor Litigation 1976-2010", p. 8, available at http://dx.doi.org/10.2139/ssrn.2189997 (last visited 17 Sep 2014).

6.3.1.2 Examples

(6.10) Traditionally, legal proceedings against sovereign debtors in foreign domestic courts have been exclusively based on an allegation of the debtor's failure to pay. Given that the contract terms in respect of payment obligation are generally unambiguous, the dispute in such proceedings mainly concerns the issue of sovereign immunity, that is, to what extent exceptions to sovereign immunity apply.[33] Following Argentina's default in 2001, several cases were brought by bondholders against Argentina before the US District Court for the Southern District of New York and then the US Court of Appeals for the Second Circuit. For instance, in *Capital Ventures International v. Republic of Argentina*, the plaintiff-appellant sued Argentina to recover amounts due to it under Argentina's US bonds and German bonds.[34] Following the district court's dismissal of the plaintiff's German bond claims, the Second Circuit reserved that decision and held that Argentina had explicitly waived its sovereign immunity to suits in US Courts on German bond claims according to the German bond offering circulars.[35] In *Aurelius Capital Partners, LP v. Republic of Argentina*, the plaintiffs-appellees sought to attach Argentine social security funds held by private corporations and scheduled to transfer to the Administration (i.e. a political subdivision of Argentina).[36] The Second Circuit reversed the district court's decision in favor of the plaintiffs and held that the commercial activity exception does not apply because the funds have not been used for a commercial activity at the time the attachment order was issued by the district court.[37]

(6.11) More interestingly, in *EM Ltd v. Republic of Argentina*, plaintiffs-appellants NML Capital Ltd and EM Ltd made an attempt to attach funds held in an account of the central bank of Argentina at the Federal Reserve Bank of New

33 Under the U.S. Foreign Sovereign Immunity Act, exceptions concerning waiver and commercial activity are of particular relevance in the context of sovereign default.33 The waiver exception provides jurisdiction in situations "in which the foreign state has waived its immunity either explicitly or by implication". The commercial activity exception is the most commonly litigated exception. It allows U.S. courts to exercise jurisdiction over a foreign sovereign when a plaintiff's claim is based upon the sovereign's act outside of the U.S. in connection with the commercial activity of the sovereign that causes a direct effect in the U.S. See 28 U.S. Code § 1605 (a). The text is available at http://www.law.cornell.edu/uscode/text/28/1605 (last visited 1 Aug 2015).

34 *Capital Ventures International v. Republic of Argentina*, 552 F 3d 289 (2nd Cir 2009).

35 *Ibid.*, p. 293. Section 13 (4) of the German bond offering circulars states: "To the extent that the Republic has or hereafter may acquire any immunity (sovereign or otherwise) from jurisdiction of any court or from any legal process [...], the Republic hereby irrevocably waives such immunity in respect of its obligations under the Bonds to the extent it is permitted to do so under applicable law".

36 *Aurelius Capital Partners, LP v. Republic of Argentina*, 584 F 3d 120 (2nd Cir 2009).

37 *Ibid.*, p. 130.

York.[38] This attempt failed when the US Court of Appeals for the Second Circuit held that the plaintiffs failed to establish that the account had become Argentina's property used for a commercial activity in the US[39] A few years later, however, the same plaintiffs-appellees succeeded in attaching Argentinean assets held in a trust administered by the US Bank Trust National Association in New York.[40] The Second Circuit affirmed the district court's decision in favor of the plaintiffs, concluding that the assets were being used to facilitate the sale of securities, which qualified as commercial activity.[41] Similarly, the same plaintiffs also succeeded in attaching the New York bank account of a sub-unit of Argentina's Ministry of Science, Technology, and Productive Innovation ("ANPCT").[42] The Second Circuit held that the account was used by the ANPCT to purchase scientific equipment, which qualified as commercial activity.[43] More recently, the same plaintiffs managed to obtain a discovery order against banks in the US and aboard, including Bank of America, to seek information concerning Argentina's assets and accounts.[44]

(6.12) Over the past decade, various creditors in different jurisdictions have made attempts to circumvent the enforcement problem by arguing that, as a result of the *pari passu* clause, sovereign debtors are prevented from making payments to other creditors without paying the litigating creditors on a *pro rata* basis.[45] A *pari passu* clause is a standard clause included in public or private international unsecured debt obligations, which often provides that "[Country X] shall ensure that its obligations hereunder shall rank pari passu among themselves and with all of its other present and future unsecured and unsubordinated Public Debt."[46]

38 *EM Ltd v. Republic of Argentina*, 473 F 3d 463, p. 465 (2nd Cir 2007).
39 *Ibid.*, pp. 475 & 481.
40 *EM Ltd v. Republic of Argentina*, 389 F App'x 38 (2nd Cir 2010).
41 *Ibid.*, p.44.
42 *NML Capital, Ltd v. Republic of Argentina*, 680 F 3d 254 (2nd Cir 2012).
43 *Ibid.*, p. 260.
44 *EM Ltd v. Republic of Argentina*, No 11-4065-CV(L), 2012 WL 3553367 (2nd Cir 2012).
45 See *Elliott Assocs. LP*, unreported September 26, 2000, General Docket No. 2000/QR/92, Court of Appeal of Brussels, 8th Chamber; *Red Mountain Finance Inc v. Democratic Republic of Congo*, No. CV 00-0164 R (C.D. Cal. 29 May 2001); *Republique Du Nicaragua v. INC invs. LLC No.2003/KR/334*, p. 2 (Ct. App. Brussels, 9th Chamber, 2004); *Macrotenic International Corp v. Republic of Argentina and EM Ltd v. Republic of Argentina* (S.D.N.Y. January 12, 2004) (No.02 CV 5932 (TPG), No. 03 CV 2507 (TPG)); *NML Capital, Ltd. v. Republic of Argentina*, No. 12-105-(L) (2d Cir. 26 Oct. 2012). See generally M. Gulati and R. Scott, The Three and a Half Minute Transaction: Boilerplate and the Limits of Contract Design (2012, Chicago); R. Olivares-Caminal, Legal Aspects of Sovereign Debt Restructuring (2009, Sweet & Maxwell); L. Buchheit & J. Pam, "The Pari Passu Clause in Sovereign Debt Instruments", 53 Emory L.J. 913 (2004).
46 R. Olivares-Caminal, Legal Aspects of Sovereign Debt Restructuring (2009, Sweet & Maxwell), p. 84; Offering Memorandum of the Government of Belize dated December 18, 2006, for the exchange of US Dollar Bonds due 2029, p. 142.

(6.13) In September 2000, a Brussels Court of Appeals issued a restraining order in *Elliott* prohibiting a fiscal agent and a payment settlement system from paying interest on Peru's Brady Plan Bonds.[47] In response to this decision, INC Belgian Law 4765 (C-2004/03482) was passed in November 2004 to prohibit attachment of cash accounts held with Belgium clearing systems.[48] Moving to the US courts, a New York district court in January 2014 was asked to consider whether the *pari passu* clause in Argentina's bonds could not be used by judgment creditors as a legal basis to interfere with Argentina's payment of its other indebtedness.[49] The court did not answer the core question but issued a discovery order asking Argentina to divulge information about government property outside the country that is used for commercial purposes.[50]

(6.14) More recently, in October 2012, the United States Court of Appeals for the Second Circuit in *NML Capital Ltd. v. Republic of Argentina* affirmed the district court's decision to issue injunctions designed to remedy Argentina's breach of the *pari passu* clause in certain bond indentures, on the grounds that Argentina had issued new debt pursuant to exchange offers in 2005 and 2010 and was making the required payments on this new debt, but had declared through legislation that it would make no payments to those still holding the old bonds.[51] Upon the Second Circuit's request to clarify how the payment formula in the injunction will operate, the district court clarified, in a subsequent order issued on 21 November 2012, that the payment formula in the injunction is intended to operate as follows: whenever Argentina pays any amount due under the terms of the exchange bonds, it must concurrently or

47 M. Gulati and R. Scott, The Three and a Half Minute Transaction: Boilerplate and the Limits of Contract Design (2012, Chicago), pp. 23-24, citing Elliott Assocs. LP, unreported September 26, 2000, General Docket No. 2000/QR/92, Court of Appeal of Brussels, 8th Chamber.

48 R. Olivares-Caminal, "The Pari Passu Interpretation in the Elliott Case: A Brilliant Strategy But An Awful (Mid-Long Term) Outcome", Hofstra Law Review, vol 40, no 39, p. 52 (2012), citing MONITEUR BELGE [M.B.] [Official Gazette of Belgium], Dec. 28, 2004, 85, 854, http://www.ejustice.just.fgov.be/mopdf/2004/12/28_1.pdf.

49 R. Olivares-Caminal,"To Rank Pari Passu or Not to Rank Pari Passu: That is The Question in Sovereign Bonds After the Latest Episode of the Argentine Saga", Law & Business Review of the Americas, vol 15, no 4, p. 753 (2009), citing *Macrotenic International Corp v. Republic of Argentina and EM Ltd v. Republic of Argentina* (S.D.N.Y. January 12, 2004) (No.02 CV 5932 (TPG), No. 03 CV 2507 (TPG)).

50 R. Olivares-Caminal, Legal Aspects of Sovereign Debt Restructuring, Legal Aspects of Sovereign Debt Restructuring (2009, Sweet & Maxwell), p. 90.

51 See *NML Capital, Ltd. v. Republic of Argentina*, No. 12-105-(L) (2d Cir. 26 Oct. 2012). For a discussion of this case, see Global Law Intelligence Unit, Allen & Overy LL.P, "The pari passu clause and the Argentine case", 27 Dec. 2012; W. Weidemaier, "Sovereign Debt After NML v. Argentina", Capital Markets Law Journal, available at http://ssrn.com/abstract=2199655 (last visited 1 Aug 2015).

in advance pay plaintiffs the same *percentage* of the amount due to them.[52] This case was subsequently filed to the Supreme Court, which refused to hear Argentina's appeal on 16 June 2014.[53]

(6.15) Based on these examples, one can conclude that sovereign debt disputes brought under dispute resolution clauses in debt instruments before domestic courts fall under two main categories: (1) claims based on the debtor's failure to repay, and (2) claims concerning a breach of the *pari pass*u clause.

6.3.2 Arbitration Clauses Under Investment Treaties

6.3.2.1 Overview

(6.16) Besides the dispute resolution clauses under bond contracts or loan agreements, creditors may also rely on investment treaties concluded between their home country and other countries for protection. The purpose of investment treaties is to provide eligible investments with powerful substantive protections. These protections often include guarantees of fair and equitable treatment to investments; promises to permit free transfers of investment returns; promises not to discriminate in favor of investments made by nationals (i.e. national treatment) or in favor of investors from third countries (i.e. most-favored nation treatment); guarantees against expropriation without prompt, adequate and effective compensations; and promises to honor contractual undertakings in respect of investments.[54] Arguably, coercive or discriminatory acts of a defaulting sovereign debtor may qualify as a breach of investment treaty obligations.[55]

(6.17) Under investment treaties, the State parties concerned agree that any disputes would be resolved by arbitration.[56] On most occasions, foreign investors are entitled to initiate arbitration against the host country directly

52 See *NML Capital, Ltd. v. Republic of Argentina*, 08 Civ. 6978 (TPG), 09 Civ. 1707 (TPG), 09 Civ. 1708 (TPG) (S.D.N.Y., 21 Nov. 2012).

53 Order List, Certiorari- Summary Disposition of 16 June 2014, available at http://www.supremecourt.gov/orders/courtorders/061614zor_2b8e.pdf (last visited 1 Aug 2015).

54 N. Blackaby et al., "Chapter 8. Arbitration Under Investment Treaties", in: Redfern and Hunter on International Arbitration, 5th ed (Oxford, 2009), paras. 8.09, 8.58-8.112; L. Reed et al., "Chapter 3: ICSID Investment Treaty Arbitration", in: Guide to ICSID Arbitration (Kluwer, 2010), pp. 73-95; M. Mcilwrath & J. Savage, "Chapter Seven: ICSID and Investment Treaty Arbitration", in: International Arbitration and Mediation: A Practical Guide (Kluwer, 2010), paras. 7.022-7.032.

55 K. Cross, "Chapter 12- Sovereign Arbitration", in: Sovereign Debt Management, R. Lastra & L. Buchheit (eds.), (Oxford, 2014), para. 12.10.

56 N. Blackaby et al., "Chapter 1 on An Overview of International Arbitration", in: Redfern and Hunter on International Arbitration (Oxford, 2009), para. 1.229.

for alleged breaches of treaty obligations. Different from a classic agreement to arbitrate that is made between the parties themselves, in investment treaties the State party seeking foreign investment makes a "standing offer" to arbitrate any future dispute between itself and a foreign investor of the other State party to the treaty.[57] An "agreement to arbitrate" is only formed when a dispute actually arises and the foreign investor accepts this offer to arbitrate.[58]

(6.18) Statistics show that, as of today, 2222 bilateral investment treaties and 274 other international investment agreements have been concluded and entered into force.[59] The total number of publicly known arbitration initiated by foreign investors against the host country reached 568 by the end of 2013.[60] Among these cases, 98 States have been respondents.[61] Since 2006, investment arbitration has become relevant in the context of sovereign debt restructuring.

6.3.2.2 Examples

(6.19) Between 2006 and 2008, three groups of bondholders have initiated arbitration at the International Centre for Settlement of Investment Disputes ("ICSID") against Argentina following the debt default in 2001, pursuant to the Agreement between the Argentine Republic and the Republic of Italy on the Promotion and Protection of Investments dated 22 May 1990 ("Argentina-Italy BIT").[62] In these cases, the bondholders alleged that Argentina repudiated its obligations under their bonds and refused to negotiate with them by making a unilateral exchange offer.[63] They continued that Argentina enacted legislation repudiating all obligations owed to them under the bonds, thereby destroying the value of their investments.[64] They requested the arbitral tribunal to declare that Argentina has breached its obligation under the Argentina-Italy BIT by "failing to ensure fair and equitable treatment and full

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57 *Ibid.*, para. 1.230; J. Lew, et al., "Chapter 28 Arbitration of Investment Disputes", in: Comparative International Commercial Arbitration, (Kluwer, 2003), para. 28-12.

58 N. Blackaby et al., "Chapter 1 on An Overview of International Arbitration", in: Redfern and Hunter on International Arbitration (Oxford, 2009), para. 1.230.

59 See UNCTAD official website, available at http://investmentpolicyhub.unctad.org/IIA (last visited 1 Aug 2015).

60 UNCTAD IIA Issues Note, Recent Developments in Investor-State Dispute Settlement, April 2014, p. 1, available at http://unctad.org/en/PublicationsLibrary/webdiaepcb2014d3_en.pdf (lasted visited 1 Aug 2015).

61 *Ibid.*

62 *Abaclat and others v. Argentine Republic* (ICSID Case No. ARB/07/5); *Giovanni Alemanni and others v. Argentine Republic* (ICSID Case No. ARB/07/8); and *Ambiente Ufficio S.p.A. and others v. Argentine Republic* (ICSID Case No. ARB/08/9). See ICSID official website, available at http://icsid.worldbank.org/ICSID/FrontServlet?requestType=GenCaseDtlsRH&actionVal=ListPendin (last visited 1 Aug 2015).

63 *Abaclat and others v. Argentine Republic*, Decision on Jurisdiction and Admissibility of 4 August 2011, para. 238.

64 *Ibid.*

protection and security to their investments and by expropriating such investments without prompt, adequate and immediate compensation", and to award claimants compensatory damages.[65]

(6.20) Among these three cases, none of them has come to the stage where the arbitral tribunal issues the final award. In *Abaclat and others v. Argentine Republic*, the tribunal issued a Decision on Jurisdiction and Admissibility on 4 August 2011, upholding jurisdiction over sovereign bond disputes.[66] This case is in the merits phase now. In *Giovanni Alemanni and others v. Argentine Republic*, the tribunal has not yet issued a decision on jurisdiction and very little information is publicly available. In *Ambiente Ufficio S.p.A. and others v. Argentine Republic*, the tribunal issued a Decision on Jurisdiction and Admissibility upholding jurisdiction on 8 February 2013.[67] However, the proceeding was discontinued for lack of payment of the required advances on 1 August 2014, pursuant to ICSID Administrative and Financial Regulation 14(3)(d).[68]

(6.21) In May 2013, a Slovak bank and its Cypriot shareholder initiated ICSID arbitration against Greece after the debt restructuring, in accordance with the bilateral investment treaties concluded between Greece and Slovakia as well as Greece and Cyprus (*Poštová banka, a.s. and ISTROKAPITAL SE v. Hellenic Republic*).[69] In this case, the claimants contend that they purchased Greek bonds in 2010 and were forced to exchange their bonds for "new securities of sub-

65 *Ibid.*, para. 239; *Ambiente Ufficio S.p.A. and others v. Argentine Republic*, Decision on Jurisdiction and Admissibility dated 8 February 2013, para. 63.

66 For commentaries on this case, see K. Cross, "Chapter 12- Sovereign Arbitration", in: Sovereign Debt Management, R. Lastra & L. Buchheit (eds.) (Oxford, 2014); S.I. Strong, "Mass Procedures in *Abaclat v. Argentine Republic*: Are They Consistent with the International Investment Regime?", Yearbook on International Arbitration Vol. 3 (2013), pp. 261-283; A. Steingruber, "*Abaclat and Others v Argentine Republic*: Consent in Large-scale Arbitration Proceedings", ICSID Review (Fall 2012) 27 (2), pp. 237-246; J. Chrostin, "Sovereign Debt Restructuring and Mass Claims Arbitration before the ICSID, the Abaclat Case", 53 Harv. Int'l L.J. 505 (2012); W. Park, "The Politics of Class Action Arbitration: Jurisdictional Legitimacy and Vindication of Contract Rights", 27 Am. U. Int'l L. Rev. 837 (2012); J. Simões, "Sovereign Bond Disputes Before ICSID Tribunals: Lessons from the Argentina Crisis", 17 L. & Bus. Rev. Am. 683 (2011).

67 For a commentary on this case, see Strong, S.I., "Ambiente Ufficio S.P.A. V. Argentine Republic: Heir of Abaclat? Mass and Multiparty Proceedings", ICSID Review (2014), available at http://icsidreview.oxfordjournals.org/content/early/2014/01/16/icsidreview.sit044 (last visited 1 Aug 2015).

68 *Ambiente Ufficio S.p.A. and others v. Argentine Republic*. See ICSID official website, available at http://icsid.worldbank.org/ICSID/FrontServlet?requestType=GenCaseDtlsRH&actionVal=ListPendin (last visited 1 Aug 2015).

69 *Poštová banka, a.s. and ISTROKAPITAL SE v. Hellenic Republic* (ICSID Case No. ARB/13/8), See ICSID official website, available at https://icsid.worldbank.org/ICSID/FrontServlet?requestType=GenCaseDtlsRH&actionVal=ListPendin (last visited 1 Aug 2015).

stantially lesser value".[70] They allege that the forcible bond exchange was carried out through the newly adopted Greek Bondholder Act that "retroactively and unilaterally" amended the bond terms by inserting a so-called "Collective Action Clause" ("CAC") into outstanding Greek-law bonds.[71] According to the claimants, the CAC allows "the imposition of new terms upon bondholders against their consent if a supermajority of other bondholders consent."[72] This case is currently pending and the parties agreed to bifurcate jurisdiction from the merits.[73] The hearing on jurisdiction took place in September 2014.[74]

6.4 Problems With the Status Quo

6.4.1 Domestic Courts do not Address the "Insolvency" Problem

(6.22) As shown in Part III, section A, sovereign debt disputes brought under dispute resolution clauses in debt instruments before domestic courts can be divided into two main categories: (1) claims based on the debtor's failure to repay, and (2) claims concerning a breach of the *pari pass*u clause. For the purpose of this discussion, it is important to note that most sovereign bonds are governed by New York law or English law.

6.4.1.1 Claims Based on the Debtor's Failure to Repay

(6.23) In domestic courts, claims based on the debtor's failure to repay are determined in accordance with the terms of the debt contract, which often provides that, in the event of default, the principal of the debt may be declared due and payable.[75] When making such a determination, civil law judges are asked to investigate the fact that whether a default actually occurs without looking into the reasons behind it. In case a default indeed occurs, these judges

70 Investment Arbitration Reporter on "Bondholders' claim against Greece is registered at ICSID, as mandatory wait-period expires on another threatened arbitration", available at http://www.iareporter.com/articles/20130530_2 (last visited 1 Aug 2015).

71 *Ibid.*

72 *Ibid.*

73 *Poštová banka, a.s. and ISTROKAPITAL SE v. Hellenic Republic*, Procedural Order No.1 dated 20 December 2013, para. 14.1.

74 *Poštová banka, a.s. and ISTROKAPITAL SE v. Hellenic Republic*, Status of Proceeding, see ICSID official website, available at https://icsid.worldbank.org/ICSID/FrontServlet?requestType=GenCaseDtlsRH&actionVal=ListPendin (last visited 1 Aug 2015).

75 Information Memorandum of the Republic of Congo U.S. Dollar Notes Due 2029 dated 1 August 2008, p. 55 (on file with author); Offering Circular of the Republic of Hungary Euro Notes due 2014 dated 27 July 2009, p. 9 (on file with author); and Base Prospectus of the Emirate of Abu Dhabi Global Medium Term Note Programme dated 31 March 2009, pp. 51-52 (one file with author).

will order the debtor to repay the principal as specified in the debt contract. The fact that the sovereign debtor may be insolvent is entirely irrelevant for this determination.

(6.24) In the view of the author, the current situation is highly problematic because insolvent States simply do not have enough assets to repay every creditor in full and on time. Although the nature of sovereign States differs from that of municipalities, companies and consumers, the underlying insolvency problem remains the same. The key issue involved in any kind of insolvency situation is the question what should creditors get paid if they do not receive the full amount. To take the US municipality bankruptcy law[76] for an example (*note*: the status of municipalities is most similar to that of States[77]), bankruptcy judges are required by law to ensure that the amount creditors would receive is feasible and in the best interest of creditors.[78] In the event of cram-down, the impaired dissenting creditors should not be discriminated unfairly and should be treated in a fair and equitable manner.[79] In comparison, in the context of sovereign debt, civil law judges would not be able to analyze the key issue of how much should creditors get paid if not the full amount, because the contract law applicable to a particular dispute does not contain similar principles as US municipality bankruptcy law. In essence, civil law judges in domestic courts do not address the concept of insolvency of a sovereign State.

76 The U.S. Bankruptcy Code defines a "municipality" as a "political subdivision or public agency or instrumentality of a state." It includes cities and towns, villages, counties, taxing districts, municipal utilities, and school districts. A municipality may be a debtor in a Chapter 9 case if (a) it has been "specifically authorized" to be a Chapter 9 debtor, b) is "insolvent" and (c) has either (i) obtained majority approval of creditors in each class for the proposed plan of reorganization, or (ii) negotiated in "good faith" with creditors and failed to obtain such a majority, or (iii) is unable to negotiate with creditors because such negotiations are "impracticable." See 11 U.S.C. §101(40), United States Courts: Chapter 9 Municipality Bankruptcy, available at http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/Chapter9.aspx (last visited 1 Aug 2015); Z. Clement et al., "Important Issues in a Chapter 9 Case for a Municipality", 24 October 2011, available at http://www.nortonrosefulbright.com/knowledge/publications/94035/important-issues-in-a-chapter-9-case-for-a-municipality (last visited 1 Aug 2015).

77 A municipality's insolvency is determined on the basis of a cash-flow analysis, not budget deficiency analysis; a municipality is insolvent when it is unable to pay its debts as they become due. *In re Hamilton Creek Metropolitan District*, 143 F.3d 1381 (10th Cir. 1998); *In Re City of Bridgeport*, 129 B.R. 332 (Bankr. D. Conn, 1991).

78 See 11 U.S.C. §943 (b) (7), available at http://www.law.cornell.edu/uscode/text/11/943 (last visited 1 Aug 2015).

79 Section 901(a) explicitly makes Section 1129(b)(1) dealing with the bankruptcy of companies applicable for municipalities. See 11 U.S.C. §1129(b)(1), available at http://www.law.cornell.edu/uscode/text/11/1129 (last visited 1 Aug 2015).

6.4.1.2 Claims Concerning a Breach of the Pari Passu Clause

(6.25) Claims concerning a breach of the *pari passu* clause are decided on the basis of the wording of the clause. As mentioned above, most *pari passu* clauses provide that bonds of that particular issue shall rank equally among themselves. Some clauses also state that the debtor's payment obligation under that particular issue shall rank equally with all other existing and future unsubordinated and unsecured external indebtedness.

(6.26) To date, the meaning of the *pari passu* clause still remains highly controversial.[80] In *NML Capital Ltd. v. Republic of Argentina*, the US district court judge issued injunctions designed to remedy Argentina's breach of the *pari passu* clause in certain bond indentures, on the grounds that Argentina had issued new debt pursuant to exchange offers in 2005 and 2010 and was making the required payments on this new debt, but had declared through legislation that it would make no payments to those still holding the old bonds. Accordingly, whenever Argentina pays any amount due under the terms of the exchange bonds, it must concurrently or in advance pay plaintiffs the same percentage of the amount due to them. In order not to violate the injunctions and not to pay plaintiffs the full amount of the original bonds, Argentina defaulted on its interest payment to exchange bondholders on 30 July 2014.[81] Needless to say, interpreting *pari passu* clause in this manner would have serious impact on the workability of future sovereign debt restructuring. Furthermore, the judgment left the issue of whether payments to multilateral creditors would breach the *pari passu* clause entirely open, simply noting that the plaintiffs had not argued that preferential payments to the IMF made by Argentina could similarly entitle the plaintiffs to ratable payments.[82]

(6.27) The *NML Capital* case is a good example to illustrate the inappropriateness of interpreting the *pari passu* clause in the absence of an insolvency law system for sovereign States. Under any insolvency law, claims of creditors are placed in different classes. According to the UNCITRAL Legislative Guide on Insolvency Law, the purpose of classification of claims is to "satisfy the requirements to provide fair and equitable treatment to creditors, treating similarly situated claims in the same manner and ensuring that all creditors

80 See Global Law Intelligence Unit, Allen & Overy LL.P, "The pari passu clause and the Argentine case"; M. Wright, "The Pari Passu Clause in Sovereign Bond Contracts: Evolution or Intelligent Design?", 1 Hofstra L. Rev. 40 (2011); B. Remy Chabot & M. Gulati, "Santa Anna and His Black Eagle: The Origins of the Pari Passu", 18 Feb 2014, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2397929 (last visited 1 Aug 2015).

81 Reuters news, "Argentina fails to reach debt agreement, default looms", available at http://www.reuters.com/article/2014/07/30/us-argentina-debt-idUSKBN0FZ0AM20140730(last visited 1 Aug 2015).

82 *NML Capital, Ltd. v. Republic of Argentina*, No. 12-105-(L) (2d Cir. 26 Oct. 2012), p. 21.

in a particular class are offered the same menu of terms by the reorganization plan".[83] Although the general rule is to put secured creditors in one class and unsecured creditors in another, the Legislative Guide mentions that ordinary unsecured creditors can be divided into "different classes based upon their varying economic interests."[84] In determining commonality of interest, the relevant criteria may include "the nature of debts giving rise to the claims".[85] Therefore, it would be wrong to interpret the *pari passu* clause without analyzing the nature of debt giving rise to the claims and determining whether these claims should receive equal treatment.

6.4.2 Investment Treaty Tribunals' Jurisdiction is Limited to Sovereign Acts

(6.28) As explained above, most investment treaties grant foreign investors the right to initiate arbitration against the host country directly for alleged breaches of obligations specified in the treaty in question, which often include guarantees of fair and equitable treatment to investments. Unlike judges in domestic courts, arbitrators in investment treaty tribunals are capable of addressing the key question what should creditors get paid if they do not receive the full amount, because the treaty obligation of fair and equitable treatment entails principles that are somewhat similar to US municipality bankruptcy law – (1) there should be a reasonable relationship of proportionality between the charge or weight imposed to the foreign investor and the aim sought to be realized by any expropriatory measure adopted by the sovereign State,[86] and (2) similar cases should not be treated differently and without reasonable justification.[87] Importantly, these principles take into account the interests of both debtors and creditors, and could possibly strike a balance among their conflicting interests.

6.4.2.1 General Principle

(6.29) In the absence of an international insolvency regime for States, investment treaty tribunals seem to be the ideal forum to play the role of bankruptcy

83 See UNCITRAL Legislative Guide on Insolvency Law (2004), p. 218, available at http://www.uncitral.org/pdf/english/texts/insolven/05-80722_Ebook.pdf (last visited 1 Aug 2015).

84 *Ibid.*, p. 222.

85 *Ibid.*

86 *Técnicas Medioambientales Tecmed, S.A. v. United Mexican States* (ICSID Case No. ARB (AF)/00/2), Award of 29 May 2003, para. 122. In support of this proposition, the tribunal cited several decisions of the European Court of Human Rights: In the case of *Mellacher and Others v. Austria*, Judgment of December 19, 1989, 48, p. 24; In the case of *Pressos Compañía Naviera and Others v. Belgium*, Judgment of November 20, 1995, 38, p. 19.

87 *Saluka Investment BV v. Czech Republic* (UNCITRAL), Partial Award of 17 March 2006, para. 313.

courts. Unfortunately, however, not all sovereign debt claims can be brought to investment treaty tribunals. It should be emphasized that a mere breach of the debt contract by a sovereign State should be differentiated from a breach of investment treaty obligations; the former situation does not automatically trigger State responsibility.[88] A State's debt contract is not a treaty itself and cannot involve State responsibility as an international obligation.[89] The claim of breach of contract will be determined in accordance with the applicable domestic law.[90]

(6.30) Nevertheless, breach of a sovereign debt contract not governed by international law may entail State responsibility when there is a separate breach of a treaty obligation or a customary international law obligation governing the treatment of a foreigner and foreign property.[91] To put it differently, while a mere breach by a State of a contract with foreign investors does not violate international law, a sovereign act of a State contrary to such a contract may do so.[92] Arbitrary or repudiatory measures, in which the State seeks to breach a contractual obligation by use of its sovereign authority, are listed in case law as governmental breaches of this kind.[93]

(6.31) For instance, the arbitral tribunal in *Biwater Gauff*, having stated that the breach of contract does not *per se* constitute a breach of international law for the purpose of expropriation, held that a denial of justice need not be established, but rather "the critical distinction is between situations in which a State acts merely as a contractual partner and cases in which it acts *iure imperii*, exercising elements of its governmental authority".[94] In *Waste Manage-*

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88 M. Sasson, "Chapter 6: Contract versus Treaty Claims", in: Substantive Law in Investment Treaty Arbitration: The Unsettled Relationship between International Law and Municipal Law (Kluwer, 2010), p. 150; I. Brownlie, Principles of Public International Law (Oxford, 2008), pp. 546–547.

89 I. Brownlie, Principles of Public International Law (Oxford, 2008), p. 549.

90 *Ibid.*

91 A. Newcombe & L. Paradell, "Chapter 9 – Observance of Undertakings", in: Law and Practice of Investment Treaties: Standards of Treatment (Kluwer Law International 2009), p. 438, citing S.M. Schwebel, "On Whether the Breach by a State of a Contract with an Alien is a Breach of International Law", in Zanardi *et al.*, eds, International Law at the Time of its Codification: Essays in Honour of Roberto Ago (Milano: A. Giuffrè, 1987), *reprinted in* S.M. Schwebel, Justice in International Law: Selected Writings of Stephen M. Schwebel (Cambridge: Grotius, 1994), p. 425; and C.F. Amerasinghe, *State Responsibility for Injuries to Aliens* (Oxford: Clarendon Press, 1967), pp. 66-69.

92 A. Newcombe & L. Paradell, "Chapter 9 – Observance of Undertakings", in: Law and Practice of Investment Treaties: Standards of Treatment (Kluwer, 2009), p. 439.

93 *Ibid.*, citing *Sempra Energy International v. Argentina* (Award, 28 Sep. 2007), para. 310; and *Impregilo S.p.A. v. Pakistan* (Decision on Jurisdiction, 22 Apr. 2005), para. 260.

94 Biwater Gauff (Tanzania) Limited v. United Republic of Tanzania (ICSID Case No. ARB/05/22), Award dated July 24, 2008, paras. 457-458, available at https://icsid.worldbank.org/

ment, the arbitral tribunal found that persistent non-payment of debts assumed by a State in breach of a contract cannot be equated with a violation of an investment treaty provision, if it does "not amount to an outright and unjustified repudiation of the transaction and provided that some remedy is open to the creditor to address the problem".[95] The tribunal further concluded that "an enterprise is not expropriated just because its debts are not paid or other contractual obligations towards it are breached" and that it is not the function of the investment treaty in question to "compensate for failed business venture, absent arbitrary intervention by the State amounting to a virtual taking or sterilizing of the enterprise".[96]

(6.32) More importantly, the arbitral tribunal in *Abaclat* addressed this issue in the sovereign debt context. At the outset, the tribunal noted that "[i]t is in principle admitted that with respect to a BIT claim an arbitral tribunal has no jurisdiction where the claim at stake is a pure contract claim".[97] The tribunal explained that a claim is not a pure contract claim "where the equilibrium of the contract and the provisions contained therein are unilaterally altered by a sovereign act of the Host State. This applies where the circumstances and/or the behavior of the Host State appear to derive from its exercise of sovereign State power".[98] Given that Argentina enacted the Emergency Law to modify its payment obligations under bonds, the tribunal found that the present dispute does not derive from a mere breach of sovereign bonds but "from the fact that [Argentina] intervened as a sovereign by virtue of its State power to modify its payment obligations towards its creditors in general".[99]

6.4.2.2 Possible Exception

(6.33) Based on the foregoing, one can conclude that the jurisdiction of an investment tribunal over sovereign debt disputes is limited to claims derived from sovereign acts, excluding pure contract claims. In this context, it is worth mentioning that an exception to this principle is the so-called "Umbrella Clause" provided in some investment treaties, which requires host States to

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ICSID/FrontServlet?requestType=GenCaseDtlsRH&actionVal=ListConcluded (last visited 1 Aug 2015).

95 Waste Management, Inc. v. United Mexican States (ICSID Case No. ARB(AF)/00/3), Award dated April 30, 2004, para. 115, available at http://www.italaw.com/sites/default/files/case-documents/ita0900.pdf (last visited 1 Aug 2015).

96 *Ibid.*, para. 160.

97 *Abaclat and others v. Argentine Republic*, Decision on Jurisdiction and Admissibility of 4 August 2011, para. 316.

98 *Ibid.*, para. 318.

99 *Ibid.*, paras. 321 & 324.

observe any obligations or commitments undertaken towards investments.[100] However, the actual meaning of an umbrella clause is often heavily debated. Case law indicates that international investment tribunals have adopted four different approaches in interpreting umbrella clauses.[101] Whereas a few tribunals read umbrella clauses very narrowly and required claimant to show clear and convincing evidence that the shared intent of the contracting States was that any alleged breach of a contract with the State constitutes a breach of the investment treaty,[102] some tribunals took the opposite position and held that an umbrella clause automatically transforms a contractual obligation between a State and an investor into an international obligation.[103] Other tribunals expressed the view that an umbrella clause only grants jurisdiction over treaty claims, including claims based on the violation of the investment treaty by the State as a sovereign but not claims where the State acted other than as a sovereign.[104] Notably, one tribunal went further to hold that the umbrella clause covered commitments arising in relation to contracts with the State, but "the extent of the obligation is still governed by the contract and it can only be determined by reference to the terms of the contract".[105] This tribunal stayed the arbitration pending a decision on the contractual claim to be determined in accordance with the dispute settlement mechanism provided in the contract.[106]

100 A. Newcombe & L. Paradell, "Chapter 9 – Observance of Undertakings", in: Law and Practice of Investment Treaties: Standards of Treatment (Kluwer, 2009), p. 436.

101 M. Sasson, "Chapter 7: Umbrella Clauses: When a Breach of Contract May Become a Breach of Treaty", in: Substantive Law in Investment Treaty Arbitration: The Unsettled Relationship between International Law and Municipal Law (Kluwer, 2010), p. 182.

102 *Société Générale du Surveillance SA v. Pakistan* (ICSID Case No. ARB/01/13), Decision of the Tribunal on Objections to Jurisdiction dated August 06, 2003, available at https://icsid.worldbank.org/ICSID/FrontServlet?requestType=GenCaseDtlsRH&actionVal=List Concluded (last visited 1 Aug 2015).

103 Fedax N.V. v. Republic of Venezuela (ICSID Case No. ARB/96/3), Award dated March 9, 1998, 5 *ICSID Rep.* 200 (2002); CMS Gas Transmission Company v. Argentine Republic (ICSID Case No. ARB/01/8), Award dated May 12, 2005, available at https://icsid.worldbank.org/ICSID/FrontServlet?requestType=GenCaseDtlsRH&actionVal=List Concluded (last visited 1 Aug 2015).

104 *Pan American Energy LLC and BP Argentina Exploration Company v. Argentina* (ICSID Case No. ARB/03/13), Decision on Preliminary Objections dated 27 July 2006, available at http://italaw.com/cases/808 (last visited 1 Aug 2015); *El Paso Energy International Company v. Argentina* (ICSID Case No. ARB/03/15), Decision on Jurisdiction dated 27 April 2006, available at http://www.italaw.com/documents/elpaso-jurisdiction27april2006.pdf (last visited 1 Aug 2015).

105 *Société Générale du Surveillance SA v. Philippines* (ICSID Case No. ARB/02/6), Decision on Objections to Jurisdiction dated 29 January 2004, para. 127, available at http://italaw.com/cases/documents/1019 (last visited 1 Aug 2015).

106 *Société Générale du Surveillance SA v. Philippines* (ICSID Case No. ARB/02/6), Decision on Objections to Jurisdiction dated 29 January 2004, available at http://italaw.com/cases/documents/1019 (last visited 1 Aug 2015).

(6.34) In light of the general principle limiting jurisdiction to sovereign acts and the controversial meaning of umbrella clauses, it is likely that foreign bondholders would not be able to bring before investment treaty tribunals claims arising out of a sovereign debt restructuring process that involves purely voluntary debt renegotiation. In other words, unless the sovereign debtor enacts legislation or exercises other governmental authority to impair bondholders' rights in the restructuring process, foreign bondholders will not be eligible to resort to investment arbitration.

6.5 Perspectives of Further Development

(6.35) With the aim to explore the perspective of further development in the field of settlement of sovereign debt disputes, this Part describes the characteristics of dispute resolution methods that involve a third-party decision maker, and then assesses the applicability of these methods to disputes arising from sovereign debt matters. Among the dispute resolution methods specified in Article 33 of the UN Charter,[107] mediation, conciliation, arbitration and judicial settlement are the widely used methods with a third-party decision maker involved. Mediation and conciliation are two processes where the parties request a third person or persons ("mediator" and "conciliator") to assist them in their attempt to reach an amicable settlement of their dispute.[108] While the conciliator may recommend to the parties a solution to the dispute, the mediator does not usually make recommendations.[109] Both the mediator and conciliator cannot impose a solution to the dispute on the parties.[110] By contrast, in arbitration and adjudication, a third person or a panel of third persons ("arbitrator" and "judge") considers the facts and arguments and then makes

107 Article 33 (1) of the United Nations Charter provides that "The parties to any dispute, the continuance of which is likely to endanger the maintenance of international peace and security, shall, first of all, seek a solution by negotiation, enquiry, mediation, conciliation, arbitration, judicial settlement, resort to regional agencies or arrangements, or other peaceful means of their own choice", available at http://www.un.org/en/documents/charter/chapter6.shtml (last visited 1 Aug 2015).

108 J. Paulsson et al. (eds), "Chapter 8: Choosing ADR/tiered dispute resolution methods", in: The Freshfields Guide to Arbitration Clauses in International Contracts, 3rd edition (Kluwer 2010), p. 117; Article 1 (3) of the UNCITRAL Model Law on International Commercial Conciliation, available at http://www.uncitral.org/pdf/english/texts/arbitration/ml-conc/03-90953_Ebook.pdf (last visited 1 Aug 2015).

109 J. Paulsson et al. (eds), "Chapter 8: Choosing ADR/tiered dispute resolution methods", in: The Freshfields Guide to Arbitration Clauses in International Contracts, 3rd edition (Kluwer 2010), p. 117.

110 *Ibid.*

a binding decision.[111] In this respect, it should be explained that the assessment of the applicability of conciliation to sovereign debt disputes would not be included due to the great similarity between mediation and conciliation.

6.5.1 Sovereign Debt Mediation

6.5.1.1 Mediation of Sovereign Debt Disputes

(6.36) In 2014 we have witnessed the first mediation case of a sovereign debt dispute. As a result of the injunction order issued by Judge Thomas Griesa in *NML Capital*, whenever Argentina pays exchange bondholders any amount due under the exchange bonds, it must concurrently or in advance pay plaintiffs the same percentage of the amount due to them.[112] In light of the 30 June 2014 deadline for Argentina to pay exchange bondholders, Judge Griesa appointed on 23 June 2014 Mr. Daniel Pollack as mediator to facilitate the negotiation between NML and Argentina.[113]

(6.37) This mediation process follows the Procedures of the Mediation Program of the US District Court for the Southern District of New York, which provide that, immediately after assignment of a case, the mediator shall contact counsel for the parties or parties themselves to determine an appropriate date, time, and location for the first mediation session.[114] On or before receipt of each party's written submissions, the mediator may schedule either a joint or individual preliminary case conference.[115] As regards subsequent sessions, the mediator shall schedule them within 30 days of the prior session.[116] The mediation process will end when the parties reach a resolution of some or all issues or when the mediator or parties conclude that resolution is not possible.[117]

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111 A. Redfern et al., "Chapter 1: An Overview of International Arbitration", Redfern and Hunter on International Arbitration (Oxford, 2009), para. 1.02; J. Paulsson et al. (eds), "Chapter 1: Choosing the method", The Freshfields Guide to Arbitration Clauses in International Contracts, 3rd edition (Kluwer, 2010), p. 3.

112 See *NML Capital, Ltd. v. Republic of Argentina*, 08 Civ. 6978 (TPG), 09 Civ. 1707 (TPG), 09 Civ. 1708 (TPG) (S.D.N.Y., 21 Nov. 2012).

113 News item, "Griesa appoints mediator for talks between Argentina and holdout hedge funds", available at http://en.mercopress.com/2014/06/24/griesa-appoints-mediator-for-talks-between-argentina-and-holdout-hedge-funds (last visited 1 Aug 2015).

114 Article 4 (a), Procedures of the Mediation Program of the United States District Court Southern District of New York (12/9/2013), available at http://www.nysd.uscourts.gov/docs/mediation/Mediation%20Program%20Procedures.12.9.13.pdf (last visited 1 Aug 2015).

115 *Ibid.*, Article 4 (b).

116 *Ibid.*, Article 4 (c).

117 *Ibid.*, Article 4 (d).

(6.38) Despite of several sessions organized by the mediator, the parties were not able to reach any agreement. As a result, Argentina missed the 30 July deadline (one-month grace period after 30 June) to pay exchange bondholders and thus triggered a default event.[118] As of today, no agreement has been reached yet.

6.5.1.2 Lessons From Municipality Bankruptcy Mediation

(6.39) When analyzing the desirability of sovereign debt mediation, the use of mediation in a similar context, namely the US municipality bankruptcy, merits some discussion. As a response to the US Chapter 9 bankruptcy case of the city of Vallejo in California, the California legislature passed the California Assembly Bill 506. Entered into force on 1 January 2012, the Bill mandates that a municipality participate with its creditors in at least 60 days of mediation, conducted by a state-approved mediator with sufficient bankruptcy experience, before it may file for bankruptcy under Chapter 9.[119] The legislature hoped that the incorporation of mediation into municipal filings would allow these proceedings to reach amicable solutions more quickly and efficiently.[120] In 2012, three municipal debtors were planning to file Chapter 9 bankruptcy in California, which were the first and only cases so far that were required to adhere to this Bill.[121] Unfortunately, all three municipal debtors could not reach comprehensive agreement with their creditors through mediation and filed for bankruptcy eventually.[122] Nevertheless, in *re City of*

118 News item, "Argentina default? Griesafault is much more accurate", available at http://www.theguardian.com/business/2014/aug/07/argentina-default-griesafault-more-accurate (last visited 1 Aug 2015).

119 A. B. 506, 2011-12 Leg., Reg. Sess. (Ca. 2011), available at http://www.leginfo.ca.gov/pub/11-12/bill/asm/ab_0501-0550/ab_506_bill_20110815_amended_sen_v94.pdf (last visited 1 Aug 2015).

120 A. B. 506, 2011-12 Leg., Reg. Sess. (Ca. 2011), p. 5, available at http://www.leginfo.ca.gov/pub/11-12/bill/asm/ab_0501-0550/ab_506_bill_20110815_amended_sen_v94.pdf (last visited 1 Aug 2015)

121 The City of Stockton, California, filed first in late June 2012. It was followed by The Town of Mammoth Lakes in July 2012 and The City of San Bernardino in August 2012. See M. Galen, "Chapter 9 Bankruptcy in California: The Efficacy of Mandating Alternative Dispute Resolution in Municipal Bankruptcy Filings", 15 Cardozo J. Conflict Resol. 547, p. 554.

122 Chapter 9 Voluntary Petition, In re City of Stockton, California, No. 12-32118 (E.D. Cal. 2012), ECF No. 1, available at http://www.caeb.uscourts.gov/documents/Forms/Misc/Voluntary%20Petition%20-%20City%20of%20Stockton.pdf (last visited 1 Aug 2015) ; Chapter 9 Voluntary Petition, In re Town of Mammoth Lakes, California, No. 12-32463 (E.D. Cal. 2012) ECF No. 1, available at http://www.caeb.uscourts.gov/documents/Forms/Misc/MammothVP.pdf (last visited 1 Aug 2015); Chapter 9 Voluntary Petition, In re City of San Bernardino, California, No. 12-28006 (C.D. Cal. 2012) ECF No. 1, available at http://www.cacb.uscourts.gov/sites/cacb/files/documents/cases-of-interest/SBerdo_petition.pdf (last visited 1 Aug 2015).

Stockton, the city was able to conclude tentative agreements with nearly half of the creditors in mediation sessions.[123]

(6.40) Outside California, mediation has also become popular in Chapter 9 municipality bankruptcies. In the well-known bankruptcy of *Detroit*, the Hon. Steven W. Rhodes from the US Bankruptcy Court for the Eastern District of Michigan Southern Division issued a Mediation Order on 13 August 2013. This Order provides that the court finds it necessary and appropriate to "order the parties to engage in the facilitative mediations of any matters that the Court refers in this case."[124] It also appointed Chief District Judge Gerald Rosen from the US District Court for the Eastern District of Michigan as judicial mediator.[125] The judicial mediator is authorized to engage in facilitative mediation on discovery, substantive issues and process issues, as referred by the court, with such other mediators, judicial or non-judicial, as the judicial mediator may designate.[126]

(6.41) The Mediation Order further provides that "[a]ll proceedings, discussions, negotiation, and writings incident to mediation shall be privileged and confidential, and shall not be disclosed, filed or placed in evidence."[127] "If a settlement is reached, the agreement shall be reduced to writing."[128] "For each mediation session, the judicial mediator shall have the authority to establish the mediation process, including the submission of documents, the attendance of parties with authority to settle, the procedure governing the mediation, and the schedule for the mediation."[129] By various orders, the Hon. Steven W. Rhodes referred matters such as "[t]he treatment of the claims of the various creditor classes in a plan of adjustment" to mediation.[130] Approximately one year later, Hon. Steven W. Rhodes confirmed in November 2014 the proposed plan of adjustment.[131] In confirming the plan, Hon. Steven

123 In re City of Stockton, Outcome of AB506 Mediation Sessions, available at http://www.stocktongov.com/files/AB506_Mediation_Outcome.pdf (last visited 1 Aug 2015).
124 Mediation Order dated 13 August 2013, In re City of Detroit, Michigan, No. 13-53846, p. 1 (on file with the author).
125 *Ibid.*
126 *Ibid.*
127 *Ibid.*
128 *Ibid.*
129 *Ibid.*
130 First Order Referring Matters to Facilitative Mediation dated 16 August 2013, In re City of Detroit, Michigan, No. 13-53846 (on file with the author); Second Order Referring Matters to Facilitative Mediation dated 22 August 2013, In re City of Detroit, Michigan, No. 13-53846 (on file with the author); Third Order Referring Matters to Facilitative Mediation dated 7 October 2013, In re City of Detroit, Michigan, No. 13-53846 (on file with the author);
131 Oral Opinion on the Record dated November 7, 2014, In re City of Detroit, available at http://www.mieb.uscourts.gov/sites/default/files/notices/Oral_Opinion_on_Detroit_Plan_Confirmation_Judge_Rhodes_FINAL_for_Release.pdf (last visited 1 Aug 2015).

W. Rhodes noted that "[t]he settlements that the mediators assembled in this case are extraordinary and unprecedented."[132]

6.5.1.3 Assessment

(6.42) As a form of alternative dispute resolution, mediation is a flexible and informal process. In mediation, the parties meet with a neutral third party (the "mediator") to discuss their respective interests and positions and identify options for a settlement agreement that is acceptable to both.[133] The mediator assists the parties in reaching the mutually agreeable solution to the dispute by defining the key issues, examining the strengths and weaknesses of each party's positions, and summarizing areas of agreement and disagreement. The mediator does not impose a solution on the parties and usually does not even recommend one.[134] The main advantages of mediation are that it can lead to a fast and less costly resolution of the dispute, and can produce creative outcomes in complex disputes that are often unavailable in courts.[135] Due to the principle of party autonomy, the parties may be willing to resort to mediation as it allows them to retain control of the process.[136] Furthermore, the parties enjoy confidentiality during the mediation process. All discussions with the other party and the mediator are subject to confidentiality, and may not be used as evidence in other legal proceedings.[137]

(6.43) One key shortcoming of mediation, however, is that it has no set procedure and could in theory continue indefinitely if the parties refuse to compromise. This is particularly unfavorable for disputes arising out of sovereign debt restructurings, because a delay in the resolution of the disputes could have serious impact on the debtor country's economy. To take the mediation of Argentine debt for an example, the mediation has been ongoing for over many months and yet no agreement has been reached between Argentina and

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132 *Ibid*., p. 44.

133 N. Alexander, "Chapter 1: Global Trends in Mediation: Riding the Third Wave", in: Global Trends in Mediation, Global Trends in Dispute Resolution, Vol. 1, 2nd Edition (Kluwer, 2006), p. 9.

134 J. Paulsson et al. (eds), "Chapter 8: Choosing ADR/tiered dispute resolution methods", in: The Freshfields Guide to Arbitration Clauses in International Contracts, 3rd edition (Kluwer, 2010), p. 117.

135 Local Civil Rule 83.9 (Alternative Dispute Resolution), United States District Court Southern District of New York, available at http://www.nysd.uscourts.gov/docs/mediation/Local%20Civil%20Rule%2083.FINAL.pdf (last visited 1 Aug 2015).

136 N. Alexander, "Chapter 8: UNCITRAL and International Mediation", in: International and Comparative Mediation, Global Trends in Dispute Resolution, Vol. 4 (Kluwer, 2009), p. 344.

137 M. Mcilwrath & J. Savage, "Chapter Four: International Settlement Negotiation and Mediation", in: International Arbitration and Mediation: A Practical Guide, (Kluwer, 2010), para. 4-021.

NML Capital.[138] In fact, it is possible that no agreement will be reached at all. In California, although legislature has made mediation compulsory before any Chapter 9 bankruptcy filing, the usefulness of such mediation seems debatable. Among the three cases where compulsory mediation was utilized, debtors and creditors in none of these cases were able to reach comprehensive agreement in order to avoid bankruptcy filing. In *Stockton*, however, the city concluded tentative agreement with nearly half of the creditors prior to the bankruptcy filing, thereby reducing the number of issues that need to be addressed in bankruptcy. Arguably, mediation might work well in the shadow of an insolvency law system. In theory, debtors and creditors are more likely to commit to good faith negotiation when they know that they might be worse off in the event of strict application of insolvency law principles after bankruptcy filing. With respect to post-filing mediation, the *Detroit* case is a good example but these mediation sessions took place in the context of a bankruptcy proceeding and did not serve as an alternative to the filing of bankruptcy.

6.5.2 Sovereign Debt Arbitration

6.5.2.1 Arbitration of Sovereign Debt Disputes

(6.44) It should be clarified at the outset that the phrase "sovereign debt arbitration" should be distinguished from the term "investment arbitration involving sovereign debt disputes". Sovereign debt arbitration refers to arbitral proceedings initiated in accordance with arbitration agreements concluded between debtors and creditors themselves. By contrast, investment arbitration involving sovereign debt disputes refers to cases brought under arbitration clauses in investment treaties concluded between debtor countries and the home countries of creditors. Despite of a relatively large number of arbitration clauses included in sovereign debt instruments, no creditor has ever initiated sovereign debt arbitration pursuant to such clauses.

(6.45) In the past decade, a number of proposals have sought to employ arbitration in the context of sovereign debt restructuring, advocating its use not simply as the dispute resolution forum for disagreements between the debtor and certain creditors, but as an overall mechanism for debt restructuring in the event of crisis.[139] These proposals differ in specifics and the degree

138 Reuters news, "UPDATE 1-Argentina sees 'better possibility' of holdout debt deal in 2015", available at http://www.reuters.com/article/2014/11/04/argentina-debt-idUSL1N0SU02A 20141104 (last visited 1 Aug 2015).

139 See Jubilee, "Chapter 9/11? Resolving international debt crises – the Jubilee Framework for international insolvency", Jan. 2002, available at http://probeinternational.org/library/wp-content/uploads/2011/02/9-11.pdf (last visited 1 Aug 2015); K. Raffer, *Debt Workout*

to which arbitration would be institutionalized, but share a common overall approach. All proposals would submit the process of sovereign debt restructuring, currently accomplished through negotiations separately with different types of creditors, to a single process of third-party determination by an *ad hoc* or standing arbitral tribunal.[140]

(6.46) For example, Kunibert Raffer proposed a Fair and Transparent Arbitration Process, in which an *ad hoc* arbitration panel should adjudge which percentage of debts insolvent debtors are obligated to repay.[141] Pursuant to an arbitration agreement, the debtor and its creditors should appoint one or two arbitrators and the appointees should select one more member to reach an uneven number.[142] The foundational principles of the US municipality bankruptcy law, such as protection of the debtor's governmental powers, the right of the affected population to voice their views, and the best interest of creditors, would apply to the international arbitration process.[143] To facilitate participation of representatives from the debtor country, the arbitration proceedings should be located near to the debtor country.[144]

(6.47) Another example is the standing Sovereign Debt Tribunal ("SDT") advocated by Christoph Paulus and Steven Kargman.[145] This proposal envisages a tribunal modeled after the Iran-United States Claims Tribunal comprised of a small number of arbitrators, who will be selected by the UN Secret-

Mechanisms: Debt Arbitration (2004), available at http://www.helsinkiprocess.fi/netcomm/ImgLib/24/89/ hp_track2_raffer.pdf; G. Paulus & S. Kargman, *Reforming the Process of Sovereign Debt Restructuring: A Proposal for a Sovereign Debt Tribunal,* Prepared for Presentation to the United Nations Workshop on "Debt, Finance and Emerging Issues in Financial Integration". (April 2008); Erlassjahr, "Resolving Sovereign Debt Crises – Towards a Fair and Transparent International Insolvency Framework", Sep. 2010, available at http://www.erlassjahr.de/english/towards-an-international-insolvency-framework.html (last visited 1 Aug 2015), and AFRODAD, "Fair and Transparent Arbitration on Debt", 2002, available at http://www.afrodad.org/Publications/FTA/fta%20issues%20paper%202002.pdf (last visited 1 Aug 2015).

140 See "Arbitration and Sovereign Debt", Paper prepared by the Steering Committee of the Netherlands Government and the Permanent Court of Arbitration, Jul. 11, 2012, para. 9, available at http://www.slettgjelda.no/filestore/ArbitrationandSovereignDebt.pdf (last visited 1 Aug 2015).

141 K. Raffer, *Debt Workout Mechanisms: Debt Arbitration*, p. 5 (2004), available at http://www.helsinkiprocess.fi/netcomm/ImgLib/24/89/ hp_track2_raffer.pdf (last visited 7 Sep 2014).

142 *Ibid*., p. 6.

143 *Ibid*.

144 *Ibid*.

145 See G. Paulus & S. Kargman, *Reforming the Process of Sovereign Debt Restructuring: A Proposal for a Sovereign Debt Tribunal,* Prepared for Presentation to the United Nations Workshop on "Debt, Finance and Emerging Issues in Financial Integration" (April 2008), available at http://iiiglobal.org/component/jdownloads/viewdownload/366/5382.html (last visited 1 Aug 2015).

ary-General or individuals appointed by the UN Secretary-General.[146] The arbitrators would elect one of their members as president of the tribunal, whose tasks would include drafting the procedural rules for the tribunal and appointing the arbitrators for each particular case.[147] The number of arbitrators could be either one or three, depending on the particular circumstances of the case.[148]

(6.48) For SDT to have jurisdiction, it is advisable to include an arbitration clause in each sovereign bond issue, so as to ensure pre-crisis consensus among the parties to arbitration.[149] The arbitration mechanism could be triggered by an announcement of default by a sovereign debtor, or by the creditors if the parties so agree.[150] The substantive rules governing the dispute would not be the law of a particular jurisdiction, but rather a discrete, international "law merchant," drawn from the general principles of insolvency law established by leading international institutions, such as the World Bank, UNCITRAL, and the IMF.[151] Moreover, SDT may decide on the technical legal validity of the claims of individual creditors.[152] It may also be given competence to consider others issues, such as what constitutes "sustainable debt" for the particular sovereign debtor; whether the underlying economic assumptions underpinning a particular restructuring plan are reasonable; whether the parties have engaged in good faith negotiations; the feasibility and reasonableness of the proposed restructuring plan; whether the debt in question constitutes "odious debt" and what, if any, implication follow from a determination on this issue.[153]

6.5.2.2 Lessons From the BIS Tribunal and the IUSCT

(6.49) For discussions on the desirability and feasibility of these sovereign debt arbitration proposals, the examples of the Tribunal concerning the Bank for International Settlements ("BIS Tribunal") and the Iran-US Claims Tribunal ("IUSCT") could provide some useful guidance. Established in 1930, the BIS Tribunal is a standing arbitral tribunal with the Permanent Court of Arbitration ("PCA") in The Hague serving as the registry.[154] The BIS Tribunal was created

146 *Ibid*., pp. 6 & 7.
147 *Ibid*., p. 8.
148 *Ibid*.
149 *Ibid*., p. 9.
150 *Ibid*., p.13.
151 *Ibid*., p. 14.
152 *Ibid*., p. 10.
153 *Ibid*., p. 11.
154 Information on the Hague Arbitral Tribunal, available at http://www.bis.org/about/arb_trib.htm (last visited 1 Aug 2015). Established in 1899 by the Convention for the Pacific Settlement of International Disputes, the Permanent Court of Arbitration is an intergovern-

for future disputes and the basis for its jurisdiction derives from the arbitration clause included in the Hague Agreement of 20 January 1930, which provides, in Article XV, that "[a]ny dispute, whether between the Governments signatory to the present Agreement or between one or more of those Governments and the Bank for International Settlements, as to the interpretation or application of the New Plan shall… be submitted for final decision to an arbitration tribunal of five members appointed for five years".[155] Among the five members of the arbitral tribunal, the chairman "shall be a citizen of the United States of America, two shall be nationals of States which were neutral during the late war; the two other shall be respectively a national of Germany and a national of one of the Powers which are creditors of Germany."[156]

(6.50) In March 2001, disputes arose concerning the compensation to be paid to private shareholders for the shares that had been recalled by the BIS on 8 January 2001.[157] Article 54 (1) of the BIS Statutes provides that, if any dispute arises between the BIS and its shareholders regarding the interpretation or application of the Statutes, the dispute "shall be referred for final decision to the Tribunal provided for by the Hague Agreement of January 1930".[158] On 23 March 2001, the BIS Tribunal adopted Rules for Arbitration between the Bank and Private Parties to supplement the procedural rules provided in Annex XII of the 1930 Hague Agreement.[159] In accordance with Article 26 of the Rules of Procedure, the BIS Tribunal "shall apply the instruments relevant to the case as well as other relevant principles of law".[160] On 19 September 2003, the BIS Tribunal issued a Final Award, which asked the BIS to pay to each claimant CHF 7,977.56 per share previously owned by the claimant plus 5%

mental organization with 116 member states. It provides services for the resolution of disputes involving various combinations of states, state entities, intergovernmental organizations, and private parties. See http://www.pca-cpa.org/showpage.asp?pag_id=1027 (last visited 1 Aug 2015).

155 The New Plan refers to this Agreement, the Experts' Plan of 7 June 1929 and the Protocol of 31 August 1929 all together, which were accepted as a complete and final settlement for Germany of the financial questions resulting from the War. See Article I and Article XV of the Hague Agreement of 20 January 1930, available at http://www.pca-cpa.org/showpage.asp?pag_id=1157 (last visited 1 Aug 2015).

156 See Article XV of the Hague Agreement of 12 January 1930, available at http://www.pca-cpa.org/showpage.asp?pag_id=1157 (last visited 1 Aug 2015).

157 Bank for International Settlements, Press Release dated 22 September 2003, available at http://www.pca-cpa.org/showpage.asp?pag_id=1157 (last visited 1 Aug 2015).

158 Article 54 (1) of the Statutes of the Bank for International Settlements, available at http://www.bis.org/about/legal.htm (last visited 1 Aug 2015).

159 Bank for International Settlements, Partial Award dated 22 November 2002, para. 14, available at http://www.pca-cpa.org/showpage.asp?pag_id=1157 (last visited 1 Aug 2015).

160 Article 26 of the Rules for Arbitration between the Bank for International Settlements and Private Parties, available at http://www.pca-cpa.org/showpage.asp?pag_id=1157 (last visited 1 Aug 2015).

interest.[161] The BIS Tribunal also decided the counterclaim of the BIS against one of the claimants, awarding the BIS its costs in defending a case initiated by that claimant in a US court in violation of the arbitration agreement.[162] Currently there is no case pending before the BIS Tribunal.

(6.51) Based in The Hague, the Iran-United States Claims Tribunal is a standing arbitral tribunal established in 1981 to settle disputes arising out of the November 1979 hostage crisis at the US Embassy in Tehran and the subsequent freezing of Iranian assets by the US[163] Algeria served as intermediary to help Iran and the US find a mutually acceptable solution, which was recorded in two Declarations.[164] Pursuant to Article 17 of the General Declaration and Article II of the Claims Settlement Declaration, the IUSCT has jurisdiction over (1) claims of US nationals against Iran and of Iranian nationals against the US that arise out of debts, contracts, expropriations or other measures affecting property rights; (2) certain claims between the two governments relating to the purchase and sale of goods and services; (3) disputes between the two governments concerning the interpretation or performance of the two Declarations; and certain claims between the US and Iranian banking institutions.[165]

(6.52) The IUSCT "shall consist of nine members or such larger multiple of three as Iran and the United States may agree are necessary to conduct its business expeditiously".[166] Each government shall appoint three members; the six members appointed shall select the remaining three members and appoint one of them as the president of the IUSCT.[167] The applicable rules for the IUSCT is the arbitration rules of the United Nations Commission on International Trade Law except to the extent modified by the parties or the

161 Members of the arbitral tribunal were Prof. Michael Reisman (Chairman), Prof. Dr. Jochen A. Frowein, Prof. Dr. Mathias Krafft, Prof. Dr. Paul Lagarde and Prof. Dr. Albert Jan van den Berg. See Bank for International Settlements, Press Release dated 22 September 2003, available at http://www.pca-cpa.org/showpage.asp?pag_id=1157 (last visited 1 Aug 2015).

162 See Bank for International Settlements, Press Release dated 22 September 2003, available at http://www.pca-cpa.org/showpage.asp?pag_id=1157 (last visited 1 Aug 2015).

163 Official website of the Iran-United States Claims Tribunal, available at https://www.iusct.net/Pages/Public/A-About.aspx (last visited 1 Aug 2015).

164 Official website of the Iran-United States Claims Tribunal, available at https://www.iusct.net/Pages/Public/A-About.aspx (last visited 1 Aug 2015).

165 Article 17 of the Declaration of the Government of the Democratic and Popular Republic of Algeria (General Declaration) dated 19 January 1981 and Article II of the Claims Settlement Declaration dated 19 January 1981, available at https://www.iusct.net/Pages/Public/A-Documents.aspx (last visited 1 Aug 2015).

166 Articles III (1) of the Claims Settlement Declaration dated 19 January 1981, available at http://www.iusct.net/General%20Documents/2-Claims%20Settlement%20Declaration.pdf (last visited 1 Aug 2015).

167 Article III (1) of the Claims Settlement Declaration dated 19 January 1981, available at http://www.iusct.net/General%20Documents/2-Claims%20Settlement%20Declaration.pdf (last visited 1 Aug 2015).

IUSCT.[168] The IUSCT shall decide disputes "on the basis of respect for law, applying such choice of law rules and principles of commercial and international law as the Tribunal determines to be applicable, taking into account relevant usages of the trade, contract provisions and changed circumstances".[169] All decisions and awards issued by the IUSCT shall be final and binding.[170] To date, the IUSCT has decided over 3,900 cases.[171]

6.5.2.3 Assessment

(6.53) Arbitration is a dispute resolution mechanism in which parties to a legal dispute agree to submit their disagreement to a person or persons whose expertise or judgment they trust, for a binding decision.[172] This decision is final and enforceable, with only limited opportunities for review, generally restricted to addressing gross violations of due process.[173] As regards its form, arbitration may be distinguished between *ad hoc* arbitration and institutional arbitration. *Ad hoc* arbitrations are administered by the parties themselves, and by the tribunal, without the involvement of any permanent institution.[174] In contrast, institutional arbitrations take place within the framework of a specialized arbitral institution, permitting the arbitrators to draw on the assistance and experience of the institution in the conduct of proceedings.[175]

(6.54) In the context of sovereign debt, first of all, arbitration's appeal lies in its offer of a neutral forum, distinct from the national systems of either party to the dispute and in which both parties are accorded an equal opportunity in selecting the tribunal or individual arbitrator.[176] A second advantage of

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168 Article III (2) of the Claims Settlement Declaration dated 19 January 1981, available at http://www.iusct.net/General%20Documents/2-Claims%20Settlement%20Declaration.pdf (last visited 1 Aug 2015).

169 Article V of the Claims Settlement Declaration dated 19 January 1981, available at http://www.iusct.net/General%20Documents/2-Claims%20Settlement%20Declaration.pdf (last visited 1 Aug 2015).

170 Article IV of the Claims Settlement Declaration dated 19 January 1981, available at http://www.iusct.net/General%20Documents/2-Claims%20Settlement%20Declaration.pdf (last visited 1 Aug 2015).

171 Official website of the Iran-United States Claims Tribunal, available at http://www.iusct.net/Default.aspx (last visited 1 Aug 2015).

172 N. Blackaby, et al., Redfern and Hunter on International Arbitration, 5th ed. (Oxford, 2009), para. 1.02.

173 N. Blackaby, et al., Redfern and Hunter on International Arbitration, 5th ed. (Oxford, 2009), para. 1.02.

174 G. Born, International Commercial Arbitration – Commentary and Materials, 2nd ed. (Transnational, 2001), p. 13.

175 N. Blackaby, et al., Redfern and Hunter on International Arbitration, 5th ed. (Oxford, 2009), para. 1.158.

176 N. Blackaby, et al., Redfern and Hunter on International Arbitration, 5th ed. (Oxford, 2009), para. 1.91.

arbitration is its flexibility – parties enjoy the freedom to adapt arbitral procedures to meet the specific needs of a particular dispute.[177] As sovereign debt disputes involve potentially complex issues, different categories of debt instruments and multiple types of creditors, the ability to easily modify arbitral procedure may be advantageous. A third advantage of arbitration is associated with the parties' ability to choose arbitrators they like with experience and expertise relevant to the dispute.[178] For sovereign debt arbitration, the parties may select individuals with the background of sovereign debt restructuring and/or insolvency law. A final oft-cited advantage of arbitration is its enforceability. Thanks to the New York Convention, foreign arbitration agreements and arbitral awards may easily be recognized and enforced by courts located in the territory of Contracting parties to the Convention, with the latter subject only to narrow exceptions in the event of serious violations of due process in the conduct of the arbitration.[179] To date, there are 150 Contracting parties to the New York Convention.[180] When a sovereign debt dispute arises, the enforceability of arbitration agreements could serve to frustrate efforts by creditors seeking individual relief in alternate fora.

(6.55) With respect to the key proposals for sovereign debt arbitration, Raffer's proposal for a Fair and Transparent Arbitration Process takes the form of *ad hoc* arbitration. By contrast, the proposed Sovereign Debt Tribunal envisages a new institution to be created under the framework of the United Nations. In the view of the author, *ad hoc* arbitration may not be ideal for sovereign debt disputes, because its full effectiveness depends on cooperation between the parties and no institution is available to provide trained staff to administer the arbitration.[181] Moreover, the arbitral process may appear more authoritative when an institution is involved. Notably, both the BIS Tribunal and the IUSCT are institutional arbitrations. While the BIS Tribunal functions under the framework of the Permanent Court of Arbitration, the IUSCT has its own registry to assist the judges in the conduct of proceedings.

(6.56) Despite various advantages of arbitration, one key disadvantage concerns the legal basis for arbitral jurisdiction. As a general matter, the jurisdiction of the arbitral tribunal is based on the parties' consent to submit the

177 J. Lew et al., Comparative International Commercial Arbitration (Kluwer, 2003), paras. 1-14.

178 J. Paulsson et al. (eds), "Chapter 1: Choosing the method", in: The Freshfields Guide to Arbitration Clauses in International Contracts, 3rd ed. (Kluwer, 2010), p. 5.

179 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, done at New York, June 10, 1958, 21 U.S.T. 2517, T.I.A.S. No. 6997, 330 U.N.T.S. 38.

180 Status of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, available at http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/NYConvention_status.html (last visited 1 Aug 2015).

181 N. Blackaby et al., "Chapter 1 on An Overview of International Arbitration", in: Redfern and Hunter on International Arbitration (Oxford, 2009), paras. 1.157 & 1.163.

dispute to arbitration.[182] In the context of sovereign debt, such consent could be expressed through the inclusion of an arbitration clause in individual debt instruments, which would provide recourse to arbitration in the event that the debtor country seeks to restructure its debt.[183] One limitation is that such an arbitral process could extend only to new debt instruments that contain an arbitration clause, but not to existing loans or bonds.[184] This limitation is found in both the proposal for a Fair and Transparent Arbitration Process and the Sovereign Debt Tribunal proposal. Alternatively, an arbitral tribunal for sovereign debt restructuring, either *ad hoc* or institutional, may be established on the basis of an international treaty.[185] This approach could be very effective but largely depends on the political will of governments.

6.5.3 Sovereign Debt Adjudication

6.5.3.1 Adjudication of Sovereign Debt Disputes

(6.57) The term "sovereign debt adjudication" refers to an international insolvency court for sovereign States. At present, there is no international insolvency regime for States and thus no insolvency court for them. From November 2001 through April 2003, the International Monetary Fund proposed a treaty-based framework to restructure sovereign debt –the Sovereign Debt Restructuring Mechanism ("SDRM").[186] Among other things, the SDRM proposal intends to establish, through an amendment of the IMF Articles of Agreement, a dispute resolution forum called the Sovereign Debt Dispute Resolution Forum ("SDDRF"). The IMF Managing Director would appoint 7-11 qualified persons to the selection panel, which would identify 12-16 candidates to constitute the pool of judges.[187] After receiving the list of candidates, the IMF Board of Governors would vote on it on an up or down basis. If the list were rejected, the process would have to start all over again.[188] Once a crisis arises, four judges would be impaneled by the president of the SDDRF in a manner that

182 N. Blackaby, et al., Redfern and Hunter on International Arbitration, 5th ed. (Oxford, 2009), para. 1.39.
183 "Arbitration and Sovereign Debt", Paper prepared by the Steering Committee of the Netherlands Government and the Permanent Court of Arbitration, Jul. 11, 2012, para. 13, available at http://www.slettgjelda.no/filestore/ArbitrationandSovereignDebt.pdf (last viewed 1 Aug 2015).
184 *Ibid.*
185 *Ibid.*, p. 14.
186 S. Hagan, "Designing a Legal Framework to Restructure Sovereign Debt", 36 Geo. J. Int'l L. 299 (2005), pp. 300-301.
187 IMF, *The Design of the Sovereign Debt Restructuring Mechanism-Further Considerations*, prepared by the Legal and Policy Department and Review Departments, November 27, 2002, p. 59.
188 *Ibid.*, p. 61.

ensures impartiality.[189] The president would then appoint one of them as the supervisory judge to oversee the proceedings and to make initial determinations; the other three impaneled members would constitute an appeals panel.[190]

(6.58) The SDDRF would have powers regarding the conduct of the proceedings and dispute resolution,[191] but no authority to challenge decisions of the Executive Board, including with regard to the adequacy of a debtor's policies or the sustainability of the debtor's debt for purposes of the IMF financial assistance.[192] When resolving disputes, the SDDRF would apply the relevant national law for substantive issues, for example an interpretation of the validity of a claim, and apply its own law for procedural issues, for example claims of undue influence on certain creditors or abuse of the voting process.[193] In addition, the SDDRF would resolve disputes that may arise regarding the creation of additional creditor classes not specified in the treaty, if the treaty so allows.[194] Decisions issued by the SDDRF would be binding on the parties but not in other cases.[195]

6.5.3.2 Lessons from the ITLOS

(6.59) Speaking of newly established specialized tribunals, the International Tribunal for the Law of the Sea ("ITLOS") is one of the most recent examples. Based in Hamburg, Germany, the ITLOS is an independent judicial body created by the United Nations Convention on the Law of the Sea ("UNCLOS"), which was adopted in December 1982 and entered into force in November 1994.[196] The ITLOS has jurisdiction over any dispute concerning the interpretation or application of UNCLOS as well as all matters specifically provided for in any other agreement that confers jurisdiction on the ITLOS.[197] It is open to States, intergovernmental organizations and private entities.[198] UNCLOS contains a

189 *Ibid.*, p. 63.
190 *Ibid.*, p. 64.
191 *Ibid.*, p. 66.
192 *Ibid.*, p. 67.
193 *Ibid.*, p. 68.
194 IMF, Sovereign Debt Restructuring Mechanism – Further Considerations, prepared by the International Capital Markets, Legal, and Policy Department and Review Departments, August 14, 2012, p. 27.
195 IMF, *The Design of the Sovereign Debt Restructuring Mechanism-Further Considerations*, prepared by the Legal and Policy Department and Review Departments, November 27, 2002, p. 68.
196 ITLOS official website, available at http://www.itlos.org/index.php?id=15&L=0 (last visited 1 Aug 2015).
197 Article 21 of the ITLOS Statute, available at http://www.itlos.org/index.php?id=12&L=0%25255CoOpensinter (last visited 1 Aug 2015).
198 Article 20 of the ITLOS Statute, available at http://www.itlos.org/index.php?id=12&L=0%2-5255CoOpensinter (last visited 1 Aug 2015).

comprehensive system for the settlement of disputes that provides for four alternative means: the ITLOS, the ICJ, an arbitral tribunal constituted in accordance with Annex VII to the Convention, and a special arbitral tribunal constituted in accordance with Annex VIII to the Convention.[199] A State party is free to choose one or more of these means by a written declaration.[200]

(6.60) The ITLOS is composed of 21 judges, elected from "persons enjoying the highest reputation for fairness and integrity and of recognized competence in the field of the law of the sea".[201] The guiding principles for election are that the representation of the principal legal systems of the world and equitable geographical distribution shall be assured and that there shall be no fewer than three members from each geographical group as established by the UN General Assembly.[202] Moreover, judges are elected by the States parties to the Convention from a list of persons nominated by them; Each State party may nominate up to two persons having the qualifications mentioned in the ITLOS Statute.[203] The procedure to be followed for the conduct of cases before the ITLOS is explained in the ITLOS Statute and the Rules of the Tribunal (ITLOS/8) as amended on 17 March 2009.[204] To date, 23 cases have been submitted to the ITLOS.[205]

6.5.3.3 Assessment

(6.61) International adjudication is a dispute resolution mechanism that provides binding and final decisions on the basis of international law through a standing court. Compared with arbitration that leaves the appointment of arbitrators, the applicable law and rules of procedures upon the parties to decide, adjudication relies on pre-constituted court structures and preset procedures, which the parties maintain less control.[206] Moreover, the attitudes towards confidentiality are different in arbitration and adjudication. While

199 Article 287 of the United Nations Convention on the Law of the Sea, available at http://www.itlos.org/index.php?id=12&L=0 (last visited 1 Aug 2015).
200 *Ibid.*
201 Article 2 (1) of the ITLOS Statute, available at http://www.itlos.org/index.php?id=12&L=0%25255CoOpensinter (last visited 1 Aug 2015).
202 Articles 2 (2) & 3(2) of the ITLOS Statute, available at http://www.itlos.org/index.php?id=12&L=0%25255CoOpensinter (last visited 1 Aug 2015).
203 Article 4 (1) of the ITLOS Statute, available at http://www.itlos.org/index.php?id=12&L=0%25255CoOpensinter (last visited 1 Aug 2015).
204 See ITLOS Statute and the Rules of the Tribunal (ITLOS/8), available at http://www.itlos.org/index.php?id=12&L=0%25255CoOpensinter (last visited 1 Aug 2015).
205 ITLOS official website, available at http://www.itlos.org/index.php?id=10&L=0 (last visited 1 Aug 2015).
206 M. Indlekofer, "Chapter 2: Public International Arbitration in Today's Dispute Settlement Framework", International Arbitration and the Permanent Court of Arbitration, International Arbitration Law Library, Vol. 27 (Kluwer, 2013) p. 120.

court proceedings are generally open to the public, only very rarely that the public is permitted to attend an arbitral proceeding.[207]

(6.62) Among the few permanent international courts, the International Court of Justice is without doubt the most important one. Established in 1945, the ICJ is the principal judicial organ of the UN.[208] It is composed of 15 judges, who are selected by the General Assembly and the Security Council for terms of office of nine years.[209] As regards its case docket, the ICJ settles, in accordance with international law, legal disputes between States submitted to it by them and handles requests for advisory opinions on legal questions referred to it by UN organs and specialized agencies.[210] Given that only States may be parties in cases before the ICJ,[211] sovereign debt disputes between a debtor country and its private creditors would automatically fall outside the scope of the ICJ's jurisdiction.

(6.63) Then the question becomes whether it would be advisable to follow the development in the field of the law of the sea by establishing a specialized international insolvency tribunal to settle sovereign debt disputes. The SDDRF is an example of such a specialized tribunal. Composed of experts in this field, the SDDRF will settle disputes involving both substantive and procedural issues, including, but not limited to, an interpretation of the validity of a claim, claims of undue influence on certain creditors, and claims of abuse of the voting process. Decisions issued by the SDDRF would be binding on the parties but with no precedential value. Viewed from this perspective, the SDDRF process appears to be fundamentally similar to an arbitral mechanism, in which there is also no system of binding precedents.[212]

(6.64) In light of such similarity, it is important to assess the costs involved to set up a SDDRF process and an arbitral mechanism. To start with, an arbitral mechanism does not entail any start-up cost. Arbitration is a flexible way of resolving disputes and the parties to an arbitration will only be required to pay when an actual dispute arises. By contrast, establishing a specialized

207 For example, the public was allowed to attend the hearings in the *Abyei* arbitration. See *Abyei* arbitration, available at http://www.pca-cpa.org/showpage.asp?pag_id=1306 (last visited 1 Aug 2015).

208 Article 92 of the Charter of the United Nations, available at https://www.un.org/en/documents/charter/chapter14.shtml (last visited 1 Aug 2015).

209 Articles 3, 4 & 13 of the Statute of the International Court of Justice, available at http://www.icj-cij.org/documents/index.php?p1=4&p2=2&p3=0 (last visited 1 Aug 2015).

210 Article 96 of the Charter of the United Nations, available at https://www.un.org/en/documents/charter/chapter14.shtml (last visited 1 Aug 2015).

211 Article 34(1), ICJ Statute, available at http://www.icj-cij.org/documents/index.php?p1=4&p2=2&p3=0 (last visited 1 Aug 2015).

212 N. Blackaby et al., "Chapter 1 on An Overview of International Arbitration", in: Redfern and Hunter on International Arbitration (Oxford, 2009), para. 1.113.

tribunal needs a budget for the purposes of building or renting a courtroom and recruiting staff for a secretariat for such tribunal. Furthermore, an arbitral mechanism does not require any maintenance cost when there is no pending dispute, but a specialized tribunal does require so. For example, the budget of ITLOS for 2013-2014 is EUR 21,239,120.[213] This feature of arbitration is particularly desirable in the context of sovereign debt because sovereign debt crises do not happen frequently. Last but not least, while most specialized tribunals only ask the parties to pay a small fee to bring a dispute, the costs involved in an actual arbitration case are not necessarily high. It is reported that on average costs borne by the parties to present their cases constitute 82% of the total costs of that arbitration.[214] The parties are likely to encounter the same costs to present their cases at a specialized tribunal. The remaining 18% of the total costs of an arbitration goes to the arbitral tribunal and the registry. It is extremely difficult to estimate the amount of such costs because it largely depends on the complexity of the case and the length of the arbitral proceeding. In any event, one could possibly argue that the benefits a specialized tribunal brings may not necessarily outweigh the costs involved in creating such a tribunal.

6.6 Conclusion

(6.65) Following the adoption of the UN Resolution "Towards the establishment of a multilateral legal framework for sovereign debt restructuring processes", the debate on a suitable mechanism for the resolution of sovereign debt disputes has become even more relevant. The differing interests of stakeholders in every aspect of sovereign lending and borrowing as well as debt restructuring should be governed by the rule of law. Special emphasis should be placed on establishing a dispute settlement mechanism that takes into account the needs of all stakeholders in this particular context. This mechanism should also learn from the experiences of all other dispute settlement machineries.

(6.66) Among the above-discussed three kinds of dispute settlement mechanisms, mediation is the most flexible and informal process and can in principle lead to a fast and less costly resolution of the dispute. In mediation, the parties retain control of the process and the mediator cannot impose a solution on them. In the author's view, this makes mediation less attractive in general

213 ITLOS official website, available at http://www.itlos.org/index.php?id=149&L=1AND1%253D1 (last visited 1 Aug 2015).

214 ICC Publication No. 843, ICC Techniques for Controlling Time and Costs in Arbitration (2007), available at https://eguides.cmslegal.com/pdf/arbitration_volume_II/CMS%20GtA_Vol%20II_4_3_ICC%20Techniques.pdf (last visited 1 Aug 2015).

because it could in theory continue indefinitely if the parties refuse to compromise. This is particularly unfavorable for disputes arising out of sovereign debt restructurings, because a delay in the resolution of the disputes could have serious impact on the debtor country's economy.

(6.67) On the other hand, both arbitration and adjudication could offer a binding solution. Unlike adjudication, arbitration is a more flexible process, in which the parties enjoy the freedom to adapt arbitral procedures to meet the specific needs of a particular sovereign debt dispute that involves potentially complex issues, different categories of debt instruments and multiple types of creditors. In arbitration, the parties could also choose arbitrators they like with experience and expertise relevant to the dispute. Adjudication, in contrast, relies on pre-constituted court structures and preset procedures, which the parties maintain less control. In the author's view, arbitration seems to be a more preferable mechanism than adjudication given its flexibility.

(6.68) With respect to the legal basis for arbitral jurisdiction, the easiest way is to establish an arbitral tribunal for sovereign debt restructuring on the basis of an international treaty. In light of the current development to negotiate a multilateral legal framework for sovereign debt restructuring at the UN General Assembly, the political feasibility of a treaty-based arbitral tribunal for sovereign debt restructuring is no longer questionable. This idea might even be implemented in the very near future. In this respect, the author suggests that a future treaty-based arbitral tribunal for sovereign debt restructuring could be modeled after the Tribunal concerning the Bank for International Settlements. Unlike the Iran-United States Claims Tribunal, the BIS Tribunal does not have its own registry but utilizes the registry service provided by the Permanent Court of Arbitration. Similarly, a future sovereign debt tribunal could also use the service provided by other arbitral institutions, such as the Permanent Court of Arbitration and the P.R.I.M.E. Finance.[215] Notably, this model allows for the establishment of a standing arbitral tribunal at very low costs. Given that sovereign debt crisis does not happen every day, a BIS-type arbitral tribunal that is available at all times but only involves costs at the time of crisis seems much more attractive than any other proposal in this respect.

215 Established in 2012, P.R.I.M.E. Finance is an arbitral institution that specializes in disputes concerning complex financial transactions. For more information, see http://primefinance disputes.org/about-us/ (last visited 1 Aug 2015).

Summary

In the absence of any international insolvency regime for sovereign States, sovereign debt defaults are dealt with using an *ad hoc*, individual case-by-case approach in which most rules are invented along the way. In practice, the sovereign debtor is compelled to seek debt relief from creditors before or shortly after the default via an extension of the maturity of a creditor's claim and, or in combination with a reduction of the value of this claim. Such relief is obtained by renegotiating the relevant debt instruments (mostly contracts) with different types of creditors, including multilateral financial institutions, governments, commercial banks and bondholders.

This dissertation explores the relationship among creditors in sovereign debt restructuring and specifically focuses on the issue of inter-creditor equity. At the outset, it should be mentioned that the phrase "sovereign debt restructuring" refers to the methods through which sovereign debtors (being sovereign States) obtain debt relief. The word "equity" is to be understood as the state or quality of being just and fair. In the context of inter-creditor equity it therefore means a just and fair treatment of each creditor.

This dissertation consists of three published articles, one forthcoming book chapter and one unpublished article as listed below. The selection of topics focuses on the core issues regarding inter-creditor equity in the context of domestic insolvency law. It is largely inspired by international news coverage on the legal reform of sovereign debt restructuring in the past three years and is in itself enough to demonstrate the different aspects of sovereign debt restructuring.

1. Question the Unquestionable Beauty of a Collective Proceeding for All Sovereign Debt Claims (*International Insolvency Review* Vol. 22: 85-105 (2013); re-published in *Norton Journal of Bankruptcy Law and Practice* Vol. 22, No. 5: 551- 576 (2013))

2. Policy Implication of Poštová Tribunal's Jurisdiction Over Sovereign Bonds: Bankruptcy Cram-Down and ICSID Arbitration (*Norton Journal of Bankruptcy Law and Practice* Vol. 23, No. 5: 604- 633 (2014))

3. New IMF Initiative Revives Old Inter-Creditor Issues (*Tijdschrift voor Insolventierecht* Vol. 19, No. 5: 177- 186 (2013))

4. The Missing Element of a Single Limb Voting Procedure: Fair and Equitable Treatment Standard in Sovereign Debt Restructuring (*Forthcoming* book chapter in: R. Hofmann (ed.), International Investment Law and the Global Financial Architecture, Elgar Publishing 2015)

5. Settlement of Sovereign Debt Disputes: the Present State of Law and Perspectives of Further Development (unpublished)

Chapter 1 introduces my six research questions:

1) whether a collective proceeding for all claims is desirable for sovereign debt restructuring;
2) how to protect the interest of minority bondholders in respect of the approval of a debt adjustment plan;
3) whether claims in a pre-default context should be treated as accelerated for voting purposes through the operation of one-tier aggregated collective action clauses ("CACs");
4) how to design rules regarding the ranking between government creditors and private creditors;
5) whether investment arbitration could serve as an appropriate forum to develop a safeguard provision for CACs with a single-limb voting procedure; and, finally,
6) what is the most desirable mechanism for the settlement of sovereign debt disputes concerning inter-creditor equity. These research questions are treated in separate chapters.

Chapter 2, entitled "*Question the Unquestionable Beauty of a Collective Proceeding for All Sovereign Debt Claims*," discusses inter-creditor equity and the establishment of a legal framework for sovereign debt restructuring in a general context without distinguishing the type of creditors. It begins with a description of various reform proposals addressing the relationship between multilateral, bilateral and commercial creditors and the different views expressed regarding the treatment of these creditors, ranging from equal treatment to separate treatment to comparable treatment. While studying these different views, I have found that nearly all proposals envisage a "collective" proceeding that would include "all" sovereign debt claims without explaining any reasons for such an "all inclusive" vision, which is partly caused by the fact that nearly all national bankruptcy proceedings are "collective" in character. This chapter adopts a critical approach to these views and questions the application of the fundamental theory of collectivity in bankruptcy law to the context of financially distressed sovereign States. It discusses the issue of collectivity from two distinctive aspects: (1) the desirability of a collective proceeding, and (2) the inclusion of all claims in sovereign debt restructuring.

In assessing the desirability of a collective proceeding, this chapter explains that the need for a collective proceeding in national bankruptcy law is justified by two main theories – the common pool problem and the creditors' bargain theory. The common pool problem refers to the situation in which self-interested creditors have every incentive to collect as many of the debtor's assets as quickly as they can, because the creditors who are first to collect suffer none of the deleterious effects of their collection actions. Thus, the creditors' pursuit of their collection remedies is viewed as analogous to the overfishing of a common pool. Relying on the empirical data concerning the number of instances of litigation against sovereign debtors in the US and UK courts between 1976 and 2010, this chapter maintains that a small number of individual actions that may diminish the debtor's pool of assets cannot be compared with the overfishing situation in a common pool. This chapter further explains that, according to the creditor's bargain theory, a collective proceeding is only desirable when it is in the best interests of both unsecured and secured creditors, and that secured creditors would only agree to be included in the same proceeding as unsecured creditors if their rights are well preserved through priority rules. Having analyzed the incomparably different nature of multilateral/bilateral claims, I conclude that it is impossible to weigh political and financial considerations and to devise a priority order between multilateral/bilateral claims and commercial claims. Therefore, multilateral/bilateral claims and commercial claims should not be included in a collective proceeding regarding sovereign debtors.

With respect to the inclusion of "all" claims, this chapter identifies the scope of creditors affected by inter-creditor equity by discussing the "temporary" nature of the sovereign debt crisis and the "alive" feature of the limited pool of sovereign assets. It maintains that where the pool of assets is constantly replenished, the issue of inter-creditor equity does not concern all creditors because the fact that certain creditors grant lesser debt relief does not necessarily require other creditors to grant more. The conflict of interest among creditors exists only during the temporary period when there are not enough assets for everyone. To further support this argument, the chapter discusses the reasons for non-applicability of the automatic acceleration principle in national bankruptcy law in the sovereign debt context through its analysis of the non-liquidable nature of sovereign debtors and the legislative motivation for the adoption of the automatic acceleration principle for municipal debtors in US Chapter 9 on municipality bankruptcy.

Chapter 3 "*Policy Implication of Poštová Tribunal's Jurisdiction Over Sovereign Bonds: Bankruptcy Cram-Down and ICSID Arbitration*" focuses on the issue of inter-creditor equity in the context of sovereign bond restructuring. Given the significant number of bondholders involved in each restructuring, it is evident that it is virtually impossible for the sovereign debtor to engage in direct negotiation with each individual bondholder. In practice, sovereign bond restructurings are conducted through exchange offers or amendments of the original contract terms. Under the exchange offer approach, the sovereign debtor invites bondholders to exchange their bonds for new bonds of lesser value. With respect to the amendment of the original contract terms, collective action clauses have been introduced into sovereign bond documentation to facilitate the process. CACs could enable a qualified majority of bondholders to bind all (other) holders of the same bond issuance to a change of the contract terms, including a change to the maturity date as well as to the amount of interest and principal.

This chapter addresses issues arising out of the adoption of the Greek Bondholder Act during the 2012 Greek debt restructuring. Following the Greek debt restructuring, *Poštová* Banka A.S. (a Slovak entity) and its shareholder Istrokapital S.E. (a Cypriot entity) initiated arbitration against Greece in May 2013 at the International Centre for Settlement of Investment Disputes, pursuant to the bilateral investment treaties concluded between Greece and Slovakia as well as Greece and Cyprus. The claimants contend that they purchased Greek bonds in 2010 and were forced to exchange their bonds for new securities of substantially lesser value. They allege that the forcible bond exchange was carried out through the newly adopted Greek Bondholder Act that retroactively and unilaterally amended the bond terms by inserting a CAC into outstanding Greek-law bonds. According to the claimants, the CAC allows the imposition of new terms upon bondholders against their consent only if a supermajority of other bondholders consent.

Having analysed the nature of the Greek Bondholder Act, I come to the conclusion that what the Act introduced was not an ordinary CAC but something similar to cram-down procedures in national insolvency law. Notably, the Act enables a qualified majority of bondholders to bind all holders of the affected domestic debt to the restructured terms even where the needed majority of creditors for the restructuring would not be attained within a single bond issue. Put differently, the Act eliminates the power of a creditor or a group of creditors to obtain a blocking position in an individual issuance. As a result, in this chapter it is argued that the Act shares some elements of the cram-down procedure in US Chapter 9 on municipality bankruptcy, under which an impaired class could be forced to accept a proposed plan. However, it is also pointed out that the elimination of the power of a creditor to obtain a blocking position in an individual issuance only resembles the cram-down procedure if claims of an individual issuance differ from that of other issuances so that they constitute a particular class by themselves. In this respect, I refer to the UNCITRAL Legislative Guide on Insolvency Law, which provides that ordinary unsecured creditors can be divided into different classes based upon the different nature of debts giving rise to the claims. To apply this criterion to the Greek debt restructuring, in this chapter it is maintained that the nature of an individual issuance differs from that of other issuances with different maturities. Due to different residual maturities involved, the same restructuring term extended to all bondholders implies large differences in the present value haircut across the existing bonds.

This chapter then provides a detailed description of the safeguard provision for the cram-down procedure in US Chapter 9 on municipality bankruptcy. Such a provision prohibits unfair discrimination against each impaired dissent creditor class and also incorporates the fair and equitable treatment principle. To quote the language of that provision, the court shall confirm the plan under the cram down procedure "… if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan."

With this safeguard provision in mind, in this chapter I note that foreign investors are entitled to initiate arbitration under most investment treaties against the host country directly for alleged breaches of treaty obligations through arbitration clauses, which often include fair and equitable treatment principle. The principle of fair and equitable treatment in this context has been interpreted by arbitral tribunals as covering two notions that are similar to the safeguard provision under municipality bankruptcy law: (a) prohibition of unfair discrimination, and (b) legitimate expectations and the obligation of proportionality. Based on the similarities between the safeguard provision for the cram-down in municipality bankruptcy in the US and the fair and equitable treatment principle under investment treaties, I develop the argument that investment arbitration is an appropriate forum to develop a safeguard provision for cram-downs in the context of sovereign debt restructuring. In its concluding remarks, I am emphasizing that arbitral tribunals should be entrusted to exercise their discretion and determine complex and delicate issues concerning sovereign debt. After all, a legal framework for sovereign insolvency can only arise if it can be built over time.

Chapter 4 "*New IMF Initiative Revives Old Inter-Creditor Issues*" provides extensive comments on the IMF's staff paper on "Sovereign Debt Restructuring – Recent Developments and Implications for the Fund's Legal and Policy Framework" dated 26 April 2013. The staff paper was prepared in response to recent debt restructurings, including the largest restructuring in history in Greece, as well as ongoing litigations brought by Argentine bondholders. It does not provide concrete reform proposals, but identifies four issues to be studied further through follow-up staff papers or other research studies: (1) the staff's observation that debt restructurings have often been too little and too late; (2) the collective action problem in sovereign debt restructurings, especially in pre-default contexts; (3) the growing role and changing composition of official lending that call for a clearer framework for official sector involvement; and (4) the IMF's lending into arrears policy that the collaborative, good faith approach should be adopted to resolve external private arrears.

This chapter addresses inter-creditor equity in relation to the second and third issues. The second issue concerns the collective action problem in sovereign debt restructuring, especially in pre-default contexts. The collective action problem refers to the situation in which creditors will become less willing to accept the restructuring offer when other creditors may be able to recover their claims in full, even though it would be in the collective best interest of all creditors to agree to a restructuring as soon as possible. In essence, it is a problem that arises out of the concern of inter-creditor equity. According to the IMF's staff paper, there is merit in designing a more robust form of aggregated CACs for international sovereign bonds to overcome this collective action problem. The paper notes that only four countries have included aggregation clauses in their sovereign bonds to date – Argentina, the Dominican Republic, Greece and Uruguay. These aggregation clauses contain a two-tier voting system: (1) 75 (Greece) or 85 (Argentina, the Dominican Republic and Uruguay) percent of the aggregated outstanding principal of all series to be affected, and (2) 66⅔ percent of the outstanding principal of each individual series to be affected. However, the paper emphasizes that the two-tier aggregation clauses have limitations. For instance, it still enables a creditor or a group of creditors to obtain a blocking position in a particular issue. In order to address this limitation, the paper suggests that the two-tier voting thresholds in the existing aggregation clauses could be replaced with one-tier voting threshold, which disallows blocking minorities in single bond series.

An aggregation clause with one-tier voting threshold that disallows blocking minorities in single bond series, I believe, may present the risk of discriminating minorities with different maturities by empowering majorities to impose an agreement on minorities in a pre-default context. For instance, creditors holding long-term maturity bonds may impose an unfavorable treatment on creditors with short-term maturity bonds, and vice versa. This problem does not exist in a post-default context, because all claims will be accelerated and considered to have the same maturity, i.e., all will be due and payable. In a pre-default context, however, it is inappropriate to treat claims as accelerated for voting purposes in the context of one-tier aggregated CACs. Unlike the prepack arrangements in the non-sovereign context, in this chapter it is explained that unsecured creditors holding sovereign bonds may have less incentive to voluntarily agree on the acceleration of their claims, simply because the likelihood of a general default and insolvency in the sovereign debt context is comparatively small. Given that sovereign debtors can raise revenue through taxation, the pool of assets, although limited, is not still but alive. In addition, States can never be liquidated, thus rendering sovereign debt crisis merely temporary. When the debt crisis is over in a few years, the sovereign debtor will again be able to repay everyone. Therefore, in this chapter it is suggested that claims in a pre-default context should not be treated as accelerated for voting purposes through the operation of one-tier aggregated CACs.

The third issue in the IMF's staff paper relates to the growing role and changing composition of official lending that call for a clearer framework for official sector involvement. In this respect, it is submitted that the IMF's position on the issue of inter-creditor equity is self-contradictory. On the one hand, the IMF maintains that the debtor and creditors should have the freedom to negotiate the debt restructuring strategy, thereby assuming that debt negotiation is a matter that concerns only the debtor and creditor(s) in the negotiation, but not other creditors outside the negotiation. On the other hand, the IMF is worried about the growing number of creditors that are non-Paris Club members as well as the uneven debt negotiation practices across country cases, which indicates its concern for inter-creditor equity. I conclude that this self-contradictory position flows from the fact that the IMF is a multilateral lender itself.

Rules regarding the ranking between official bilateral creditors and private creditors, I suggest, should be developed in a realistic way. As it is impossible to weigh political considerations, the differences between official creditors and private creditors are simply non-comparable. As a result, it take a position in favor of the separate treatment of official and private creditors as well as a general rule that does not specify details of separate treatment, but simply requires all creditors to take a loss in order to contribute to the recovery of debt crisis. This chapter emphasizes that all creditors do not need to be treated equally, but in a manner that reflects the different bargains they have struck with the debtor.

Chapter 5, entitled "*The Missing Element of a Single Limb Voting Procedure: Fair and Equitable Treatment Standard in Sovereign Debt Restructuring*," criticizes the recent reform initiative advocated by the IMF in its paper on "Strengthening the Contractual Framework to Address Collective Action Problems in Sovereign Debt Restructuring" dated 2 September 2014. This staff paper suggests to introduce a few contractual reforms designed to tackle collective action problems so as to achieve orderly sovereign debt restructurings. Among other things, the paper advocates in favor of a single CAC with a menu of voting procedures, including (1) a series-by-series voting procedure, (2) a two-limb aggregated voting procedure, and (3) a single-limb voting procedure with the possibility for sub-aggregation. Given that the CAC's function is to enable a qualified majority of bondholders to bind all holders of the same series to an amendment of the bond terms, different voting procedures permit different levels of influence that minority bondholders could potentially exercise over the restructuring process. Under options (1) and (2), for example, a creditor or a group of creditors could obtain a blocking position in a particular series and effectively prevent the operation of CAC in that series. By contrast, a single-limb voting procedure in option (3) will enable contract terms to be amended on the basis of a single vote across all affected instruments, thereby limiting the ability of holdout creditors to undermine the restructuring process. As explained in the staff paper, the success of the newly adopted Greek Bondholder Act in the 2012 debt restructuring prompted the introduction of this single-limb voting procedure.

This chapter analyses the nature of the single-limb voting procedure and emphasizes its resemblance to cram-down procedures in bankruptcy law.

Whereas the cram-down procedure in the US municipality bankruptcy contains a safeguard provision which ensures minimum protection for each impaired dissent creditor class through the prohibition of unfair discrimination and through the inclusion of the fair and equitable treatment principle (as elaborated in Chapter 3), it is notable that the single-limb voting procedure is silent about creditor protection in this context. In searching for a safeguard provision for the single-limb voting procedure, I have discovered the similarities between the safeguard provision for cram-down procedures and the fair and equitable treatment principle under investment treaties. For this reason, it is submitted that investment arbitration could serve as an appropriate forum to develop a safeguard provision for the single-limb voting procedure. However, not all sovereign debt claims can be brought to investment treaty tribunals. While a mere breach by a state of a contract with foreign investors does not violate international law, a sovereign act of a State contrary to such a contract may do so. Hence, arguably claims concerning the enactment of the Greek Bondholder Act may be brought before investment treaty tribunals, but not claims arising out of the contractual operation of CACs with a single-limb voting procedure in sovereign bonds.

In my concluding remarks I point out that investment arbitration could serve as an appropriate forum to develop a safeguard provision for the single-limb voting procedure but not as an appropriate forum to apply the safeguard provision once developed, as not all sovereign debt claims can be filed before investment treaty tribunals. The search for an appropriate forum to apply the safeguard provision constitutes an entirely different issue and merits careful consideration and discussion elsewhere.

Chapter 6 on "*Settlement of Sovereign Debt Disputes: the Present State of Law and Perspectives of Further Development*" explores the issue concerning the search for an appropriate forum to apply the safeguard provision identified in Chapter 5 in a broader context. This chapter was prepared after the adoption of the UN Resolution "Towards the establishment of a multilateral legal framework for sovereign debt restructuring processes" on 9 September 2014. This resolution decides to elaborate and adopt a multilateral legal framework for sovereign debt restructuring processes with a view to increasing the efficiency, stability and predictability of the international financial system and achieving sustained, inclusive and equitable economic growth and sustainable development.

The chapter begins with a description of the *status quo* of the settlement of sovereign debt disputes, including cases at domestic courts filed under the dispute resolution clauses in bonds or loan contracts as well as cases before investment arbitration tribunals initiated pursuant to investment treaties. Having analysed the *status quo*, it is pointed out that judges in domestic courts do not address the concept of insolvency of a sovereign State. Apart from the fact that such a court may not have jurisdiction to decide on such a matter, it is my contention that these judges would not be able to analyze the key issue of how much should creditors get paid if not the full amount, because the contract law applicable to a particular dispute does not contain similar principles as bankruptcy law. With respect to claims arising out of *pari passu* clauses, judges interpret these clauses on the basis of their wording. Most *pari passu* clauses provide that bonds of that particular issue shall rank equally among themselves. Some also state that the debtor's payment obligation under that particular issue shall rank equally with all other existing and future unsubordinated and unsecured external indebtedness. These judges, I submit, would not analyze the nature of debt giving rise to the claims and determine whether these claims should receive equal treatment as bankruptcy judges do. Furthermore, this chapter addresses the jurisdiction of investment treaty tribunals and emphasizes that arbitral tribunals established under investment treaties have no jurisdiction where the claim at stake is a pure contract claim, as opposed to a claim that alledgedly breaches the obligations specified in investment treaties. A claim is not viewed as a pure contract claim where the circumstances and/or the behavior of the host State appear to derive from its exercise of sovereign State power.

With the aim to explore the perspective of further development in the field of alternatives for settlement of sovereign debt disputes, this chapter compares the characteristics of mediation, arbitration and adjudication, and then assesses the applicability of these methods to disputes arising from sovereign debt matters. In respect of mediation, in this chapter the only example of sovereign debt mediation involving Argentina is presented. It also discusses several examples of municipal debt mediation in the US involving cities such as Stockton and Detroit. This chapter finds mediation a flexible and informal process, which can lead to a fast and less costly resolution of the dispute and can produce creative outcomes in complex disputes that are often unavailable in courts. One key shortcoming of mediation, however, is that it has no set procedure and could in theory continue indefinitely if the parties refuse to compromise. This is particularly unfavorable for disputes arising out of sovereign debt restructurings, because a delay in the resolution of the disputes could have serious impact on the debtor country's economy.

In case of arbitration, this chapter summarises a couple of academic proposals in favor of the establishment of an arbitral tribunal for sovereign debt disputes. The jurisdiction of such a tribunal would derive from arbitration agreements concluded between debtors and creditors themselves. Importantly, such a tribunal is to be differentiated from investment treaty tribunals, which are constituted pursuant to entirely different legal instruments, i.e. arbitration clauses in investment treaties concluded between debtor countries and the home countries of creditors. For discussions on the desirability and feasibility of these sovereign debt arbitration proposals, this chapter offers examples of the Tribunal concerning the Bank for International Settlements and the Iran-US Claims Tribunal. As regards the advantages of arbitration, this chapter places emphasis on the neutrality of the forum, the flexibility of the proceeding as well as the enforceability of arbitral awards. Furthermore, the parties in arbitration could choose the arbitrators they prefer, with experience and expertise relevant to the dispute. For sovereign debt arbitration, the parties may select individuals with the background of sovereign debt restructuring and/or insolvency law. Despite various advantages of arbitration, one key disadvantage concerns the legal basis for arbitral jurisdiction. As a general matter, the jurisdiction of the arbitral tribunal is based on the parties' consent to submit the dispute to arbitration. In the context of sovereign debt, such consent could be expressed through the inclusion of an arbitration clause in individual debt instruments, which would provide recourse to arbitration in the event that the debtor country seeks to restructure its debt. One limitation is that such an arbitral process could extend only to new debt instruments that contain an arbitration clause, but not to existing loans or bonds.

Finally, this chapter explores the topic of sovereign debt adjudication, which refers to an international insolvency court for sovereign States. This chapter recounts the attempts made by the IMF from 2001 to 2003 to establish a treaty-based framework to restructure sovereign debt – the Sovereign Debt Restructuring Mechanism. It also provides an overview of the International Tribunal for the Law of the Sea as a recent example of newly established specialized tribunals. This chapter notes that international adjudication is a dispute resolution mechanism that provides binding and final decisions on the basis of international law through a standing court. Compared with arbitration that leaves the appointment of arbitrators, the applicable law and rules of procedures upon the parties to decide, adjudication relies on pre-constituted court structures and preset procedures, which the parties maintain less control. Furthermore, in this chapter I assess the question of whether it would be advisable to follow the development in the field of the law of the sea by establishing a specialized international insolvency tribunal to settle sovereign debt disputes. Given that the start-up and operational costs needed for a specialized tribunal will certainly be significantly higher than that necessary for the conduct of an arbitral proceeding, my final argument is that the benefits a specialized tribunal could bring may not outweigh the costs involved in creating such a tribunal.

Overall, in my research I argue that a multilateral legal framework for sovereign debt restructuring should not take the form of a collective proceeding and should not include claims with all kinds of maturities. In the context of a cram-down procedure, a safeguard procedure should be favored to ensure that any amendment of the contract terms imposed by majority bondholders is fair and equitable with respect to minority bondholders who have voted against the amendment. In my view, investment arbitration could serve as an appropriate forum to develop such a safeguard provision. A new arbitral tribunal, preferably modelled after the tribunal concerning the Bank for International Settlements, could apply the safeguard provision once developed, because not all sovereign debt claims can be filed before investment treaty tribunals.

Samenvatting
(Dutch Summary)

Onderlinge billijkheid tussen crediteuren in de herstructurering van staatsschuld: op weg naar het opzetten van een multilateraal juridisch raamwerk

In de afwezigheid van een internationaal insolventieregime voor soevereine staten, wordt soeverein kredietverzuim behandeld op basis van een ad hoc benadering van individuele zaken, waarbij de meeste regels gaandeweg gemaakt worden. In de praktijk is de soevereine debiteur verplicht om schuldenverlichting te zoeken bij crediteuren vóór of kort na de ingebrekestelling door middel van een verlenging van de vervaltermijn van de schuldvordering van een crediteur, al dan niet in combinatie met een vermindering van de waarde van deze vordering. Zulke verlichting wordt bereikt door het heronderhandelen van de relevante schuldinstrumenten (voornamelijk contracten) met verschillende typen crediteuren, waaronder multilaterale financiële instellingen, overheden, commerciële banken en obligatiehouders.

Dit proefschrift verkent de relaties tussen crediteuren in de herstructurering van soevereine schulden, en richt zich specifiek op de kwestie van billijkheid tussen crediteuren onderling. Hierbij moet genoemd worden dat 'herstructurering van soevereine schuld' verwijst naar de methodes waardoor soevereine debiteuren (nl. soevereine staten) schuldverlichting bereiken. Het woord 'billijkheid' moet begrepen worden als de staat of kwaliteit van het rechtvaardig en eerlijk zijn. In de context van onderlinge billijkheid slaat dit derhalve op de rechtvaardige en eerlijke behandeling van iedere crediteur.

Dit proefschrift bestaat uit drie gepubliceerde artikelen, één aankomend boekhoofdstuk en één ongepubliceerd artikel, zoals hieronder opgesomd. De keuze van onderwerpen is gericht op essentiële kwesties aangaande onderlinge billijkheid in de context van binnenlands insolventierecht. Deze is grotendeels geïnspireerd door internationale berichtgeving over de juridische hervorming van de herstructurering van staatsschulden in de afgelopen drie jaar, en is op zichzelf voldoende om de verschillende aspecten van de herstructurering van staatsschulden te demonstreren.

1. 'Question the Unquestionable Beauty of a Collective Proceeding for All Sovereign Debt Claims' (*International Insolvency Review* Vol. 22: 85–105 (2013); hergeplubliceerd in *Norton Journal of Bankruptcy Law and Practice* Vol. 22, No. 5: 551- 576 (2013))

2. 'Policy Implication of Poštová Tribunal's Jurisdiction Over Sovereign Bonds: Bankruptcy Cram-Down and ICSID Arbitration' (*Norton Journal of Bankruptcy Law and Practice* Vol. 23, No. 5: 604- 633 (2014))

3. 'New IMF Initiative Revives Old Inter-Creditor Issues' (*Tijdschrift voor Insolventierecht* Vol. 19, No. 5: 177-186 (2013))

4. 'The Missing Element of a Single Limb Voting Procedure: Fair and Equitable Treatment Standard in Sovereign Debt Restructuring' (Forthcoming book chapter in: R. Hofmann (ed.), *International Investment Law and the Global Financial Architecture,* Elgar Publishing 2015)

5. 'Settlement of Sovereign Debt Disputes: the Present State of Law and Perspectives of Further Development' (ongepubliceerd)

Hoofdstuk 1 leidt mijn zes onderzoeksvragen in:

1) of een collectieve procedure voor alle vorderingen wenselijk is voor de herstructurering van staatsschulden;
2) hoe de belangen van minderheidsobligatiehouders beschermd kunnen worden met betrekking tot de goedkeuring van een aanpassingsplan voor schulden;
3) of vorderingen in het stadium vóór ingebrekestelling versneld behandeld moeten worden ten behoeve van stemmingsdoeleinden door middel van het instellen van ééntraps geaggregeerde collectieve-actieclausules ("CACs");
4) hoe regels te ontwerpen met betrekking tot de rangschikking tussen publieke en private crediteuren;
5) of investeringsarbitrage een gepast forum zou kunnen zijn om een beschermingsclausule te ontwikkelen voor CACs met een eenmalige stemmingsprocedure;
6) wat het meest wenselijke mechanisme is voor de regeling van staatsschuldgeschillen met betrekking tot onderlinge billijkheid. Deze onderzoeksvragen worden in afzonderlijke hoofdstukken behandeld.

Hoofdstuk 2, getiteld "*Betwijfel de onbetwijfelbare schoonheid van een collectieve procedure voor alle soevereine schuldvorderingen*," bespreekt onderlinge billijkheid en de oprichting van een juridisch raamwerk voor soevereine schuldenherstructurering in een algemene context, zonder onderscheid in het type crediteur.

Het begint met een beschrijving van diverse hervormingsvoorstellen voor de relatie tussen multilaterale, bilaterale en commerciële crediteuren en hun verschillende visies op de behandeling van deze crediteuren, variërend van gelijke behandeling tot separate behandeling tot vergelijkbare behandeling. Tijdens het bestuderen van de verschillende zienswijzen, heb ik ontdekt dat bijna alle voorstellen een "collectieve" procedure voorstaan, die voor "alle" soevereine schuldvorderingen moet gelden, zonder daarbij de redenen achter een dergelijke "alomvattende" visie uit te leggen, hetgeen gedeeltelijk wordt veroorzaakt door het feit dat bijna alle nationale faillissementsprocedures een "collectief" karakter hebben. Dit hoofdstuk neemt een kritische benadering tot deze zienswijzen, en trekt de toepassing van de fundamentele collectiviteitstheorie in faillissementsrecht op soevereine staten, die in financiële moeilijkheden verkeren, in twijfel. Het bespreekt de kwestie van collectiviteit vanuit twee afzonderlijke aspecten: (1) de wenselijkheid van een collectieve procedure, en (2) het hierin opnemen van alle vorderingen met betrekking tot soevereine schuldenherstructurering.

Om de wenselijkheid van een collectieve procedure te beoordelen, legt dit hoofdstuk uit dat de behoefte aan een collectieve procedure in binnenlands faillissementsrecht wordt gerechtvaardigd door twee voornaamste theorieën – het gemeenschappelijke-vijverprobleem en de crediteurenonderhandelingstheorie. Het gemeenschappelijke-vijverprobleem verwijst naar de situatie waarin crediteuren uit eigenbelang zo snel mogelijk zo veel mogelijk activa van de debiteur proberen te incasseren, omdat de crediteuren die als eerste incasseren niet de schadelijke gevolgen hiervan dragen. Zodoende wordt het najagen van incasseringsmiddelen door crediteuren gezien als analoog aan het overbevissen van een gemeenschappelijke vijver. Op basis van empirische gegevens van het aantal procesvoeringen tegen soevereine debiteuren in gerechtshoven in de VS en VK tussen 1976 en 2010, stelt dit hoofdstuk dat het kleine aantal individuele zaken die de hoeveelheid beschikbare activa van de debiteur kunnen verminderen, niet vergelijkt kan worden met de situatie van overbevissing in een gemeenschappelijke vijver. Dit hoofdstuk legt verder uit, dat in overeenstemming met de crediteurenonderhandelingstheorie een collectieve procedure alleen wenselijk is wanneer dit in het belang van zowel concurrente als preferente crediteuren is, en dat preferente crediteuren alleen zouden toestemmen deel te nemen aan dezelfde procedure als hun rechten behouden blijven door prioriteitsregels. Na het onvergelijkbaar verschillende karakter van multilaterale/bilaterale vorderingen geanalyseerd te hebben, concludeer ik dat het onmogelijk is om politieke en financiële overwegingen af te wegen, en om een prioriteitsvolgorde tussen multilaterale/bilaterale vorderingen en commerciële vorderingen in te stellen. Derhalve moeten multilaterale/bilaterale vorderingen en commerciële vorderingen niet in één collectieve procedure jegens soevereine debiteuren opgenomen worden.

Met betrekking tot het opnemen van "alle" vorderingen, identificeert dit hoofdstuk de crediteuren die belang hebben bij onderlinge billijkheid, door het bespreken van de "tijdelijke" natuur van de soevereine schuldencrisis en het "levende" karakter van de beperkte soevereine bezittingen. Het stelt dat wanneer de hoeveelheid bezittingen constant aangevuld wordt, de kwestie van onderlinge billijkheid niet alle crediteuren betreft, omdat het feit dat sommige crediteuren minder schuldenverlichting bieden, niet noodzakelijkerwijs andere crediteuren verplicht om meer te bieden. De tegenstrijdige belangen onder crediteuren bestaan alleen gedurende de tijdelijke periode dat er niet genoeg activa zijn voor iedereen. Om dit argument verder te ondersteunen, bespreekt het hoofdstuk de redenen voor niet-toepasbaarheid van het automatische versnellingsprincipe in binnenlands faillissementsrecht in de context van staatsschuld, door middel van een analyse van het niet-liquideerbare karakter van soevereine debiteuren en de legislatieve motivatie voor de aanname van het automatische versnellingsprincipe voor gemeentelijke debiteuren in US Chapter 9 over gemeentelijk faillissement.

Hoofdstuk 3 "*Beleidsimplicaties van de rechtsbevoegdheid van het Poštová tribunaal over soevereine obligaties:* cram-down *bij faillissement en ICSID arbitrage"* richt zich op de kwestie van onderlinge billijkheid tussen crediteuren in de context van soevereine obligatieherstructurering. Vanwege het aanzienlijke aantal obligatiehouders dat betrokken is bij iedere herstructurering, is het duidelijk dat het vrijwel onmogelijk is voor de soevereine debiteur om in directe onderhandelingen te treden met iedere individuele obligatiehouder. In de praktijk worden soevereine obligatieherstructureringen uitgevoerd door middel van een uitwisselingsaanbod of een aanpassing van de oorspronkelijke contractvoorwaarden. Onder de uitwisselingsaanpak nodigt de soevereine debiteur de obligatiehouders uit om hun obligaties in te wisselen voor nieuwe obligaties met een lagere waarde. Wat het aanpassen van de oorspronkelijke contractvoorwaarden betreft, zijn er collectieve-actieclausules in de documentatie van soevereine obligaties ingevoerd om het proces te faciliteren. CACs kunnen het mogelijk maken voor een gekwalificeerde meerderheid van obligatiehouders om alle (andere) houders van dezelfde obligatie-uitgifte aan een verandering van de contractvoorwaarden te binden, zowel een verandering van de verlooptijd als van de hoogte van de rente en de hoofdsom.

Dit hoofdstuk pakt daarmee de kwesties aan die voort zijn gekomen uit de aanname van de Griekse Obligatiehouderswet tijdens de Griekse schuldenherstructurering van 2012. Volgend op de Griekse schuldenherstructurering begonnen Poštová Banka A.S. (een Slowaakse entiteit) en diens aandeelhouder Istrokapital S.E. (een Cypriotische entiteit) arbitrage jegens Griekenland in mei 2013 in het Internationaal Centrum voor Beslechting van Investeringsgeschillen, in navolging van de bilaterale investeringsverdragen tussen Griekenland en Slowakije, en tussen Griekenland en Cyprus. De eisers beweren dat zij in 2010 Griekse obligaties hebben gekocht, en vervolgens gedwongen zijn om hun obligaties in te wisselen voor effecten van substantieel lagere waarde. Ze voeren aan dat de gedwongen obligatiewissel werd uitgevoerd onder de nieuw aangenomen Griekse

Obligatiehouderswet, die met terugwerkende kracht en eenzijdig de voorwaarden heeft aangepast door een CAC in te voegen bij uitstaande obligaties die onder Grieks recht vallen. Volgens de eisers staat de CAC een oplegging van nieuwe voorwaarden aan obligatiehouders tegen hun wil alleen toe als een supermeerderheid van overige obligatiehouders ermee instemt.

Na de aard van de Griekse Obligatiehouderswet te analyseren, kom ik tot de conclusie dat wat de wet invoerde geen gewone CAC was, maar iets dat vergelijkbaar is met *cram-down* procedures in binnenlands insolventierecht. De wet maakt het mogelijk voor een gekwalificeerde meerderheid van obligatiehouders om alle houders van de betreffende binnenlandse schulden aan de geherstructureerde voorwaarden te binden, zelfs als de benodigde meerderheid van crediteuren voor het herstructureren niet binnen één obligatie-uitgifte verkregen zou worden. Met andere woorden, de wet elimineert het vermogen van een crediteur of groep van crediteuren om een blokkerende positie in te nemen binnen individuele uitgiftes. Als gevolg hiervan stelt dit hoofdstuk dat de wet gemeenschappelijke elementen heeft met de *cram-down* procedure in US Chapter 9 over faillissement van gemeentes, waarbij een afgewaardeerde klasse gedwongen kan worden om een voorstel te accepteren. Echter, het wijst er ook op dat de eliminatie van het vermogen van een crediteur om een blokkerende positie in te nemen alleen op een *cram-down* procedure lijkt, als de vorderingen ten aanzien van een individuele uitgifte verschillen van andere uitgiftes, zodat ze een afzonderlijke klasse vormen. In dit opzicht refereer ik aan de UNCITRAL Legislative Guide on Insolvency Law, die bepaalt dat gewone concurrente crediteuren verdeeld kunnen worden in verschillende klassen op basis van de verschillende aard van de schulden, die ten grondslag liggen aan de vorderingen. Om dit criterium op de Griekse schuldenherstructurering toe te passen, stelt dit hoofdstuk dat de aard van individuele uitgiftes verschilt van andere uitgiftes met verschillende vervaltermijn. Vanwege de verschillende vervaltermijnen die hierbij betrokken zijn, leidt het opleggen van dezelfde herstructureringsvoorwaarden aan alle obligatiehouders tot grote verschillen in de waardevermindering van de diverse obligaties.

Dit hoofdstuk geeft vervolgens een uitvoerige beschrijving van de beschermingsclausule voor de *cram-down* procedure in US Chapter 9 over het faillissement van gemeentes. Een dergelijke clausule maakt oneerlijke discriminatie jegens elke afgewaardeerde klasse concurrente crediteuren onmogelijk en incorporeert tevens het principe van eerlijke en billijke behandeling. Om de formulering van de betreffende clausule aan te halen, zal het hof het plan onder de *cram-down* procedure bevestigen "…als het plan niet op oneerlijke wijze discrimineert, en eerlijk en billijk is, met inachtneming van iedere klasse van vorderingen of belangen die wordt afgewaardeerd volgens het plan, en dit plan niet accepteert."

Met deze beschermingsclausule in gedachten merk ik in dit hoofdstuk op dat buitenlandse investeerders onder de meeste investeringsverdragen het recht hebben om arbitrage te beginnen tegen het gastland zelf voor vermeende breuk van verdragsverplichtingen door middel van arbitrageclausules, waarin meestal het principe van eerlijke en billijke behandeling is opgenomen. Het principe van eerlijke en billijke behandeling is in deze context door arbitragetribunalen zodanig geïnterpreteerd, dat het twee begrippen omvat, die vergelijkbaar zijn met de beschermingsclausule onder gemeentelijk faillissementsrecht: (a) het tegengaan van oneerlijke discriminatie, en (b) legitieme verwachtingen en de verplichting van proportionaliteit. Gebaseerd op de overeenkomsten tussen de beschermingsclausule voor *cram-down* in gemeentelijk faillissement in de VS en het principe van eerlijke en billijke behandeling onder investeringsverdragen, ontwikkel ik de stelling dat investeringsarbitrage een geschikt forum is om een beschermingsclausule te ontwikkelen voor *cram-downs* in de context van soevereine schuldenherstructurering. In de conclusie van het hoofdstuk benadruk ik dat arbitragetribunalen de ruimte gegeven moet worden om hun oordeel uit te oefenen, en complexe en delicate kwesties met betrekking tot soevereine schuld te bepalen. Ten slotte kan een juridisch raamwerk voor soevereine insolventie alleen ontstaan als het met verloop van tijd opgebouwd kan worden.

Hoofdstuk 4 '*Een nieuw initiatief van het IMF doet oude onderlinge kwesties tussen crediteuren herleven*' geeft een uitgebreid commentaar op het werkdocument van het IMF 'Sovereign Debt Restructuring –Recent Developments and Implications for the Fund's Legal and Policy Framework" van 26 april 2013. Het werkdocument is opgesteld in antwoord op recente schuldenherstructureringen, waaronder de grootste herstructurering in de geschiedenis in Griekenland, alsmede lopende procesvoeringen door houders van Argentijnse obligaties. Het stelt geen concrete hervormingen voor, maar identificeert vier kwesties die verder bestudeerd moeten worden door middel van opvolgende werkdocumenten of andere onderzoeken: (1) de observatie van het personeel dat schuldenherstructureringen vaak te zuinig en te laat zijn; (2) het probleem van collectieve actie in soevereine schuldenherstructureringen, in het bijzonder in predefault context (vóór de ingebrekestelling); (3) de groeiende rol en veranderende samenstelling van overheidsleningen, die vragen om een duidelijker raamwerk voor de betrokkenheid van de publieke sector; en (4) het IMF's leenbeleid voor betalingsachterstanden, namelijk dat een collaboratieve, te goeder trouw aanpak genomen moet worden om externe private achterstanden op te lossen.

Dit hoofdstuk pakt onderlinge billijkheid tussen crediteuren aan met betrekking tot het tweede en derde vraagstuk. Het tweede vraagstuk is van belang voor het collectieve-actieprobleem in soevereine schuldenherstructurering, met name in predefault context. Het collectieve-actieprobleem verwijst naar de situatie waarin crediteuren minder bereidwillig worden om een herstructureringsvoorstel aan te nemen als andere crediteuren hun schuldvorderingen in het geheel kunnen invorderen, ook al zou het in het algemeen belang van alle crediteuren zijn om zo snel mogelijk een akkoord te bereiken over herstructurering. Dit is in essentie een probleem dat voortkomt uit zorgen over onderlinge billijkheid tussen crediteuren. Volgens het IMF werkdocument valt er voordeel te putten uit het ontwerpen van meer robuuste vorm van geaggregeerde CACs voor internationale staatsobligaties om dit collectieve-actieprobleem te overkomen. Het document merkt op dat tot op heden slechts vier landen aggregatieclausules in hun staatsobligaties hebben opgenomen: Argentinië, de Dominicaanse Republiek, Griekenland en Uruguay. Deze aggregatieclausules bevatten een tweetraps stemsysteem: (1) 75 (Griekenland) of 85 (Argentinië, de Dominicaanse Republiek, Uruguay) procent van de geaggregeerde uitstaande hoofdsom van alle betrokken obligatiereeksen, en (2) 66,67 procent van de uitstaande hoofdsom van iedere individuele betrokken reeks. Echter, het document benadrukt dat de tweetraps aggregatieclausules beperkingen hebben. Ze maken het bijvoorbeeld nog steeds mogelijk voor een crediteur of een groep crediteuren om een blokkerende positie in te nemen aangaande een specifieke kwestie. Om deze beperking aan te pakken, stelt dit document voor dat de tweetraps stemdrempel in de huidige aggregatieclausules vervangen kan worden door een ééntraps stemdrempel, die geen ruimte laat voor blokkerende minderheden vanuit individuele obligatiereeksen.

Een aggregatieclausule met een eentraps stemdrempel, die geen blokkerende minderheden vanuit individuele obligatiereeksen toelaat, brengt naar mijn inschatting het risico mee dat minderheden met verschillende vervaltermijnen gediscrimineerd worden, door meerderheden in staat te stellen om minderheden een overeenkomst op te dringen in een predefault context. Zo kunnen crediteuren in bezit van obligaties met een lange looptijd nadelige behandeling van crediteuren met korte termijn obligaties doordrukken, en vice versa. Dit probleem bestaat niet in een postdefault context (na de ingebrekestelling), omdat alle vorderingen versneld worden en allemaal dezelfde vervaltermijn krijgen, namelijk dat alle vorderingen terstond en in hun geheel opeisbaar zijn. In een predefault context is het echter ongepast om vorderingen als versneld te behandelen voor stemmingsdoeleinden in de context van eentraps geaggregeerde CACs. Anders dan pre-pack regelingen in de niet-soevereine context, legt dit hoofdstuk uit dat concurrente crediteuren in bezit van staatsobligaties minder reden hebben om vrijwillig in te stemmen met de versnelling van hun vorderingen, simpelweg omdat de waarschijnlijkheid van een algehele ingebrekestelling en insolventie in de context van staatsschuld relatief klein is. Aangezien soevereine debiteuren hun inkomen kunnen vergroten door middel van belastingen, staat de hoeveelheid activa, hoewel die beperkt is, toch niet vast, maar is het daarentegen een levend iets. Bovendien kunnen staten nooit geliquideerd worden, waardoor een soevereine schuldencrisis slechts tijdelijk is. Als de schuldencrisis een paar jaar later over is, is de soevereine debiteur wederom in staat om iedereen terug te betalen. Derhalve stelt dit hoofdstuk voor dat vorderingen in een predefault context niet versneld behandeld moeten worden voor stemmingsdoeleinden door het in werking stellen van eentraps geaggregeerde CACs.

Het derde vraagstuk uit het IMF werkdocument heeft betrekking op de groeiende rol en veranderende samenstelling van overheidsleningen, die vragen om een duidelijker raamwerk voor de betrokkenheid van de publieke sector. In dit opzicht wordt aangevoerd dat de positie van het IMF inzake de kwestie van onderlinge billijkheid tussen crediteuren tegenstrijdig is. Aan de ene kant stelt het IMF dat debiteur en crediteuren de vrijheid moeten hebben om de strategie voor schuldenherstructurering te onderhandelen, waarbij het aanneemt dat de onderhandeling van schulden alleen betrekking heeft op de debiteur en crediteur(en) in de onderhandeling, maar niet op de crediteuren buten de onderhandeling. Aan de andere kant is het IMF bezorgd over het groeiend aantal crediteuren dat geen lid is van de Club van Parijs, alsook over ongelijke onderhandelingspraktijken schuldenzaken van verschillende landen, hetgeen de bezorgdheid van het IMF over onderlinge billijkheid tussen crediteuren weergeeft. Ik concludeer dat dit tegenstrijdige standpunt voortvloeit uit het feit dat het IMF zelf een multilaterale geldschieter is.

Regels met betrekking tot de rangschikking tussen openbare bilaterale crediteuren en private crediteuren moeten, zo stel ik, op een realistische manier ontwikkeld worden. Aangezien het onmogelijk is om een afweging te maken van politieke overwegingen, zijn de verschillen tussen openbare en private crediteuren simpelweg niet vergelijkbaar. Ten gevolge hiervan, neem ik zowel stelling in ten gunste van de afzonderlijke behandeling van openbare en private crediteuren, als voor een algemene regel die geen details van afzonderlijke behandeling specificeert, maar die simpelweg alle crediteuren ertoe verplicht om een verlies te nemen, om bij te dragen aan de herstelling van de schuldencrisis. Dit hoofdstuk benadrukt dat niet alle crediteuren gelijk behandeld hoeven te worden, maar op een manier die de diverse overeenkomsten reflecteert die ze met de debiteur hebben gesloten.

Hoofdstuk 5, getiteld '*Het missende element van een eenarmige stemprocedure: een standaard voor eerlijke en billijke behandeling in de herstructurering van staatsschulden*,' bekritiseert het recente hervormingsinitiatief dat het IMF voorstaat in het document 'Strengthening the Contractual Framework to Address Collective Action Problems in Sovereign Debt Restructuring' van 2 september 2014. Dit werkdocument stelt voor om een aantal contractuele hervormingen in te voeren om collectieve-actieproblemen te overkomen, teneinde ordelijke herstructureringen van staatsschuld te bereiken. De paper pleit onder andere voor het opstellen van één CAC met een menu aan stemprocedures, waaronder (1) afzonderlijke stemmingen per obligatiereeks, (2) een tweearmige geaggregeerde stemprocedure, en (3) een eenarmige stemprocedure met een mogelijke subaggregatie. Aangezien CACs de functie hebben om een gekwalificeerde meerderheid obligatiehouders in staat te stellen om alle houders van dezelfde reeks aan een aanpassing van de obligatievoorwaarden te binden, staan verschillende stemprocedures verschillende niveaus van invloed toe aan minderheidsobligatiehouders in het herstructureringsproces. Onder opties (1) en (2) kan een crediteur of een groep crediteuren een blokkerende positie binnen een specifieke reeks verkrijgen en de uitvoering van de CAC in die reeks zodoende voorkomen. Daarentegen maakt een eenarmige stemprocedure onder optie (3) het mogelijk om de contractvoorwaarden aan te passen op basis van één stemming onder alle betrokken instrumenten, daarbij het vermogen beperkend van volhardende crediteuren om het herstructureringsproces te ondermijnen. Zoals in de werkdocument wordt uitgelegd gaf het succes van de nieuw aangenomen Griekse Obligatiehouderswet aanleiding tot deze eenarmige stemprocedure.

Dit hoofdstuk analyseert de aard van de eenarmige stemprocedure en benadrukt de overeenkomstigheid ervan met *cram-down* procedures in faillissementsrecht. Terwijl de *cram-down* procedure in gemeentelijk faillissement in de VS een beschermingsclausule bevat, die minimale bescherming verzekert voor iedere afgewaardeerde dissidente klasse van crediteuren door het verbieden van oneerlijke discriminatie en door het opnemen van het principe van eerlijke en billijke behandeling (zoals uitgelegd in hoofdstuk 3), is het opmerkelijk dat de eenarmige stemprocedure zwijgt over de bescherming van crediteuren in dit opzicht. In mijn zoektocht naar een beschermingsclausule voor de eenarmige stemprocedure heb ik de overeenkomsten ontdekt tussen de beschermingsclausule voor *cram-down* procedures en het principe van eerlijke en billijke behandeling onder investeringsverdragen. Om deze reden voer ik aan dat investeringsarbitrage als een gepast forum kan dienen voor het ontwikkelen van de eenarmige stemprocedure. Echter, niet alle vorderingen van staatsschuld kunnen voor investeringsverdragtribunalen gebracht worden. Terwijl enkel een breuk door een staat van een contract met een buitenlandse investeerder geen schending van het internationaal recht is, kan een soevereine handeling van een staat in tegenstrijd met een dergelijk contract dat wel degelijk zijn. Daardoor kunnen mogelijk vorderingen aangaande de bekrachtiging van de Griekse Obligatiehouderswet voor investeringsverdragtribunalen gebracht worden, maar geen vorderingen die voortkomen uit de contractuele uitvoering van CACs met een eenarmige stemprocedure in staatsobligaties.

In mijn conclusie wijs ik erop dat investeringsarbitrage als een gepast forum kan dienen om een beschermingsclausule voor de eenarmige stemprocedure, maar niet als een gepast forum om de beschermingsclausule toe te passen als die eenmaal ontwikkeld is, omdat niet alle vorderingen van staatsschuld bij investeringsverdragtribunalen ingediend kunnen worden. De zoektocht naar een geschikt forum voor het toepassen van de beschermingsclausule is een geheel andere kwestie, die zorgvuldige overweging en discussie elders behoeft.

Hoofdstuk 6 over de '*Beslechting van geschillen over staatsschuld: de huidige staat van het recht en perspectieven op verdere ontwikkeling*' verkent de kwestie aangaande het vinden van een geschikt forum om de in hoofdstuk 5 geïdentificeerde beschermingsclausule in een bredere context toe te passen. Dit hoofdstuk is geschreven na het aannemen van de VN-resolutie 'Towards the establishment of a multilateral legal framework for sovereign debt restructuring processes' op 9 september 2014. Deze resolutie besluit om een multilateraal juridisch raamwerk aan te nemen en uit te breiden voor herstructureringsprocessen van staatsschuld met de blik op het verbeteren van efficiëntie, stabiliteit en voorspelbaarheid van het internationale financiële systeem, en op het bereiken van bestendige, inclusieve en billijke economische groei en duurzame ontwikkeling.

Het hoofdstuk begint met een beschrijving van de status quo van de geschillenbeslechting van staatsschuld, waaronder zowel zaken vallen die voor binnenlandse gerechtshoven zijn gebracht, onder de geschillenbeslechtingsclausules in obligaties of leningscontracten, alsook zaken voor investeringsarbitragetribunalen overeenkomstig investeringsverdragen. Na analyse van de status quo, wordt erop gewezen dat rechters in binnenlandse gerechtshoven zich niet bezighouden met het concept van insolventie van een soevereine staat. Naast het feit dat een dergelijk hof niet de rechtsbevoegdheid heeft om over een dergelijke zaak te oordelen, beweer ik dat deze rechters niet in staat zijn om de cruciale kwestie te analyseren, namelijk hoeveel crediteuren betaald zouden moeten krijgen als niet de volledige som, omdat het contractrecht dat toepasbaar is op een specifiek geschil, niet dezelfde principes bevat als faillissementsrecht. Met betrekking tot vorderingen die voortkomen uit *pari passu* clausules, interpreteren rechters deze clausules op basis van hun bewoordingen. De meeste *pari passu* clausules bepalen dat obligaties van die specifieke uitgifte onderling gelijke rangschikking hebben. Sommige stellen voorts dat de betalingsverplichting van de debiteur onder die specifieke uitgifte gelijke rangschikking heeft als alle andere bestaande en toekomstige niet-achtergestelde en ongewaarborgde externe schuldenlast. Deze rechters, zo beweer ik, zouden niet de aard van de schuld analyseren die aanleiding geeft tot de vorderingen, en niet bepalen of deze vorderingen gelijke behandeling moeten krijgen, zoals faillissementsrechters dat doen. Verder gaat dit hoofdstuk in op de rechtsbevoegdheid van investeringsverdragtribunalen en benadrukt dat arbitragetribunalen gevestigd onder investeringsverdragen geen rechtsbevoegdheid hebben als de betreffende vordering een pure contractvordering is, in tegenstelling tot een vordering die een vermeende breuk van verplichtingen uit investeringsverdragen betreft. Een vordering wordt niet als een pure contractvordering gezien wanneer de omstandigheden en/of het gedrag van de gaststaat afgeleid lijken te zijn van diens uitoefening van soevereine staatsmacht.

Met het doel om het perspectief van verdere ontwikkeling te verkennen op het gebied van alternatieven voor de beslechting van staatsschuldgeschillen, vergelijkt dit hoofdstuk de karakteristieken van bemiddeling, arbitrage en berechting, en beoordeelt vervolgens de toepasbaarheid van deze methodes op geschillen die voortkomen uit staatsschuld. Wat betreft bemiddeling wordt in dit hoofdstuk het enige voorbeeld van de bemiddeling van staatsschuld gepresenteerd waar Argentinië bij betrokken was. Het bespreekt ook een aantal voorbeelden van bemiddeling bij gemeentelijke schuld in de VS, in het geval van steden als Stockton en Detroit. Dit hoofdstuk komt tot de ontdekking dat bemiddeling een flexibel en informeel proces is, wat kan leiden tot een snelle en goedkopere oplossing van het geschil, en creatieve uitkomsten kan voortbrengen in ingewikkelde geschillen, die vaak niet beschikbaar zijn in de rechtszaal. Een cruciale tekortkoming van bemiddeling is evenwel dat het geen vaste procedure heeft, en dat het in theorie oneindig kan voortduren als de partijen weigeren om toe te geven. Dit is bij uitstek onbehulpzaam bij geschillen die voortkomen uit een herstructurering van staatsschuld, omdat een vertraging in de oplossing van de geschillen serieuze gevolgen kan hebben voor de economie van het debiteurland.

Wat betreft arbitrage vat dit hoofdstuk een aantal academische voorstellen samen, die pleiten voor het vestigen van een arbitragetribunaal voor geschillen aangaande staatsschuld. De rechtsbevoegdheid van een dergelijk tribunaal zou afgeleid worden uit arbitrageovereenkomsten die tussen debiteuren en crediteuren zelf tot stand zijn gebracht. Het is van belang dat een dergelijk tribunaal onderscheiden wordt van investeringsverdragtribunalen, die overeenkomstig geheel verschillende juridische instrumenten bestaan, te weten arbitrageclausules in investeringsverdragen tussen debiteurenlanden en de thuislanden van crediteuren. Voor de bespreking van de wenselijkheid en uitvoerbaarheid van deze arbitragevoorstellen voor staatsschuld biedt dit hoofdstuk voorbeelden van de Bank voor Internationale Betalingen en het Tribunaal inzake vorderingen tussen Iran en de Verenigde Staten. Wat betreft de voordelen van arbitrage, legt dit hoofdstuk nadruk op de neutraliteit van het forum, de flexibiliteit van het proces, alsmede de afdwingbaarheid van een arbitrale uitspraak. Tevens kunnen de partijen in de arbitrage zelf de arbiters kiezen, met voor het geschil relevante ervaring en expertise. Voor de arbitrage van staatsschuld, kunnen de partijen personen selecteren met een achtergrond in de herstructurering van staatsschuld en/of insolventierecht. Ondanks de diverse voordelen van arbitrage, is er een cruciaal nadeel met betrekking tot de juridische basis van rechtsbevoegdheid. Als een algemene regel is de rechtsbevoegdheid van het arbitragetribunaal gebaseerd op de instemming van de partijen om het geschil voor arbitrage in te dienen. In de context van staatsschuld kan aan zulke instemming uitdrukking worden gegeven door het opnemen van een arbitrageclausule in de afzonderlijke schuldinstrumenten, die zou voorzien in de inschakeling van arbitrage in het geval dat het debiteurland schulden wil herstructureren. Een beperking is dat een dergelijk arbitrageproces zich alleen zou uitstrekken tot nieuwe schuldinstrumenten waarin een arbitrageclausule is opgenomen, maar niet tot bestaande leningen en obligaties.

Ten slotte verkent dit hoofdstuk het onderwerp van berechting van staatsschuld, dat verwijst naar een internationaal insolventieregime voor soevereine staten. Dit hoofdstuk haalt de pogingen van het IMF tussen 2001 en 2003 om een op verdragen gebaseerd raamwerk op te richten om staatsschulden te herstructureren aan – het 'herstrucureringsmechanisme voor staatsschulden.' Het geeft ook een overzicht van het Internationale Hof voor het Recht van de Zee als een recent voorbeeld van nieuw opgerichte gespecialiseerde tribunalen. Dit hoofdstuk merkt op dat internationale rechtspraak een geschillenbeslechtingsmechanisme is dat bindende en definitieve uitspraken verschaft op basis van internationaal recht door een permanente rechtbank. Vergeleken met arbitrage, dat de benoeming van arbiters, toepasbaar recht en de regels van procedures aan de partijen om zelf te beslissen, is berechting afhankelijk van vooropgezette rechtbankstructuren en vooringestelde procedures, waarover de partijen minder controle behouden. Tevens geef ik in dit hoofdstuk een beoordeling van de vraag of het aan te bevelen is om de ontwikkelingen op het gebied van het recht van de zee te volgen, door een gespecialiseerd internationaal insolventietibunaal op te richten voor het beslechten van geschillen over staatsschuld. Aangezien de opstart -en operationele kosten van een gespecialiseerd tribunaal zeker aanzienlijk hoger zullen zijn dan wat noodzakelijk is voor een arbitrageprocedure, is mijn uiteindelijke standpunt dat de voordelen die een gespecialiseerd tribunaal zou kunnen brengen, niet opwegen tegen de kosten van het opzetten bij een dergelijk tribunaal.

Over het geheel genomen, beargumenteer ik in mijn onderzoek dat een multilateraal juridisch raamwerk voor de herstructurering van staatsschulden niet de vorm van een collectieve procedure zou moeten aannemen, en geen vorderingen met verschillende vervaltermijnen zou moeten omvatten. In de context van een *cram-down* procedure, zou er voorkeur gegeven moeten worden aan een beschermingsprocedure om te verzekeren dat iedere aanpassing van de contractvoorwaarden die afgedwongen wordt door een meerderheid van obligatiehouders eerlijk en billijk is ten aanzien van de minderheidsobligatiehouders die tegen de aanpassing stemmen. In mijn opinie kan investeringsarbitrage als een geschikt forum dienen voor het ontwikkelen van een dergelijke beschermingsclausule. Een nieuw arbitragehof, bij voorkeur gemodelleerd naar voorbeeld van het tribunaal inzake de Bank voor Internationale Betalingen, zou de beschermingsclausule kunnen toepassen wanneer deze ontwikkeld is, omdat niet alle vorderingen van staatsschuld voor investeringsverdragtribunalen gebracht kunnen worden.

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Yanying Li was born on 23 November 1987 in Chongqing, China. She studied law at the Zhejiang Gongshang University in China, where she graduated *cum laude* in 2008. She then moved to the United States and completed the LL.M Program in Transnational Business Practice at the Pacific McGeorge School of Law, where she received a scholarship of 80 percent tuition for distinguished academic record. During 2009-2010, she joined the Advanced LL.M Program in European and International Business Law at Leiden University with a scholarship of 50 percent tuition for distinguished academic record. Besides the advanced LL.M, she also participated in the research-oriented Talent Programme of the Graduate School of Legal Studies at Leiden University. During her Ph.D study at Leiden, she completed a three-month research fellowship at the Lauterpacht Centre for International Law, University of Cambridge.

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In the range of books published by the Meijers Research Institute and Graduate School of Leiden Law School, Leiden University, the following titles were published in 2013, 2014 and 2015

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