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Sovereign debt and holdout disruption

A good faith and relational contract approach

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CHAPTER 1

1 Sovereign Debt and Holdout Disruption

1.1 The Concept of Sovereign Debt

The term 'sovereign debt' may be generically described as debts owed by a sovereign entity (a country or other legally recognized[14] sovereign) in its capacity as such. However, sovereign debt does not easily yield to one definition because of the inherent difficulty in identifying and categorizing all the items in a country's balance sheet to identify what is 'debt' and then determining what portion of that debt is legally the sovereign's. This thesis focuses on external sovereign debt, and for this reason I define "sovereign debt", for purposes of this thesis, as debt that a country owes in its capacity as a sovereign entity to persons outside of its borders.[15] The term "sovereign debt", "external debt" or "debt" as used in this thesis should therefore be understood to refer to external sovereign debt (as herein defined), unless the contrary is stated or the context requires otherwise.

There are two key ingredients in my definition of "sovereign debt". First, it must be external, not domestic.[16] Secondly, it must be owed by the country in its sovereign capacity (i.e., it must be

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[14] Under public international law (for the law on sovereignty and recognition of sovereigns under public international law, see Malcom Shaw, INTERNATIONAL LAW (9th ed. 2021); and James Crawford, BROWNLIE'S PRINCIPLES OF PUBLIC INTERNATIONAL LAW (9th ed., 2012)).

[15] This definition partly adopts the definition of sovereign debt by Udaibir S. Das, Michael G. Papaioannou, and Christoph Trebesch as "debt issued or guaranteed by the government of a sovereign state" (Udaibir S. Das, Michael G. Papaioannou, and Christoph Trebesch, *Sovereign Debt Restructurings 1950 – 2010: Literature Survey, Data and Stylized Facts*, IMF WORKING PAPER WP/12/203 (2012)), at 7, but also emphasizes the critical element that makes the debt external – the holders of the debt. See also Celine Tan, *Reframing the debate: the debt relief initiative and new normative values in the governance of third world debt*, INT. J.L.C (2014), at 250 (agreeing with the International Law Association's definition of sovereign external debt as debt contracted by the state that is expressed in some foreign currency typically payable abroad, governed by some external law and subject to the jurisdiction of external courts). However, contemporary definition of sovereign debt no longer requires that the obligation of public sector entities be guaranteed by the state for it to be sovereign debt (see the definition of external public debt by the World Bank in the International Debt Statistics (2022), at 28).

[16] For discussions and distinctions between external and domestic debt, see IMF, EXTERNAL DEBT: DEFINITION, STATISTICAL COVERAGE AND METHODOLOGY (March 15, 1998); Ugo Panizza, *Domestic and External Public Debt in Developing Countries*, UNCTAD DISCUSSION PAPERS 188/2008 (2008), at 4; and Ugo Panizza, Federico Sturzenegger and Jeromin Zettelmeyer, *International Government Debt*, UNCTAD DISCUSSION PAPERS 199/2010 (2010), at 2. IMF Special Drawing Rights (SDRs) (which are international reserve assets created by the IMF, allocated to members to supplement existing official reserves, and held only by the depositaries of IMF members, a limited number of international financial institutions that are authorized holders, and the IMF itself through the General Resources Account) are also considered external debt, because: (a) they are recorded on the balance sheet of the member country as a long-term debt liability to non-residents, with a corresponding entry on the financial assets side; (b) countries are required to pay interest on the allocation they have received, and arrears arise if payments are not made; and (c) a country would be required to repay its allocation of SDRs in certain circumstances, such as upon termination of its participation in the SDR Department of the IMF or upon liquidation of the SDR Department. See IMF, *SDR Allocations: Frequently Asked Questions on their Statistical Treatment*, available at

public debt). Thus, private sector debt (save to any extent that they are guaranteed by the sovereign) does not qualify as sovereign debt, notwithstanding that private sector debt could also significantly affect a country's balance of payment position.[17] Perhaps the most authoritative source on what constitutes public debt in international finance has been the Public Sector Debt Statistics: Guide for Compilers and Users. The Public Sector Debt Statistics: Guide for Compilers and Users defines public debt as including all liabilities of public sector units, excluding equity (ownership and similar shareholding interests in corporate entities) and investment fund shares, financial derivatives and employee stock options.[18] For purposes of this definition, "total debt" or "total debt liabilities" is defined as consisting of all liabilities that are debt instruments; and a "debt instrument" is defined as a financial claim that requires payment(s) of interest and/or principal by the debtor to the creditor at a date, or dates, in the future.[19] The International Debt Statistics 2022 (a work product of the staff of the World Bank, with external contributions) also defines public (external[20]) debt as "an external obligation of a public debtor, including all levels of government, state-owned enterprises, public corporations, development banks, and any other autonomous public bodies of government".[21] Publicly guaranteed debt – an external obligation of a private debtor that is guaranteed for repayment by a public entity – is also considered as part of external debt.[22]

I focus on external debt in this thesis because domestic debts are not typically considered problematic (or, at least, not as problematic as external debt) in sovereign debt restructuring for several reasons. First, they are mostly issued under domestic law and not typically held by foreign investors. Therefore, the sovereign can easily change the term of the debt contract using its domestic legislation or other policy instruments. A fairly recent and notorious example is the

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https://www.imf.org/external/np/exr/faq/pdf/sdrfaqsta.pdf (last visited June 11, 2023), and Organization for Economic Co-operation and Development (ed), DEBT STOCK, DEBT FLOWS AND THE BALANCE OF PAYMENTS, available at http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/1994/01/01/000009265_3970716143445/Rendered/PDF/multi0page.pdf (last visited June 11, 2023).

[17] Michael Richard Pearce, *Moratoriums on Foreign Sovereign Debts*, 15 PHIL. Y.B. INT'L L. (1989) 48, at 49 (arguing that the exclusion of private debt from the definition of sovereign external debt is somewhat arbitrary as public international law issues can arise when states block payments on private foreign debt owed by their nationals or when they suspend payment on their domestic debt owed to foreign nationals, since, from an economic point of view, each must be satisfied from the same pool of foreign exchange, which is usually controlled by the debtor state through its central bank).

[18] PUBLIC SECTOR DEBT STATISTICS: GUIDE FOR COMPILERS AND USERS (IMF ed., 2013) (Revised Second Printing). The Public Sector Debt Statistics: Guide for Compilers and Users is a product of the international agencies that participate in the Inter-Agency Task Force on Finance Statistics (TFFS) in close consultation with national compilers of public sector debt and government finance statistics. The 2013 Revised Second Printing is an updated version of the print first published on December 8, 2011 by the IMF and was put together by the Bank for International Settlements, The Commonwealth Secretariat, the European Central Bank, Eurostat, IMF, OECD, Paris Club, UNCTAD and the World Bank Group.

[19] *Id.* at 3.

[20] External debt refers to the debt obligations of a country that are held by non-residents. See The External Debt Statistics: Guide for Compilers and Users (IMF ed., 2014) at 5.

[21] World Bank. 2022. *International Debt Statistics 2022*. Washington, DC: World Bank. doi:10.1596/978-1-4648-1800-4. License: Creative Commons Attribution CC BY 3.0 IGO, at 204.

[22] *Id.*

Greek Bondholder Act of 2012, which the government of the Hellenic Republic used to force all holders of its domestic law-governed bonds to participate in its 2012 debt restructuring.[23] Secondly, most domestic debts are issued in local currency. Thus, a country facing a domestic debt crisis could, barring possible monetary union restrictions, simply print more of its currency (at the risk of inflation and other monetary policy consequences) to pay the debt.[24] Thirdly, external debt repayment typically involves capital leaving the country, thus depressing economic activity and making further repayments even more difficult; domestic debt typically does not.[25]

Domestic debt does not, therefore, appear to pose as much serious risks to a country's fiscal and financial health and balance of payment position as external debt. It needs to be emphasized, however, that as much as the above reasons to focus on external debt in the discourse over sovereign debt restructuring may still be valid, countries typically still pay careful attention to the management of domestic debt as it implicates several dynamics in both domestic and international financial systems: governments increasingly issue domestic debt in foreign currency and/or governed under foreign law; in today's world a domestic debt instrument could be ultimately held by a foreigner or could be easily traded to a foreigner; a government's radical or disruptive change in domestic debt instruments could prove disastrous rather than helpful to its economy, for instance, a misinformed or poorly-timed restructuring of domestic debt held by pension funds or predominantly within the local banking system could wipe out people's savings and could cripple rather than improve a struggling economy.[26] Zambia, for instance, refused to include its local currency domestic bonds held by foreigners in its currently ongoing (as of May 2023) debt restructuring (even in the face of arguments that it could deliver more debt relief), arguing that inclusion of domestic bonds in the restructuring could unravel the country's macroeconomic stability.[27]

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[23] Leland Goss, *Sovereign debt restructuring made easy?* 32 INT'L FIN. L. REV. 62 (2013-2014) (on the power of a sovereign to use legislation to alter the terms of its domestic debt – citing Greece and Argentina as examples); and Stephen J. Choi, Mitu Gulati and Eric A. Posner, *Pricing terms in sovereign debt contracts: a Greek case study with implications for the European crisis resolution mechanism*, 6(2) CAPITAL MARKETS LAW JOURNAL, 163 (2011) (on the power of a sovereign to use its legislation to alter the terms of bonds issued under its laws – citing Greece as an example, although in the case of Greece, the majority of the investors in its domestic law bonds were in fact foreigners).

[24] It is noteworthy that there has been an increase in foreign investors investing in local currency government debt as reported in the IMF's Staff Note for the G20 IFAWG of June 15, 2018 (at para. 12). A Financial Times article of October 2019 indicated that foreign investors hold about 29 percent of Russia's local currency domestic debt (Max Seddon and Henry Foy, *Russia looks at alternatives to dollar for energy transactions*, FINANCIAL TIMES, October 13, 2019). This is hardly a side-show. A Forbes report of April 2019 also indicated that there is nearly US$ 8 trillion worth of local currency sovereign bonds outstanding, accounting for over 40% of the notional value of emerging market bonds outstanding…and trading in these bonds accounts for between half and three-quarters of volume on any given day (Kevin McPartland, *Understanding The $15 Trillion Market For Emerging Market Bonds*, FORBES, April 25, 2019).

[25] John Addis, *Why the debt crisis matters*, CRICKEY (August 30, 2011) available at www.crikey.com.au/2011/08/30/what-is-sovereign-debt/ (last visited June 16, 2023).

[26] Anna Gelpern, *Sovereign Debt Crisis: Creditor's Rights vs. Development*, ASIL PROCEEDINGS (2003). Notable, also, is the lesson from the Greek 2012 restructuring where the need to recapitalize banks that sustained losses due to haircuts imposed by the country meant that up to EUR 8 billion (or 19 percent of GDP) in debt relief otherwise delivered by the restructuring was wiped out.

[27] Joseph Cotterill, *Zambian finance minister criticizes creditor delays in debt restructuring*, FINANCIAL TIMES, February 12, 2023.

The discourse on holdout disruption (i.e., the strategic use of litigation in domestic courts by sovereign creditors who refuse to participate in a sovereign debt restructuring to disrupt the sovereign debt restructuring process and obtain repayments on their debt outside of the restructuring process, which is discussed in detail at sub-Chapters 1.4 and 1.5) in this thesis is focused on private commercial debt (i.e., debt owed by sovereigns to private sector lenders, also called "private debt")[28], because this thesis is about holdout disruption of sovereign debt restructuring through litigation in domestic courts and/or arbitration. This by no means indicates that viewpoints or other solutions distilled from the enterprise of this thesis would not be applicable to other forms of sovereign debt; it only acknowledges the reality that holdout disruption has been a phenomenon known only in the framework of the restructuring of private commercial debt, mostly sovereign bonds. The term "sovereign bond" is a financial market term for debt issued by sovereigns by way of bonds issued and traded in the capital markets and subscribed to (bought) by investors as a form of debt securities investment. It is also sometimes called "bonded debt". While the majority of contemporary holdout disruption (including of the 'vulture' kind (see sub-Chapter 1.4 below)) occur in the context of the restructuring of sovereign bonds, it has also occurred, though much less frequently than in the restructuring of sovereign bonds, in the context of the restructuring or renegotiation of other types of private commercial debt.[29] Moreover, to the extent that sovereign bonds and other private commercial debt are relational contracts, solutions to holdout disruption from a relational contract approach would be equally applicable to the restructuring of sovereign bonds as it would to other types of private commercial debt.

1.2 A Brief Overview of Sovereign Debt Restructuring

The term "sovereign debt restructuring" loosely refers to an exercise through which a sovereign debtor agrees (or attempts to agree) with its creditor(s) to alter the terms of the debt instrument(s), usually for purposes of managing the sovereign debtor's unsustainable debt burden. This definition, however loose, is not controversial and is in consonance with the definitions generally used in international finance lexicon.[30] Although some writers tend to equate debt restructuring with debt rescheduling, the terms are not coterminous. Debt

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[28] Where the discourse is not on holdout disruption, the term "sovereign debt" may be used in the generic sense of a sovereign's external debt or private commercial debt, depending on the context.

[29] Landmark holdout and vulture cases not involving sovereign bonds include *Allied Bank International v. Banco Credito Agricola de Cartago* 566 F. Supp. 1440 (S.D.N.Y. 1983); *Pravin Banker Associates Ltd v. Banco Popular del Peru* 165 B.R. 379 (S.D.N.Y. 1994); *Elliot Associates v. Peru* 109 F.3d 850 (2nd Cir. 1997); *Donegal International v Zambia* [2007] EWHC 197 (Comm); [2007] 1 Lloyd's Rep. 397; *Kensington International v Republic of Congo* [2003] EWCA Civ 709.

[30] See sample definitions in The External Debt Statistics: Guide for Compilers and Users (IMF ed., 2014), *supra* note 20, *id*. See also Udaibir S. Das, Michael G. Papaioannou, and Christoph Trebesch, *Sovereign Debt Restructurings 1950 – 2010: Literature Survey, Data and Stylized Facts*, IMF WORKING PAPER WP/12/203 (2012), at 7; Charles W. Mooney, Jr., *A Framework for Formal Sovereign Debt Restructuring Mechanism: The KISS Principle (Keep it Simple, Stupid) and Other Guiding Principles,* FACULTY SCHOLARSHIP, PAPER 1547 (2015) at 2; and François Gianviti, Anne O. Krueger, Jean Pisani-Ferry, André Sapir and Jürgen von Hagen, *A European Mechanism for Sovereign Debt Resolution: A Proposal*, Volume X, BRUEGEL BLUEPRINT SERIES (2010) at 2.

rescheduling is a process whereby a country agrees with its creditor to reschedule the repayment profile of the debt (typically involving a lengthening of maturities) in order that the country may better manage its finances and be able to repay the debt according to the new payment profile. While debt rescheduling is a form of debt restructuring, the whole universe of sovereign debt restructuring encompasses many concepts and the restructuring process could take on several forms and may be mixed and matched to the needs of the sovereign and its creditors to obtain the best restructuring terms.[31]

The need to restructure sovereign debt normally arises when a country's debt stock relative to its income (usually expressed in terms of debt to gross domestic product (GDP) ratios in international monetary and financial jargon) reaches such levels that the debtor country could no longer afford to repay the debt at all or without foregoing other critical financial and fiscal responsibilities needed to maintain a cohesive and functional socio-economic and political order in the country. The creditors of a corporate borrower in this position can call in the receiver[32] to operate the business for their benefit or force the corporation into bankruptcy and distribute its assets. The corporate debtor in countries with United States-like corporate bankruptcy reorganization regime could also seek legal protection from its creditors while it attempts to undergo some arrangements to exit insolvency and avoid liquidation.[33] None of these options are available to a sovereign debtor. It must pay up or hope that it strikes a bargain with its creditors to restructure the debt.

On the other hand, the sovereign enjoys several legal and structural protections not available to corporate debtors. While creditors may seek liquidation of a corporation and distribution of its assets in satisfaction of its debts, sovereign creditors cannot liquidate a country and distribute its assets. Further, obtaining judgements and enforcing them against the assets of the sovereign pose such legal hurdles that a bet on either obtaining the judgement or successfully enforcing it,

[31] Other forms of sovereign debt restructuring include debt exchange (where new debt instruments, typically containing a cocktail of new terms more in favor of the distressed debtor are exchanged for the original debt instruments under which old terms the debtor's debt profile had become unsustainable), debt conversion (where original debt is discharged and replaced with some other debt or debt-like obligation, such as debt-for-nature, debt-for-development, etc., deals), and debt assumption (where a third party steps in and assumes the debt obligation of the original debtor on same or renegotiated terms, while the original debtor is discharged).

[32] A receiver is a common law term for a person appointed by a court or the creditors to manage the affairs of a bankrupt or insolvent borrower and to distribute its assets in liquidation as may be ordered by the court or agreed between the debtor and creditors.

[33] Chapter 11 of the United States Bankruptcy Code (11 U.S.C. §§ 301, 303) allows a debtor to remain in possession of its assets and may be able to manage its affairs in a manner approved by and under supervision of the court, under a plan of reorganization that must be approved by its affected creditors. The United States Chapter 11 bankruptcy law has been a major and popular lifeline for distressed corporate debtors allowing them to reorganize their affairs through an insolvency episode and return to profitability while avoiding liquidation. It has been adopted (with some variations) in several jurisdictions around the world, including in the European Union (see the EU's Restructuring Directive of 2019) and the United Kingdom (see the UK's Corporate Insolvency and Governance Act of 2020).

even in creditor-friendly jurisdictions, is a gamble for the brave, well-resourced, and patient.[34] It is thus in the best interests of both the sovereign borrower and its creditors that unsustainable sovereign debt be restructured; and creditors should be encouraged to negotiate a restructuring once a distressed sovereign approaches them for that in good faith.

The potential for regional and international contagion or outright financial crisis from a poorly-managed sovereign debt crisis should also serve as enough impetus for other stakeholders in the international financial community to pay close attention and provide any possible assistance towards the management, particularly restructuring, of unsustainable sovereign debt. This is because a sovereign debt crisis could rarely be ring-fenced; it typically brings with it other economic, social, and political issues of significant proportion, and is rarely confined to the borders of the debtor country.

1.3 Approaches to Sovereign Debt Restructuring

It is now common for academic writers and commentators in international finance to discuss two approaches to sovereign debt restructuring: the so-called "statutory approach" and "contractual approach".[35] While it is hardly contestable that sovereign debt restructuring, as an exercise between the borrower and its creditors, is inherently a contractual exercise regardless of what approaches or instruments the parties decide to use for their purposes, the label "contractual approach" has been more commonly used to refer to the use of contractual clauses (particularly collective action clauses (CACs) and pari passu clauses) in sovereign debt instruments to tackle the problem of holdout disruption. CACs are contractual terms in sovereign debt (typically bond)

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[34] For some readings on these unique characteristics of sovereign debt and the relationship between the sovereign borrower and its creditors, see Lee Buchheit and Elena Daly, *Minimizing Holdout Creditors: Carrots, in* SOVEREIGN DEBT MANAGEMENT (Rosa M. Lastra and Lee Buchheit eds., 2014) at 3; S. Ari Mushell, *The Weight of the World on its Shoulders: How US-style Reform at the IMF can Ease the Global Sovereign Debt Crisis*, 31 JOURNAL OF INTERNATIONAL BANKING LAW AND REGULATION 3 (2016) at 151-160; Annerose Tashiro, *Sovereign Insolvency*, EUROPEAN LAWYER 5 (2010); and Celine Tan, *Reframing the debate: the debt relief initiative and new normative values in the governance of third world debt*, INT. J.L.C 251 (2014).

[35] See for instance Mooney, Jr, *supra* note 30, at 15 (proposing a "Sovereign Debt Restructuring Law (SDRL)" that would apply to sovereigns as debtors and which "embraces the statutory approach"); Gianviti, Krueger, Pisani-Ferry, Sapir and Hagen, *supra* note 30, at 13 (noting that "procedures to deal with insolvency in debt contract is referred to as the contractual approach", which is "distinguished from the 'statutory approach' in which procedures spelled out in domestic or international law would be followed and bind the parties"); Juan Pablo Bohoslavsky & Matthias Goldmann, *An Incremental Approach to Sovereign Debt Restructuring: Sovereign Debt Sustainability as a Principle of Public International Law*, 41(2) YALE JOURNAL OF INTERNATIONAL LAW ONLINE, available at HTTPS://PAPERS.SSRN.COM/SOL3/PAPERS.CFM?ABSTRACT_ID=2865845# (last visited June 11, 2023) (discussing "statutory" and "contractual" approaches to sovereign debt restructuring, highlighting the weaknesses of each and proposing an "incremental approach" to sovereign debt restructuring); Rodrigo Olivares-Caminal, *Statutory Sovereign Debt Resolution Mechanisms, in* SOVEREIGN DEBT MANAGEMENT, *supra* note 34, at 334-356 (discussing the IMF-proposed "Sovereign Debt Restructuring Mechanism" among other proposals for "statute-based" sovereign debt restructuring); and Christoph G. Paulus, *A Standing Arbitral Tribunal as a Procedural Solution for Sovereign Debt Restructurings, in* SOVEREIGN DEBT AND THE FINANCIAL CRISIS: WILL THIS TIME BE DIFFERENT? 317 - 329 (Carlos A. Primo Braga and Galli A. Vincelette, eds., 2010) (proposing a standing tribunal, not established by treaty but which jurisdiction would have to be incorporated into debt instruments, for the enforcement of sovereign debt restructuring agreements).

instruments that enable a given proportion of the creditors to agree to certain actions that modify the original terms of the debt instrument. Pari passu clauses are provisions in bond and bank loan instruments which provide for an equal ranking[36] of the debt in question with all other unsecured and similarly ranked (in contractual priority of payment) sovereign debt of the sovereign borrower/issuer.

Contractual clauses are simply one set of tools for the purposes of sovereign debt restructuring as a contractual exercise, with CACs being the most potent and popular. While these clauses constitute important tools in sovereign debt restructuring, the reference to their use (particularly CACs) as *the contractual approach* to sovereign debt restructuring, particularly as opposed to *the statutory approach*, needs to be understood in its context. Sovereign debt restructuring as a contractual exercise can be accomplished with or without the aid of CACs or more of these contractual clauses.[37] In fact, it appears that this undue focus on contractual clauses as representative of contractual sovereign debt restructuring has unfortunately deflected attention from other aspects of contract law, theory, and practice that could have been explored in the quest to tackle holdout disruption of sovereign debt restructuring, including, as I now do in this thesis focusing on good faith and the relational contract approach.

The statutory approach, on the other hand, and as variously proposed in international finance discourse, consists of variegated proposals and ideas on how to address key challenges of sovereign debt restructuring, particularly holdout disruption, by institutionalizing a supra-national legal mechanism for sovereign debt restructuring, which, in most forms proposed, would consist of both administrative and judicial or quasi-judicial frameworks for the restructuring of sovereign debt. I undertake a detailed discussion on the statutory approach's promises and shortcomings at sub-Chapter 2.1 of this thesis. The distinction that writers and commentators often make between contractual and statutory approaches to sovereign debt restructuring, thus, merely reflects a nascent quest to explore public law-centered options as alternative approaches to sovereign debt restructuring as a contractual exercise because of its perceived shortcomings, particularly the problem of holdout disruption (see sub-Chapter 1.4 below).

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[36] While New York and some English and Brussels courts accepted arguments in *NML v. Argentina* (discussed in full below at sub-Chapters 1.4 and 1.5 below) that the pari passu clause forbids payment to consenting creditors unless holdouts are also ratably paid, it is generally considered that these arguments were wrong because the pari passu clause does not require ratable payment but rather only secures the equality of ranking of the creditors, especially in the sense that none is subordinated to the other, but not that one could not be paid under revised terms if another refused such payment. See Allen & Overy Global Law Intelligence Unit, *Uses and Abuses of Collective Action Clauses in Sovereign Bonds*, 14(3) BUS. L. INT'L. 269 (2013) at 276.

[37] In a survey of sovereign debt exchanges from 2014 to 2020, including nine exchanges of sovereign bonds, 2 of the sovereign bond exchanges either had no CACs or were accomplished without the use of CACs. See IMF*, The International Architecture for Resolving Sovereign Debt Involving Private-Sector Creditors – Recent Developments, Challenges, and Reform Options*, September 23, 2020, at 10. Besides CACs are typically bespoke to sovereign bonds (although nothing prohibits the use of like contractual provisions in intercreditor agreements for other private commercial sovereign debt), and other types of sovereign debt workouts such as Paris Club treatments and London Club deals are accomplished without CACs.

The statutory and contractual approaches alike command significant following in international financial discourse, although the statutory approach appears to command greater following in the academia than it does in official circles. I dedicate Chapter 2 of this thesis to a discussion on the promises and imperfections of both the contractual and statutory approaches as a necessary background on the current state of play in sovereign debt restructuring, the imperfections of the current framework, and the need for other viable legal solutions such as I explore under the duty of good faith and the relational contract approach. Critical gaps and shortcomings in both the contractual and statutory approaches, as would be seen in the discussion in Chapter 2, make it imperative that alternative viable solutions that could be implemented under the current domestic and international legal framework, such as I propose in this thesis, are given more than a cursory look.

1.4 Holdout Disruption of Sovereign Debt Restructuring

1.4.1 Holdouts Defined

"Holdout creditor" is such a common vocabulary in international financial lexicon that most writers do not bother to define it. Everyone seems to understand what they mean, and discussions of holdouts tend to hinge mostly on their disruption of sovereign debt restructuring rather than who they are or what they do. When writers deem it necessary to say what they are, descriptions rather than definitions have been, understandably, used.

However, I will define the term in this thesis because of the focus on holdout disruption. For purposes of this thesis, therefore, I define the term "holdout creditor" or "holdout" as a sovereign creditor who refuses participation in a sovereign debt restructuring, and takes adjudicative action (either in domestic courts or arbitral tribunals) against the sovereign debtor to stop the restructuring exercise, stop the implementation of the restructured debt deal, and/or enforce the payment of its debt (typically in full) outside the framework of the restructuring. My definition of holdout creditor here is broadly in consonance with the definitions and descriptions used by other writers and commentators on this subject.

Rick Antonoff defined holdouts as "… creditors whose participation is necessary to make a restructuring work but who decline to participate in the hope that they will recover payment in full, or at least more than they expect to recover in the restructuring".[38] Chuck Fang, Julian Schumacher, and Christoph Trebesch described holdouts as those who "… free-ride, reject the haircut suffered by other creditors, and possibly go to court, resulting in less debt relief and the risk of disruptive litigation".[39] Lee Buchheit, Guillaume Chabert, Chanda Delong, and Jeromin Zettelmeyer described holdout creditor as "… an importunate maverick creditor that declines to join the restructuring and threatens to pursue legal remedies" on the theory that "if the sovereign

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[38] Rick Antonoff, *Out-Of-Court Debt Restructuring and The Problem of Holdouts and Free Riders*, CORPORATE COUNSEL BUSINESS JOURNAL (September 19, 2013).

[39] Chuck Fang, Julian Schumacher, Christoph Trebesch*, Restructuring Sovereign Bonds: Holdouts, Haircuts and the Effectiveness of CACs*, ECB WORKING PAPER SERIES No 2366 (January 2020).

debtor receives debt relief from most of its lenders, this will increase the likelihood that the sovereign will have the money to pay [them] off".[40] Steven Schwarcz described the "holdout problem" as "a type of collective action problem in which certain creditors, such as vulture funds, refuse to agree to a reasonable debt restructuring plan that proposes to change critical terms, hoping to receive more than their fair share of a settlement".[41] Alison Wirtz described the "holdout problem" as "one of the threats to a sovereign debt restructuring program … that a subset of creditors will refuse to agree to the bond exchanges or other proposed terms and pursue full repayment under the original bond terms through litigation".[42] UNCTAD defined "holdouts" as "investors who refuse to negotiate and demand that the debt instruments be honoured in full".[43]

In general international finance context, holdout creditors may be: (a) retail investors (probably scattered all over the world) who may refuse to participate in a restructuring because they view the terms as not good enough, do not fully understand the terms, or for some other reason have a genuine reason to refuse participation; (b) creditors (retail investors or otherwise) who come to the negotiation table with genuine intention to make a deal with the sovereign debtor once the terms are fair enough, but could also refuse to participate if they do not believe that the sovereign is offering fair restructuring terms or otherwise acting in good faith; and (c) creditors who have pre-conceived stance of no-cooperation and whose primary goal is to free-ride the process in order to maximize profit. This latter type (c) of creditors are mostly sophisticated investors (typically hedge funds) and they constitute the bulk of the class of creditors which I define as "holdout creditors" for purposes of this thesis. Holdouts falling into types (a) or (b) would fall within the definition of "holdout creditors" for purposes of this thesis, if regardless of the underlying reason for their refusal to participate in the restructuring, they employ litigation or arbitration with a view to stop the restructuring exercise, stop the implementation of the restructured debt deal, or enforce the payment of their debt outside the framework of the restructuring exercise. The critical and defining element in my definition of a holdout creditor, for purposes of this thesis, is its disruptive use of litigation or arbitration to stop the restructuring exercise, stop the implementation of the restructured debt deal, or force the payment of its own debt outside of the restructuring framework under circumstances in which such litigation or arbitration for payment of its debt threatens the success of the debt restructuring exercise; and, in this sense, any creditor could be a holdout creditor, even though, in practice, large and sophisticated hedge funds have been notorious for this phenomenon. When corporate creditors pursue distressed debt of developing countries for maximum profit either as holdout creditors generally or in specific pursuit of a distressed debt (whether or not restructuring proposals are on the table) they are more commonly referred to as "vulture funds" or "vulture creditors".

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[40] Lee Buchheit, Guillaume Chabert, Chanda Delong, and Jeromin Zettelmeyer, *The Restructuring Process, in* SOVEREIGN DEBT: A GUIDE FOR ECONOMISTS AND PRACTITIONERS 344 (Abbas, Pienkowski, and Rogoff, eds., 2020).

[41] Steven L. Schwarcz, *Sovereign Debt Restructuring: A Model-Law Approach*, DE GRUYTER (2016).

[42] Alison Wirtz, *Bilateral Investment Treaties, Holdout Investors, and Their Impact on Grenada's Sovereign Debt Crisis*, 16 CHI. J. INT'L L. 249 (2015).

[43] UNCTAD, *Sovereign Debt Restructuring and International Investment Agreements*, IIA ISSUES NOTE NO. 2 (July 2011).

Holdout disruption mostly takes the form of enforcement proceedings, usually in domestic courts of major financial centers where the holdout may sue either to stop the sovereign from making payments on the restructured debt, unless payments are also made on the debt of the holdouts (ratably – as have been variously and successfully argued by Andreas Lowenfeld and accepted by New York and Brussels courts in the case of *Elliot Associates v. Peru*[44]) or to specifically enforce payments (usually all of principal, accrued and compounded interest, fees, and costs) on the debt they refused to tender for restructuring. Research shows that holdouts have historically earned very high returns and their successes have led to a greater incentive to holdout from regular restructuring processes.[45]

1.4.2 The Consequences of Holdout Disruption

The desire of the holdout to protect its rights and further its interests often collide head-on against the contractual rights of the sovereign debtor to reap the benefits of the sovereign debt contract by continuing to deploy the loan for the purposes of which it was contracted (which rights subsist even in default and restructuring scenarios), the right of the sovereign to enjoy the benefits of debt sustainability under a restructured debt profile, as well as the contractual rights of the other creditors under common debt instruments or subject to the same restructuring exercise as the holdouts who have agreed to the restructuring under the sovereign debt contractual framework. As Chapters 5 and 6 of this thesis discuss, the contractual right of both the sovereign and other creditors to reap the benefits of their bargain is protected under both English and New York law by the duty of good faith, while the disruptive effect of holdout disruption jeopardizes this right.[46]

1.4.3 Academic and Policy Viewpoints on Holdout Disruption

The dominant academic and policy viewpoint is that holdout disruption poses critical threats to sovereign debt restructuring, particularly in the case of privately held sovereign bonds, deserving of an effective solution. This viewpoint is widely acknowledged and documented in the literature of international finance.[47] For this dominant viewpoint, holdout disruption has been, since the

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[44] Discussed in detail at Chapter 7 of this thesis.

[45] Rohan Pitchford and Mark L. J. Wright, *On the Contribution of Game Theory to the Study of Sovereign Debt and Default*, (29)(4) OXFORD REVIEW OF ECONOMIC POLICY, 649–667 (2013), at 662. See also Manmohan Singh, *Recovery Rates from Distressed Debt – Empirical Evidence from Chapter 11 Filings, International Litigation, and Recent Sovereign Debt Restructurings*, IMF WORKING PAPER, (WP/03/161) (2003) (noting that holdout creditors have averaged recovery rates of about 3 to 20 times their investment, equivalent to returns, net of legal fees, of 300 to 2000 percent).

[46]For a general reading on the disruptive effects of holdouts see Buchheit and Daly, *Minimizing Holdout Creditors: Sticks, supra* note 34, at 15; Jonathan I. Blackman and Rahul Mukhi, *The Evolution of Modern Sovereign Debt Litigation: Vultures, Alter Egos, and Other Legal Fauna, in A Modern Legal History of Sovereign Debt (Anna Gelpern and G. Mitu Gulati, Special eds.),* 73 FALL LAW & CONTEMP. PROBS. 47; and Julian Schumacher, Christoph Trebesch, and Henrik Enderlein, *The legal cost of default: How creditor lawsuits are reshaping sovereign debt markets*, CEPR POLICY PORTAL (July 16, 2018).

[47] See Michael Waibel, SOVEREIGN DEFAULTS BEFORE INTERNATIONAL COURTS AND TRIBUNALS, 121-128 (2011); Buchheit and Daly, *Minimizing Holdout Creditors: Carrots, supra* note 34, at 3; Buchheit and Daly, *Minimizing Holdout Creditors:*

Latin America debt crisis of the 1980s[48], a recognized major barrier to orderly sovereign debt restructuring as well as a major source of global financial instability which has, as discussed at sub-Chapter 1.5 below, steadily grown into a near-intractable global crisis particularly during the Argentina debt imbroglio of the early 2000s.

There is, however, a minority of academic voices that have questioned the dominant viewpoint and argue rather that holdout disruption, despite its demonstrable effects on sovereign debt restructuring, is either good for a number of reasons (discussed at sub-Chapter 1.4.3.2 below) or is not of such material adverse consequences to warrant the concerted attempt across the broad spectrum of the international financial community to combat it. I discuss these views in the following two sub-chapters before summarizing at sub-Chapters 1.4.3.3 and 1.4.3.4, for purposes of this thesis, the adverse effects of holdout disruption (including of the 'vulture' variety (see sub-Chapter 1.4.3.4)) warranting the efforts of the international financial community to combat it and the enterprise of this thesis.

1.4.3.1 The Majority and Dominant View

The dominant view shared by most academic writers and policy commentators alike agree that holdout disruption constitutes a serious threat to successful restructuring of sovereign debt with several adverse consequences for sovereign borrowers and the international financial system, and variously canvass the need to prevent holdout creditors from free-riding or disrupting the restructuring of sovereign debt. Lee Buchheit[49], Mitu Gulati[50], Stephen Choi[51], Phillip Wood[52],

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Sticks, supra note 34; Mauro Megliani, *Vultures in courts: why the UNCTAD principles on responsible financing cannot stop litigation*, LEIDEN JOURNAL OF INTERNATIONAL LAW 849 (2015); Lee Buchheit, *Sovereign Debt Restructuring: The Role of the Official Sector in Sovereign Debt Workouts*, 6 CHI. J. INT'L L. 333 (2006); Jill Fisch and Caroline Gentile, *Vultures or Vanguards: The Role of Litigation in Sovereign Debt Restructuring*, 53 Emory L. J. 1043, at 1085; Anne Krueger & Sean Hagan, *Sovereign Debt Workouts: An IMF Perspective,* 6 CHI. J. INT'L L. 203 (2006).

[48] G. Mitu Gulati & Kenneth N. Klee, *Sovereign Piracy*, 56 BUS. LAW. 635 (2001), at 637-638.

[49] Buchheit and Daly, *Minimizing Holdout Creditors: Carrots, supra* note 34.

[50] Michael Bradley and Mitu Gulati, *Collective Action Clauses for the Eurozone*, REVIEW OF FINANCE, Vol. 18, Issue 6, (October 2014), at 2045–2102; Robert E. Scott, Stephen J. Choi & Mitu Gulati, *Anticipating Venezuela's Debt Crisis: Hidden Holdouts and the Problem of Pricing Collective Action Clauses,* 100 B.U. L. REV. 253 (2020); G. Mitu Gulati and Kenneth N. Klee, *Sovereign Piracy,* 56(2) THE BUSINESS LAWYER 635-651 (2001).

[51] Stephen J. Choi, Mitu Gulati, & Eric A. Posner, *The Dynamics of Contract Evolution* 88(1) NYU LAW REV. (2013); Stephen J. Choi & G. Mitu Gulati, *Contract as Statute,* 104 MICH. L. REV. 1129 (2006); Stephen J. Choi & G. Mitu Gulati, *Innovation in Boilerplate Contracts: An Empirical Examination of Sovereign Bonds,* 53 EMORY L.J. 929 (2004).

[52] Phillip Wood, *Pari Passu Clauses: What Do They Mean?,* 18 JOURNAL OF INTERNATIONAL BANKING AND FINANCE LAW (2003); Phillip Wood, *Adverse Impact of Argentina Case,* FINANCIAL TIMES, December 3, 2012; Phillip Wood, THE LAW AND PRACTICE OF INTERNATIONAL FINANCE (2019).

Michael Waibel[53], Odette Lienau[54], Matthais Goldmann[55], Mark Weidemaier[56], Rodrigo Olivares Caminal[57], and Steven Schwarcz[58], are among the several experts in the field who have all variously lent their academic voices to the call for a recognition of the dangers posed by holdout disruption to sovereign debt restructuring and for the adoption of measures to mitigate these dangers.

A December 2013 study by Schumacher, Trebesch, and Enderlein analyzing sovereign defaults in courts since 1976 found a "strong increase in creditor litigation" with "almost 50 percent of sovereign debt restructurings" involving "creditor lawsuits abroad".[59] Another 2018 study noted that "specialized distressed debt funds have emerged as a new type of holdout plaintiffs since the 1990s, which often buy debt at a discount and then sue for full repayment and who now account for two-thirds of all new cases".[60] These researchers also warned that the legal risks of holdout disruption are here to stay and "looking ahead, there are few reasons to assume that the legal risk on sovereign debt will decrease soon" and even the "most widely discussed policy reforms – such as newly designed collective action clauses (CACs) – are unlikely to fully prevent holdout litigation in future debt crises".[61] Other studies have also shown that notable holdout disruption of the restructuring of the debt of countries such as Peru and Argentina are neither exceptions nor outliers but "part of a general trend" showing that the risk of litigation in the context of sovereign default and restructuring has increased greatly since the 1980s.[62] According

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[53] Michael Waibel, *Opening Pandora's Box: Sovereign Bonds in International Arbitration*, 101 AM. J. INT'L L. 711 (2007).
[54] Odette Lienau, *The Challenge of Legitimacy in Sovereign Debt Restructuring*, 57 HARV. INT'L. L.J. 151 (2016).
[55] Armin von Bogdandy and Matthias Goldmann*, Sovereign Debt Restructurings as Exercises of International Public Authority: Towards a Decentralized Sovereign Insolvency Law, in* SOVEREIGN FINANCING AND INTERNATIONAL LAW: THE UNCTAD PRINCIPLES ON RESPONSIBLE SOVEREIGN LENDING AND BORROWING (2013); Matthias Goldmann, *Public and Private Authority in a Global Setting: The Example of Sovereign Debt Restructuring*, 25 IND. J. GLOBAL LEGAL STUD. 331 (2018); Matthias Goldmann, *Foreign Investment, Sovereign Debt, and Human Rights, in* SOVEREIGN DEBT AND HUMAN RIGHTS, (Ilias Bantekas and Cephas Lumina, eds., 2018).
[56] W. Mark C. Weidemaier, *Sovereign Immunity and Sovereign Debt*, 2014 U. ILL. L. REV. 67 (2014); W. Mark C. Weidemaier & Anna Gelpern, *Injunctions in Sovereign Debt Litigation*, 31 YALE J. ON REG. 189 (2014); Weidemaier, W. Mark C., *Reforming Sovereign Lending Practices: Modern Initiatives in Historical Context, in* SOVEREIGN FINANCING AND INTERNATIONAL LAW: THE UNCTAD PRINCIPLES ON RESPONSIBLE SOVEREIGN LENDING AND BORROWING (Carlos Espósito, Yuefen Li, and Juan Pablo Bohoslavsky, eds., 2013).
[57] Rodrigo Olivares-Caminal, LEGAL ASPECTS OF SOVEREIGN DEBT RESTRUCTURING (2009); Rodrigo Olivares-Caminal, *Rank Pari Passu or Not to Rank Pari Passu: That Is the Question in Sovereign Bonds after the Latest Episode of the Argentine Saga*, 15 LAW & BUS. REV. AM. 745 (2009); Rodrigo Olivares-Caminal, *Sovereign bonds: A Critical Analysis of Argentina's Debt Exchange Offer*, 10(1) JOURNAL OF BANKING REGULATION, 28-45 (2018).
[58] Steven Schwarcz, *Global Decentralization and The Subnational Debt Problem*, 51(4) DUKE LAW JOURNAL 1179 (2002); Steven L. Schwarcz, *A Minimalist Approach to State Bankruptcy*, 59 UCLA L. REV. 322 (2011); Steven L. Schwarcz, *Looking Forward: 2005-2010 - A Sovereign Debt Restructuring Reverie*, 6 CHI. J. INT'L. L. 381 (2005); Steven L. Schwarcz, *Sovereign Debt Restructuring: A Bankruptcy Reorganization Approach*, 85 CORNELL L. REV. 956 (1999); Steven L. Schwarcz, *Sovereign Debt Restructuring: A Model-Law Approach*, DE GRUYTER 6(2) 343–385 (2015).
[59] Julian Schumacher, Christoph Trebesch, and Henrik Enderlein, *Sovereign Defaults in Court*, (2013) at 8-12.
[60] Julian Schumacher, Christoph Trebesch, Henrik Enderlein, *The legal cost of default: How creditor lawsuits are reshaping sovereign debt markets*, CEPR POLICY PORTAL (July16, 2018).
[61] *Id*.
[62] Julian Ams, Reza Baqir, Anna Gelpern, and Christopher Trebesch, *Sovereign Default, in* PUBLIC DEBT THROUGH THE AGES (2018), at 23-24.

to Robert Scott, Stephen Choi and Mitu Gulati, "… the research on sovereign restructurings shows that these holdout creditors (usually fewer than 5 percent of the bondholders) have been a consistent feature of sovereign restructurings over the past two decades and that the activist creditors who have successfully held out have, in many instances, received lucrative recoveries".[63]

From a human rights perspective, the Independent Expert to the United Nations Human Rights High Commissioner has published several reports highlighting the debilitating effects of holdout disruption of sovereign debt restructuring (including the vulture variety) on human rights of people in developing countries. These effects include diversion of resources needed for social services in the debtor country towards payments of outsized amounts of debt to successful holdouts, political instability, and a lack of capacity of the debtor country to effectively plan and implement its national development objectives.[64]

At the international financial institutional level, major multilateral development and financial institutions (including the IMF, World Bank, and the ECB), have been consistent in their view that holdout disruption poses a major threat to sovereign debt restructuring and the stability of the international financial system, and in their concerted efforts to contain holdout disruption, through the use of CACs, led by the IMF.[65] The push for use of CACs and other contractual instruments in sovereign debt restructuring has been the key response that these institutions proffer as a solution to the holdout problem.[66]

1.4.3.2 The Minority View

Although practitioners, policy makers, and academics alike overwhelmingly acknowledge the disruptive effect of holdout disruption, and many warn that it remains a potent threat to successful restructuring of sovereign debt and the larger international financial architecture, some writers, *albeit* of the minority view, see holdout creditors (including the vulture types) as doing more good than harm, and so not deserving of the criticism they get in international finance discourse.

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[63] Scott, Choi & Gulati, *supra* note 50, at 260.

[64] For the mandate and work of the Independent Expert, visit https://www.ohchr.org/en/issues/development/iedebt/pages/iedebtindex.aspx (last visited June 11, 2023).

[65] See IMF, SOVEREIGN DEBT RESTRUCTURING – RECENT IMPLICATIONS FOR THE FUND'S LEGAL AND POLICY FRAMEWORK (April 26, 2013); IMF, THE INTERNATIONAL ARCHITECTURE FOR RESOLVING SOVEREIGN DEBT INVOLVING PRIVATE-SECTOR CREDITORS – RECENT DEVELOPMENTS, CHALLENGES, AND REFORM OPTIONS (September 23, 2020); World Bank, *Orderly Sovereign Debt Restructuring: Missing in Action*, (POLICY RESEARCH WORKING PAPERS, 2012-2017); UNCTAD, *Sovereign Debt Restructuring and International Investment Agreements*, IIA ISSUES NOTE No. 2 (July, 2011).

[66] See ECB, *Collective Action Clauses in the Euro Area*, available at https://europa.eu/efc/efc-sub-committee-eu-sovereign-debt-markets/collective-action-clauses-euro-area_en (last visited June 11, 2023); IMF, *Strengthening the Contractual Framework to Address Collective Action Problems in Sovereign Debt Restructuring*, (October, 2014); IMF, *Fourth Progress Report on Inclusion of Enhanced Contractual Provisions in International Sovereign Bond Contracts*, (March, 2019); and UNCTAD, *Sovereign Debt Workouts: Going Forward, Roadmap and Guide* (April, 2015).

Hal Scott, in his criticism of the United States and the New York Federal Reserve's *amici* briefs against holdout disruption of the Argentine debt restructuring of the 2000s, blamed sovereigns for overborrowing and argued that the United States should give creditors the same rights against sovereign borrowers that the creditors have against private borrowers,[67] and stop supporting the IMF's promotion of CACs as preferred contractual instruments of sovereign debt restructuring.[68] Scott may be considered one of the strongest sympathetic voices for holdouts, even going as far as discouraging the use of CACs. His main arguments focused on contractual rights of creditors, United States policy (which he argued should be pro-market and which he insisted was being undermined by the United States' position on holdout disruption and the use of CACs), and the overborrowing of debtor countries. Academic research, data, and analyses, however, appear to show that the uniqueness of sovereigns makes it inapposite to apply private contract or other applicable private creditor laws to sovereign debt restructuring without modifications necessary to cater for the sovereign's unique attributes, and so do not seem to support Scott's views.[69] Scott's criticism of the United States for abandoning a pro-market policy also does not seem to be supported by the United States' policy actions and statements alike (including its *amici briefs*) promoting the use of contractual clauses in managing the problem of holdout disruption of sovereign debt restructuring which do not appear to be evidence of anti-market policy and have not in fact been opposed by the market itself. Quite the contrary, the International Capital Markets Association (ICMA), a key representative group of market makers, has been the most prominent market promoter of the use of CACs, introducing the now popular enhanced CACs and Specimen MVPs, respectively discussed in sub-Chapters 2.2.3.1 and 2.2.6 of this thesis. Finally, Scott's blaming of countries for overborrowing, while plausible on the face of it, does not account for the reality, as I already discussed in sub-Chapter 1.2 above, that the need to restructure sovereign debt does not arise simply because a country overborrowed, as unsustainable debt burden could arise due to many factors besides borrowing in excess.

Another argument in favor of holdouts is that they punish or discourage opportunistic behavior by sovereign debtors who may want to take advantage of their unique position as sovereigns to escape their valid contractual debt obligations. According to Jill Fisch and Caroline Gentile, "holdout creditors, by refusing to participate in restructurings of sovereign debt, serve as a check on opportunistic defaults and onerous restructuring terms. Moreover, the prospect of holdout by minority creditors may limit collusive behavior among the majority of the creditors. Holdout creditors, particularly vulture funds, also promote the functioning of the international capital markets. For example, by reducing the likelihood of opportunistic defaults, holdout creditors increase capital flows to sovereign debtors."[70] These authors concede that "holdout disruption is not an unqualified good [and] in some cases, the disruptive effects of holdout litigation outweigh

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[67] Hal Scott, *Sovereign Debt Default: Cry for the United States, Not Argentina*, WASHINGTON LEGAL FOUNDATION, CRITICAL LEGAL ISSUES, WORKING PAPER SERIES NO. 40 (2006), at 41.
[68] *Id*, at 40.
[69] See Buchheit and Daly, *Minimizing Holdout Creditors: Carrots*, *supra* note 34; Stephen J. Choi, Mitu Gulati, & Eric A. Posner, *The Dynamics of Contract Evolution*, 88(1) NYU LAW REVIEW. 1 (2013); and Steven L. Schwarcz, *A Minimalist Approach to State 'Bankruptcy'*, 59 UCLA LAW REVIEW 322-353 (2011).
[70] Jill Fisch and Caroline Gentile, *Vultures or Vanguards?: The Role of Litigation in Sovereign Debt Restructuring*, 53 EMORY LAW JOURNAL 1043 (2004), at 1051.

its positive effects", but argue that "critics of holdout litigation have not made the case for broad reforms that would eliminate holdout litigation".[71] There is merit in taking a stand against opportunistic behavior, but the possibility that holdouts could also help police opportunistic behavior by sovereign debtors is only marginally consequential. Holdouts do not set out as 'police' of the international financial system and then only incidentally disrupt sovereign debt restructuring; quite the opposite, they set out to disrupt sovereign debt restructuring and it may be that in doing so the ability or incentive of sovereign borrowers to engage in opportunistic behavior is incidentally reduced. In any case, reducing opportunistic behavior by sovereign borrowers does not present the sovereign creditors with any better opportunity of getting paid, since a complete or partial payment default is the typical fallout of an unrestructured unsustainable debt[72]; neither does it present the sovereign debtor with any better prospect of achieving debt sustainability because the unsustainability of sovereign debt does not depend on the political will to pay or the integrity to pay according to ability. Hence, policing potential sovereign borrowers' opportunistic behavior is not a good trade-off for combating holdout disruption and enabling distressed countries restructure their unsustainable sovereign debt.

It has also been argued that vulture holdouts play a key role in the fluidity of transactions (which is necessary for the ability of sovereigns to issue debt which in turn depends on the ability of the investors to trade the debt in the secondary market for sovereign debt after the initial purchase from the sovereign – so-called market liquidity) in sovereign bonds because the vultures are able to buy up distressed debts in the secondary market when such debts may otherwise have been illiquid, and the market further depressed. These vulture holdouts, it is argued, are able to trade on these otherwise toxic assets thus making the market liquid and functional and by implication making it possible for countries (even poorer ones) to be able to issue bonds because there would always be a market for their debt, even when distressed. This argument does not appear plausible for several reasons. First, the liquidity of the sovereign debt market depends a lot more on sovereign, market, and other risk factors than on the willingness of vulture or other hedge funds to trade on defaulted or distressed debt.[73] Second, countries with unsustainable debt burdens have been able to issue debts with record oversubscriptions after completing a successful restructuring of their distressed debt and sometimes even after they have had a battle with holdouts.[74] In fact, history and evidence show that if holdouts disrupt the restructuring, the

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[71] *Id*.

[72] The latest example is Ghana's 2022 sovereign debt crisis. See Jonathan Wheatley, *Ghana halts payments on large swaths of foreign debt*, FINANCIAL TIMES, December 19, 2022.

[73] Tamon Asonuma, Marcos Chamon, Aitor Erce, and Akira Sasahara, *Costs of Sovereign Defaults: Restructuring Strategies, Bank Distress and the Capital Inflow-Credit Channel*, IMF WORKING PAPER WP/19/69 (2019); Tamon Asonuma, *Sovereign Defaults, External Debt, and Real Exchange Rate Dynamics*, IMF WORKING PAPER WP/16/37 (2016).

[74] Udaibir S. Das, Michael G. Papaioannou, and Christoph Trebesch, *Sovereign Debt Restructurings 1950–2010: Literature Survey, Data, and Stylized Facts*, IMF WORKING PAPER, WP/12/203 (2012); Tamon Asonuma, *Serial Sovereign Defaults and Debt Restructurings*, IMF WORKING PAPER, WP/16/66 (2016); Tamon Asonuma, Marcos Chamon and Akira Sasahara, *Trade Costs of Sovereign Debt Restructurings: Does a Market-Friendly Approach Improve the Outcome?*, IMF WORKING PAPER, WP/16/222 (2016). Notably, the bonds which Argentina issued in April 2016 – the first since its 2001 default and decade-long battle with the vulture funds and other holdouts and issued the same

sovereign's ability to reenter the market and issue more debt instruments would be delayed and the cost of the issuance more expensive.[75] Third, there is no evidence that the liquidity of sovereign debt and the international debt capital markets is affected when vulture and other hedge funds do not gobble up distressed sovereign debt.

Finally, there is the seemingly neutral argument which does not see holdouts as a concern either because they are just an indication of normal market function or because they do not appear to be significantly disruptive to sovereign debt restructuring. The former reason is put forward by writers such as Jill Fisch and Caroline Gentile who see holdout as what a prudent business concern would do in such circumstance and which should only (if necessary) be managed using contract clauses to which they agree a priori.[76] Wolfgang Eggert, Maximilian Stephan, Janine Temme, and Handirk von Ungern-Sternberg, in their study, concluded that holdout behavior is "not a destructive investor behavior but an investment decision" because holdout behavior increases with expected payments.[77] In the authors' conclusion, "…each restructuring includes an interval in which a holdout is more beneficial than consent [and] this interval can be used as a reason why investors make a rational decision against restructuring without taking strategic aspects into account".[78] This argument misses the issue. The question is not about the quality of an investment decision but its legal and economic effects on the sovereign debtor's ability to enjoy the benefits of the debt it contracted and effectively manage its unsustainable debt, including by means of a restructuring when necessary, as well as its impact on the contractual rights of the sovereign debtor and other creditors. The latter reason, namely the comparative irrelevance of holdout disruption problem, speaks to older history and is disproved by later history. The IMF, for instance, expressed one such view in its 2012 policy paper that "… despite lengthy negotiations and delays in restructuring cases, creditor coordination and holdouts have not generally been a major problem".[79] But, this view was understandably short-lived as Argentina's battles with the holdouts ran its course and the deleterious effects of holdout disruption in practice became all too obvious and too serious to be ignored; and thus the IMF, from its 2013 policy papers discussing holdouts and sovereign debt workouts, has been unequivocal in its acknowledgement of the serious impediment of holdout disruption to successful restructuring of sovereign debt as well as being a major champion of the use of CACs to address this problem. As stated in the IMF's April 26, 2013 policy paper, "… while private creditors as a group may recognize that support for a rapid restructuring is in their own interest, they may hesitate to agree to a restructuring out of concern that other creditors may hold out and press for full payment on the original terms after the agreement has been reached. Thus, collective action

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year after that battle ended – were four times oversubscribed. See Hugh Bronstein and Sarah Marsh, *Argentina returns to global debt markets after 15-years*, REUTERS, April 19, 2016.

[75] Florian Kirsch and Ronald Rühmkorf, *Sovereign Borrowing, Financial Assistance, and Debt Repudiation*, 64 ECON. THEORY 777-804 (2017); Das, Papaioannou, and Trebesch, *supra* note 74; Marc Flandreau and Juan H. Flores, *Bonds and Brands: Foundations of Sovereign Debt Markets, 1820–1830*, 69(3) THE JOURNAL OF ECONOMIC HISTORY (2009).

[76] Fisch and Gentile, *supra* note 70, at 1047.

[77] Wolfgang Eggert, Maximilian Stephan, Janine Temme & Handirk von Ungern-Sternberg*, Holdout Behaviour, A Question of Diversification, Risk Aversion, and Expectation*, APPLIED ECONOMICS LETTERS, 23(9) 623-626 (2016).

[78] *Id*, at 626.

[79] IMF, *A Survey of Experiences with Emerging Market Sovereign Debt Restructurings,* (June 5, 2012) at 1.

problems could either make restructuring unsuccessful due to the holdout strategy or cause delay due to uncertainty about creditor participation."[80] By 2020, the IMF even acknowledged that even enhanced CACs (EA and ICMA Models, discussed at sub-Chapter 2.2.3 below) "are not a panacea [to holdout disruption] [and] holdouts can still disrupt restructurings…".[81]

1.4.3.3 The Impacts of Holdout Disruption in General

While I acknowledge the minority viewpoint (to which I have also variously responded above), I agree, for several reasons which I summarize below, with the majority view that holdout disruption poses a major challenge to the restructuring of sovereign debt deserving of effective combat.

First, holdout disruption frustrates the restructuring exercise, and could result in a failure of the restructuring exercise. A holdout can obtain a court injunction to stop the restructuring process if it rejects the sovereign debtor's offer and hold the restructuring exercise hostage unless the debtor country pays it off. Where the holdout holds a significant amount of the sovereign debt, it could, without even participating in the process, prevent the restructuring exercise from taking off or stop it in its tracks.[82]

Second, where the restructuring deal has been agreed, a holdout can block the implementation of it, again unless the sovereign debtor pays off the holdout, and such pay off of the holdout could ultimately derail the implementation of the restructured debt deal and force the sovereign debtor into a disorderly default. The pari passu doctrine as interpreted and applied by New York and Brussels courts in *Elliot Associates v. Peru*[83] (as requiring that payments on restructured debt could not be made unless holdouts were first or simultaneously paid in equal proportion with the consenting creditors) has become a powerful instrument in the hands of holdouts in this regard, which the holdouts have been able to wield successfully against sovereign debtors and co-creditors participating in debt restructuring process. I discuss the classical case of *NML v. Argentina* in sub-Chapter 1.5 of this thesis and the case of *Elliot Associates v Peru* at Chapter 7.[84]

Third, holdouts discourage good-faith participation in sovereign debt restructuring. If the sovereign is seen to be giving in to holdouts and paying them off in full, other creditors could be disincentivized to agree to a restructuring deal with reductions in nominal value of outstanding principal or interest of the debt (commonly known as haircuts in debt restructuring lexicon), since

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[80] IMF, *Sovereign Debt Restructuring – Recent Developments and Implications for the Fund's Legal and Policy Framework*, April 26, 2013.

[81] IMF, *The International Architecture for Resolving Sovereign Debt Involving Private-Sector Creditors – Recent Developments, Challenges, and Reform Options*, September 23, 2020, at 30.

[82] See Buchheit and Daly, *Minimizing Holdout Creditors: Sticks*, *supra* note 34, at para. 2.09, Giselle Datz, *Placing Contemporary Sovereign Debt: The Fragmented Landscape of Legal Precedent and Legislative Pre-emption, in* SOVEREIGN DEBT DIPLOMACIES: RETHINKING SOVEREIGN DEBT FROM COLONIAL EMPIRES TO HEGEMONY (Pierre Pénet and Juan Flores Zendejas, eds., 2021), at 259-276.

[83] 948 F.Supp. 1203 (S.D.N.Y. 1996).

[84] Affaki, *Revisiting the Pari Passu Clause, in* SOVEREIGN DEBT MANAGEMENT, *supra* note 34, at 39-46.

they could simply hold out and get paid in full. Ultimately, the more creditors refuse participation and demand payment in full, the more unlikely that the restructuring exercise would succeed.[85]

Fourth, holdouts increase the economic burden of impoverished or otherwise struggling economies. Compounded interest, legal, and other fees and costs often combine to balloon the face value of the original debt to gargantuan proportions. Scarce resources are drained away from these economies to pay off bounties to holdouts who successfully sue the sovereign, thereby draining away resources needed for basic human development and maintaining a functional socio-political system. The ability of the sovereign debtor to deploy the debt to productive uses is further compounded by this debilitating holdout effect as other aspects of the sovereign debtor's financial and economic situations are negatively impacted.[86]

Fifth, holdouts usually delay the completion of the restructuring process and thereby cause protracted market exclusion of the sovereign debtor. During the times that the holdout battles it out with the sovereign, the sovereign is normally unable to access international debt capital markets, thus starving it of a critical source of borrowing resources. When the sovereign returns to the markets, its cost of borrowing may, depending on several factors, significantly increase, thus causing more pains to the country and by implication to its populace who ultimately bear the brunt of it all.[87]

Finally, holdouts threaten the stability of the international financial system. A sovereign debt crisis is not capable of being ring-fenced to one country, as we have seen around the world but particularly in Africa, Europe, and Latin America. It is in the interest of the entire international financial community that sovereign debt restructuring succeeds because a crisis could easily spread from one country to another and threaten regions and potentially the entire world. The flurry of activities to contain holdout disruption across multilateral development banks and monetary institutions cross the world, especially since the Argentine and Greek debt crises of 2002-2012, has been in acute recognition of this reality.[88]

1.4.3.4 The Aggravated Disruptive Impact of Vulture Holdouts

As I earlier indicated in sub-Chapter 1.4.1 above, when specialized hedge funds pursue the distressed (defaulted or about to be defaulted) debt of developing countries with the aim to refuse participation in any renegotiation of the debt and to sue for the full value of the debt

[85] Lee Buchheit and Mitu Gulati, *Breaking the sovereign debt impasse*, FINANCIAL TIMES (September 26, 2022), Buchheit and Daly, *Minimizing Holdout Creditors: Sticks, supra* note 34, at 11-13; Fang, Chuck; Schumacher, Julian; Trebesch, Christoph, *Restructuring sovereign bonds: Holdouts, haircuts and the effectiveness of CACs*, KIEL WORKING PAPER, No. 2175 (2021), at 15-21.

[86] Cephas Lumina, *Sovereign Debt and Human Rights: Making the Connection, in* SOVEREIGN DEBT AND HUMAN RIGHTS (Ilias Bantekas & Cephas Lumina, eds., 2019) at 169-185.

[87] Datz, *supra* note 82, *id*.; Odette Lienau, *The Longer Term Consequences of Sovereign Debt Restructuring, in* SOVEREIGN DEBT MANAGEMENT*, supra* note 34, at 92-96.

[88] IMF, *The International Architecture for Resolving Sovereign Debt Involving Private-Sector Creditors—Recent Developments, Challenges, and Reform Options* (2020).

(usually plus accumulated compounded and interest, fees, and costs) they are more commonly referred to as "vulture funds" or "vulture creditors".[89] I use the term "vulture culture" to refer to this business practice of secondary market sovereign debt traders who buy distressed debts (mostly of developing countries) at steep discounts and seek to recover the entire principal and accumulated interest plus costs from the debtor countries, usually through litigation in creditor-friendly jurisdictions, and typically with *a priori* intent to refuse participation in a restructuring of that debt. Vulture funds typically bring their claim against their victims as holdout creditors, and at first look there may seem to be no difference between a generic or regular holdout creditor and a vulture creditor. The distinction that I draw between a generic holdout and the vulture culture is based primarily on the business culture/ethics of the vulture creditors (mostly bordering on the immoral); the kind of debt they target (distressed debt of the poorest and most vulnerable countries); and their investment motives (to profit maximally on the debt with an aforethought intent to refuse participation in any restructuring of the debt).[90]

But for the foregoing particular attributes of the vulture culture, there could be little or no use in drawing any distinction between vultures and regular holdouts, since in nearly all manifestations of the vulture culture the vulture activity is only one of a few or several businesses that the vulture fund undertakes as part of its investment portfolio.[91] In some cases, however, the vulture activity is so explicit that the creditor's only business is pursuit of the distressed debt. In the case

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[89] United Nations Commission on Human Rights' former Independent Expert, Cephas Lumina, defined Vulture Funds as "private commercial entities that acquire, either by purchase, assignment, or some other form of transaction, defaulted or distressed debts, and sometimes actual court judgments, with the aim of achieving a high return". See *Report of the Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, Particularly Economic, Social and Cultural Rights*, A/HRC/14/21, April 29, 2010, at 4. See also Devi Sookun, STOP VULTURE FUNDS LAWSUITS: A HANDBOOK (2010); SOVEREIGN DEBT AND HUMAN RIGHTS (Ilias Bantekas & Cephas Lumina, eds (2019)); Mauro Megliani, *Vultures in courts: why the UNCTAD principles on responsible financing cannot stop litigation*, LEIDEN JOURNAL OF INTERNATIONAL LAW 849 (2015); and Fisch & Gentile, *supra* note 49.

[90] See Christopher Wheeler and Amir Attaran, *Declawing the Vultures: Rehabilitation of a Comity Defense in Sovereign Debt Litigation*, 39 STAN. J. INT'L. L 253, at 262-263; Ilias Bantekas & Cephas Lumina, eds, *id*; and Africa Development Bank Group, *Vulture Funds in the Sovereign Debt Context*, available at https://www.afdb.org/en/topics-and-sectors/initiatives-partnerships/african-legal-support-facility/vulture-funds-in-the-sovereign-debt-context (last visited June 11, 2023).

[91] For some examples of the practical manifestations of the vulture culture see *Donegal International v. Zambia* [2007] EWHC 197 (Comm); [2007] 1 Lloyd's Rep. 397 (pursuing Zambian distressed debt in the United Kingdom); *Lordsvale Finance v. Bank of Zambia* [1996] QB 752 (also pursuing Zambian distressed debt in the United Kingdom); *Camdex International Ltd. v. Bank of Zambia* [1996] 3 All ER 431 (CA); [1997] CLC 714 (CA) (also pursuing Zambian distressed debt in the United Kingdom); *Hamsah Investments Ltd. v. The Republic of Liberia*, Case No. 2008/587 (High Court of Justice, London), judgment of November 26, 2009 (unreported) (pursuing Liberia's distressed debt in the United States and United Kingdom); Democratic Republic of the *Congo v. FG Hemisphere Associates LLC (No. 1)* [2011] HKEC 747; [2011] 14 HKCFAR 95 (pursuing Congolese distressed debt in the United States and Hong Kong); and *Elliot Associates v. Banco de la Nacion*, No 96 Civ. 7916, (2000), U. S. Dist. LEXIS 14169, (SNDY Sept. 29, 2000) (pursuing Peruvian distressed debt in the United States and Belgium). The Belgian government effectively overruled the *Elliot* decision in November 2004 by enacting a law (Law 4765 [C-2004/03482]) (the Belgian Federal Public Service Finance Amendment Law) precluding holdout creditors from obtaining orders blocking payments through Euroclear in the future.

of *Donegal International v. Zambia*[92], for instance, the creditor was incorporated as a special purpose vehicle which only business was the pursuit of the Zambian debt.

If regular generic holdout creditors hinder successful restructuring of sovereign debt, vulture creditors not only constitute the same hinderance but could be much harder to manage for a number of reasons. First, their business motive of pursuing the distressed debt with a preconceived intent to sue on it for the full value plus costs predisposes them to holdout disruption. They are thus unlikely to heed any call for haircut or similar sacrifices normally called for to help a sovereign debtor restructure its debt and get back to sound economic footing. Secondly, their purchase of the debt at steep discounts at the secondary market and the lure of a full recovery on the (unrestructured) contract terms plus costs recovery makes litigation particularly appealing to them, since they stand to lose very little but could gain so much.[93] They are therefore more likely to hold out from restructurings and enjoy a disruptive free ride on the rest of the creditors.[94] Thirdly, vulture funds often owe their corporate provenance to long, obscure, and shady corporate origins leading to tax havens and jurisdictions with little or no regulatory oversight.[95] Some of them are incorporated as special purpose vehicles and often disbanded as soon as the chase of the distressed debt is over or becomes manifestly too risky.[96]

A number of key initiatives have been undertaken in some countries to stem the rise of the threat of the vulture culture.[97] The judgement of the Supreme Court of Belgium, delivered on May 31, 2018, which rejected the request of NML Capital Ltd. seeking to overturn the Belgian anti-vulture funds law (the "Loi Relative à la Lutte Contre les Activités des Fonds Vautours") (Anti-Vulture Funds Activities Law) was a particularly notable judicial rebuke to the vulture culture.[98] Also, notable as key impetus in the nascent efforts by the international community to curb the vulture culture is the resolution of the European Parliament (adopted on April 17, 2018) which, *inter alia*,

[92] [2007] EWHC 197 (Comm); [2007] 1 Lloyd's Rep. 397.

[93] Elliot, for instance, reportedly earned a return on investment of 494 percent on the Peru debt. See Wheeler and Attaran, *Declawing the Vultures: Rehabilitation of a Comity Defense in Sovereign Debt Litigation*, 39 STAN. J. INT'L. L 253, at 262.

[94] Schumacher, Trebesch, and Enderlein, *supra* note 60 (also warning about the increasing market exclusion and other risks posed by the litigious tactics of sophisticated hedge funds who buy distressed sovereign debt only with intent to sue (and not participate in any restructuring) on the debt).

[95] Thomas Laryea, *Donegal v. Zambia and the Persistent Debt Problems of Low Income Countries*, 73 LAW AND CONTEMP. PROBS., 192-200.

[96] This was the case in Donegal International's pursuit of the Zambian debt. See *Donegal International Ltd v Zambia*, [2007] EWHC 197 (Comm); [2007] 1 Lloyd's Rep. 397.

[97] In response to the vulture culture some countries have either passed or introduced legislation to curtail the vulture culture. These include the UK's "Debt Relief Developing Countries Act 2010" (enacted in 2010), the US "Stop Vulture Funds" bill (introduced in 2008 but may have died in Congress), the Belgian "Loi Relative à la Lutte Contre les Activités des Fonds Vautours" (passed on July 1, 2015), and the French "Loi n° 2016-1691 du 9 décembre 2016 relative à la transparence, à la lutte contre la corruption et à la modernisation de la vie économique" (Law on Transparency, Anti-Corruption, and the Modernization of Economic Life) (the "Sapin II" law) which came into force on December 11, 2016 and, among other things, introduced legislation curbing several vulture activities. For a useful comparison of the provisions of the legislative measures in the United Kingdom, Belgium, and France, see a comparative table by Jubilee Debt Campaign at https://jubileedebt.org.uk/blog/france-passes-law-clip-vulture-funds-wings (last visited June 11, 2023).

[98] Judgement no. 61/2018 of May 31, 2018 (Roll no. 6371).

called on "Member States to adopt, on the Commission's initiative, a regulation based on the Belgian law on combating vulture fund debt speculation".[99]

1.5 Illustrative Case – Argentina vs The Vultures and Other Holdouts

Argentina in the 2000s presents the best illustrative example, to date, of holdout disruption in practice as well as the best illustration of the danger to sovereign debt restructuring and the international financial architecture posed by holdout disruption. The holdouts that battled Argentina were both generic holdouts and vultures, thus making this illustrative not only of disruption by vulture funds but also by generic holdouts. I set out here a synopsis of the Argentine saga from default in 2001 to ultimate settlement with the holdouts in 2016 (a 15-year global battle) to illustrate holdout disruption in practice. This thesis sets out much detail of this case here for a number of reasons: first there is a real need to demonstrate the deleterious effect of holdout disruption in practice, and this case is fitting because of its breath, duration, issues it raised, and the laws examined; second this case was litigated on various aspects across two continents (North America and Europe) and several countries (United States, United Kingdom, France and Germany) thus showcasing the potential breadth and depth of holdout disruption across countries; and third because such chronology of the events and the litigations makes for a complete and better understanding of the case which would, in turn, aid the reader in better understanding and appreciating the impact of holdout disruption and the seriousness of the challenge it poses to sovereign debt restructuring.

Following protracted economic crises dating back from the late 1990s, failed IMF interventions, drastic capital controls and a spate of riots and looting throughout the country, Argentina defaulted on debt worth about US$ 80 billion (which, at that time, was the biggest default in history), and subsequently held two rounds of restructurings in 2005 and 2010, making an initial take-it-or-leave-it offer of about 35 percent of the nominal value of the debt to the bondholders.[100] The owners of about 94 percent of the bonds accepted the exchanges, and Argentina vowed never to pay the holdouts.[101]

The holdout litigation that ensued was intense and far-reaching. The bonds unilaterally 'restructured' by Argentina were subject to the laws of various jurisdictions. In the first case brought by the holdout creditors against Argentina in Germany, the court of first instance in Frankfurt, in 2003, decided in favor of the creditors. The court rejected Argentina's defense based

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[99] European Parliament Resolution of April 17, 2018 on Enhancing Developing Countries' Debt Sustainability (2016/2241(INI) (P8_TA-PROV(2018)0104).

[100] *Sovereign Debt: A Lose-Lose Proposition*, FREE EXCHANGE ECONOMICS, THE ECONOMIST (June 22, 2014). See also Andreas Lowenfeld, INTERNATIONAL ECONOMIC LAW, (2008) at 740-742; Thomas C. Baxter, Jr. & David Gross, *Special Immunities: Central Bank and Immunity*, *in* SOVEREIGN DEBT MANAGEMENT, *supra* note 34, at 118-125; Gabriel Gomez-Giglio, *A New Chapter in the Argentine Saga: The Restructuring of the Argentine Sovereign Debt*, 20 JOURNAL OF INTERNATIONAL BANKING LAW AND REGULATION 7, 345 (2005); and Victoria Paz, *Restructuring of Sovereign Debt and Crisis in Argentina: Payment out of Central Bank Reserves*, 26 JOURNAL OF INTERNATIONAL BANKING LAW AND REGULATION 1 (2011) at 40.

[101] FREE EXCHANGE ECONOMICS, THE ECONOMIST, *id*.

on its (Argentina's) emergency law, on the ground, inter alia, that a sovereign debtor cannot unilaterally free itself from its own obligations. Accordingly, the court issued a judgement in favor of the creditors and ordered that Argentina's real property (lands and fixtures on lands) in Germany be attached by court order and used for the satisfaction of the debt.[102] The German Court of Appeal in Frankfurt stayed the judgment of the lower court on the ground that the effect of a declaration of emergency by a foreign sovereign on private actions raised a question of international law to be decided by the Constitutional Court.[103]

In February 2006, however, and before the German Constitutional Court could rule on the matter, the Court of Appeal decided that Argentina could no longer invoke the state of emergency necessity, since President Kirchner had declared, in March 2005, that the restructuring of its debt had resolved Argentina's insolvency. The court compared Argentina's debt situation with the indebtedness of other countries in Europe, which were either in the same precarious debt situation as Argentina, or even worse off, and alluded to the consistent growth of the Argentine economy since 2002 including the fact that it managed to pay off the IMF.[104]

In its decision on the matter, the German Constitutional Court (in a majority judgement) upheld the rights of the holdout creditors seeking judgments against Argentina.[105] It rejected Argentina's defense of state of emergency, being of the view that while the defense of necessity is recognized in international law, the literature makes a distinction, in the applicability of that defense, between relations between states, on the one hand, and relations between a state and private persons, on the other hand – the defense being applicable in the case of the former but not the latter. The court concluded that unless it could be shown that there is a rule of customary international law by which the necessity defense could be transferred from relationships under international law to relationships under private law, Argentina could not avail itself of that

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[102] Judgment of 21st Civil Chamber, *Landgericht*, Frankfurt, of 14 March 2003; 2-21-O 294/02 (on liability), 2-21-O 509/02 (on attachment).

[103] Decision 8U 52/03 of the German Court of Appeal, Frankfurt, on July 7, 2003.

[104] Decision 8U 107/03 of February 16, 2006. Several critics also lampooned Argentina's arguments that the unilateral haircuts and take-it-or-leave-it debt restructuring were meant to pull the country out of a crippling economic turmoil. They mostly argued that at the time that Argentina unilaterally imposed the haircuts on its creditors, all available indices pointed to the fact that Argentina was recovering from its economic malaise and that its economy was already on the rebound per critical economic metrics in the country. Critics therefore described Argentina's debt default as unavoidable, but the unilateral haircuts it imposed on its creditors as inexcusable. They readily pointed to the fact that Argentina was able to pay off the IMF between the 2001 default declaration and 2006 and argued that the country's actions respecting its creditors were nothing but a forceful expropriation of property. See, for instance, Arturo Porzecanski, *From Rogue Creditors to Rogue Debtors: Implications of Argentina's Default*, 6 CHI J. INT'L. L., 311 (2005), at 317-325; and Scott, *supra* note 67, at 2-7. However, it appeared that the international financial community, for the most part, viewed the restructuring as part of Argentina's legitimate efforts to deal with its economic crises and therefore opted not to interfere with the process. The high degree of "acceptance" of the proposal among the creditors (76 per cent by 2005 and 94 percent by 2010) appeared to justify this view. See Mauro Megliani, SOVEREIGN DEBT: GENESIS-RESTRUCTURING-LITIGATION, (2015), at 36-38 (discussing the difficulties posed by holdouts in implementing Argentina's restructured debt and how the country attempted to manage the implementation in the face of the crises).

[105] For the decision of the German Federal Constitutional Court, see BVerfG, Order of the Second Senate of 08 May 2007 - 2 BvM 1/03 - paras. (1-99) (English version).

defense. While the court noted the provisions of Article 25 of the International Law Commission's Articles on State Responsibility, it was of the view that the defense of necessity provided therein applies only "in a relationship to which international law applies"; and, as the court saw the matter, it was a country-private actor relationship to which international law did not apply.[106]

For the cases brought against Argentina in the New York courts, there was little doubt as to what the outcomes would be. The courts of New York, already reputed as creditor-friendly especially when it comes to enforcement of creditor rights against sovereign debtors,[107] roundly rejected the arguments which Argentina presented in justification of its restructuring efforts and against the cases brought against it.

Thus, in *Lightwater Corporation Ltd. v. Republic of Argentina*,[108] (the first of the series of cases), the New York District Court not only refused to agree with Argentina on all the defenses it proffered before both the German courts and New York courts, it also rejected Argentina's additional argument before it – that there is a principle of international law which could bar plaintiffs from bringing a court action for enforcement of their bonded debt at a time when the issuer is having severe economic crisis.[109]

Next, in the case of *EM Ltd. v. Republic of Argentina*[110], EM Ltd., a holder of defaulted Argentine debt, filed an action against Argentina in the United States District Court for the Southern District of New York to recover more than US$ 700 million in interest and principal owed on an Argentine bond it had acquired. EM moved for summary judgment, and the Court granted the motion on September 12, 2003, awarding final judgment to EM Ltd. in the amount of US$ 724.8 million. The

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[106] In its conclusion, the German Constitutional Court stated that "The question as to recognition, under customary law, particularly of economic or financial state necessity, and as to its preconditions concerning the degree of peril of vital state interests, can remain unresolved here. Because, in any event, an economically or financially defined state of necessity can also not be pled by a state vis-à-vis private individuals so long as there is no rule under international customary law which recognises the transferability of the defence of necessity from relationships under international law to relationships under private law", thus suggesting that it could reach a different conclusion if a case is made out that the sovereign debtor-creditor relationship is also subject to some (public) international law. Judge Lübbe-Wolff dissented from the majority opinion in this case. The Judge was of the view that, contrary to the majority view, the defense of necessity should avail the debtor country in private as well as public law disputes. In the words of the jurist, "The ruling of the Senate, by contrast, means that the plea of state necessity under international law, since it is not to be applicable in private-law disputes before national courts, can play a role neither in judgment nor in enforcement proceedings. Accordingly, private creditors – including those who knowingly purchased government bonds with unfavourable risk assessments and correspondingly favourable interest prospects as a speculative investment … can from now on, even in the face of catastrophic domestic breakdowns in the debtor state, not only have their demands recognised in Germany, but can also enforce those demands by way of execution against assets of the debtor state which are intended for sovereign purposes if the corresponding waiver of immunity is present in the loan terms").

[107] See earlier precedents such as *Republic of Argentina v. Weltover*, 504 U. S. 607 (1992); *Allied Bank International v. Banco Credito Agricola de Cartago*, 757 F.2d 516 (2d Cir. 1985); and *CIBC Bank and Trust Company v. Banco Central do Brasil*, 770 F. 2d 1385 (5th Cir. 1985).

[108] 02 Civ. 3804 (TPG), 02 Civ. 3808 (TPG), 02 Civ. 5932 (TPG) (S.D.N.Y. Apr 14, 2003).

[109] *Id,* at 3-4.

[110] 03 Civ. 2507 (TPG), 2003 WL 22120745 (S.D.N.Y. Sept. 12, 2003) (amended by *EM Ltd v. Republic of Argentina*, 03 Civ. 2507(TPG), 2003 WL 22454934 (S.D.N.Y. Oct. 27, 2003)).

decision of the District Court was affirmed by the Court of Appeal for the Second Circuit.[111]

EM Ltd. brought an action in a New York court against Argentina to enforce the judgment, and another holdout creditor, NML Ltd. (which at that time had also brought an action against Argentina in a New York court but was yet to obtain a judgment), also joined the action seeking pre-judgment attachment of Argentine assets in the United States.[112] The plaintiffs asked the courts for an order stopping the exchange of the bonds, which were being exchanged pursuant to the restructuring arrangement between Argentina and the consenting creditors, as those bonds were being tendered to the Bank of New York as exchange agent. The court first granted the order of attachment, but a day before the scheduled exchange, it vacated the order on the ground that part of the contractual rights of the sovereign was the right to cancel the bonds as they were tendered. The Circuit Court affirmed this decision, without resolving the issue whether the tendered bonds were property belonging to Argentina (in which case the creditors could lawfully have them attached in satisfaction of their debt) or not.[113] In further proceedings on the case, EM Ltd., on December 30, 2005, moved, in the District Court, for an ex parte order (i.e., a court order made for a limited duration, to avert an imminent injury to a legal right, after the hearing of only one party to the case) in aid of enforcement and sought further orders of the court that monies which the Argentine Central Bank (Banco Central de la Nacion) was about to pay to the IMF, using its Central Bank's funds at the Federal Reserve Bank of New York, be seized and applied for the payment of its debt. The plaintiffs were initially granted temporary orders seizing the monies which the Argentine Central Bank was about to pay to the IMF[114], but on January 12, 2006 the orders were vacated by a different Judge on the grounds, chiefly, that: (i) those monies belonging to the Argentine Central Bank belonged to a different entity, under the separate identity doctrine;[115] (ii) making payment to the IMF was not a commercial activity, and therefore could not come under the commercial activities exception under the Federal Sovereign Immunities Act; and (iii) the funds held at the New York Federal Reserve were immune, being the assets of a foreign central bank. The Circuit Court upheld this decision,[116] but the United States Supreme Court, on October 1, 2007, granted certiorari (i.e., an order of the United States Supreme Court agreeing to hear arguments in a case brought to it on appeal) and ordered a

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[111] See *EM Ltd. v. Republic of Argentina*, 382 F.3d 291, 292-94 (2d Cir. 2004).

[112] See *NML Capital Limited & Another v. The Republic of* Argentina, 2005 WL 743086 (SDNY 2005).

[113] The Circuit Court affirmed on the ground that it would not disturb an exercise of jurisdiction by the District Court where, as it saw it, the discretion was properly exercised. See *EM Ltd v. Republic of Argentina*, 131 Fed. Appx. 745 (2d Cir. May 13, 2005).

[114] *EM Ltd. v. Banco Central de la República Argentina* (see Fed. R. Civ. P. 69(a)). NML Ltd. contemporaneously sought and obtained ex parte orders of prejudgment attachment and temporary restraining orders concerning the same assets (see Fed. R. Civ. P. 64).

[115] That is, that property belonging to the Central Bank was not property belonging to the Republic, and thus could not be used to satisfy judgment against the Republic. See *NML v. Republic of Argentina*, 02 Civ. 3804, 2005; WL 743086 (S.D.N.Y. Mar. 31, 2005). See also *EM Ltd. v. Rep. of Argentina*, 05-1525-cv (L); and *NML Capital v. Rep. of* Argentina, 05-1543-cv (L).

[116] See *EM Ltd. v. Republic of Argentina* 473 F. 3d 463 (2d Cir. 2007).

review of the decision.[117]

Following the review ordered by the Supreme Court, the District Court, on April 7, 2010, granted the attachment orders sought by the plaintiffs on the ground that the Central Bank was an agent of Argentina. According to the presiding Judge, "the record shows that the Central Bank has been a servant of the Republic in enabling the Republic to pay off billions of dollars of debt, for political or diplomatic reasons, the public has desired to pay, leaving the plaintiff bondholders to their difficult judicial struggle".[118]

In two other cases, however, both the District Court of New York and the 2nd Circuit refused attachment of assets belonging to other organs of the Argentine State on the ground (as the District Court earlier reached in *NML v. Argentina*) that assets belonging to such distinct state entities were not assets belonging to the Republic of Argentina, and could therefore not be used to satisfy judgments against the Republic.[119]

Still laboring under unsustainable debt after its 2005 restructuring, Argentina launched yet another round of debt restructuring by way of an exchange of its existing bonds for new bonds under newly agreed terms, offering a 75 percent haircut to investors for about US$ 18 billion of debt, in May 2010. However, the 2010 episode like previous episodes did not quite take off nor was implemented as contemplated as continuing and consistent holdout disruption ensured that Argentina could not pay the participators in any of the restructuring episodes without making simultaneous payments to the holdouts on their debts outside of the restructuring exercise, ultimately resulting in Argentina's inability to implement the 2005 restructuring exercise and leaving it with unsustainable debt and lack of market access until it finally settled with the holdouts (see below) in 2016.

By the time that Argentina had its second round of debt restructuring in 2005, NML Ltd. already obtained judgment against Argentina in New York District Courts in a string of 11 cases.[120] NML Ltd. then brought a court action to enforce the judgments at New York courts.[121] On February 23, 2012, in *NML Capital v Argentina*,[122] the U.S. District Court held that Argentina violated the pari passu clause in its old unrestructured bonds and enjoined Argentina from making payments to

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[117] 128 S. Ct. 109 (2007). In the meantime, Argentina already, on January 3, 2006, repaid its debt to the IMF using the Banco Central de la República Argentina's assets. The Central Bank's funds at the Federal Reserve Bank of New York were not used in connection with that payment, although it was not clear whether the funds might have been used for this purpose in the absence of the court-ordered restraints on the transfer of the funds.

[118] See *EM Ltd v. The Republic of Argentina*, 03 Civ. 2507 (S.D.N.Y., April 7, 2010).

[119] See *Aurelius Capital Partners, LP v. Republic of Argentina* (2d Cir. 10/15/2009), and *Capital Ventures Int'l v. Republic of Argentina*, 280 F. Appx. 14, 15 (2d Cir. 2008).

[120] For details of the history and background of NML's litigation against Argentina, see *EM Ltd. v. Republic of Argentina*, 473 F. 3d 463, 466 (2d Cir. 2007). By 2014, the total accumulated judgement debt owed to NML by Argentina had reached a staggering US$ 2.5 billion. See also Harvard Law Review, Statutory Interpretation: *Republic of Argentina v. NML Capital Ltd.*, 128 HARV. L. REV. 381 (2014).

[121] NML Ltd.'s and EM Ltd.'s enforcement actions were both assigned to the same judge (Judge Griesa) and then consolidated.

[122] *NML Capital, Ltd. v. Argentina*, No. 08 Civ 6978 (TPG) (S.D.N.Y. Feb. 23, 2012).

creditors on its 2005 and 2010 restructurings without making payments to the holdouts concurrent with or in advance of any payments to holders of the 2005 and 2010 restructured bonds. The injunctive orders were affirmed on appeal by the Circuit Court with a remand to the District Court with instructions for a clarification of the scope of the injunctive orders.[123] In a subsequent amended order, the District Court clarified that the orders applied not only to Argentina but also to Argentina's "agents" and "other persons who are in active concert or participation with Argentina".[124] Again, the Circuit Court, on August 23, 2013, affirmed the clarified orders of the District Court, but granted a stay of enforcement of the District Court's injunctions pending the outcome of Argentina's petition to the United States Supreme Court for certiorari against the District Court's orders which Argentina sought on ground of sovereign immunity.[125]

On June 16, 2014, the United States Supreme Court delivered the *coup de grace*. It refused, despite multiple amici briefs filed in support of Argentina's position by several countries, international financial institutions and other organizations, commercial banks and some investors, to hear Argentina's appeal over the New York District and Circuit Courts' orders mandating that Argentina must make payments to the holdouts concurrent with or in advance of any payments to holders of the 2005 and 2010 restructured bonds. It also held that while the United States Federal Sovereign Immunities Act indeed grants sovereign states' assets in the United States immunity from attachment and execution, that immunity does not extend to discovery suits (i.e., petitions to compel disclosure of who holds assets and where they are held) on those assets.[126] Thus, the United States Supreme Court not only declined to reverse the injunctive orders of the lower courts, it further opened up a leeway for the holdouts to obtain any information they may need on the whereabouts of Argentina's (and in the future, any other sovereign's) assets in the United States, who holds them, and who may be dealing with them.

Argentina was thus left with no options than surrender to the holdouts or default on its restructured bonds, as it consistently argued that it cannot afford to pay the holdouts as well as holders of the restructured bonds without seriously harming its struggling economy.[127] On Wednesday, July 30, 2014, after more than five hours of intense negotiation, the court-appointed mediator said that the country would, "imminently be in default" on about US$ 20 billion worth

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[123] *NML Capital Ltd. v. Republic of Argentina*, 699 F.3d 246 (2d Cir. 2012).

[124] *NML Capital Ltd. v. Republic of Argentina*, No. 08 Civ. 6978 (TPG), 2012 WL 5895784 (S.D.N.Y. Nov. 21, 2012).

[125] *NML Capital, Ltd. v. Argentina*, No. 12-105 (2d Cir. 2013).

[126] See *Republic of Argentina v. NML Capital Limited*, 573 U.S. (2014).

[127] See the following insightful commentaries on the effect of Argentina's dilemma. Lawrence Hurley and Sarah Marsh, *Supreme Court Rejects Argentina appeal in bond fight*, REUTERS (Monday June 16, 2014); Nicole Hong and Brent Kendall, *Supreme Court Sides with Holdout Creditors in Argentina Debt Case*, THE WALL STREET JOURNAL (June 16, 2015); and Andrew Harrer, *U.S. top court rejects Argentina appeal in bond fight*, CNBC (June 16, 2015). See also Gabriel Gomez-Giglio, *A New Chapter in the Argentine Saga: The Restructuring of the Argentine Sovereign Debt*, 20 JOURNAL OF INTERNATIONAL BANKING LAW AND REGULATION 7, (2005) at 43-45; Megliani, *supra* note 104, at 373-377; Baxter, Jr. & Gross, *Special Immunities: Central Bank and Immunity*, *in* SOVEREIGN DEBT MANAGEMENT, *supra* note 34, at 121-125; and Diego Devos, *Special Immunities: Bank for International Settlements, in* SOVEREIGN DEBT MANAGEMENT, *supra* note 34, at 130-137.

of debt obligations, after it failed to make a US$ 539 million interest payment on its bonds.[128] Standard & Poors declared Argentina in default that same day.[129] Argentina remained in default and frustrated (along with holders of its restructured bonds) until the country was ultimately forced into a negotiated settlement with the holdouts in February 2016.[130]

Holdout disruption of the Argentine debt restructuring was not limited to courts. Holdouts also resorted to international arbitration, and for the first time in history, the international investment arbitration mechanism of the International Center for the Settlement of Investment Disputes (ICSID) was successfully invoked by holders of sovereign bonds against a sovereign debtor. First, certain Italian investors took Argentina to the ICSID, claiming compensation resulting from the haircut, on the ground that the Argentine restructuring was tantamount to expropriation and violated fair and equitable treatment standards under the Italy-Argentina bilateral investment treaty (BIT).[131] In two of the cases filed at ICSID and upon a preliminary objection by Argentina on grounds, among others, of jurisdiction, the ICSID Tribunal found that the sovereign debt restructuring fell within the scope of the BIT and that the ICSID Tribunal had jurisdiction to determine the cases.[132] One of the cases[133] was apparently discontinued for lack of payment of the required advances, pursuant to ICSID Administrative and Financial Regulation 14(3)(d), on August 18, 2015.[134] The Italian investors eventually reached a settlement with Argentina on the claims in December 2016.

The Argentine debacle is quintessential in the study of holdout disruption leading to failure of sovereign debt restructuring. It shows how well-resourced and determined holdouts are able to weaponize politics, the law, and the markets to their fullest advantage. The holdouts utilized all available market, legal, and political apparatus available to them from the United States to Europe to disrupt Argentina's attempt to restructure its unsustainable debt and ultimately forced the country into a settlement largely on their own terms and for an amount nearly twice the size (in principal) of the original debt. There is little to suggest that the creditors that accepted Argentina's tender and submitted their debt to haircuts of up to 75 percent would feel anything but a sense of regret. Thus, the deleterious effects of holdout disruption are demonstrably felt

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[128] Mike Patton, *Argentina Defaults on its Debt…Again*, FORBES (August 1, 2014).

[129] Camila Russo and Katia Porzecanski, *Argentina Declared in Default by S&P as Talks Fail* BLOOMBERG BUSINESS (July 31, 2014).

[130] Daniel Bases, Richard Lough and Sarah Marsh, *Argentina, Lead Creditors Settle Debt Battle for $4.65 billion*, REUTERS (March 1, 2016).

[131] *Giovanna a Beccara and others v. Argentine Republic*, ICSID Case No. ARB/07/5. See also *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.

[132] *Ablacat and Others (case formerly known as Giovanna A Beccara and Others) and The Argentine Republic* (ICSID Case No. ARB/07/5) (2011) (decision on jurisdiction and admissibility); and *Ambiente Ufficio S.P.A. and Others (case formerly known as Giordano Alpi and Others) and the Argentine Republic* (ICSID Case Bo. ARB/08/9) (2013) (decision on jurisdiction and admissibility).

[133] *Giovanni Alemanni and others v. Argentine Republic* (ICSID Case No. ARB/07/8).

[134] https://icsid.worldbank.org/apps/ICSIDWEB/cases/pages/casedetail.aspx?CaseNo=ARB/07/8 (last visited June 11, 2023).

not only by the country whose debt is being restructured but on the larger international financial architecture.

There is little to suggest that any future target country would get any better treatment from holdout creditors or that the systemic shocks to the international financial architecture could get any milder. Quite the contrary, more recent studies suggest that holdout disruption represents an ever-increasing threat to successful restructuring of sovereign debt and stability of the international financial system.[135] With the debt stock of emerging economies increasing with every increase in their growth dynamics and several developed economies under severe debt and deficit strains, holdouts would only have gotten smarter, bolder, and better-resourced when tomorrow comes.

1.6 Recent Anti-Holdout Statutory Measures in New York and United Kingdom

In apparent recognition that sovereign debt restructuring is still under significant peril from holdout disruption, even with the ICMA model collective action clauses (discussed at sub-Chapter 2.2), the legislatures of the State of New York and the United Kingdom recently initiated measures aimed at imposing certain statutory restrictions on enforcement of sovereign debts outside officially-supported (i.e., under the auspices of the IMF, World Bank, G20, etc.) restructuring frameworks and at curtailing further holdout disruption.

In the United States, the measure takes the form of a recently (February 2023) introduced bill in the State Assembly for a law that would seriously curtail holdout disruption in New York courts with respect to the debts of countries under debt sustainability, restructuring, or other like debt relief programs implemented under the auspices of the United States and relevant multilateral institutions such as the IMF and the World Bank, by subjecting sovereign debt creditor claim on debts of such countries to three strict enforcement eligibility tests:

(i) it must comport with burden-sharing standards (in other words the debt must have been subjected to the debt restructuring process and emerged as a claim having jointly borne the restructuring burden with other creditors – i.e., no holdout claims);
(ii) it must meet robust disclosure standards, including intercreditor data sharing; and
(iii) recovery is limited only up to the proportion that would have been recoverable by the United States, pursuant to the relevant debt sustainability, relief, or restructuring program, if the federal government were the creditor in question.[136]

In other words, the bill seeks to bar applicable holdout claims entirely from enforcement in New York courts, and subject recovery on qualifying claims only to such portion of the debt as would

[135] Schumacher, Trebesch, and Enderlein, *supra* note 46; Giselle Datz & Katharine Corcoran, *Deviant Debt: Reputation, Litigation, and Outlier Effects in Argentina's Debt Restructuring Saga,* NEW POLITICAL ECONOMY (2019), DOI: 10.1080/13563467.2019.1598959; and Jeannette Abel, THE RESOLUTION OF SOVEREIGN DEBT CRISES: INSTRUMENTS, INEFFICIENCIES AND OPTIONS FOR THE WAY FORWARD (2019).
[136] See Bill No. NY A02970 of the 2023-2024 Regular Session of the State of New York, of February 1, 2023 (introduced by House Member Kelles Fahy).

have been recoverable should the United States itself had been one of the creditors and subjected its debt to the restructuring process. Of course, it is to be seen if the bill is enacted into law. The Financial Times reported that the bill has been praised by some as a good step toward curtailing holdout disruption but criticized by others, particularly market makers and their advisors, as potentially hurtful to the very debtor countries it purports to help (by potentially raising their borrowing costs) and also as an overkill because, in the opinion of those practitioners, CACs already do a good job of enhancing creditor coordination.[137]

In the United Kingdom, the initiative takes the form of a (2023) parliamentary committee report calling for a UK legislation to:

"(a) prevent low-income countries facing debt distress from being sued by private creditors for a sum greater than that those creditors would have received had they participated in the Common Framework [i.e., the G20 Common Framework for debt restructuring[138]]; or

(b) make debt restructuring agreements binding for all private creditors, if the agreement is supported by at least two-thirds of private creditors."[139]

While the UK initiative does not appear to pose as radical a threat to holdout disruption as the New York bill (and is not yet concretized in the form of a draft law), it is also potentially a very potent threat to holdout disruption because it would insulate the debts of countries undergoing a debt restructuring program under the Common Framework from private creditor enforcement action or force private creditors (holding debt governed by English law, one must presume) to accept a restructuring proposal supported by a two third majority, thus effectively improving on the efforts of the ICMA Model CACs and Specimen MVPs (respectively discussed at sub-Chapters 2.2.3.1 and 2.2.6) and taking creditor coercion to a level that the market would not.

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The negative effects of holdout disruption have not gone unnoticed across the academic, political, market, and judicial world. In fact, even before the end of the Argentine struggle with NML and other creditors, thanks to the February 2016 settlement, major stakeholders across the international financial community have joined efforts aimed at curtailing the menace. Given the realities of the international political economy, stakeholders appeared convinced that the best means of curtailing holdout disruption was by the use of contractual clauses. Efforts on the use of contractual clauses to combat holdout disruption have centered on collective action clauses

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[137] Jonathan Wheatley, *Investors brace for new law on sovereign debt workouts*, FINANCIAL TIMES, June 5, 2023.

[138] Launched possibly as an immediate response to the debt crisis that followed COVID-19, the Common Framework was set up by the G20 as the (yet) only multilateral systematic framework for debt forgiveness and debt restructuring. It has continued to exist after the end of the COVID-19 pandemic and calls have been made to strengthen the framework. If legislative efforts in the United Kingdom and New York which have both referenced the framework are enacted, there is a possibility that the Common Framework could become a major supranational instrumentality for sovereign debt restructuring.

[139] UK Parliament, Debt relief in low-income countries (Seventh Report of Session 2022–23), 10 March, 2023.

(CACs) because these clauses are designed to help facilitate collective decision making among creditors and would thus potentially bind holdouts to conform to the collective will of the whole. As a policy response, the European Union introduced a set of modified CACs for use in euro area bonds; as a market response, the International Capital Markets Association (ICMA) also introduced a set of modified CACs for use in sovereign bond transactions; and academic opinions as well as international financial institutions have, in varying degrees, hailed these enhanced contractual clauses as preferred answers to holdout disruption.[140] On the other hand, contractual clauses are known to have limitations, which many, while acknowledging their usefulness, fear could render them ineffective tools against holdout disruption. Hence, calls for the so-called statutory approach to sovereign debt restructuring have continued to gain traction among academic and policy commentators alike.

I devote Chapter 2 of this thesis to a discussion of both the statutory and contractual approaches, their promises and limitations, with particular focus on CACs (as currently preferred tools for combating holdout disruption) and particularly the key innovations of the EU and ICMA, and why these contractual clauses may not be enough to address the problem of holdout disruption.

[140] Detailed analyses of these enhanced CACs and academic commentaries on them are done in sub-Chapter 2.2 of this thesis.