Placing Contemporary Sovereign Debt:

The Fragmented Landscape of Legal Precedent and Legislative Preemption

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Abstract: Since 2003, the battle between holdout creditors and the Argentine government in US courts has inspired a number of judicious studies on its legal underpinnings and repercussions. It has also prompted so-called "anti-vulture funds" laws in countries like the UK, Belgium and France. Despite these developments, the role of place in debt restructurings has remained relatively neglected. The paper analyzes domestic laws protecting foreign debtors from minority holdout litigation and injunctive orders in federal courts that incite contractual changes as part of a fragmented landscape of local, and at times overlapping, spheres of sovereign debt governance, paradoxically embedded in a deeply integrated global financial system. A key finding of this analysis is that while contracts ground debt dynamics in specific jurisdictions (financial centers), they do not reduce uncertainty in the outcomes of sovereign debt restructurings. Moreover, financial centers have functioned not only as sites for private market-making, but also for public experimentation in international debt processes.

Sovereign debt as a contract has often been overlooked by social scientists when theorizing the outcomes of default (Weidemaier and Gulati 2015). Although it is reasonable to sum up debt dilemmas – as economists have usually done – into the crucial questions of why lend and why repay in the absence of a global bankruptcy court, differences in the common "template" of a bond contract crucially inform the legal rules of the debt game (Choi et al. 2013). Interpretations followed by international courts of even boilerplate contractual clauses, which by definition appear in most contracts, can diverge, leading to unexpected outcomes when litigation is pursued by creditors in foreign courts. Since the 1990s, and given more restricted applications of sovereign immunity laws, "foreign governments that default on their debts can be hauled into national courts just like private debtors" (Weidemeier and Gelpern 2013: 190, Weidemeier 2014, Mustafa and Molle 2016).

Indeed, since the turn of the century, the audacity and tenacity of minority holdout creditors has been raising concerns among governments in key financial centers, such as London and Brussels, that these so-called "vulture funds" are not only disruptive of sovereign debt restructurings, but also impair debt relief programs, particularly the World Bank's Highly Indebted Poor Country Initiative. In the past eight years, legislators in Belgium, London and Paris approved laws attempting to preempt holdout litigation. These initiatives were boosted by a New York district court ruling in favor of Argentina's creditors in the country's long battle with NML Capital (a hedge fund who chose not to participate in either the 2005 or 2010 debt restructurings of the bonds defaulted on in 2001). Argentina's appeal was rejected by the Second Circuit Court of Appeals and the US Supreme Court refused a review of the case.

Given that sovereign debt is notoriously difficult to enforce because sovereigns can keep their assets far from the reach of creditors, the turning point in the case came when the New York District Court judge issued an injunctive order declaring that financial intermediaries who assisted Argentina in its attempt to repay the exchanged bonds bondholders without also repaying NML would be in contempt of court. Forced to pay NML in full if it expected to have its payments to creditors of exchanged bonds processed, Argentina defaulted again in 2014. Beyond the dynamics particular to the parties involved, the "court's injunctions cast a shockingly wide net"(Samples 2014: 80-81). The district court judge's "judicial gamble" turned the tables of the sovereign debt game to the creditors' advantage (Weidemeier and Gelpern 2014, Guzman 2016).

Although the Argentine court saga has inspired a number of judicious studies on its legal underpinning and repercussions, the role of place in debt restructurings has remained relatively neglected. Even despite local legislative developments preempting "vulture funds" from hijacking restructuring processes, the dots have yet to be connected, mapping out the salience of local authority with extraterritorial ambitions in sovereign debt processes. Judicial outcomes in holdout litigation and "anti-vulture funds" laws, it is argued here, instantiate sovereign bond finance, broadly regarded as global, footloose, and volatile.

Since the Brady Plan of the 1980s, when debts defaulted on earlier in that decade were securitized, bonds replaced bank loans as the primary instrument for emerging markets to access foreign and domestic credit. This widespread process of debt securitization was part of a new phase of globalization, marked particularly by financial deregulation and capital market integration. On the one hand, emerging markets would be able to access credit more broadly, securing debt deals under different laws (domestic and foreign), in different currencies and with various maturity structures. On the other hand, domestic policy autonomy would be inevitably constrained by the whims of often overly-reactive global investors (Strange 1995, Andrews 1994, Maxfield 1998). In particular, it was argued that developing countries' governments who chose to implement policies that contradicted financial markets' expectations could be "disciplined" or "punished" by the threat of capital outflows[1] (Mosley 2003, Brooks et al. 2015, Kaplan and Thomsson 2014). This "electronic herd" of global investors was not only diverse but mimetic, tracking common indexes, benchmarks and reproducing the actions of market leaders in a context of information asymmetry (Friedman 1999, Santiso 2003). Moreover, financial players operated much more swiftly than ever before, at times exaggerating "market adjustments" (despite or beyond economic fundamentals), sometimes leading to "sudden stops" in capital flows because of financial contagion from currency crises (Calvo 1998, Kim and Wei 1999, Calvo and Mendonza 2000, Kaminksky and Schmukler 2003). Place was hence easily blurred in

[1] In Mosley's (2003:17) analysis of the impact of global capital on national government's policy room of maneuver, she justifies her focus on sovereign bond markets stating that it "provides a *most likely* location for the operation of financial pressures… The interest rates charged to governments for accessing the bond market (…) strongly influences the interest rates paid by other actors in the national economy. Therefore, the impact of bond market activity on national governments is quite direct (emphasis in the original).

depictions of late 20th and early 21st century global finance. These were accounts of deliberate or inadvertent convergence in market movements and policy reforms, all subject to overwhelming and inescapable financial volatility.

The empirical analysis of contemporary debt litigation and legislative efforts to preempt holdout disruptions to debt restructurings in foreign courts reveals the importance of place not only when it comes to distinct sites for arbitration of and deliberations on major financial transactions. Place is also indicative of specific sites of legislative diffusion in the fragmented landscape of local debt governance. These legislative initiatives with extraterritorial ambitious are pieces of the ad hoc nature of contemporary debt restructurings which reveal two paradoxical conclusions. First, while the specificity of contractual choice of law grounds (instantiates) debt dynamics in specific jurisdictions (financial centers), they can render these dynamics more uncertain (despite the diffusion of collective action clauses) given litigation risks. Second, when debt procedures are institutionalized *de facto* or *de jure* in certain jurisdictions, the need for global coordination is arguably greater due to the potential for jurisprudential overlap and disruptions to the payments pipeline, used as sites for the enforcement of legal orders on recalcitrant debtors. The analysis also makes clear that the outcome of individual debt-related international litigation sets important spillover effects that spur action towards redefining contracts and restructuring frameworks to preempt the kind of protracted litigation that Argentina experienced in US courts. Even if holdout creditor litigation in foreign courts is not the norm (i.e., average outcome) in sovereign debt restructurings, beyond a legal precedent in a traditional sense, spillover effects from international litigation informally institutionalize deviant outcomes in the way debt processes are reconsidered internationally. The methodological implication is that protracted international litigation and the legislative steps taken in some financial centers to prevent "vulture fund's" legal action against sovereign debtors in distress are revealing of instances in which outliers become 'trend setters', sparking new strategic arrangements that try to prevent a similar occurrence in the future.

I. Bringing Place Back In

Since the Brady Plan of the 1980s, when debts defaulted on earlier in that decade were securitized, bonds replaced bank loans as the primary instrument for emerging markets to access foreign and domestic credit. Government bond finance was made possible given the "numerous holders of sovereign debt covering a very wide geographic distribution and varying in size and sophistication from retail to institutional investors" (Marx et al. 2006: 57). Yet the transition from commercial banks to bond markets was mired in concerns that an ever expanding group of diverse bondholders from all over the world would encounter collective action problems in debt negotiations that would render those both more difficult and more protracted than in previous decades. In analyses of the consequences of financial globalization to domestic policymaking, scholars remarked the ways in which bond finance (in contrast to bank credit) left developing countries' governments with less room to move. Deviating from the preferences of global investors for monetary stability and fiscal discipline could ignite capital outflows, increase the cost of credit, or both (Strange 1995, Andrews 1994, Andrews and Willett 1997, Mosley 2003, Brooks et al. 2015, Kaplan and Thomsson 2014).

To be sure, as Flandreau et al. (2009:1) remark, this "emergence of global finance [associated with the 1990s financial globalization] was really a re-emergence". By 1900, "the use of modern communications to transmit prices; the development of a very broad array of private debt and equity instruments, and the widening scope for insurance activities; the expanding role of government bond markets internationally; and the more widespread use of forward and futures contracts, and derivative securities" spread to and linked major economic financial centers from Europe to the Americas, Asia, and Africa. Nonetheless, the evolution of international capital markets has not been linear. Rather, not only has broader financial integration been interrupted by domestic political imperatives that led to protectionism and capital controls, but, beyond macroeconomic policy switches, the "microeconomics of financial globalization" has endured marked changes (Flandreau 2017, Obstfeld and Taylor 2003).

When it comes to foreign debt, as Flandreau (2017: 160) argues, "the way the business of originating and distributing foreign debt is organized" has gone through a "profound transformation" in the 20th century. Before the interwar era, underwriters functioned as "gatekeepers of liquidity and certification agencies". While the less prestigious underwriters originated bonds most likely to default, more reputable intermediaries dealt with less risky bonds. In contrast, thanks to the rise of rating agencies who provide assessments of sovereign risk, today "defaults are randomly distributed across underwriters", who have "become aggressive competitors in a new Speculative Grade market" that did not exist in the past

(Flandreau et al. 2009: 7). Then, the underwriting business was highly concentrated. It provided a number of services for which large fees were collected. Quality standards were high and most bonds originated were akin to today's investment grade securities. Nowadays, the business has become less concentrated among a few firms that, given economies of scale, charge less for their services (independently of bond spreads). Quality standards have decreased and there is very limited cooperation between the borrower and the underwriter (Flandreau et al. 2009: 11).

These historical discontinuities among financial intermediaries in the sovereign bond market are also suggestive of the blurriness of place. Although "gatekeeping" tasks are concentrated among a few rating agencies headquartered in New York City, a more diversified market where tenuous relationships between issuers and underwriters are the norm, suggests that location is often either overlooked or taken for granted when it comes to the "microeconomics of foreign currency debt issuance" (Flandreau et al. 2009: 1).

For sovereign debtors, place is pertinent particularly when it comes to debt issuance and decisions about currency denomination, choice of law and stock market listings (de Fontenay et al. 2016) . When it comes to the currency denomination of sovereign bonds place matters in a "sinful" way. In their 2005 study, *The Pain of Original Sin*, Eichengreen, Hausmann and Panizza (2005) found that bond markets are dominated by five currencies: the US dollar, the euro, the yen, the pound sterling, and the Swiss franc. Of all the bonds issued by countries that do not issue one of these currencies, 85% were denominated in one of these five currencies. For the authors, the countries borrowing in foreign currency suffered from the "original sin" since exchange rate depreciations make it more difficult for them to service their debts. In an updated study covering data from 1999 to 2008, Hausmann and Panizza (2011) report an increase in emerging market debt issued in the currency of the issuer, yet that still amounted to only 4.1% of the total bonds outstanding in 2008. Although original sin declined in the first decade of the millennium, it did so "only marginally and in a few countries". Rather than "redemption", some developing countries opted for "abstinence" - i.e., lower net debt. The important implication is that financial globalization has yet to ease credit concerns for developing countries, given that market access is subject to all-to-common exchange rate risks. For a majority of debtors, foreign currency issuance remains the name of the credit game.

In addition, sovereigns that issue bonds governed by foreign law almost always submit to courts in the designated jurisdiction. Weidemeier and Gulati (2017) see this decision as one that encompasses a tradeoff between credibility and flexibility. Issuing bonds in foreign currency and subject to foreign law means that emerging market nations can generally take advantage of lower interest rates than those charged for domestic-law, domestic-currency bonds, instead of contending with shocks that lead to currency depreciation and increase the costs of servicing their foreign debts (Buchheit 2013, Olivares-Caminal 2013, Eichengreen et al. 2003). However, foreign law bonds are likely more difficult to restructure than domestic law ones and, for this reason, are "widely thought to be safer investments than bonds governed by the sovereign's domestic law". The debtor hence trades debt management flexibility for a more credible commitment to repayment and/or stricter contract enforcement. Indeed, creditors seem to believe that "foreign courts will more rigorously enforce sovereign debt obligations" (Weidemeier and Gulati 2017: 9-10). Overall, "when deciding where to file a lawsuit, plaintiffs consider, among other things, which state's laws are more favorable to their claim" (Whytock 2009: 100). This explains why a substantial portion of emerging market sovereign bonds are governed by New York or English law (Weidemeier and Gulati 2017, Das et al. 2012). Far from a technicality, "choice of law rules have significant economic consequences" not only for debtors, but also creditors and the financial centers whose laws rule these contracts more often than not (Whytock 2009: 101- 102).

During the 1980s, in order to allow New York to compete more effectively with London, attempts were made to liberalize the American Uniform Commercial Code requirement for major financing transactions (Potts 2016). In effect, this validated stipulations of New York law without any requirement of a reasonable connection between the transaction and New York. According to the New York Bar (2013), "these provisions embody a legislative policy to support New York's pre-eminent position in global finance by providing legal certainty to contractual provision selecting New York laws. The New York position is a close approximate of that of English law, which may be selected by the parties even if the transaction has no real connection with the UK at all". In effect, this meant that Euromarket contracts, which in the late 1960s had boosted London's financial status further, could select New York law, thus "expand[ing] the financial space over which New York laws and courts would govern" (Potts 2016: 533).

Therefore, it is when sovereign debt is seen in its most basic form - i.e., as contract - that place becomes crucial. While international law (including treaties) "may determine such questions as whether a new government will inherit the debts of a prior government, how to allocate responsibility for debt when a country dissolves into separate states, and whether national courts must enforce judgments entered by courts of another nation", for the most part "customary international law is mandatory", binding even those nations that do not follow it. Crucially, in the US, it is *municipal* law that regulates the relationship between sovereign states and the individuals and entities subject to their jurisdiction, including rules that "define the parties' primary obligations, such as rules of contract interpretation; jurisdictional rules that determine when domestic courts may hear sovereign debt disputes; procedural and evidentiary rules that govern the details of litigation in those courts; and rules for enforcing court judgments" (Weidemaier and Gulati 2017).

For their part, debtors, eager for lower borrowing costs, often voluntarily waive sovereign immunity in debt contracts. That is to say, countries "cede aspects of their sovereignty to provide assurances of repayment". This fact challenges some assumptions in the scholarship on sovereign debt both in economics and political science. First, as Weidemeier and Gulati (2017:5) explain, "the assumption that contracts are irrelevant to the sovereign debt markets is premised on the belief that creditors cannot easily obtain and enforce judgments against sovereigns". Yet, sovereigns, themselves, can commit to "promises in the bond contract that expand creditor enforcement rights. These include waivers of immunity from suit, waivers of immunity from execution, as well as a suite of contract terms, such as terms facilitating service of process, to pave the way to the courthouse". Second, and in the same vein, the scholarship on global capital as a constraining (to varying degrees) force relative to government's policy autonomy overlooks the ways in which sovereigns not only expose themselves to exchange rate risk by issuing debt in foreign currency, but even more directly, voluntarily accept (on paper) to subject themselves to the authority of foreign courts as commercial actors no longer shielded by sovereign immunity. Therefore, sovereigns approach international bond markets more exposed than it is often assumed. Beyond the disciplining influence of private capital flows, self-constraining contracts - a taken-for-granted part of the political economy of debt - are routine in bond finance.

Contemporary dynamics involving litigation against sovereigns are informed by the 1976 passage of the Foreign Sovereign Immunities Act (FSIA) in the United States, and the State Immunity Act of 1978 (SIA) in the United Kingdom. These are the key legislative references in the transition from "absolute" to "restrictive" immunity. Under these laws, no longer were sovereigns "presumptively immune from suit even when engag[ing] in commercial activity abroad". Rather, "under the modern, restrictive theory of immunity, sovereigns are presumptively not immune from suit for commercial acts". In fact, while before 1976 virtually no bond contained a waiver of immunity from suit, since then all foreign issued sovereign bonds waived immunity from suit[2] (Weidemeier and Gulati 2017: 7, Weidemeier 2014).

Immunity waivers notwithstanding, without the means to enforce a judge's order (seizing sovereign assets or disrupting trade), a victory in litigation and profitable vindication for a holdout creditor are not one and the same. Waivers of immunity from suit did not change this reality (Weidemeier 2014). Yet, although courts "were reluctant to enforce privately-negotiated immunity waivers until relatively late in the twentieth century", the tables have turned more recently (Weidemaier and Gulati 2016: 34). The NML v Argentina case is the epicenter of this challenging shift. To this case and the legislative efforts sparked by holdout litigation we turn next.

II. Litigation , Legislation, Location: Correlations and Extrapolations

In the absence of a uniform set of procedures coordinated by a global equivalent to a bankruptcy court, sovereign debt restructurings have been ad hoc developments (Rieffel 2003) Speaking in 2013, Lee Buchheit (2013: 110), one of the most seasoned lawyers in the field, put it clearly: "For 30 years sovereign debt restructurings have gotten done. We have done them (…) more or less satisfactorily. There has been remarkably little litigation in sovereign debt workouts in 30 years, considering the size of the affected debt stocks". Moreover, as Marx et al. (2006: 69) point out, "given the larger investor base and the diversity of debt instruments, a surprising fact is the length of time taken to resolve sovereign debt workouts [in the 1990s and the first decade of the 21st century] has been shorter than in the 1980s".

Yet, in the midst of these seemingly regular patterns, outliers, such as Argentina, having experienced a much longer and more contentious international legal battle than most other debtors, are more than a statistical anomaly. Even beyond a legal precedent (in a traditional

[2] A similar pattern is identified in accounts of international arbitration. Waibel (2011) explains that, "by the early twentieth century, a small handful of sovereign loan contracts allowed creditors to bring claims before arbitral tribunals. For over a century, international tribunals have also (if rarely) heard disputes arising from sovereign debt obligations".

sense), spillover effects from international litigation informally institutionalize the deviant outcome in the way debt processes are reconsidered internationally. That is why it is all the more pertinent to track domestic decision making with broader repercussions.

"Anti-vulture funds" laws in the UK, Belgium and France compose the so-far incipient-but-evolving landscape of judicial and legislative responses to debt disputes, which "normalize" outlier maneuvers through legal preemption. Domestic laws protecting foreign debtors from minority holdout litigation and injunctive orders in federal courts that incite contractual changes have extraterritorial repercussions by design or diffusion. They present some opportunities and foreclose others for sovereign creditors and debtors *in particular jurisdictions*. Hence they ultimately reveal a fragmented topography of *local,* and at times overlapping, spheres of sovereign debt governance, paradoxically embedded in a deeply integrated global financial system.

Background: Holdout Litigation in the 1990s

In 1992, *Republic of Argentina* v. *Weltover* opened the door for holdout creditors to bring their cases to US courts. However, the case did not yield a clear-cut legal pathway of favorable judgments for the creditors[3]. An early suit brought against Panama by an Elliott Associates (the litigant against Argentina in the 2000s) pre-cursor company in 1995 was dismissed on the hedge fund's unwillingness to disclose its investors, a step necessary for holdout creditors when starting litigation. By 1997, the Southern District of New York Court barred claims brought by Elliott against Peru on nonperforming debt, arguing that the hedge fund was in conflict with the champerty rule - i.e., an agreement forbidding the purchase of debt with the intent to bring about a lawsuit. Yet, the Second Circuit Court of Appeals reversed the District Court's opinion (Blackman and Mukhi 2010).

Elliott filed another lawsuit against Peru in US courts in 2000. This time the hedge fund's plan centered on a "novel interpretation" of the *pari passu* ("on equal footing") clause, standard in bond contracts since the mid-nineteenth century and "containing the borrower's promise to ensure that the obligation will always rank equally in right of payment with all of the borrower's other subordinated debts" (Blackman and Mukhi 2010: 55, Gelpern 2016, Chodos 2016).

[3] *Republic of Argentina v. Weltover Inc.* 504 US 607 (1992).

Although most legal treatments understand the clause to mean "ranking debt owed to different creditors ratably" (Gelpern 2016), Elliott argued that *pari passu* in this case meant that Peru could not pay creditors of restructured debt without paying the hedge fund proportionally[4]. Elliott won a judgment of US$56 million, enforceable through Peru's assets in the US used for commercial activity (IMF 2001). Given that Peru had virtually no such assets in New York, Elliott targeted the third parties involved with bond payments - i.e., the sovereign's fiscal agents and clearinghouses (Weidemaier, et al., 2013, IMF 2001: 12). With insufficient time to appeal the orders obtained by Elliott, Peru decided to settle and avoid defaulting on its Brady bond payments coming due (Blackman and Mukhi 2010).

Elliott's success reverberated through sovereign debt litigation circles. Not only had a holdout creditor received a favorable judgment, but it was also able to obtain a restraining order to prohibit the payment of interest to other bondholders until payments were made to that holdout creditor. A chain reaction of hedge fund litigation followed, and other enforcement actions were brought to court exploring the same strategy. Yet, most did not succeed. By 2003, the *pari passu* clause was no longer receiving favorable judgments in courtrooms around the world (Blackman and Mukhi 2010, Bratton 2004). Even so, with the Argentine default in 2001 (the largest in history at the time), concerns that creditor coordination problems would plague debt restructuring procedures grew significantly.

These concerns led to efforts by the IMF to establish a Sovereign Debt Restructuring Mechanism (SDRM) in 2003, heavily inspired by Chapter 11 of the US Bankruptcy Code (Miller 2002, Buchheit 2013). Despite the Fund's advocacy, initially backed by the Bush administration, the SDRM never came to pass, thanks to significant opposition from private creditors, the US government (who later favored a less "bureaucratic" approach), and some debtor governments (who worried that the mechanism would mean higher borrowing costs or lower private capital inflows into their economies) [Helleiner 2008]. Instead, collective action clauses (CACs) have become a constant in bond contracts since 2003. This also had a lot to do with investors' frustration with holdout litigation and Argentina's long court battle (Gelpern and Gulati 2013).

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[4] Gelpern (2016) finds "three court rulings [outside the US] from the 1930s and an arbitral decision from 1980, all of which address the meaning of *pari passu* at some length, and lend qualified support to the interpretation" of ratable ranking, which underpinned the decisions about Peru and the more widely debated case of Argentina discussed here.

Nonetheless, CACs alone do not eliminate the holdout problem. After all, 'creditors can and do target small [bond] series trading at a deep discount, where they can buy a blocking position with relative ease, holdout and threaten to sue" the sovereign debtor (Committee on International and Economic Policy Reform 2013: 18, IMF 2013). This became clear in the 2012 Greek debt restructuring. Even through, in order to try and avoid the Argentine experience, the Greek Parliament managed to retrofit a collective action mechanism on local law bonds (93% of all debt eligible for restructuring), more than half of all foreign-law bonds (3.1% of the total debt) in the restructuring deal failed to get the needed votes to have their terms amended (Zettlemeyer et al. 2013). To avoid litigation at a time when the country faced a serious political crisis, Greece paid holdout creditors US$ 552 million on May 15, 2012 (*Reuters*, May 15, 2012). The experience made evident that CACs are a welcome change to bond contracts, yet the clauses do not entirely prevent litigation brought about by holdout creditors (Petrick et al. 2012, Gelpern 2013, Buchheit et al. 2013, Bohoslavsky and Goldmann 2016).

Therefore, fears that foreign debt litigation can proliferate and obstruct orderly restructurings remain. A study of creditor lawsuits filed in the US and UK against sovereign debtors between 1976 and 2010 reveals a significant rise in creditor litigation numbers since the 1970s, with more lawsuits filed by holdout creditors (Schumacher et al. 2013). The trend is even more significant since the year 2000, "despite the fact that the number of sovereign defaults has declined". Unsurprisingly, 90 percent of these litigation cases were led by hedge funds. Overall, however, litigation cases remain low and the number of litigation successes - i.e., settlements or successful attachments of sovereign assets – is smaller still (Schumacker et al. 2012: 28). This is not to say that holdout litigation is not disruptive. As Blackman and Mukhi (2010: 51) explain: "the progression of modern sovereign debt litigation is linked to the successes and failures of the legal strategies employed by (…) professional plaintiffs in obtaining judgements against [debtor] states and trying to collect on them".

The UK's Debt Relief Act of 2010

In response to a successful "vulture fund"-triggered lawsuit to recover claims on Zambian and Liberian debt at a significant discount in British courts, the UK Parliament enacted the Debt

Relief (Developing Countries) Act on April 8, 2010[5] (Wozny 2017, Muse-Fisher 2014). At first blocked by a Conservative representative, the "bill was pushed through as part of the pre-election wash-up, gaining House of Lords support and making its way to royal assent" (*The Guardian*, April 8, 2010). It focuses on public and publicly guaranteed foreign debt of countries participating in the World Bank's Highly Indebted Poor Country Initiative[6] introduced in 1996. Under this legislation, commercial creditors suing HIPC debtors in foreign courts cannot recover more than the amount recoverable if the debt were reduced in accordance with the HIPC initiative. This diminishes the incentives for holdouts to pursue litigation against these particular sovereigns in UK courts. Also, given that "the DRA applies to foreign judgements or arbitration awards on qualifying debt, vulture funds cannot easily shop for more favorable laws and ask UK courts to enforce the judgement" (Wozny 2017:729-30).

The law's limitations are clear, however. It only applies to HIPC countries and does so retroactively. Muse-Fisher (2014: 1696-97) explains that "the U.K. Government feared that in the absence of similar legislation in other major financial jurisdictions (notably New York), a forward-looking application of the law, covering future indebtedness, would chill the degree to which sovereign lenders and creditors would choose English law to govern future debts." In 2013, this initiative sparked the same legislation in three British Crown Dependencies: the Isle of Man, Guernsey and Jersey (Wozny 2017, Bohoslavsky and Raffer 2017) . In 2015 and 2016, Belgium and France (respectively) also passed laws attempting to limit holdout creditors' disruptive strategies in foreign courts.

The Belgian Anti-Vulture Fund Law[7]

Belgian legislation against vulture funds was first prompted by Kensington International (an international investment fund) trying to execute a foreign award against the Democratic Republic of Congo in Belgian Courts. The award amounting to US$121.4 million in 2005 was much higher than the price Kensington had paid for Congolese bonds in secondary markets,

[5] Available at: http://www.legislation.gov.uk/ukpga/2010/22. The law became permanent on May 16, 2011
[6] As of January 2018, 36 countries are part of the initiative. http://www.worldbank.org/en/topic/debt/brief/hipc
[7] Literal translation of the original: *Loi relative à la lutte contre les activités de fonds vauteurs*.

US$1.8 million[8] (Iversen 2015: 29). Getting to enforcement was the next step for Kensington's lawyers who tried to seize DRC funds worldwide, including 10.3 million euros of Belgian government funds that were part of an aid package targeting the construction of a thermal power station in the DRC. Reacting to this development, the Belgian Senate unanimously approved a resolution against these aggressive creditors. As in the UK, the legislators' key concern was with the "possibility that holdout creditors could circumvent multilateral efforts geared towards the reduction or cancellation of debts of very poor countries" (Iversen 2015: 30). However, because this resolution did not exempt public money that was not intended for development aid from attachment and because it targeted all creditors, "including (non-vulture) funds that pursued legitimate goals", another effort was put in place to broaden the scope of this initiative (Sourbron and Vereeck 2017: 6).

This happened in July, 2015, when the Belgian House of Representatives unanimously passed its "anti-vulture funds" law (*Le Figaro*, July 1, 2015; Richelle 2016; Sourbron and Vereeck 2017). The bill's draft of April 2015 cites several cases of vulture fund-driven litigation in foreign courts as its motivation: *Elliott Associates v. Peru* in Belgium (1996-1999), *Kensington International v. the DRC* in Belgium (cited above), *FG Hemisphere v. the DRC* in a Jersey Court in 2004, *Donegal International v. Zambia* in British courts (2007), and, of course, *NML v. Argentina* in New York courts (with critical judicial decisions stated in 2008 and 2012)[9]. The law established that "if a Belgian court finds a fund acting as a 'vulture', the latter cannot claim more than the discounted price it paid. Anything above the purchasing price is deemed illegitimate" (Sourbron and Vereeck 2017: 7). Judges would have to show an "illegitimate advantage" was being sought by the vulture funds. This "illegitimate advantage" is determined if any one of the following applies: the sovereign debtor is in a state of insolvency, payment of the claim would impact the debtor's finances negatively, the creditor's headquarters are located in a tax heaven, "the creditor systematically uses legal procedures to recover its loans" and/or refuses to cooperate with the debtor (Wozny 2017: 738). In addition, and crucially, illegitimacy was determined by the "manifest disproportion between the purchase price and the face value of the debt purchased" (Sourbron and Vereeck 2017: 7).

[8] Kensington International v Republic of Congo (2005). Available at: http://image.guardian.co.uk/sysfiles/Guardian/documents/2005/12/15/KensingtonJudgmentAppro.pdf

[9] Belgian Chamber of Representatives (2015), *Projet de loi relative à la lutte contre les activités des fonds vautours*, DOC 54 1057/005, Available at: http://www.dekamer.be/FLWB/PDF/54/1057/54K1057005.pdf

Its political appeal notwithstanding, the law met with opposition by local financial representatives and the Institute of International Finance (Kaluma 2015). At first, "none of the arguments was strong enough to substantially alter, let alone repeal the law" (Sourbron and Vereeck 2017: 8). Expediency, characteristic of holdout litigants' maneuvers, was also evident in the ways legislators moved to better substantiate their preemptive attempts in the face of new challenges from "vulture funds". These creditors tried to undermine the law "by lobbying for another bill aimed at weakening sovereign immunity and strengthening the ability to seize diplomatic goods" *within* the limit of the debt's purchase price. If these sovereign assets pursued did not exceed the purchase price, vulture funds could state that there was no "illegitimate advantage" in their claims[10]. Once more, Belgian legislators acted quickly. On July 24, "a meticulously amended version of the bill" foreclosing this route was passed and published in the Belgian Gazette on September 3, 2015 (Sourbron and Vereeck 2017: 9).

Yet, "vulture funds" persisted. NML Capital Ltd and Yukos Universal Limited tried to fight the Diplomatic Immunities Law in the Belgian Constitutional Court. This time the funds' tenacity paid off to some extent. In its judgement on April 27, 2017 the Court confirmed the validity of the August 2015 Act "whereby the immunity from execution of foreign States and international organizations was strengthened in Belgian legislation" (Theeuwes and Dopagne 2017). Yet it "relaxe[d] the rules of attachment as intended by the Belgian legislator", deciding "that in accordance with the Treaty of Vienna of April 18, 1961, a specific waiver remains required for the attachment of goods for diplomatic purposes, but that in line with international law, a *general* waiver suffices for the attachment of non-diplomatic, non-commercial goods" (Sourbron and Vereeck 2017: 9, emphasis added).

Indicative of the international diffusion of this kind of legislation, Theeuwes and Dopagne (2017) remark that "by and large, this ruling of the Belgian Constitutional Court echoes the 8 December 2016 decision of the French Constitutional Council, which confirmed the validity of the recent French law adopted partially on the blueprint of the Belgian Act of 23 August 2015". This French legislative initiative is described next.

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[10] Belgian law, in accordance with the 2004 UN Convention on Jurisdictional Immunities of States and their Property, does not allow attachment of foreign state property used for non-commercial public purposes unless an explicit waiver of immunity is part of the contract. Yet "the Belgian law also requires that the waiver is granted in a specific way. It is the latter clause that came under attack" (Sourbron and Vereeck 2017: 9). The content of the UN Convention can be found here: http://legal.un.org/ilc/texts/instruments/english/conventions/4_1_2004.pdf (assessed on February 13, 2018).

France's Sapin II

On November 8, 2016, the Law on Transparency, Anti-corruption Measures and the Modernization of the Economy, presented by Michel Sapin, Minister for the Economy and Finance, to the Council of Ministers, was approved by the French National Assembly. After undergoing the scrutiny of the French constitutional court, French Law n° 2016-169, known as Sapin II, was finally enacted. The law was proposed by the *Agence Française Anticorruption* and reflects a broad agenda to strengthen French anti-corruption regulations[11] (*The National Law Review* 2017). Among its proposed reforms, this law "affects the enforcement of foreign decisions and arbitral awards rendered against States" and "seeks to clarify the protection of the property of foreign States situated in France". Ultimately, the "law retains a general exemption from immunity in respect to situations where the State has 'expressly consented' to provisional or enforcement measures being taken". Yet enforcement of diplomatic and consular property still does require a specific waiver by the State (Dupoirier et al. 2016).

Key to our discussion here, article 60 of Sapin II "provides special rules in order to avoid the seizure of the property of foreign States in France by investment funds holding debt securities that have been purchased at discounted value or in other circumstances of distress against economically vulnerable States". However, the provision's reach is limited. It only applies to debt securities: (a) acquired *after* the entry into force of the law (December 11, 2016), and (b) against sovereign debtors in default or undergoing a restructuring, which "were recipients of the official development assistance of the OECD when the security was issued" (Dupoirier et al. 2016).

To be sure, none of these legislative initiatives discussed here does away with the threat of disruptive "vulture funds" litigation against sovereign debtors. The laws attempt to restrict holdout creditors' ability to pocket more money than they paid for the debts in contention, especially protecting Highly Indebted Poor Countries and adding more hoops for funds to jump when attempting to seize sovereign property despite immunity waivers. Holdout creditors suing sovereigns in foreign courts, however, can continue to explore loopholes in existing legislation and have a lot of forum shopping left to pursue. Indeed, given that most sovereign bonds are

[11] The text of the law can be found at: http://www.assemblee-nationale.fr/14/pdf/ta/ta0830.pdf

issued under New York or English law (IMF 2013) and no legislative action has been pursued in the US yet, ample room remains for holdout creditors to attempt to conquer the perennial challenges of sovereign debt enforcement in New York courts, especially since the outcome of Argentina's battle with NML Capital has turned the tables in favor of creditors.

The Injunctive Remedy in Argentina's Battle in US Courts

Rejecting both the 2005 and 2010 exchange offers presented to creditors for bonds defaulted in 2001, NML Capital (a hedge fund subsidiary of Elliott) pursued payment in US courts. In the September 2011 hearing for the Southern District of New York (SDNY), the lawyers for Argentina argued that the Foreign Sovereign Immunities Act protected its bond payment actions. In December 2011, New York District Court Judge Griesa ruled in favor of NML. For him, Argentina violated the *pari passu* clause ("equal treatment") when it continued paying bondholders of restructured bonds while refusing to pay holdout creditors[12]. Judge Griesa hence read the *pari passu* clause as forbidding Argentina from paying its other creditors unless it also paid NML "proportionally", and saw Argentina's regular payments to its bondholders but not to holdout creditors as a subordination of non-restructured bonds[13] (Gelpern 2013, Cotterill 2013).

Expecting Argentina to defy his orders, judge Griesa issued an injunction in 2012 prohibiting the country from paying its restructured debt unless it paid NML in full[14] (Gelpern 2013). Crucially, the injunctive order threatened to sanction financial third parties working with Argentina to allow for the repayment of exchange bondholders without payment to NML as well. In fact, the amended injunction of 2012 cited each of these financial intermediaries, making clear the extraterritorial ambition of the order. Given our focus on place, it is worth quoting in full

[12] The *pari passu* clause, a common addition to sovereign debt contracts, was stipulated in Argentina's original 1994 debt contract as a promise to treat all payment obligations as equal 'in ranking with other unsecured external' debt commitments of the country (Gelpern 2013: 3).
[13] The Argentine Congress passed a lawt, he Padlock Law (or, locally, *ley cerrojo*) in February 2005 prohibiting the Executive from reopening the exchange without the holdout creditors (*Clarín* 2012). This law supported judge Griesa's reading of subordination which undermined the key premise in the *pari passu* clause (Samples 2014).
[14] Injunctions are perceived as a remedy that should be granted when a plaintiff has no other option and only if the remedy is consistent with the equitable exercise of a court's power (Weidemaier and Gelpern 2014).

paragraph 2(f) of the injunction, extending it to entities outside of the US who could be held in contempt of the court order:

> "…(1) the indenture trustees and/or registrars under the Exchange Bonds (including but not limited to The Bank of New York Mellon f/k/a/ The Bank of New York); (2) the registered owners of the Exchange Bonds and nominees of the depositaries for the Exchange Bonds (including but not limited to Cede & Co. and The Bank of New York Depositary (Nominees) Limited) and any institutions which act as nominees; (3) the clearing corporations and systems, depositaries, operators of clearing systems, and settlement agents for the Exchange Bonds (including but not limited to the Depository Trust Company, Clearstream Banking S.A., Euroclear Bank S.A./N.V. and the Euroclear System); (4) trustee paying agents and transfer agents for the Exchange Bonds (including but not limited to The Bank of New York (Luxembourg) S.A. and The Bank of New York Mellon (including but not limited to the Bank of New York Mellon (London)); and (5) attorneys and other agents engaged by any of the foregoing or the Republic in connection with their obligations under the Exchange Bonds.[15]"

According to Weidemaier and Gelpern (2014: 190) the District Court's ruling was remarkable, as the resulting injunction "produced the most potent remedy against a foreign government in recent memory".

Although the Supreme Court of the United States refused to respond to Argentina's challenge of the district court's interpretation of *pari passsu*, it did respond to the country's second question, involving "post-judgment discovery" of debtors' assets by the litigating creditors. After obtaining debt-collection actions against Argentina in the Southern District of New York, NML Capital sought to search for Argentina's executable (not immune) property, and subpoenaed two nonparty banks for the records of the country's global transactions. In support of Argentina, the US government filed a brief with the Supreme Court stating that affirming the District Court's ruling could harm international relations by provoking "reciprocal adverse treatment of the US in foreign courts" (quoted in UNCTAD 2014). Despite the US government's plea, the Supreme Court held that the Foreign Sovereign Immunities Act *does not* immunize sovereign debtors

[15] FED. R. CIV. P. 65(d)(2)(c), available at: http://www.shearman.com/files/upload/Arg5- Order-112112.pdf.

against post-judgment discovery of their assets outside of the United States.[16] After all, as stated by Justice Scalia, writing for the majority, Argentina had waived its sovereign immunity from the jurisdiction of courts in the United States in the contracts it signed when it sold the bonds. Indeed, having agreed to pay its debt in New York, in US currency and having "expansively waived immunity", Argentina "voluntarily ceded many of the sovereign prerogatives it might reasonably expect in a wholly-domestic matter" (Weidemeier and Gelpern 2013: 18-19).

Outlier Effects

For some legal scholars, the case brought up against Argentina by NML set a key precedent in the history of sovereign debt restructuring. Samples qualifies this legal battle as "a true factual outlier", explaining that even though "the Second Circuit partially recognized Argentina as a 'uniquely recalcitrant' debtor, [the] NML [case] represents the most exceptional sovereign debt situation in modern history". In the same vein, Gelpern stated that the case ultimately yielded "the best collection device since gunboat diplomacy and certainly the most generalizable" (quoted in *Institutional Investor*, 22 June, 2015).

Understanding the Argentine case as a critical juncture in debt disputes, the US government submitted a statement to the District Court, stating that Judge Griesa's judgment had the practical and potentially dangerous effect of allowing "a single creditor to thwart the implementation of an internationally supported restructuring plan". The US and other governments worried that creditors would now have an incentive to litigate for a better deal rather than accept the terms of a debt restructuring as set up by the defaulting debtor. As a result, the risk of holdouts would increase (Alfaro 2014, IMF 2013). Indeed, this was part of an international campaign that included a 2014 United Nations General Assembly resolution calling for the establishment of a "multilateral legal framework for sovereign debt restructuring processes" (United Nations General Assembly 2014).

The US Court of Appeals, however, insisted that it was "highly unlikely that in the future sovereigns w[ould] find themselves in Argentina's predicament" given the fact that collective action clauses (allowing for a majority – usually 75% - of creditors to decide the outcome of a

[16] Republic of Argentina v. NML Capital, Ltd. 573 U.S. ___ (2014)

restructuring) “have been included in 99% of the aggregate value of New York-law bonds issued since January 2005, including Argentina’s 2005 and 2010 Exchange Bonds”[17]. Yet, this view has been strongly disputed by legal scholars and policymakers who assert that CACs alone do not eliminate the holdout problem. After all, “creditors can and do target small [bond] series trading at a deep discount, where they can buy a blocking position with relative ease, holdout and threaten to sue” the sovereign debtor (Committee on International and Economic Policy Reform 2013, p. 18, IMF 2013).

Not only has the Argentine case set a legal precedent but it has put in motion preemptive reactions by other sovereigns in the form of contractual changes beyond CACs. One example is that of Belize, who “explicitly stated in the February 2013 debt exchange offer as well as the legislation authorizing the terms of exchanged bonds that the *pari passu* clause in the restructured bonds does not require Belize to pay all items of its public debt on a ratable basis to prevent the holdout strategy employed against Argentina and to mitigate litigation risks”. Indeed, this is now a trend. IMF (2015, p. 8) analysis of new sovereign bond contracts reveals that all post-October 2014 debt issuances that have included enhanced CACs also included modified *pari passu* clauses. Even those issuances that did not include enhanced CACs, did incorporate the modified *pari passu* clause.

These contractual changes reflect guidelines set up by the London-based International Capital Market Association as a result of the 2013 deliberations by a “US-government orchestrated an informal group of creditors, bankers, lawyers, and government officials” that composed the “Sovereign Debt Roundtable” meetings. Key elements in the published guidelines were the promotion of revamped CACs and the clarification of the wording of the *pari passu* clause aimed at “neutraliz[ing its] legal importance” (Wigglesworth and Moore 2016).

Attempts at contractual preemption against holdout litigation notwithstanding, threats remain likely. That is because the modifications refer to new debt contracts, but add no relief to the large outstanding stock of debt that does not feature such contractual provisions. In 2014, the IMF estimated that this amounts to US$ 900 billion, of which approximately 46% are governed by English law and 50% by New York law. Only 6% of the outstanding stock includes enhanced CACs, 4% of which are governed by New York law. Moreover, of this outstanding debt stock,

[17] http://business-finance-restructuring.weil.com/wp-content/uploads/2012/12/NML-Capital-v-Rep-of-Argentina_12-105L-Oct-26-2012-CA2.pdf

71% will mature within the next ten years. The bonds governed by New York law face a higher risk of holdout disputes given the New York court decisions regarding Argentina. 39% of those will take ten years of more to mature (IMF 2015, p. 10).

III. Connecting the Dots: Local Laws, Global Reach, Overlap

The local legislative and judicial decisions described above ambitioned extraterritorial impact. That is not surprising. As Whytock (2009: 98) explains, a decision by a domestic court involving a transnational actor can transcend the case, sending "a signal to transnational actors that the court will make a similar decision under similar circumstances in the future". Therefore, "the substantive function of domestic courts in global governance has not only direct effects on the litigants, but also indirect shadow effect on the strategic behavior of transnational actors more generally" (*ibid*: 99-100). Holdout litigation in British, Belgian and American courts prompted legislative preemptive efforts seeking to reach beyond national borders. Sourbron and Vereeck's (2017: 7) recall that "during their formal discussion, the Belgian members of parliament pointed out that although an international solution is preferable, a national law may set an example and expedite international action". In fact, "the Belgian legislators urged the Belgian government to convince its European counterparts to adopt their model-law". How far this will go is still history in the making.

What is clear is that in this new landscape of local debt governance, legislative and judicial determination may overlap, challenging one another. Such is the case of judge Griesa's injunctive order in the NML v. Argentina case. The order raised concerns about conflict of laws. As mentioned above, Euroclear was named among the "third parties" involved in Argentina's payments pipeline, "despite the Belgian law, which on its face appears to immunize [Euroclear] from court orders" like judge Griesa's injunction (Wiedemeier and Gelpern 2013: 33). In the text of the Belgian Law Against Vulture Funds it was explicitly stated that: "Regardless of the law applicable to the legal relationship between the creditor and the debtor state, no enforceable title can be obtained in Belgium, nor any measure of custody or enforcement can be taken in Belgium at the request of the creditor to obtain payment in Belgium if that payment purveys an illegitimate advantage as defined by law." This means that Belgian courts can block payments in Belgium to vulture funds, while a foreign court order that endorses the claims by vulture funds cannot be enforced in that country (Sourbron and Vereeck 2017: 7).

The rationale for the injunction issued by judge Griesa was that extraterritorial scope was needed to force Argentina to comply – a point supported by the Court of Appeals, despite vehement opposition by foreign financial intermediaries (Weidmeier and Gelpern 2013: 34). In the statement it submitted the US Supreme Court, Euroclear (2014: 7) accused the "lower court's exercise of jurisdiction" of being "exorbitant" by explicitly constraining the activities of international financial intermediaries, and reaching euro-denominated bonds "held entirely outside the US, (…) governed by English law", and whose payments "occur outside the US". For Euroclear's lawyers, the injunction expanded "the authority of the US courts beyond the borders of the US to activities carried out by governmental and other institutions in Europe" (p. 8-9). To make matters worse, the injunctive order was "in direct conflict with Belgian law", which prohibited "attachment or blocking of (…) any cash transfer"… given its detrimental effect on "the proper functioning of payment or settlement systems and hence to (…) the credibility and the liquidity of national and international financial markets" (p. 10). Indeed, as concluded by Weidemeier and Gelpern (2013: 33), the precedent of **"**burden[ing] systematically important market utilities with the risk of contempt sanctions to enforce ordinary private debts" is too costly an attempt at enforcement, made even more concerning "when it comes to foreign institutions governed by foreign law that reject this very remedy"**.**

IV. Conclusion

The legislative initiatives and judicial decisions tracked here reveal intended and unintended consequences beyond their respective jurisdictions. As uncoordinated efforts that are either limited in application (the UK and French laws) or overlapping in scope (the injunctive order in the NML v. Argentina case and the Belgian anti-vultures law), they are emblematic of how ad hoc mechanisms, perceived as mostly productive in the 1990s (Rieffel 2003), have evolved. This is a landscape of official experimentation that in some instances restricts and in others enables holdout creditors' particularly disruptive litigation in foreign courts. Contractual changes and new laws can reduce some of the risks to which some sovereigns are exposed when seeking foreign bond finance, yet they do not systematically reduce the uncertainty that seems to feed holdouts' strategies and still rules sovereign defaults outcomes.

In the present ambiguous and fragmented "debt regime", where public and private experimentation rule the day, place has regained prominence not simply as an element in contractual decisions or strategic (and concentrated) site for instantiating global financial transactions (Sassen 1991), but as the (by definition, contingent) locus for domestic rule making on debt restructurings with an extraterritorial reach. As Li (2015: 341) cautions, debt contracts will continue to lead to potentially disrupting outcomes "if the major financial centers like New York or London do not revise their laws on debt contracts". Some level of model-law diffusion (Schwarcz 2015) has been underway but each effort has its clear limitations. Promoting the kind of global outcomes that a statutory debt regime would deliver through domestic legislation seems to also require a level of transnational political and legal coordination, which has yet to be mobilized.

Finally, since the Argentine case not only set a legal precedent, but has put in motion preemptive reactions by other sovereigns in the form of contractual changes, the deviant case has been informally institutionalized into an international "new contractual normal". In this sense, it has revealed that debt restructurings are iterated games, neither reducible to generalizations about debtor-creditor (uniform) behavior, nor dismissible as singular developments without broader theoretical implications.

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