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Abstract

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Keywords

Debts, Public; Contracts; Debtor and creditor

Special Issue

Sovereign Debt as a Commodity: A Contract Law Perspective

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The ad hoc institutional configurations that facilitated the resolution of sovereign insolvency for over thirty years are fragmenting. Recent court decisions interpreting the *pari passu* clause in sovereign debt contracts reveal the dangers of pressuring common law courts to enforce contracts and mediate structural flaws in the market. The courts have dismantled sovereign protections in international law and common law checks and balances. They have gone beyond precedent to innovate remedies justified by interpreting a clause whose meaning and function were not clearly understood by the contracting parties themselves. They have also opened up a possible inter-creditor obligation that circumvents sovereign immunity legislation. This obligation imperils third party property protections and exposes the US clearing system to creditor remedies. The article argues that the current challenges require the courts to play an inadvertent, expansive regulatory role. To fulfil this role they must ensure that creditors enjoy their property (debt) without constraints and assume away the resulting externalities. In effect, enforcement sustains the legal fiction that debt is a commodity. Legal recognition of this fiction obviates negotiated debt workouts, which are premised on suspending this commodity form. The article dispels the idea that the possibility of enforcement in sovereign debt markets brings us closer to achieving the legal regime theorized as the neutral backdrop of competitive markets.

Les configurations institutionnelles ad hoc qui ont facilité le règlement de l'insolvabilité des États pendant plus de trente ans sont en cours de fragmentation. Les récentes décisions judiciaires qui ont interprété la clause *pari passu* dans les contrats de dette souveraine révèlent qu'il est dangereux de faire pression sur les tribunaux de *common law* en vue de faire exécuter les contrats et de traiter les failles structurelles du marché. Les tribunaux ont démantelé les protections souveraines offertes dans le cadre des freins et contrepoids en droit international et en *common law*. Ils ont établi de nouveaux recours sans précédent en

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s'appuyant sur l'interprétation d'une clause dont le sens et la fonction n'étaient pas clairement compris par les parties contractantes elles-mêmes. Ils ont également ouvert la voie à une éventuelle obligation entre créanciers qui vient contourner la législation sur l'immunité souveraine. Cette obligation met en péril les protections à l'égard des biens des tiers et expose le système de compensation des États-Unis aux recours intentés par les créanciers. Le présent article avance que, compte tenu des défis actuels, les tribunaux doivent jouer un rôle réglementaire discret et étendu. Pour remplir ce rôle, ils doivent s'assurer que les créanciers jouissent de leurs biens (dette) sans contraintes en ignorant les externalités qui en résultent. Dans les faits, l'exécution des contrats entretient la fiction juridique selon laquelle la dette est une marchandise. Or, la reconnaissance juridique de cette fiction rend inutiles les restructurations négociées des dettes, qui supposent la suspension de cette forme de marchandise. L'article réfute l'idée selon laquelle la possibilité d'appliquer des mesures d'exécution sur les marchés de la dette souveraine nous rapproche de l'établissement d'un régime juridique servant de toile de fond neutre aux marchés concurrentiels.

THE AD HOC INSTITUTIONAL CONFIGURATIONS that facilitated the resolution of sovereign insolvency for over thirty years are fragmenting. In the absence of an acceptable alternative, recent court decisions[1] interpreting the *pari passu* clause in sovereign debt contracts reveal the danger of pressuring common law courts to enforce contracts and paper over structural fissures in the market. The courts have dismantled international law protections and common law checks and balances

1. *Allied Bank International v Banco Credito Agricola de Cartago*, 566 F Supp 1440 (Dist Court New York, 1983); 733 F 2d 23 (Court of Appeals, 1984) [*Allied I*]; 757 F 2d 516 (2nd Circuit 1985) [*Allied II*]; *NML Capital, Ltd v Republic of Argentina*, No.08 Civ.6978 (TPG) (SDNY, December 7, 2011) [*NML pari passu* decision]; No.08 Civ.6978 (TPG) (SDNY, Feb 23, 2012) [*NML injunction order*]; 2012 WL 5895786 (SDNY Nov 21 2012) [*NML payment formula*]; 699 F.3d 246 (2d Cir 2012) [*NML I*]; 727 F.3d 230, 238 (2d Cir 2013) [*NML II*].

while going beyond precedent to craft new remedies that are ostensibly justified by interpreting a clause whose meaning and function was not clearly understood by the contracting parties themselves at the time of the contract. The courts have implicitly recognised inter-creditor obligations that circumvents sovereign immunity legislation. This invention imperils third party property protections and exposes the US clearing system to creditor remedies.

This article takes a step back from the *pari passu* dispute and discusses the (arguably long term) consequences of judicial intervention from a contract law perspective. The article argues that the current challenges faced by the courts require them to play an inadvertent yet expansive regulatory role. To fulfil this role, they must ensure that creditors enjoy their property (debt) without constraints and assume away the resulting externalities. In effect, enforcement sustains the legal fiction that debt is a commodity. Legal recognition of this fiction obviates negotiated debt workouts, which, by definition, are premised on a suspension of this commodity form. The article concludes with a discussion of the nature of legal indeterminacy, dispelling the idea that the possibility of enforcement in sovereign debt markets brings us closer to achieving a legal regime that functions as the neutral backdrop of competitive markets.

Sovereign debt crises are complicated and disruptive,[2] yet since the 1980s they have been resolved through widespread, market-driven, consensual debt workouts.[3] In most cases of default, a majority of sovereign creditors consent to restructure their debt while the minority that holds out is repaid in full at the margins.[4] For over thirty years, workouts were achieved through an ad hoc but effective mix of informal cooperation, market arrangements and formal interventions by the official sector.[5] During this period, the sovereign debt

2. Robert Z Aliber & Charles P Kindleberger, *Manias, Panics, and Crashes: A History of Financial Crises,* 7th ed (New York: Palgrave Macmillan, 2015); Mitu Gulati & Robert E Scott, *The Three and a Half Minute Transaction: Boilerplate and the Limits of Contract Design* (Chicago: The University of Chicago Press, 2013); Rosa Lastra & Lee Buchheit, eds, *Sovereign Debt Management* (Oxford: Oxford University Press, 2014).
3. Lee C Buchheit "Sovereign Debt Restructurings: the Legal Context" (BIS Papers No 72, 107) delivered at the Bank for International Settlements, July 2013, online: <www.ssrn.com/abstract=2473986> [unpublished]; Udaibir S Das, Michael G Papaioannou & Christopher Trebesch, "Sovereign Debt Restructurings 1950-2010: Literature Survey, Data, and Stylized Facts" (2012) International Monetary Fund, Working Paper No WP/12/203.
4. Arturo C Porzecanski, "From Rogue Creditors to Rogue Debtors: Implications of Argentina's Default" (2005) 6:1 Chicago J Int'l L 311 at 314.
5. Jérôme Sgard, "How the IMF did it—sovereign debt restructuring between 1970 and 1989" (2016) 11:1 CMLJ 103 at 118. See also Anna Gelpern, "Sovereign Debt: Now What?" online: (2016) 41:2 Yale J Int'l L at 119-23 <campuspress.yale.edu/yjil>.

restructuring community's repeated reliance on such arrangements constrained judicial intervention as "market participants did not treat this routine restructuring process as a violation of bond covenants."[6] This situation has changed. Since the sovereign debt crises in Argentina,[7] Greece,[8] and Ukraine,[9] there is now disturbing evidence that the institutional configurations that sustained debt workouts can no longer be taken for granted. Presently, there is no acceptable alternative to these essentially ad hoc, customised configurations, as the market and structural conditions that made them possible have shifted.[10] This article examines the changing role of the judiciary in the face of this transition. This examination is informed by an emerging consensus in the literature that, in the absence of a viable alternative, the courts will be pressured to play a more expansive role and intervene in disputes they are poorly positioned to resolve.[11]

As parties to simple debt contracts, a sovereign's creditors are guaranteed access to the courts. On default there is often "a rush to the courthouse."[12]

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6. Gelpern, *ibid* at 104. For a description of the "sovereign debt restructuring community," see Anna Gelpern & Mitu Gulati, "Public Symbol in Private Contract: A Case Study" (2006) 84 Wash U L Rev 1627.
7. Brad Setser & Anna Gelpern, "Pathways through Financial Crises: Argentina" (2006) 12 Global Governance 465.
8. Gelpern *supra* note 5 at 129-37.
9. Neil Buckley, Roman Olearchyk & Shawn Donnan, "Legal Fight Looms over Ukraine's $3bn debt to Russia" *Financial Times* (15 October 2015), online: <www.ft.com/content/f7a04f1e-7354-11e5-bdb1-e6e4767162cc>.
10. Gene Frieda, "Sovereign Debt Markets" in Lastra & Buchheit, *supra* note 2, 287. Here, Frieda also discusses the cyclical and structural changes in the market preceding and following the 2008 financial crises. The possibility of an alternative has been repeatedly raised by multilateral institutions such as the IMF and the United Nations, though none have been accepted. See Anne Krueger, "International Financial Architecture for 2002: A New Approach to Sovereign Debt Restructuring" (Address delivered at the National Economists' Club Annual Members' Dinner of the American Enterprise Institute of Washington, DC, 26 November 2001) [unpublished], online: <www-personal.umich.edu/~kathrynd/IMFDebtRestructuring.Krueger.pdf>. For an introduction to the UNCTAD debt restructuring initiative, see Yuefen Li, "Lessons learned from debt crisis and ongoing work on sovereign debt restructuring and debt resolution mechanisms" (Address delivered at ECOSOC Special Meeting on External Debt Sustainability, New York, 23 April 2013) [unpublished], online: <www.un.org/esa/ffd/ecosoc/debt/2013/presentation_Li.pdf>.
11. This view is consistent with empirical evidence that indicates a significant increase in sovereign debt litigation. See W Mark C Weidemaier & Ryan McCarl, "Creditor Remedies" in Lastra & Buchhei, *supra* note 2, 139 at 143; Julian Schumacher, Christoph Trebesch & Henrik Enderlein, "Sovereign defaults in Court: The Rise of Creditor Litigation" (2014) at 10, online: <www.ssrn.com/abstract=2189997>. See also Gelpern, *supra* note 5.
12. For evidence of a rush to the courthouse in Argentina and Peru, see Schumacher, Trebesch & Enderlein, *ibid* at 11.

However, for all intents and purposes, sovereign debt contracts are unenforceable and have been so since sovereign states reacted to the adoption of restricted immunity regimes by immunizing their attachable assets from creditor suits.[13] But in 2012, for the first time in the history of sovereign debt, debtor obligations became enforceable in US law[14] and the problem of weak enforcement was at an end. However, the possibility of enforcement elicited more negative than positive responses from scholars and markets alike.[15]

Argentina refused to countenance some creditor claims, and in the face of this intransigence courts were under pressure to interpret the *pari passu* clause in sovereign bond contracts[16] in a manner that papered over confusion about its meaning in the market.[17] *Pari passu* clauses are standard terms in debt contracts that specify how creditors will be paid in the event of a default. A well-developed literature examines the implications of this clause and the deep confusion over its meaning amongst market actors and the official sector.[18] This article's inquiry into the judicial role and the wider questions about the role of law in sustaining debt markets is motivated by the fundamental indeterminacy in the meaning of a standard term in bond contracts.

Another implication of the *pari passu* decisions is the real possibility that an expansive post-default judicial role will stymie consensual debt workouts and in the process lengthen debt crises, require extensive and potentially significant taxpayer-funded bailouts, and impose unremitting austerity on the citizens

13. In the US, legislation was tabled to restrict the absolute sovereign immunity protections sovereigns enjoyed in international law. See *Foreign Sovereign Immunities Act*, USC § 1605 (1976).
14. *NML I*, *supra* note 1.
15. For a discussion of the rejection of the court's ratable payment interpretation of the clause, see Lee C Buchheit & Jeremiah S Pam, "The Pari Passu Clause in Sovereign Debt Instruments" (2004) 53 Emory LJ 869 at 877-91; for an argument that the rateable payment interpretation was contrary to conventional understanding of the clause, see G Mitu Gulati & Kenneth N Klee, "Sovereign Piracy" (2001) 56:2 The Business Lawyer 635 at 650. Positive responses were largely confined to judgment-holders and the courts. For views in favour of the ratable payment interpretation in US law and third party injunctions see Brief for Amicus Curiae Kenneth W Dam in support of Affirmance, *NML I*, *supra* note 1; Brief of Washington Legal Foundation as Amicus Curiae in Support of Appellees Urging Affirmance, *ibid.* A market association responded by providing a template of the clause. See International Capital Market Association, "Collective action clauses," online: <www.icmagroup.org/Regulatory-Policy-and-Market-Practice/Primary-Markets/primary-market-topics/collective-action-clauses> [ICMA].
16. See Buchheit & Pam, *ibid*.
17. ICMA, supra note 15.
18. See Gulati & Scott, *supra* note 2.

of debtor states.[19] The decline of the ad hoc institutional configurations that evolved to achieve earlier debt workouts is an opportunity to better understand how enforcement action by the courts stymies consensual market-driven debt workouts. According to Lee Buchheit and Elena Daley the chemistry that sustains debt workouts relies on a mixture of a sovereign's "unique vulnerability to creditor lawsuits" and their "unique degree of protection against creditor remedies."[20] In the absence of attachable sovereign assets, the courts enforce debt obligations by threatening the attachment of third-party claims and back their threat by enjoining the US clearing system. In so doing they both peel back this protection and enhance sovereign vulnerability. In the absence of countervailing formal or informal authority that can restore this "chemistry" and limit judicial intervention, debt workouts are in jeopardy. As has been discussed in the literature, NML does seem to offer "a unique remedy for a unique case."[21] However, the NML route to judicial enforcement has ramifications beyond the four corners of a contract dispute. In the absence of non-judicial restraints on enforcement, I expect that this issue will recur in the future.[22]

There are two views on the nature of the institutional configurations that facilitated debt workouts.[23] José Ocampo characterises this thirty-year period as a chaotic "non-system" reactive to conflicting and disparate creditor interests. Debt workouts, if and when they happened, were random events. Anna Gelpern, on the other hand, argues that there was order in these unique configurations: Coordination between the informal Paris and London clubs[24] was reinforced by formal organizations such as the IMF and buttressed in the early period by long term relationships between commercial banks and debtor states. Though the balance Ocampo tracks between creditor rights and sovereign protections reflects the fundamental chemistry that sustains debt workouts mentioned

19. Gelpern, *supra* note 5 at 46.
20. Lee C Buchheit & Elena L Daley, "Minimising Holdout Creditors: Carrots" in Lastra & Buchheit, *supra* note 2, 4.
21. Weidemaier, *supra* note 11 at 149.
22. This is consistent with the view that, from a contract law perspective, sovereign debt litigation represents the "hard cases that make bad law." See Anna Gelpern "Contract Hope and Sovereign Redemption" (2013) 8:2 CMLR 132 at 133.
23. José Antonio Ocampo, "A Brief History of Sovereign Debt Resolution and a Proposal for a Multilateral Instrument" in Martin Guzman, José Antonio Ocampo & Joseph E Stiglitz, eds, *Too Little, Too Late: The Quest to Resolve Sovereign Debt Crises* (New York: Columbia University Press, 2016) 190 at 192; Gelpern, *supra* note 5.
24. The Paris Club comprises a group of officials from major creditor countries whose role is to find co-ordinated and sustainable solutions to payment difficulties experienced by debtor states. The London Club is an informal group of major private creditors set up to discuss debt restructurings. See online: <www.clubdeparis.org>.

above, he sheds no light on what sustained debt workouts. Gelpern fills this gap by highlighting key factors such as "[c]hanging capital flows, old creditors' weakening commitment to past practices,"[25] and the absence of an acceptable alternative that market actors would coalesce behind. Both authors propose ways to negotiate the current period, in which debt workouts are no longer inevitable as market outcomes.[26] This article builds on this new consensus to track the parallel and evolving judicial role over the same period.

The article examines three decades of post-default enforcement litigation. Over this period the courts consistently expanded their remit, setting the scene for the current situation in which it is now possible to shoehorn the complexity of a sovereign debt crisis and market-driven resolution into the four corners of a simple debt dispute. In this situation, judicial intervention is confined by contract law imperatives such as freedom to contract, consent, and enforceable promises to pay. The courts must strive to sustain "the semi-fiction that sovereign bonds create legally enforceable obligations."[27] However, this fiction works only as long as debt obligations are serviced. On default, the contract law imperatives that bind the court come up against the complexity of a debt crisis. This sets the conditions for an expansive judicial role. Argentina is a case in point—it refused to repay hold-out creditors while continuing to service its debt obligations to other creditors who participated in two debt workouts. In the absence of overarching institutional interventions such as an attempt by the IMF to rein in Argentina's behaviour,[28] the judicial impulse to intervene is triggered.[29] In this process of

25. Gelpern, *supra* note 5 at 46; W Mark C Weidemaier & Mitu Gulati, "A People's History of Collective Action Clauses" (2013) 54:1 Va J Int'l L 56. When compared to the period that preceded securitization of debt in the 1980s, contemporary bondholders are widely dispersed and have differing interests.
26. Gelpern, *supra* note 5 at 46.
27. Weidemaier, *supra* note 11 at 149.
28. Argentina for instance, had repaid its IMF loans by this time. An IMF presence could arguably have changed the behaviour that triggered this outcome. For a discussion on the judicial reaction to Argentina's behaviour, see Gelpern, *supra* note 5 at 69.
29. See *e.g. NML II*, *supra* note 1 at 23. This case characterizes Argentina's behaviour as "recalcitrant" as it refused to repay litigating creditors while continuing to repay non-party exchange bondholders. For justifications of this enforcement role in sovereign debt litigation, see Andrei Schleifer, "Will the Sovereign Debt Market Survive?" (2003) National Bureau of Economic Research Working Paper No 9493, online: <http://www.nber.org.ezproxy.library.yorku.ca/papers/w9493>; Hal S Scott, "Sovereign Debt Default: Cry for the United States Not Argentina" (2006) Washington Legal Foundation Working Paper No 140, online: <http://www.wlf.org/upload/Scott%20WP%20Final.pdf>; Michael P Dooley, "International financial architecture and strategic default: can financial crises be less painful?" (2000) 53:1 Carnegie-Rochester Conference Series on Public Policy 361. This impulse is also justified by

judicial intervention, and within the constraints of contract law, sovereign debt acquires its commodity form. This article's examination of the courts' expanded enforcement role delineates the commodification of sovereign debt that occurs via judicial actions that secure the litigating creditors' enjoyment of their bonds[30] irrespective of sovereign credit risks[31] and of the negative consequences for non-party creditors and the wider market.[32]

In contract law, enforcement protects the intangible property claims of creditors to payment. What is the nature of these property claims? Should these claims be protected as commodities—immutable, abstract, and inviolable? If so, at what cost? And who will eventually pay? Is enforcement justified at the cost of delayed workouts that disproportionately impose costs on "citizens, taxpayers, bank depositors and pensioners,"[33] leading sovereigns to lose "their capacity to meet the basic human needs of their citizens and to safeguard their human

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the need to uphold the rule of law signalling the established superiority of US law and legal institutions and drawing a clear line between the US and other societies that have so far been unable "to develop effective, low cost enforcement of contracts" which is viewed as "the most important source of both historical stagnation and contemporary underdevelopment in the Third World." For a discussion of this phenomenon, see Carmine D Boccuzzi Jr, Michael M Brennan & Jacob H Johnson "Defences" in Lastra & Buchheit, *supra* note 2 at 103. Secretary General Kofi Annan provides a global view in his Address to the US Chamber of Commerce in June of 1999 where he stated that "... without rules governing contracts and property rights; without confidence based on the rule of law; without trust and transparency—there could be no well-functioning markets. We know this when it comes to national economies, but we have yet to apply it fully to global markets." United Nations, Press Release, SG/SM/7022 "Secretary-General, Addressing United States Chamber of Commerce, Highlights Fundamental Shift of United Nations Attitude Towards Private Sector" (8 June 1999), online: <http://www.un.org/press/en/1999/19990608.SGSM7022.html>.

30. Juan J Cruces & Tim R Samples, "Settling Sovereign Debt's 'Trial of the Century'" (2016) 31 Emory Int'l L Rev 5.
31. For a discussion of the implications of markets ignoring sovereign credit risk in the lead up to the financial crisis of 2008, see Frieda, *supra* note 10 at 287; S I Strong, "Rogue Debtors and unanticipated Risk" (2014) 35:4 U Pa J Int'l L 1139.
32. W Mark C Weidemaier & Gelpern Anna, "Injunctions in Sovereign Debt Litigation" (2014) 31:1 Yale J on Reg 189.at 192; Julian Schumacher, "Sovereign Debt Litigation in Argentina: Implications of the Pari Passu Default" 1:1 JFR 143; Tim R Samples, "Rogue Trends in Sovereign Debt: Argentina, Vulture Funds, and Pari Passu Under New York Law" (2014) 35:1 Nw J Int L & Bus 49 at 76; Rodrigo Olivares-Caminal, "The Pari Passu Interpretation in the Elliott Case: A Brilliant Strategy but an Awful (Mid-Long Term) Outcome?" (2011) 40:1 Hofstra L Rev 39.
33. Gelpern, *supra* note 5 at 46.

rights."[34] More generally, enforcement opens up questions about the role of the law in sovereign debt markets. Is the legal recognition of debt as a commodity a turning point? Does this recognition signal an incipient legal regime that will ensure the achievement of efficient outcomes in competitive markets, or is it a second-best intervention that should trigger instead a call for the exercise of public authority to sustain market-driven debt workouts and, in the process, limit the judicial role?[35]

This article draws out the implications of the property claim in what are contractual disputes. This focus is informed by an incipient literature that engages in a similar exercise in relation to the regulation of financial market transactions.[36] Sovereign debt litigation opens up an interesting inquiry into the judicial role in this relatively underdeveloped[37] area of research. The recognition of debt as a commodity allows the courts to influence both its transferability and assignability, opening up the possibility of injunctions. In the absence of countervailing

34. *Ibid*. For a discussion of the empirical evidence of the health outcomes of austerity imposed on the Greek population, see Stuckler David & Sanjay Basu, *The Body Economic: Why Austerity Kills* (New York: Basic Books, 2013).
35. For proposals on how to limit the judicial role through amendments to the IMF Articles and within the existing statutory framework in the Eurozone, see Committee on International Economic Policy and Reform, *Revisiting Sovereign Bankruptcy: Brookings Report* (CIEPR, October 2013) at 21-28, 29-35, online <https://www.brookings.edu/wp-content/uploads/2016/06/CIEPR_2013_RevisitingSovereignBankruptcyReport.pdf> [*Sovereign Bankruptcy*]. This was also the gist of the law passed by the Belgian Government in 2005. The law was published on 28 December 2004, and entered into force on 7 January 2005. It stated: "Any cash settlement account maintained with the operator of a system or with a cash settlement agent, as well as any cash transfer, through a Belgian or foreign credit institution, to be credited to such cash settlement account, cannot be attached, put under sequestration or otherwise blocked by any means by a participant (other than the operator or the settlement agent), a counterpart or a third party." See National Bank of Belgium, *Financial Stability Review 2005 (June)* at 163, online: <www.nbb.be/doc/ts/publications/fsr/fsr_2005_en.pdf>.
36. Heather Hughes, "Financial Product Complexity, Moral Hazard and the Private Law" (2015) 20 Stan J L Bus & Fin 179. Here, Hughes identifies "a shift from a contract law to a property law rubric" in interventions to regulate the transactional complexity of financial products and opens up a discussion on new modes of regulatory intervention that follow the property in financial products (*ibid* at 182).
37. "The normative implications of a property-oriented view of financial products are under-developed" (*ibid* at 189).

legislative or regulatory authority to limit this intervention, third-party rights and the clearing system are imperilled—potentially without restraint.[38]

The commodification of sovereign debt has arisen in litigation related to private lending by creditors based in US capital markets. The contract law framing of the disputes is a feature of foreign debt issuances by emerging market sovereigns.[39] Though the US is a significant jurisdiction for debt issuances, disputes under US law are not representative of sovereign debt disputes generally.[40] The issuances in dispute were large but a small subset of total bond issuances.[41] It follows then that the contract law perspective developed here is not aimed to explain either all sovereign debt litigation or the judicial role in other jurisdictions. Recent empirical evidence of a significant rise in sovereign debt litigation suggests, however, that the perspective developed here would be generally relevant for litigation in common law jurisdictions.[42]

The article proceeds as follows. Part I analyses sovereign debt litigation from just before the securitization of debt in 1980 to the present. Building on earlier litigation that established the sanctity of contract paradigm, this Part delineates an incipient contract as property paradigm and examines the contract law justification for enforcement, namely securing creditors' enjoyment of their property. Part II examines the nature of this property claim in contract law doctrine. This discussion is focused on the promissory theory of contract and draws out the promissory basis of the property claim. This basis is central to an understanding

38. There were parallel concerns raised in early debates about the role of the courts in recognising the assignability of shares prior to the promulgation of company law statutes in the UK. Briefly, shares were contracts and, as choses in action, were unassignable in the absence of public authority that suspended the contract form and recognised its assignable and transferable property form. A discussion of this literature and its relevance to US law and sovereign debt are beyond the scope of this paper. For an overview of these cases see Ireland Paddy, "Property and Contract in Contemporary Corporate Theory" (2003) 23:3 LS 454 at 459-60.
39. Gelpern & Gulati, *supra* note 6.
40. Debt is also issued in other legal jurisdictions such as the United Kingdom, Japan, and by EU sovereigns such as Germany and Greece.
41. Alejandro Díaz De León, "Mexico's adoption of new standards in international sovereign debt contracts: CACs, pari passu and a trust indenture" (2016) 11:1 CMLJ 12. Domestic debt issuances are generally much larger than foreign bond issuances. In the case of Mexico for instance, "as of June 2015, close to 80% of the total debt was issued in local markets and domestic currency, while in 1995 80 % of the debt portfolio was external debt" (*ibid* at 13). See also Frieda, *supra* note 10.
42. The litigation dataset complied by Schumacher, Trebesch, & Enderlein indicate a significant increase in litigation in the 2000s when compared to the 1980s. They attribute this increase to diversification in demand. See Schumacher, Trebesch & Enderlein, *supra* note 11 at 1.

of the commodity form that debt takes in judicial deliberations. The implications of these legal changes are discussed in Part III. This Part highlights how a legal fiction is established in the context of metaphorical and literal markets. The debt resolution system's reliance on a legal fiction reveals the inherent indeterminacy of the law. As the legal fiction is conceptually incompatible with debt workouts, enforcement skews the distribution of the costs of sovereign debt repayment disputes towards the debtor and away from its creditors. Part IV discusses the nature of legal indeterminacy and presents conclusions.

I. FROM ALLIED TO NML: THE EVOLVING COMMODITY FORM OF DEBT

A sovereign debt dispute is, by definition, a political dispute. The repayment of debt, once issued, lays a claim to a dedicated stream of sovereign resources for sometimes considerable lengths of time. The economic shock that triggers default and the subsequent imposition of austerity and structural adjustment have disruptive systemic effects on the economy and the political fabric of the debtor state. Almost simultaneously, in a parallel universe of abstract legal concepts including 'property,' 'liability,' and 'sovereign defences,' the sovereign becomes a defendant in a contract enforcement dispute. As such, it is far from a free nation that can exercise its discretion in any way it deems necessary to deal with the crisis that triggered the default. The dispute is resolved in a domain insulated from that of discretionary sovereign acts. This Part begins with a discussion of the *Allied* set of cases, which set the benchmark for judicial intervention in sovereign debt markets.[43] This is followed by a discussion of some intervening decisions before a discussion of the *NML* (*pari passu* interpretation) litigation against Argentina.[44] This discussion tracks how the courts construct the legal fiction that sovereign debt obligations are enforceable. For the purpose of simplification, the term "debt contract" refers to promissory notes and bonds.

A. THE ALLIED LITIGATION

Allied Bank International (Allied) is a US chartered bank based in New York. It acted as an agent for a syndicate of thirty-nine creditor banks that had advanced credit to Costa Rica in 1979. Under the terms of the indenture on the promissory notes, these creditors were to be paid in New York in US dollars every

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43. *Allied I*, *supra* note 1; *Allied II*, *supra* note 1.
44. *NML II*, *supra* note 1.

six months from July 1, 1978 until July 1983. The Costa Rican banks kept to the payment schedule until 1981. In August 1981 the Costa Rican Central Bank issued a mandate that prohibited banks from making both principle and interest payments on external debt to foreign creditors in foreign currency. Any payments had to have prior approval of the Central Bank in consultation with the Ministry of Finance as, at the time, Costa Rica was renegotiating its foreign debt. While the case was pending in the New York District Court, Costa Rica's creditors agreed to dismiss the case. Costa Rica then signed a refinancing agreement with Allied continuing to represent the original creditors. However, Fidelity Union Trust (one of the thirty-nine) refused to participate in the restructuring. Costa Rica resumed payments to the thirty-eight remaining creditors.

Allied revived the enforcement case on behalf of Fidelity and sued the Costa Rican banks in the New York District Court. In its motion for summary judgment, Allied sought to accelerate the unpaid payments owed by the three state-owned banks. Allied further claimed that the promissory notes were confiscated by Costa Rica. In response, the Costa Rican banks defended themselves by mainly[45] asserting sovereign immunity from suit and the act of state doctrine. The district court refused to enter summary judgement for Allied and reasoned that a judicial determination contrary to the Costa Rican directives could embarrass the US government because it was the public, as opposed to the commercial, conduct of the Costa Rican government that prevented payment. The district court then applied the act of state doctrine to dismiss the motion.[46] The court was well within established precedent in its reasoning. However, this initial finding was challenged in the first instance by the Department of Justice (DOJ) in its amicus brief seeking rehearing.

The DOJ made three arguments which would eventually set a precedent ensuring that sovereign defaults could give rise to enforceable creditor claims in US law. The courts could abstain from intervention only if the confiscation of creditor property was within the territorial jurisdiction of the foreign state. As per the DOJ's situs analysis, the contracts were payable in the state of New York and in US dollars. Hence, the Costa Rican decrees affected creditor rights

45. The other defences raised were that the court lacked jurisdiction and the notice was not properly served.
46. The district court was following an earlier Supreme Court decision that the act of state doctrine was partly to respect the independence of every sovereign state by judicial abstention when the acts of foreign states were in issue. The key Supreme Court decisions relied on by the courts were *Underhill v Hernandez* and *Banco Nacional de Cuba v Sabbatino.* See *Underhill v Hernandez*, 168 US 250 (1897); *Banco Nacional de Cuba v Sabbatino* 376 US 398 (1964) [*Sabbatino*].

outside its territory and were thus not protected from judicial abstention under the act of state doctrine. This interpretation contravened established precedent set in *Sabbatino*.[47] In that case, the US Supreme Court found that the act of state doctrine was available where the foreign state had territorial jurisdiction.[48] Relying on its *situs* analysis, the DOJ moves away from precedent set in *Underhill* and *Sabbatino*[49] to argue "that if any part of the transaction took place within the United States, or if the place of performance, enforcement, or collection was … located in the United States, the doctrine was unavailable."[50] The DOJ did not specify any legal grounds for its proposed departure from established law. In effect, to perform its enforcement role the court was expected to go beyond its common law, precedent-confined remit. The DOJ was establishing a template for enforceability under US law.

Following on from the doctrinal discussion above, the DOJ's interpretation removed a ground for judicial abstention—the act of state defence, an established sovereign protection in international law. The DOJ's interpretation established the enforceability of Fidelity's claim in the US courts and in doing so directed judicial attention towards the private law dimensions of the dispute—rather than determining the case on the issue of sovereign defences under international law. In their now unprecedented private enforcement role, on default, the US courts could protect the intangible property claims of US creditors. As will be discussed below, this intervention opened up a can worms: The courts do not clarify what the contract law basis of a creditor's private property claims are. In a market marked by creditor heterogeneity, the essential indeterminacy of the basis of each individual creditor claim was papered over. Furthermore, on default, formation and performance are now conflated (as affirmed in the DOJ's *situs* analysis). One corollary of the DOJ's argument is that the performance of the non-payment terms of the bond by the debtor does not matter. In other words, under the DOJ's interpretation, the good faith actions of the debtor become irrelevant to the determination of a contractual dispute. The main implication of the DOJ's interpretation was that default is viewed as a confiscation of creditor

47. *Ibid*.
48. *Ibid* at 421.
49. *Ibid*.
50. James Thuo Gathii, "The Sanctity of Sovereign Loan Contracts and its Origins in Enforcement Litigation" (2006) 38:2 Geo Wash Int'l L Rev 251 at 276.

property, and this view justifies individual enforcement action in US courts.[51] Further, judicial intervention would reinforce the immutability and inflexibility of creditor claims. As will be discussed in more detail later, this template would have ramifications on third party non-claimants.

In view of the ongoing payments being made by Costa Rica, on appeal, the Second Circuit affirmed the district court's dismissal[52] on the grounds of another established sovereign defence: the principles of comity. The court found that Allied was required to recognise the validity of the Costa Rican directives that triggered the default.[53] The court found that even though the *situs* of the debt was within the United States, the conduct of the Costa Rican government—which culminated in the debt restructuring—was consistent with US law and policy.[54] With its finding of consistency, the court was upholding the international law principle of comity, and was reinforcing what was an important sovereign protection in international law.

Significantly, the court deferred to the consensual debt workout agreed to by a majority of Costa Rica's creditors on the grounds that they would be bound to the government's reorganisation of debt. Following common law precedent[55] the Second Circuit drew an analogy between the ongoing government reorganisation and Chapter 11 corporate bankruptcy. In this context the prohibitions imposed by the Costa Rican government became an automatic stay and therefore could be recognised as such in the common law. As this reading was akin to a common law insolvency, default was not a repudiation, but rather "merely a deferral of payments while it attempted in good faith to renegotiate its obligations."[56] Like the district court, the *Allied I* court initially resisted intervention on the grounds of precedent and US policy on consensual debt workouts. The *Allied I* court also deferred to market initiative and limited its role in the dispute. Finally, it acknowledged the situation the Costa Rican government found itself in and the reasons that justified its decision to default. All of this was, however, contrary

51. In a similar vein, Gathii argues that the Second Circuit's decision in the Allied case was informed by classical legal thought of the "late nineteenth and early twentieth centuries the period of early capitalism in the United States [where] the judicial response to holdouts has been to understand freedom of contract as embodying freely made choices that should not be interfered with by either the lenders or borrowers or even the courts" (*ibid* at 269).

52. *Allied I*, *supra* note 1 at 519.

53. *Ibid*.

54. *Ibid*.

55. The court referred to the Supreme Court decision in *Canada Southern Railway Co v Gebhard*, 109 US 527 (1883) [*Canada Southern*]. Here the court held that government bondholders would be bound by a debt restructuring undertaken by the government.

56. *Allied I*, *supra* note 1 at 522.

to the arguments set out in the DOJ's intervention in the *Allied I* court. Their submission asserted both the irrelevance of the wider context in determining the suit and the good faith actions of the debtor. *Allied I* led to another instrumental intervention by the DOJ, which filed two amicus briefs in response calling for a rehearing and for a reversal on rehearing of *Allied I*.

Following on from its first intervention, the DOJ sought to demarcate the competence of the US courts. They argued that "the *Allied I* court had misconstrued U.S. foreign policy on debt adjustment"[57] on three grounds:

> First, it argued that the United States leadership and involvement in the cooperative rescheduling of debt through the Paris Club and through Federal Assistance under the Foreign Assistance Act only applied to and affected sovereign defaults on debt borrowed from other sovereign lenders rather than debt borrowed from private lenders. As such *Allied I* was argued to have applied the notion of cooperative debt adjustment to debt borrowed on the private market while it was only designed to apply to borrowing between sovereigns.[58]

This argument exceptionalized private debt workouts even though, in the background, a majority of Costa Rica's creditors had already consented to participate in the workout and Costa Rica was already servicing the new debt. The assertion that the restructuring of private debt was not US policy implicitly affirmed the inviolability of individual creditor property on default. This affirmation was underpinned by the DOJ's second reason for setting aside *Allied I*, where they "argued that *Allied I* misconstrued U.S. support for cooperative debt adjustment as a basis to undermine the rights of private creditors to obtain effective remedies, including due process safeguards against expropriation of their property through enforcement litigation."[59] Finally, it was argued "that cooperative debt was just one of several policies of the U.S. government and that the *Allied I* court wrongly presumed that Costa Rica's unilateral restructuring of its debt was excusable as a result."[60]

The DOJs arguments decontextualized the dispute, as they were silent on extenuating factors—such as the reorganisation of an economy in the face of a national economic crisis—that would matter in this private law dispute. The intervention obviated the distinction between excusable default and wilful

57. Gathii, *supra* note 50 at 279-80.
58. *Ibid* at 280.
59. *Ibid* at 284. This intervention ignored the finding in the lead case relied on by the *Allied I* court (*i.e.*, *Canada Southern*) that recognised the legal validity of both debt restructurings consented to by a majority of a sovereign's creditors and the subsisting due process claims of holdout creditors like Fidelity.
60. *Ibid*.

repudiation that was accepted in international commercial law. Further, the fact that a majority of its creditors consented to a debt workout would not give the debtor de jure protection against creditor claims in US law. The focus of the resistance by Fidelity and *amici* to the bankruptcy analogy was to establish the legal position that non-payments of sovereign debt would constitute a unilateral confiscation of each individual creditor's property.

The DOJ's intervention was contrary to the actions of the executive branch of the US government that had certified Costa Rica as eligible to receive federal assistance, which would not have been forthcoming if the "executive branch found that the default constituted an expropriation."[61] In effect, to make the enforcement of debt contracts possible in US law, judicial intervention had to go beyond accepted precedent. In the process, established common law checks and balances on the exercise of judicial discretion were dismantled.

The *Allied I* decision was also resisted by a campaign led by creditor banks, the business press, and organisations such as the National Foreign Trade Council, the Rule of Law Committee, and the New York Clearing House.[62] They claimed:

> *Allied I* legitimized unilateral repudiation of sovereign loan contracts without any remedies for U.S. financial institutions and this lack of creditor protection under New York Law (as interpreted by the Second Circuit) made all loans to developing countries susceptible to similar repudiation.[63]

This campaign by investors and other market actors reflected the concerns raised by the DOJ. The intervention sought by the parties resisting *Allied I* did not demand the legal validation of the actions of Costa Rica's creditors—as market actors they were consenting to the debt restructuring. A key concern raised here by the DOJ and other market actors was the unpredictability of whether debtors would default opportunistically in a world where the resolution of debt crisis was made easier. In other words, if sovereign debt contracts were not actually individually enforceable, accurate predictions about debtor behaviour could not be made.

The arguments made on behalf of Fidelity—the lone holdout—the *amici*, and the market as a whole unequivocally affirmed the view that debt contracts are enforceable in full under US law. As the DOJ stated in its brief when commenting

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61. Instead the executive response would have been to trigger "a suspension of assistance as well as the imposition of economic sanctions" (*ibid*).
62. The discussion of the US government and New York Clearing House Association briefs is found in Gathii, *ibid* at 285; Christopher R Brown, "Enforcing Sovereign Lending" (1984) 3:7 Int'l Fin L Rev 5.
63. Gathii, *supra* note 50 at 285.

on the debt workout: "[W]hile [private] parties may agree to renegotiate conditions of payment, the underlying obligations to pay nevertheless remain valid and enforceable."[64] This position was accepted by "[t]en of the members of the New York Clearing house who had accepted the restructuring."[65]

On rehearing, the Second Circuit Court of Appeal reversed *Allied I* on the grounds set out by Allied and the amici.[66] The decision affirmed the view that sovereign debt was enforceable and that "except under the most extraordinary circumstances, [creditor] rights will be determined in accordance with recognized principles of contract law."[67] Finally, the finding in *Allied II* was that "[t]he Costa Rican directives are inconsistent with the law and policy of the United States. We refuse, therefore, to hold that the directives excuse the obligations of the Costa Rican banks."[68] In other words, the court affirmed the private law-nature of disputes of this kind. This is a similar point made by Gathii in his analysis when he notes:

> Rather than viewing the sovereign debt contracts that Costa Rica had with the thirty-nine other creditors as establishing relations within which the interests of both sovereign debtors and creditors converge, the court subscribed to an especially atomistic and individualistic outlook of their contractual relations.[69]

In the other similar situations involving bond payments, other courts followed *Allied II* and henceforth the view that debt contracts are enforceable was established. In *AI Credit Corp v Jamaica*,[70] the Southern District court of New York decided that a holdout creditor was under no obligations to waive its commercial rights to enforce payment by adhering to a sovereign debt restructuring that it had defected from. This was affirmed in *Nat'l Union Fire Ins.*

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64. *Ibid* at 289.
65. Gathii notes: In its brief, Costa Rica explained the alliance between Fidelity and the Clearing House banks, who had approached the restructuring differently, in the following manner:

    > [T]he Clearing House concedes that, as major banks, its members have the burden of persuading reluctant or recalcitrant banks, such as Fidelity to desist from a position of adamant rejection (citations omitted). However, the Clearing House apparently has concluded that *devotion to a perceived ideological comradeship of banking requires it to sacrifice common sense and the common good to an imagined unqualified right of Fidelity to a judgement.*

    Ibid at fn 214 [emphasis in original].
66. *Allied II*, *supra* note 1.
67. *Ibid* at 522.
68. *Ibid*.
69. Gathii, *supra* note 50 at 303.
70. 666 F Supp 629, 631-32 (SDNY 1987).

Co of Pittsburgh, PA v People's Republic of Congo,[71] where the court emphasized that the creditors participation in debt restructuring was voluntary and could not therefore be unilaterally imposed on creditors. In *Commercial Bank of Kuwait v Rifidian Bank and Central Bank of Iraq*,[72] the court extended *Allied II* to find that default occasioned by war, economic sanctions, and the freezing of its assets could be viewed as wilful default—thus making it impossible for Iraq to obtain foreign currency to repay its debts.[73] *Elliot Associates v Banco de Nacional*[74] and *Pravin Banker v Banco Popular Del Peru*[75] in both cases the courts held that creditors could exclude themselves from debt restructurings and sue for the face value of the debt. In decisions that have followed the *Allied* decisions, the classical mind set of the common law courts has been replaced by an interventionist stance with variable precedential constraints. The case law analysis in this paper reveals that with the gradual dismantling of sovereign protections in US law, courts have extended their enforcement role in an attempt to paper over the structural flaws inherent in sovereign debt markets.

Allied II also implicitly affirmed that, on default, there is no room for any intermediate extenuating circumstances between the formation of the contract and its full performance. Further, unlike other contractual contexts, and given the nature of these disputes, the judicial role extends beyond the four corners of the contract. The courts are not merely enforcing contracts but are in fact "exercising the power of the state of New York over the power of a foreign state to favour in-state multinationals banking interests."[76] In a similar vein, it has been noted that the *Allied II* court was engaged in "public decisions about what agreements to enforce or not to enforce."[77] This understanding is consistent with the view developed here that enforcement is more than a judicial intervention. Indeed, enforcement becomes a political act.[78]

In relation to specific contract doctrine, it has been argued that the "courts have largely adopted as a rule the sanctity of sovereign debt contracts when

71. 729 F Supp 936 (SDNY 1989).
72. 15 F (3d) 238 at 242-43 (2nd Cir 1994).
73. *Ibid*.
74. 194 F (3d) 363 (2nd Cir 1999).
75. 109 F (3d) 850 (2nd Cir 1997).
76. Gathii, *supra* note 50 at 307.
77. *Ibid*.
78. For a diametrically opposite outcome, see *Russell Jackson v The Peoples Republic of China*, 740 F 2d 1490 (11th Cir 1986). Here, to avoid embarrassing the Chinese government, the Secretary of State intervened through the DOJ urging "the court to refrain from deciding the case … [he] highlighted China's ability to retaliate economically against the United States should the court proceed to rule against China." Gathii, *ibid* at 309.

confronted with claims brought by holdout creditors."[79] This section discussed the *Allied* cases in order to outline how the recognition of sanctity of contract laid the groundwork for courts to play an increasingly expansive role. On the whole, it is argued here that enforcement litigation introduces legal indeterminacy and uncertainty that will eventually disrupt market-driven consensual debt workouts. The following section examines the latest changes in the courts enforcement role with an examination of *NML v Argentina*.[80]

B. NML V ARGENTINA

In 1994, Argentina began issuing debt securities ("FAA Bonds") pursuant to a Fiscal Agency Agreement. The agreement was governed by New York law. A number of individual investors bought bonds that Argentina had started issuing in 1998. Argentina defaulted on the bonds in 2001 after its president declared a "temporary moratorium" on principal and interest payments on more than $80 billion of its external debt—including the FAA bonds.[81] A minority of investors established exclusively to buy distressed Argentine debt (also known as distressed asset investors) acquired beneficial interests in the FAA bonds at a deep discount immediately before Argentina defaulted in December 2001 and at various times from the first issuance until June 2010.[82] These distressed asset investors included NML, a Cayman Islands hedge fund. Distressed asset investors are referred to as holdouts because they refuse to participate in debt

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79. *Ibid*.
80. *NML I*, *supra* note 1; *NML II*, *supra* note 1.
81. The Argentine default as with other similar events in the past was a significant event. The default was at the end of a "prolonged economic recession." Paul Blustein, *And the Money Kept Rolling In (and Out): Wall Street, the IMF and the Bankrupting of Argentina* (2006) at 193. See also Carmen M Reinhart and Kenneth S Rogoff, *This Time Is Different: Eight Centuries of Financial Folly* (Princeton University Press, 2009). "By the end of 2001, the crisis made it impossible for Argentina to service its overwhelming debt burden—some $80 billion in public external debt—while maintaining basic governmental services necessary for the health, welfare and safety of the Argentine populace." *NML II*, *supra* note 1, Petition for the Writ of Certiorari filed by the Republic of Argentina in the Supreme Court of the United States, at 7 [Argentina Writ].
82. The coupon rates on the FAA bonds ranged from 9.75 per cent to 15 per cent and the dates of maturity ranged from April 2005 to September 2031:

    > NML and similar "vulture" hedge funds seek to take advantage of the absence of bankruptcy protection in the sovereign context by bringing lawsuits for the face value of defaulted sovereign debt, obtaining judgements on which interest continues to run indefinitely, and then using aggressive means to try and execute them.

    Argentina Writ, *ibid* at 41.

workouts offered by the debtor, seeking instead to enforce their contracts for full repayment. These investors are collectively referred to as 'holdouts' as they hold out from participating in debt workouts offered by the debtor, seeking instead to enforce their contracts for full repayment.

In the absence of a bankruptcy regime for insolvent states, Argentina restructured its external debt on a voluntary basis through two global exchange offers in 2005 and 2010.[83] In the debt settlements, participating holders (called Exchange Bondholders) exchanged old, nonperforming debt for new performing debt with lower interest rates, a reduced principal, and longer maturities. The exchange offers were extended to all holders of eligible debt, including NML. Owners of the debt tendered approximately 92 per cent of the aggregate eligible debt in the exchange offers, making the Republic's sovereign debt restructuring the largest in history until Greece in 2012. However, NML and other holdouts refused to participate in either workout.

These workouts were substantively in accordance with established market practice. The only difference was that Argentina wanted to incentivize creditors to participate in the debt workouts. To that end it passed the "Lock Law" in 2005, which barred the "National Executive Power" from reopening "the swap process established in the [2005 workout]."[84] In effect Argentina was restricting itself from negotiating a deal with the holdouts. It also classified unexchanged FAA Bonds as a category separate from its regular debt and claimed that it was not in a legal position to pay that category since 2005. As a sovereign state, Argentina had decided that it was unwilling to negotiate with the holdouts. This sovereign choice notwithstanding, in the US courts it was a defendant in a contractual

83. Unable to service its debts, Argentina had no choice but to defer interest and principal payments to its bondholders. Like many nations that have faced economic crisis and unsustainable indebtedness, including the United States in the early days of its constitution, Argentina was forced to seek restructuring of both its external and internal public debt. *Ibid*.

84. *NML I*, *supra* note 1 at 6. This complemented the term in the prospectus of the exchange offer which stated:

> "Risks of not participating in [the] exchange offer" were the following: Existing defaulted bonds eligible for exchange that are not tendered may remain in default indefinitely … The Government has announced that it has no intention of resuming payments on any bonds eligible to participate in [the] exchange offer … that are not tendered or otherwise restructured as part of such transaction. Consequently, if you elect not to tender your bonds in any exchange offer there can be no assurance that you will receive any future payments in respect of your bonds.

Since 2005, the year in which Argentina began restructuring its debt, all budget laws include a mandate from Congress to the Presidents to restructure the debt until all debt in default is fully restructured. *Ibid* at 7-9.

dispute and had defaulted on its debt. The 2005 offer closed with a 76 per cent participation rate, representing a par value of $62.3 billion. Argentina had, by then, also repaid its official debt. The diminished debt overhang had allowed the country to grow in line with the expectations of the exchange bondholders.

In 2010, Argentina initiated a second exchange offer with a payment scheme substantially identical to the 2005 offer: The prospectus contained a similarly worded warning to creditors wishing to holdout,[85] and the Lock Law was suspended by the executive. Again, following these two workouts, Argentina restructured close to 92 per cent of its defaulted external debt. This restructuring was in line with market expectations as this outcome was roughly in line with debt workouts in the past.[86] Outstanding payments to the holdouts principal and interest payments on its defaulted debt amounted to $1.33 billion.[87] As in 2005, this default and restructuring were a sovereign act that were interpreted very differently when viewed through the lens of a contract law dispute. The Lock Law allowed Argentina to treat its exchange bondholders better than the holdouts, as the former had guaranteed access to payment streams denied to the latter. Argentina countered with the argument that,

> … the Passage of the Lock Law … merely prohibits the Executive from unilaterally settling defaulted claims or re-opening the exchange offer without Congressional approval, therefore did not create "a legal priority to those creditors that entered the exchange offer,"… the Law did not create any preferred creditor class.[88]

This argument would become the defining interpretation of this legislation to justify enforcement. The exchange bondholders accepted a significant discount on the face value of the FAA bonds in 2005 and 2010, as they relied on Argentina's "willingness and ability to make payments on the Exchange

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85. Existing defaulted bonds eligible for exchange that are not tendered may remain in default indefinitely. As of June 30, 2004, Argentina was in default on approximately US $102.6 billion of its public indebtedness.

    > The Government has announced that it has no intention of resuming payment on any bonds eligible to participate in [the] exchange offer … that are not tendered or otherwise restructured as part of such transaction. Consequently, if you elect not to tender your bonds in an exchange offer there can be no assurance that you will receive any future payments in respect of your bonds.

    Ibid at 7.
86. This practice is roughly in line with debt restructurings in the past.
87. The face amount of their FAA bonds was only $428 million; the lion's share of $1.33 billion claimed by Respondents represents interest on interest. Pert No 12-1494 at 11 (S Ct June 24, 2013).
88. Gulati & Scott, *supra* note 2 at 173.

Bonds."[89] Argentina fully honoured its obligations to the exchange bondholders until the second default in 2014.

NML was the lead litigant in the litigation triggered by the 2001 default.[90] The district court issued summary orders against Argentina, but NML had limited success in enforcing the judgment. The country had immunized its assets from attachment to avoid the restrictive immunity regime that has been in place in the US since 1976.[91] This immunization became the issue that eventually led NML to revive[92] an interpretation of the *pari passu* clause that was used in earlier litigation against Peru.[93] In 2011, the court accepted the NML interpretation of the clause. This was followed by a remedial order issued in 2012.[94] NML was now joined by numerous other "me too" holdouts, who all sought substantially the same relief. In exercise of his equitable jurisdiction, the judge ordered Argentina to pay the holdouts in full whenever payments were made to the exchange bondholders. The court enjoined any payments to the exchange bondholders

89. *NML II*, *supra* note 1, Exchange Bondholders Group, Petition for a Writ of Certiorari (No 13 - 251993) (Counsel Press, 2014) at 3 [EBG Cert Petition].
90. NML was eventually joined by 11 other holdouts. See *NML I, supra* note 1 at 3.
91. Carmine D Boccuzzi Jr, Michael M Brennan & Jacob H Johnson "Defences" in Lastra & Buchheit, *supra* note 2 at 106. Here, the authors discuss the issue of sovereign immunity restrictions being included in the standard waivers of jurisdictional immunity in the debt instruments and outside the contract "under the 'commercial activity' exception to immunity where the instrument provides for performance—that is payment—in the United States" (*ibid* at 106).
92. The interpretation was first raised by NML in 2004 but was withdrawn after the US DOJ and the Clearinghouse filed amicus briefs denying this interpretation. This was however before the Lock Law was passed by Argentina in 2005 and Argentina's continuing refusal to pay the holdouts. See *NML I, supra* note 1.
93. *Elliott Associates v Banco de la Nacion,* No 2000QR92 (CT App Brussels, 8th Chamber, September 26, 2000) [*Elliott Associates*]. The only instance in which holdout strategies were successful in enforcing a debtor's obligations was in *Elliot Associates*. The holdouts adopted an identical strategy by seeking to interfere with the payment flows to exchange bondholders to enforce repayment. The holdouts presented the same construction of the *pari passu* clause. This was upheld in a Brussels appeals court to suspend interest payments that were due on Brady bonds. To avoid default Peru settled out of court. The decision to settle was a political one. The concern raised at the time was that the availability of this threat gave holdouts the remedy of interfering with cross-border payments to exchange bondholders. The concern was that holdouts now had a veto over the regularisation of a country's relations with mainstream creditors and hence over its return to international capital markets. See Scott, *supra* note 29 at 6.
94. This was followed by an Order granting permanent injunction on November 21, 2012. The court relied on the case *Robert Pashaian v Eccelston Properties, Ltd*, 88 F (3d) 77 (1996). See *NML I*, *supra* note 1.

until such time as Argentina also paid the holdouts "the same fraction of the amount due them."[95] At the time of the hearing, the court

> …emphasised that (i) there was no legal authority for the requested injunction; (ii) it lacked the power to impose an otherwise non-existent condition on the Exchange Bondholders' rights to receive payments by requiring simultaneous payments to [the holdouts]; and (iii) the requested injunction would impermissibly interfere with the Exchange Bondholders' property rights.[96]

The judge repeatedly stated that though "Injunctions have 'problems' and 'problems on appeal'… compelling [Argentina] to pay Respondents' private contract debt 'overrid[es]' Exchange Bondholders' Rights."[97] Unlike the holdouts who specialise in investing in distressed funds, the exchange bondholders[98] comprised a "wide swathe of the investing public, including pension funds, charitable foundations, and endowments."[99] Both the *pari passu* interpretation and the injunctive remedy were unprecedented. The structural problem of weak enforcement would see a further expansion of the court's attempt to enforce the debtor's obligations. Further, the court's powers extend beyond the parties to the dispute: They affected the exchange bondholders and institutions in the clearing system as a whole. This injunction was affirmed by the Second Circuit.[100]

Before the District Court made its ruling, contrary decisions were being made in other courts.[101] An English common law court upheld a ruling rejecting the argument "that a *pari passu* clause entitles creditors to injunctive relief in 'a situation in which third parties are potentially exposed to penal consequences which could never be visited upon the defendant to whom the order is actually directed.'"[102] It was also argued that,

> [t]he effect on third parties also undermines the equitable basis of the injunction … [it] is designed to hold exchange bondholders and payment intermediaries

95. *NML I*, *ibid* at 5.
96. EBG Cert Petition, *supra* note 89 at 8. This was the position also taken by NML's counsel who "admitted that the Injunctions would engraft a 'condition' on the Exchange bondholders' ability to enjoy their own property that otherwise does not exist" (*ibid* at 9, n 6).
97. *Ibid* at 9, n 9.
98. A subset formed the group that filed the writ petition. On the whole the "outstanding amounts owed to Exchange Bondholders totals over $24 Billion, over $1 Billion of which will be owed to [Exchange Bondholder] members." *Ibid* at 3.
99. *Ibid*.
100. *NML II*, *supra* note 1.
101. A German court also declined to grant the holdouts relief. See *ibid* at 9, n 11.
102. *Ibid*, citing *Kensington International Limited v Republic of the Congo*, [2003] EWCA 2331 (Comm) [*Kensington*].

> hostage—in effect to force Argentina to inflict the broadest possible harm (and thus to incur the greatest reputational cost) if it insists on refusing to pay holdouts. … why should investor A obtain relief that works by inflicting collateral damage on non-party investor B and on assorted non-pay financial intermediaries?[103]

What the courts overlooked in their dismissal of the Exchange Bondholders'[104] arguments about exceeding its powers was that NML actually "wanted as its remedy … a kind of inter-creditor obligation."[105] This raised a substantive issue rather than a remedial issue about the legality of the injunction. As in the case of a default, an interference with the payment stream by the injunction would constitute a taking of creditor property. The Exchange Bondholders argued in their cert petition that their "contract rights and the funds they are entitled to receive pursuant thereto constitute 'property' within the meaning of the Fifth Amendment, which 'is addressed to every sort of [property] interest the citizen may possess.'"[106] However unlike default, the court, not the debtor, was implicated in the taking. To make this point, they argued that their "fundamental constitutional rights protecting them from government action that seizes their property for the benefit of other private citizens" were being breached.[107] Thus in such a situation "[r]eview is necessary to protect the sanctity of private property ownership and resultant limitations imposed upon judicial power by the Constitution."[108] The Second Circuit dismissed their concerns and found

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103. Weidemaier, *supra* note 11 at 145.
104. The Exchange bondholder group was a subgroup of exchange bondholders who unsuccessfully attempted to intervene in the Court of Appeal in NML's suit.
105. See Gulati & Scott, *supra* note 2 at 175; see also Declaration of Stephen Choi, *NML I*, *supra* note 1 [Choi]. There, it was brought to the notice of the court that "[n]onpayment would have an immediate and irreversible negative impact on the Exchange bondholders." Regarding the substantive effect of the injunction, the court was informed that its "injunction takes two separate obligations (the obligation to pay the exchange bondholders and the obligation to pay NML Capital and the other holdouts) and makes satisfaction of one obligation (payment to NML Capital and the other holdouts) a precondition to satisfy the other obligation (payment to the Exchange bondholders)." Choi also stated that the injunction is different from more traditional means of enforcement in that it imposes a material increase in the risk of non-payment on another class of bondholders, the Exchange Bondholders, as the means to obtain payment for another class of bondholders, NML Capital and other holdouts. See Choi, *ibid*, at paras 7, 13, 14.
106. EBG Cert Petition, *supra* note 89 at 25, n 17 citing *United States v General Motors Corporation*, 323 US 373 (1945).
107. *Ibid* at 16.
108. *Ibid* at 25.

in a footnote that "the … injunctions do not deprive Exchange Bondholders of any property."[109]

The court also stated that "the [Exchange Bondholders] can also sue [Argentina] if the injunctions lead to default."[110] This suit was not possible for several reasons. For one, as the Exchange Bondholders stated, "[i]f [Argentina] is forced into default … then the court will have already caused grave losses to the Exchange Bondholders."[111] In a declaration made to the District Court on behalf of the Exchange Bondholders, Stephen Choi stated why this loss would occur: The injunction would, he declared "materially increase the risk of non-payment for the Exchange Bondholders."[112] The injunction, he further argued, would have an "irreversible and negative impact" in addition to not receiving interest and principal payments. He also stated that "[n]on-payment will also result in a likely large decline in the price of the Exchange bonds … making it difficult if not impossible for Exchange bondholders to exit their positions through sales to other investors."[113] Choi's assessment was based on his examination of "several market metrics for the Exchange bonds [which] indicate a significantly increased risk of default following the Second Circuit's *NML Capital* Opinion."[114] Choi highlights the complexity mentioned above that makes such enforcement impossible without affecting third party claims. Though Argentina did eventually default as the injunctions blocked payments to the exchange bondholders, Choi had argued earlier that Exchange Bondholders had no option but to wait for the resolution of the dispute or sue the debtor to enforce their contracts.[115] Suing for enforcement was not problem-free, as this would come up against the structural flaw of weak enforcement. The EBG thus argued that "suit against the Republic would be futile; any judgment would go unsatisfied as demonstrated by [holdouts'] failure to collect monetary judgements against [Argentina] to date."[116]

The order also prohibited agents and other participants in the clearing system through which payments were made from "aiding and abetting Argentina's

109. *NML II*, *supra* note 1 at 14, n 10.
110. *Ibid*.
111. EBG Cert Petition, *supra* note 89 at 29, n 22.
112. Choi, *supra* note 105 at para 7.
113. *Ibid*.
114. Choi, *supra* note 105 at para 18.
115. To limit their financial losses they could follow Elliot, the parent company of NML Capital, and make a bet on default [by acquiring] "approximately $100 million of credit default swaps that pay off only if Argentina defaults on its obligations to the Exchange bondholders" (*ibid* at para 18).
116. EBG Cert Petition, *supra* note 89 at 29, n 22.

violation of the court's order."[117] Under the indentures of the Exchange bonds issued in the two workouts, Argentina made principal and interest payments to a trustee in Argentina who, in turn, made an electronic funds transfer (EFT) to US-registered Exchange Bondholders. The EFTs are made from the trustee's non-US bank to the registered holders' US bank, often routed through one or more intermediary banks. The court stated that the "Trustee is a fiduciary of the Exchange Bondholders, and not an agent of [Argentina]."[118] Hence, "[o]nce money has been transferred to the Trustee, it is the property of the Exchange Bondholders 'and [Argentina] shall have no interest whatsoever in such amounts.'"[119] As discussed above, this statement indicates the nature of the underlying substantive property claims in the bond contract: Once the contract is formed, the substantive property claim covers all monies actually transferred. In addition to the exchange bondholders, the injunction would cover third party intermediaries including the Bank of New York Mellon (the trustee for the exchange bondholders), the registered owners of the exchange bonds, and relevant clearing systems such as the Depository Trust Company and Euroclear. The EFTs made from a non-US bank are immunized from attachment by US courts as the bank is located outside the territorial jurisdiction of the US under the *Foreign Sovereign Immunities Act* of 1976.[120] However, the court did not discuss "the [Exchange Bondholders'] arguments that the Injunctions impermissibly harm innocent third parties and violate the EBG's Fifth Amendment rights."[121]

Argentina then filed a Writ petition in the US Supreme Court in February 2014 to present two questions. The first was on the issue of the *pari passu* interpretation; the second asked whether the district court has jurisdiction to "coerce a foreign sovereign into paying money damages, without regard to whether payment would be made with assets that the FSIA makes immune from "attachment, arrest and execution."[122] Several amici filed briefs in support

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117. *NML II*, *supra* note 1 at 255.
118. *Ibid* at 4.
119. *Ibid*.
120. *Foreign Sovereign Immunities Act*, USC § 6604 (1976). This act contains the sole, comprehensive scheme for obtaining and enforcing a judgement against foreign states in US Courts. See also *Argentine Republic v Amaerade Hess Shipping Corp*, 488 US 428 (1989); *Af-Cap Inc v Republic of Congo*, 462 F (3d) 417 (5th Cir 2006). FSIA "prescribes…[the] circumstances under which attachment and execution may be obtained against the property of foreign states to satisfy a judgement.". Its enactment in 1976 codified a partial lowering of the absolute immunity from suit and execution previously granted to foreign states at common law as a "a matter of grace and comity."
121. EBG Cert Petition, *supra* note 89 at 12.
122. Argentina Writ, *supra* note 81 at 25.

of Argentina's petition, including Joseph Stiglitz, Fintech Advisory Inc (an Exchange Bondholder), Mexico, and Brazil. This petition was dismissed on June 24, 2014. The EBG also filed a supporting petition in their capacity as "innocent non-party bondholders" who had suffered injuries "as a result of the injunctions issued and affirmed by the courts below." On appeal to the US Supreme Court, the Exchange Bondholders[123] raised this extension of powers as one of the central grounds on which to grant their writ petition. They argued:

> [T]his case presents the important and unsettled question of whether a federal court has the power to enter an injunction that intentionally takes and uses the private property of unoffending non-parties to a contract dispute as leverage to coerce payment of an otherwise uncollectable money judgement for the sole benefit of private litigants.[124]

They also argued that "it is not the Republic, but the district court that is taking non-parties hostage"[125] and that to do so was contrary to established precedent which:

> [D]id not address or purport to impact non-party interests in any way. It was the *defendant* that threatened to harm non-parties if the injunction was granted. In contrast … No harm was threatened to the EBG until the district court crafted unprecedented Injunctions that explicitly targeted their property … as leverage against the Republic attempting to circumvent the FSIA.[126]

The holdouts' appeal to the court's equitable jurisdiction followed years of unsuccessful attempts by the holdouts to enforce money judgements against Argentina. This appeal was part of a legal strategy that consciously avoided "securing a money judgement in an effort to portray unexceptional claims for contract damages as claims for equitable relief."[127] However, the court did not have to exercise its equitable powers. The EBG cited precedent on this point that found "[A] court may have jurisdiction over an action against a foreign state and yet be unable to enforce its judgement" and plaintiffs in such cases "must rely on the government's diplomatic efforts, or a foreign sovereign's generosity to satisfy

123. *NML I*, *supra* note 1 at 9.
124. EBG Cert Petition, *supra* note 89 at 16.
125. *Ibid* at 23.
126. *Ibid* at 24.
127. *Ibid* at 19.

its judgement."[128] Their arguments were dismissed in *NML I*.[129] Further, these petitions were ultimately dismissed by the US Supreme Court on June 24, 2014. In the face of the injunction Argentina defaulted on its payments to the exchange bondholders. This triggered a second default on July 30, 2014.

These lower court decisions are cited by Argentina's writ of certiorari as raising policy implications "of immense importance to all sovereigns, their creditors, and the international financial markets."[130] One implication is that the court can grant "by injunction an enforcement remedy that it cannot provide by an execution device, because to do so would render [sovereign] property immunities a nullity."[131] Another is that this innovation "permit[s] US courts to use their coercive powers to restrain sovereign property located outside the United States." By extension, this innovation represents "an unprecedented intrusion into the activities of a foreign state within its own territory that raises significant foreign relations concerns for the United States." Argentina claimed that an extraterritorial order that aims "to dictate the disposition of a foreign state's assets contravenes established precedent on comity."[132] The courts also overlooked the self-help remedies specified in the bond contract such as acceleration.

Eventually, the injunction was lifted on two conditions: (1) Argentina would make full payment to the holdouts in full satisfaction of their claims and (2) repeal all the legislation that prevented the state from repaying them. A court order in a private law dispute thus repealed legislation passed by a sovereign within its own territory, though the resolution of the issue was eventually achieved through

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128. *Ibid* at 19, citing *FG Hemisphere v Democratic Republic of Congo*, 637 F (3d) 373 (DC Cir 2011).
129. The Second Circuit found that "the FAA does not contain a clause limiting the remedies available for a breach of agreement. Nor does it contain a provision precluding specific performance or injunctive relief." Once the SDNY had established a breach of contract and the grounds for injunctive relief, it found that the "court had considerable latitude in fashioning the relief." This would be true even in situations where the performance required by a decree goes beyond that promised in the contract. See *NML I, supra* note 1 at 23. In situations "where 'the most desirable solution' is not possible, this Court may affirm an order of specific performance so long as it achieves a 'fair result' under the 'totality of the circumstances.'" See *NML II, supra* note 1 citing *Leasco Corporation v Taussig*, 473 F (2d) 777 (2d Cir 1972). The Court found that monetary damages were not an effective remedy for the 'harm' NML had suffered as a result of the breach. The finding was justified by the evidence that Argentina would simply refuse to pay any judgments. The court further found that "Even if damages are adequate in other respects, they will be inadequate if they cannot be collected by judgment and execution." See *NML I*, *supra* note 1 at 24.
130. Argentina Writ, *supra* note 81 at 2.
131. *Ibid*.
132. *Ibid* at 4.

political change. While the new government in Argentina was more amenable to repaying the holdouts, in the main this resolution was driven by its need to regain access primary capital markets—which it eventually did.

Another key concern raised in this litigation was the practical effect of enabling "a single creditor to thwart the implementation of an internationally structured restructuring plan."[133] This concern was raised in the US government's amicus brief supporting Argentina (unlike the *Allied* cases, in which the DOJ supported the holdout claim).[134] In response, the court made two moves in exercising its significantly expanded enforcement role. First, it secured the holdouts' enjoyment of their bonds irrespective of the risks they took in buying sovereign debt. Second, the court secured the holdouts' freedom to use their bonds for their own enjoyment irrespective of the consequence of this enjoyment for others. These are the two key incidents of sovereign debt in its commodity form, as they evolved as an unintended consequence of enforcement litigation. These incidents are discussed in more detail in Part II.

II. SOVEREIGN DEBT AS A COMMODITY

Following from the discussion in Part I, sovereign default justifies enforcement action to compensate creditors for the harm caused to them—though it is not clear how the creditors are harmed. The consistent position taken in the *Allied* cases by the official sector amici, the market, and the courts was that there was damage to creditor's property. But the legal nature of this property and how it arises is unclear. What is clear is that the basis of the harm caused to the creditors was a contractual breach by the debtor. What is also clear is that the sovereign would be held to the payment promise it made to the harmed creditors. This section fills the conceptual gaps from a contract law perspective and, in doing so, reveals the commodity form that debt takes as an unintended consequence of the courts' expanded enforcement role. The implications of this commodity form are also discussed in this section.

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133. *NML II*, *supra* note 1, Joseph Stiglitz Amicus Brief in Support of Petitioner dated 24 March 2014 in petition to the United States Court of Appeals for the Second Circuit at 7 [Stiglitz].

134. The court confined the impact of their decisions to Argentina on the grounds of the widespread adoption of "Collective Action Clauses" which will "effectively eliminate the possibility of 'holdout' litigation." The effectiveness of these clauses was raised but dismissed. This has since been raised by the government of Mexico in its amicus brief. EBG Cert Petition, *supra* note 8 at 18a, paras 25-26.

A. A CONTRACT LAW PERSPECTIVE

1. ASSUMPTIONS

This section begins with a few simplifying assumptions. First, for the purposes of developing this perspective, sovereign debt contracts are assumed to be a *sui generis* category of contracts.[135] This assumption partly accounts for the uniqueness of the sovereign debt market as a contracting environment.[136] It also partly accounts for uniqueness of the bond contract itself.[137] Second, sovereign bond contracts are assumed to be voluntary[138] transactions and as such are distinct from tort and unjust enrichment claims. This voluntariness is also assumed to be the basis of the obligations of both the sovereign and its creditors. It follows then that "the contractual rights and duties between the parties are completely specified and determined at formation"[139]—that is, when the bonds are purchased.[140] It also follows that,

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135. This is a simplifying assumption—sovereign bond contracts do not fall into the categories of contracts normally thought to be within the domain of contract law. This assumption is necessary as there is currently no theory of sovereign debt contracts requires a theory of sovereign debt contracts and is beyond the scope of this paper. Such a theory would, for instance, specify the different necessary and sufficient foundations of a debtor's legal obligations. See Alan Schwartz & Robert E Scott, "Contract Theory and the Limits of Contract Law" (2003) 4:113 Yale LJ 541.
136. This uniqueness is attributed to two features by Gulati and Scott. "On the one hand, given their official status these bonds are often considered to be the most risk-free of any securities… On the other hand, sovereign bonds are, in one sense, amongst the riskiest of investments: Because of their sovereign status, governments can default with impunity." See Gulati & Scott, *supra* note 2 at 53.
137. *Ibid*.
138. This is a contested premise as it avoids questions about the differing conceptual basis of consent and necessity especially in post-default situations where arguably sovereigns have no option but to refinance their obligations and creditors have no option but to accept the debtor's offer. Here an attempt is made to address what Peter Benson has called a "unified and coherent moral basis for contract." See Peter Benson, "Contract as a Transfer of Ownership" (2007) 48:5 Wm & Mary L Rev 1673 at 1673.
139. *Ibid* at 1674.
140. In cases where a sovereign issues debt for the first time, the sovereign and the lead underwriter negotiate over the deal documents and the debt is then sold to the clients of the underwriter. In cases where debt has recently been issued, the deal documents used to issue this debt would be used as templates. These are boilerplate contracts and "[a] sovereign that is new to the markets has an incentive to use the standard provisions as far as possible." In situations where new debt is issued as part of a restructuring, the sovereign debtor often makes "a unilateral offer to the existing creditors" which they accept if the debt workout settles. In both situations, it is assumed that the contract between the sovereign and its creditors is formed when the debt is purchased. See Gulati & Scott, *supra* note 2 at 29.

> The character and the shape of these rights is reflected in the fact that they are specified only as between the parties, not against others who are strangers to the contract and that their breach is remedied through damages or specific performance, both of which aim to put the plaintiff [creditor] in the position he or she would have been in had the defendant [debtor] performed as promised.[141]

Third, it is assumed that the breach of the sovereign debtor's promise and the harm caused to the creditor are juridically significant for the purposes of enforcement. Fourth, the creditor has ownership and property rights. The distinction between the two rights will become clearer as the discussion proceeds. Fifth, it is assumed that contract "law supposes that these remedies are necessary and sufficient to enforce by way of compensation, the rights and duties that are brought into existence by the parties' consent at contract formation."[142] Finally, it is assumed that this commodity form is unique, having developed as judges respond to debtor intransigence and thus negotiate the structural flaws in the international debt market as explained above.

This section relies on Peter's Benson's article "Contract as a Transfer of Ownership"[143] to clarify the nature of debt as a commodity as an unintended consequence of enforcement in the circumstances described. There are two main reasons why Benson provides a good starting point for this discussion. First, he establishes promises as the source of ownership rights in contract law. This proposition is consistent with the view of the court in the enforcement decisions. Second, Benson makes a distinction between contract as a transfer of ownership (his view) and contract as a transfer of property (Kant's view). The significance of this distinction will become clearer during the course of this discussion.

2. STYLIZED EXPLANATION

Based on the assumptions made above, this section develops a stylized description of the consequences of the enforcement litigation. On the formation[144] of a contract between D (a debtor) and C (a creditor), D promises to (re)pay C a defined sum of money. In addition to this promise, C acquires ownership rights

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141. Benson, *supra* note 138 at 1674.
142. *Ibid*.
143. For the purposes of this paper we are not concerned with Benson's examination of the expectation interest as the basis of compensation in contract law.
144. This is consistent with Benson's analysis, as when he states that "the legal principles governing the requisite assents—the doctrine of offer and acceptance as well as consideration—do not single out enforceable promises on the basis of their substantive content, purposes or economic significance. [Thus when it comes to enforcement] the principles of formation are content-neutral and indifferent to such considerations." See Benson, *supra* note 138 at 1677.

that are transferred through mutual assents at the time of formation.[145] A key element in the subsequent enforceability of this contract is C's acquisition of a proprietary interest in some *thing* that is yet unclear. As noted, the acquisition of a property claim by C from D is central to the judicial justification for enforcement.

If D fails to pay (and thereby does not fulfil his or her promise to pay C) then a court will enforce the contract on the grounds that C's proprietary right has been damaged. Enforcement is necessary to protect C by compensating him for the damage caused to his or her property. The question that arises here is: How does C obtain a legally protected interest? Further, does this interest include non-proprietary ownership rights to acquire, retain, and alienate the debt? The courts in the cases examined above answered this question by assuming that the debt contract itself is the source of C's rights.[146] Thus on formation, it is assumed here that the source of C's rights is D's promise to pay.[147] This focus on D's promise as the basis of C's rights is consistent with promissory theories of contract.[148] Yet D's promise is one of many different ways to explain the source of C's rights.[149] This promissory view is not immutable or fixed *a priori*, but is a function of the context in which the *Allied* cases were decided: The debt market was in transition, and attempts were being made to secure the banking system in the

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145. According to Benson, the ownership rights recognize the thing transferred to be "physically separate from individuals and also must be acquirable by individuals acting unilaterally that is, without the actual consent or participation of others. The idea of social cooperation plays no role here whatsoever." The ownership claim is individually enforceable and does not factor in any "social cooperation." See *ibid* at 1699.

146. *Ibid* at 1677.

147. In defence of this view Benson states "[a] promise of something in return for another's refraining from an activity he or she is legally permitted to do, as in the famous case of *Hamer v. Sidway* has the same legal standing and significance as the most sophisticated and commercially important business deal." *Ibid* at 1678.

148. There are different promissory theories of contract law. Benson defends a promissory theory of enforcement to counter an alternative reliance theory discussed in Fuller and Purdue. See L L Fuller & William R Perdue, Jr, "The Reliance Interest in Contract Damages: 1" (1936) 46:1 Yale LJ 52 ["Contract Damages 1"]; L L Fuller & William R Perdue Jr, "The Reliance Interest in Contract Damages: 2" (1937) 46:3 Yale LJ 373.

149. A very different justification for enforcement would be to follow a view in which "property and promises" are radically distinguished. Here "[p]roperty, but not promise, expresses a right of ownership in the large sense of having something of one's own from which one is entitled by rights to exclude others" (italics omitted). The justification for enforcement that follows from this view is that "certain promises should be enforced … not because they are understood as conferring ownership or creating a relation of exclusive right as between the parties but simple and solely because enforcement is desirable on the basis of policy considerations." Benson, *supra* note 138 at 1679 [italics omitted].

US through several interventions such as the Baker and the Brady Plans.[150] The debt market was securitized, loan agreements were being replaced by bonds, and heterogeneous private creditors—mainly non-bank commercial institutions—were replacing banks. The risks of lending to sovereigns in this context were shifted onto private investors, reducing the systemic threat to the US banking system. The judicial intervention in *Allied* can therefore be seen as an attempt to enhance creditor protection by recognising that the sovereign promise to pay is creditor property. On default, this recognition would, in theory, ensure enforcement. This understanding was a legal fiction. Given weak enforcement, the task of finding sovereign assets to satisfy creditors' claims is next to impossible.

In a typical debt issuance, the debt contract is purchased and the debtor fulfils a promise to pay by making regular payments of principal and interest owed over the life of the bond until redemption. One way to explain why the promise is significant is to view C as deferring the consumption of resources today to a point in the future at which the debt is repaid. Thus C is giving up a beneficial opportunity that he or she "would take but for the promise."[151] Therefore if D defaults, C will not be able to go back to his or her pre-contractual position, as that opportunity may no longer be available.[152] Thus the basis for compensation is an injury (a loss of an opportunity) to C that comes under his or her *exclusive* right against D. It is this need for exclusivity that raises the issue of "whether there can be such entitlements at the moment of contract formation and therefore fully established solely through the parties expressions of mutual assent."[153] Given the transactional context of the enforcement decisions, the focus of the rulings was clearly to recognise and protect C's entitlements obtained exclusively from D (and which D must eventually compensate C for) rather than other creditors or any other third party.

Following from the discussion above, it is clear that the *NML* court imposed a constraint on the entitlements of exchange bondholders, *not on D* as should

150. The Baker and Brady Plans were rolled out in 1985 and 1989 respectively. The Plans were attempts to limit the impact of expected debt defaults across Latin America on the US banking system. The successful Brady Plan was premised on the securitization of US commercial bank loans to Latin American sovereigns leading to the eventual development of modern sovereign bond markets.

151. *Ibid* at 1679.

152. This is Benson's argument against the "reliance interest" as the basis for compensation. He argues that "the reliance remedy cannot itself count as compensatory unless it repairs injury to something which comes under the promisee's exclusive right as against the promisor" (*ibid*).

153. It is the search for such entitlements that raise the issue of property claims that underpin the justification for enforcement in the promissory theory.

have happened. In response to debtor intransigence, the court contravened the contract law analysis set out above. The decisions were not supported by precedent. However, they were affirmed repeatedly, while the contracts were enforced and the holdouts were paid in full. The implication is that there exists no immutable, *a priori* common law template for enforcement. While it is possible to argue, for instance, that there are sound policy reasons for enforcement, such as an intransigent debtor and the lack of attachable assets,[154] the precedential constraints on the court were removed so the courts rely on policy arguments to justify their decisions. As described above, this outcome reflects the context in which the court is making the decision: The sovereign immunity analysis in the EBG petition reveals that the court had no choice but to take this route because any attempt to attach D's property would be extra jurisdictional and contravene sovereign immunity restrictions.[155] Therefore, from the contract law perspective developed here, there is no common law justification[156] for the judicial intervention in the *NML* litigation. Nevertheless, the decision is still binding. This outcome indicates the legal indeterminacy that marks judicial interventions in contract disputes in general: There is no one template for enforcement. The discussion here is not meant to justify a contractual argument or to counter the courts' decisions but to highlight: the creation of a legal fiction that debt is a commodity.

This development leaves open the question of how this fiction was engendered in contract law? An answer requires an examination of the basis on which C obtains an exclusive entitlement from D. This is where contract law intersects property claims. In the decisions discussed above, the courts and amici claimed consistently that D's action contravened C's due process rights. One way to understand this claim in contract law is as follows: On default D breaches the contract and thereby interferes with C's protected interest or entitlement. This interpretation presumes a prior view of the contract itself. In a manner consistent with the decisions discussed above, it is assumed that at one level the courts viewed the contract as a transfer of ownership. The object transferred "is a corporeal object" that is physically separate from both C and D and must be acquired by them "acting unilaterally, that is, without the actual consent or participation

154. As mentioned above, Fuller and Purdue offer a reliance based justification for enforcement which is distinct from the promissory account discussed here. See "Contract Damages 1," *supra* note 146.
155. Weidemaier, *supra* note 11 at 149.
156. As the English courts found in *Kensington*, *supra* note 102.

of others. The idea of social cooperation plays no role here whatsoever."[157] This transfer happens on formation of the contract between D and C.

One candidate for the corporeal object independent from both C and D is the bond certificate.[158] Once the bonds are purchased, D issues C with a bond certificate as proof of this transfer. However, this explanation—without more—does not clarify the significance of D's promise in defining C's entitlements, as discussed in the preceding paragraph. The bond certificate is a symbol of C's ownership and a necessary incident of ownership as it signals to third parties that C owns, and thereby controls, the bonds. C can appropriate the bonds (*i.e.*, take possession), can use them in any way he thinks fit, and can alienate them when he wishes. Once C's ownership rights have been established, on breach they provide justifications for enforcement—the courts must enforce contracts to protect C's ownership to acquire, use, and alienate his or her debt. As Benson notes, in the "contract as transfer of ownership view … [t]he only thing that the right ensures is that no one else can rightfully appropriate, use, or alienate the owner's object without his or her consent."[159] According to him, "the right of ownership is defined simply as an abstract right to exclude others from treating it as their own."[160]

Benson's description is premised on a distinction between a transfer of a physical thing and the agreement itself. In the case of a bond contract, does the agreement itself signal the incidents of ownership?[161] Does D then transfer something more than the debt instrument to C? One way to answer these questions is to draw a distinction between formation—the agreement between C and D—and the actual physical delivery of the debt instrument. It is the agreement that produces what Benson refers to as the juridical effect of ownership on the physical transfer of the debt instrument. He states that "[m]utual assent [between C and D] is the regulative normative idea. It is signalled through the physical acts of transfer."[162] It follows then that the physical instrument itself has no intrinsic significance, but the agreement that necessarily precedes the physical delivery of the thing does. According to Benson, once "the requisite assents exist, the question of contractual rights and duties is answered. There

157. Benson *supra* note 138 at 1699.
158. "A printed document certifying a debt owed. A bond certificate typically includes the issuer's name, the face value, interest rate, interest payment schedule." Investor Guide, "Bond Certificate," online: <http://www.investorguide.com/definition/bond-certificate.html>.
159. *Supra* note 137 at 1702.
160. *Ibid* at 1703.
161. *Ibid* at 1726.
162. *Ibid* at 1705.

is no further issue as to why the promisor must perform as promised."[163] It follows then that D's breach is an interference with the interest C acquired when the contract was formed. This answer is only a partial explanation and does not capture the uniqueness of the debt dispute, which involves intangible property. The *Allied* court unequivocally viewed D's default as a taking of C's property. Benson's account of contract as a transfer of ownership explains that a breach is significant because it damages C's ownership rights. In his view there is no property transferred—just ownership rights. This understanding is true of sovereign bond creditors, who enjoy ownership rights during the lifetime of the bond. On default these ownership rights are lost and C is harmed, but in the context of weak enforcement the harm caused to C is perceived to be more than just the loss of ownership rights: There is damage to his or her proprietary rights. This raises further questions. At what point, and how, does C obtain ownership of this property? This proprietary interest must be explained independently of physical delivery.

Benson makes a distinction between ownership and property: "*Ownership* is a more general conception consisting of any right to exclusive possession, use, or alienation of something as against another or others. *Property* is a particular instance of ownership and more precisely a specific form of acquisition"[164] Benson further distinguishes between contractual rights as ownership rights and contractual rights as property rights. He confines the latter to instances where the rights are "acquired by a unilateral act of will that requires initial physical occupancy of an external corporeal object, contract rights on other hand are acquired through the mutually related acts of two parties without the necessity of physical occupancy."[165] This explanation of ownership on its own does not capture the intangibility of debt obligations as there is no "unilateral act of will that requires initial physical occupancy."[166] Hence this view of ownership is only a partial explanation as far as intangible obligations are concerned.

In response to the question, "what exactly is the object C acquires by contract?", Benson provides two answers: (1) contract as a transfer of ownership and (2) the Kantian view of contract as a transfer of property. Both are examined here, though it is clear that the second view is consistent with the enforcement decisions discussed in Part I. This explanation also forms the basis of an account

163. *Ibid* at 1707.
164. *Ibid* at 1719 [emphasis in original].
165. *Ibid.* See also *ibid* at 1966. In Benson's explanation, physical occupancy refers to one who exercises control over a corporeal thing in private law doctrine.
166. *Ibid* at 1719.

of how sovereign debt acquires its commodity form in the law. In his discussion of the Kantian approach, Benson notes "the other party's performance or promise, not the thing promised, is the substance and object of the ownership that is acquired by a contract."[167] Using the example of the sale of a horse, Kant argues as follows,

> the object that I acquire by the contract is not at all the horse. My contract right is not with respect to the horse. The horse comes under my right of ownership only upon delivery, and then it becomes the object of my property right. At contract formation, and therefore prior to delivery, all that I have acquired is the other's deed by which that thing [that is the horse] is brought under my control so that I make it mine. Kant expresses this idea by saying that what a party acquires at contract formation is not the thing promised *but the promise itself*.[168]

Benson is critical of this formulation on the ground that in this view "the relation of rights between the contracting parties is one thing at contract formation and something different upon performance."[169] He further highlights the discrepancy between the promisee's position at formation and the rights acquired by the promisee on delivery of the thing transferred.[170] The focus of Benson's discussion is on actual physical transfers of things and services, rather than transfers of intangible debt obligations. This criticism does not apply to the sovereign debt market, given the nature of the transactions and how debt obligations are transferred. He partially agrees with Kant's view that "that the object transferred is the promise and not the thing promised [and that this] necessarily implies a change of ownership with respect to the thing as between the parties at formation."[171] However, unlike Kant, he recognises the ownership right as "a non-proprietary right of ownership that is wholly transactional as between the parties alone."[172] This view is, however, inconsistent with the approach taken by the courts.

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167. *Ibid* at 1720.
168. *Ibid* citing Immanuel Kant, *The Metaphysics of Morals* (1797), reprinted in Mary J Gregor ed, *Practical Philosophy* (New York: Cambridge University Press, 1996) at 424 [emphasis added].
169. *Ibid*.
170. Benson, *supra* note 138 at 1720. Benson argues that the Kantian approach leads to a situation in which the promise's right to performance can only be understood as a personal right against the promisor. If a third party unintentionally damages the thing promised after the contract has been entered into, but before performance has taken place, the promisor, not the promise, has standing to sue for the damage. The promisee can make such a claim only after he or she has taken possession of the thing via delivery. At this point, the promise acquires title and has the same right with respect to the thing as did the promisor (*ibid*).
171. *Ibid* at 1722.
172. *Ibid* at 1723 [emphasis omitted].

B. DISCUSSION

As discussed in the section above, the judicial decisions implicitly conflate what are otherwise two conceptually distinct aspects in Benson's formulation of "contracts as transfer of ownership"—that is, formation and performance. In the context of sovereign debt, the object that is transferred on formation is D's promise to pay. This transfer ensures that the promise to pay is now within the actual control of C. In other words, the decision about whether or not to pay (for instance to avoid a national emergency) is no longer within the authority and competence of D but has been transferred to C on formation of the contract and comes under his or her authority. This conflation of formation and performance obviates contract terms such as the self-help remedies specified in the debt contract. In the *Allied* cases, there was limited discussion of contract terms. In *NML*, on the other hand, debtor intransigence made the interpretation of the *pari passu* clause the central issue and defined the eventual remedy. The explanation here is dependant on the underlying substantive property claim.

It was clarified in *NML* that the source of a creditor's contractual entitlement to compensation is the sovereign's "promise to pay" which, in these cases, is also the source of the property rights of its creditors. There are therefore twin, interlinked justifications for enforcement: a failure of the sovereign to fulfil its promise to pay and the consequent damage to the creditor's property rights. To justify enforcement, both the sovereign's promise to pay and the creditor's property rights are juridically significant. In enforcement litigation from *Allied* onwards, creditor's property rights can only be protected if the sovereign fulfils its legal obligations to pay in full and on time. Here the combined justification for enforcement is a response to unique post-default circumstances. This combined justification also reflects how the courts manage the uncertainty inherent in the contracting context to achieve enforcement as an outcome. This intersection between the fulfilment of a sovereign's promise and the property rights of creditors as the basis for judicial enforcement characterizes the commodity form of debt.

In the law, the debt contract is defined as C's property. It is abstract, fixed *a priori*, and by definition once formed cannot change with the changing relationship between the parties or the changing transactional context (*i.e.*, market conditions). The onus is on the courts in their enforcement role to ensure that C enjoys this property and that his or her enjoyment is protected whatever the cost to others. It is in this respect that the debt contract acquires its complete commodity form. The acquisition, use, and alienation (*i.e.*, ownership rights) associated with a complete commodity do not have any externalities—or at least none that cannot be remedied with more enforcement action. Debt once purchased can be enjoyed in full without hindrance.[173] This fiction corresponds to the way in which commodities are assumed to flow in real markets: They are interchangeable with other commodities of the same type. They are fungible and commensurable in the sense that their value can be reduced to a market price as a common metric.[174] The legal fiction described above justifies intervention aimed at ensuring that debt instruments remain liquid and tradable. Such intervention is akin to a regulatory role: Courts in their expansive enforcement role have become regulators.

As has been discussed above the history of sovereign debt is the history of the countervailing pressures that lead to the commodification of sovereign bonds. Debt as a commodity is a legal fiction to justify enforcement and, as will be shown, also (worryingly) justifies official intervention in sovereign debt markets. This commodity fiction, however, embodies "two opposite elements and neither of them can be taken to its logical extreme without annihilating the other."[175] Legal uncertainty is an implication of the precarity that underpins the recognition of this legal fiction, which is discussed in Part III.

III. THE IMPLICATIONS OF THE COMMODITY FUNCTION

Whatever may be the problems of sovereign debt, the evolution of debt as a commodity fiction implicitly acknowledges that this fiction does not exist in real markets. Rather, it exists only as an outcome of courts' negotiation of the structural flaws in the market. But as this paper has argued, these deliberations are not confined to the judicial imagination or abstract legal categories. They matter in the real world, as the experiences of Costa Rica, Argentina, and the exchange bondholders attest. In *Contested Commodities*, Margaret Jane Radin offers a terminology for exploring the dichotomy between deliberations and actions in the real world. She distinguishes between literal and metaphorical markets. In literal markets, "things are exchanged for money under certain social conditions. Sellers deliver goods to buyers' buyers deliver money to sellers."[176] In metaphorical markets, "social interactions that do not involve actually handing

173. It is difficult to create a liquid market for a set of bonds when the various bonds within that set have different terms whose risks need to be evaluated and estimated individually.

174. The concept of commensurability is contested and the meaning adopted here is from Margaret Jane Radin, *Contested Commodities: The Trouble with Trade in Sex, Children, Body Arts and Other Things* (Cambridge, Mass: Harvard University Press, 2001) at 118.

175. Duncan Kennedy, "The Role of Law in Economic Thought: Essays on the Fetishism of Commodities" (1985) 34 Am U L Rev 939 at 961.

176. Radin, *supra* note 175 at 1.

over money for goods are talked about as if they did."[177] Radin also suggests that for theoretical purposes, the metaphorical market "is not necessarily intended to reflect people's actual understandings of themselves, their relationships, and activities, but rather *to make accurate predictions*."[178] As Radin understands it, commodification "elides literal and metaphorical markets … because there is no sharp divide between action and discourse—between the nature of a transaction and the discursive scheme or discursive framework in which we understand it."[179] My discussion of the conceptualization of sovereign debt as a commodity in law similarly straddles this divide between literal and metaphorical markets by offering a description of the reality of 'literal' sovereign debt litigation, the transactional context—which in turn is replete with the problems and inherent risks of sovereign lending—and the metaphorical scheme of contract law. This section extends this discussion with a view to drawing out the wider and deeper implications of the legal recognition of sovereign debt as a commodity. Apart from the fact that Radin's concerns are also about commodification and are therefore relevant for the discussion at hand, at a general level the key motivation for choosing her conceptual scheme to begin this section is her discussion of "universal commodification" as a "methodological archetype"[180] reflected in how neoclassical economic theorists see commodities in their theoretical frameworks.

A. THE METAPHORICAL MARKET

Is 'NML enforcement' informed by neoclassical economics, or is there evidence of theoretical influences that predate this literature? Gathii argues in his analysis of the *Allied* cases that the Second Circuit court was informed by classical legal thought of the "late nineteenth and early twentieth centuries the period of early capitalism in the United States [where] the judicial response to holdouts has been to understand freedom of contract as embodying freely made choices."[181] Further, these choices "should not be interfered with by either the lenders or borrowers or even the courts."[182] According to this worldview it is natural that debt contracts, once formed, should flow unhindered through the market, whatever the cost. Duncan Kennedy attributes the theoretical foundations of this view to neoclassical economics in his discussion about the role of law in economic

177. *Ibid*.
178. *Ibid.*
179. *Ibid* at 2.
180. *Ibid*.
181. Gathii, *supra* note 50 at 269.
182. *Ibid*.

thought.[183] There is some evidence that the view of debt as a commodity is consistent with neoclassical economics. More specifically, enforcement litigation and neoclassical economics may share the same worldview—in which case the prior question that must be asked is: What is the role of law in this context?

Kennedy offers the following simplified and stripped down version of the role of law in neoclassical economics:

> First, it is a condition of the theory of the efficiency of perfectly competitive markets that all valued experiences are commodities, and that there is no interference with exchange. Second, the model is often the basis for elaborate liberal arguments in favour of legislative reform designed to compensate for the inefficiency generated by deviations in the real world from the norm of competition.[184]

The question examined here is whether the view of debt as commodity as revealed in enforcement litigation shares the same understanding of the role of law. Kennedy's view is consistent with how the modern literature on sovereign debt has framed the problem of debt. The key problem regarding sovereign debt examined in the first generation of modern economic literature which developed in the 1980s was: Why would sovereigns repay their debts in a world where there is no enforceable remedy against them, as their assets are immunized from attachment? The answer was that debt is repaid as "defaults are economically costly for the debtor country,"[185] and that

> Countries will be able to borrow up to the point in which the temptation to default is balanced by its costs. In standard theories of sovereign debt, this level of debt is generally below the level at which countries would like to be able to borrow.
>
> It follows that attempts to reduce the costs of default could also reduce welfare because they would make sovereign debt more expensive and lower the maximum level of debt that a sovereign can accumulate. Conversely, attempts to improve enforcement could improve welfare even if they make debt crises more painful and protracted.[186]

The argument for defending enforcement (and resisting formal bankruptcy) was based on the ground that the alternative would eventually increase borrowing costs for debtors.[187] Thus, according to this view, enforcement per se is necessary "to compensate [creditors] for the inefficiency generated by deviations in the

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183. Kennedy, *supra* note 176 at 960.
184. *Ibid*.
185. *Sovereign Bankruptcy*, *supra* note 35 at 5.
186. *Ibid.*
187. *Ibid.*

real world from the norm of competition."[188] In this view the enforcement decisions are not only welcome but necessary.[189] Implicit in this validation of enforcement is the idea that this regime is "*the* legal regime that corresponds to full commodification and freedom of exchange."[190] More specifically, from the neoclassical perspective the argument being made here is that with this legal regime in place "it makes sense to say that there is a determinate efficient outcome for a perfectly competitive regime."[191] It can be argued that the NML enforcement template replicates enforcement as an efficient outcome for a perfectly competitive market. The implications of this view are discussed in more detail in section C, which follows an examination of whether commodification is actually evidenced in the literal market.

B. THE LITERAL MARKET

The discussions in this section illustrate the ways in which the commodification of debt actually plays out in literal markets. In his amicus brief in support of Argentina's writ of petition, Joseph Stiglitz highlights the wider implications of the *NML* decision for third parties.[192] He emphasizes the externalities that arise from the decision. Stiglitz also discusses how the decision makes the *pari passu* clause a "guarantee that any future creditors of any future bond issuance will not receive payment before the holdouts of any previous litigation."[193] He states that the benefits to the holdouts far outweigh what any other affected party will receive.[194] Stiglitz notes that the debtor will be adversely affected, as the decision allows the holdouts "to effectively thwart the debtor's ability to issue future debt … at any time thereafter."[195] Further, the decision creates "new uncertainty about the country's future and the size of its debt burden. The uncertainty itself would impede growth and access to credit, diminishing greatly the benefits of

188. Kennedy, *supra* note 176 at 960.
189. This argument is similar to the putative argument expressed as a defence of the NML enforcement decision: "... some might argue that this is exactly the bargain struck by an issuer … At the time of the loan, a sovereign may reap he benefits of such a promise in the form of lower borrowing costs, greater market access, and the like. So why should anyone object when it is later held to its promise?" See Weidemaier, *supra* note 11 at 145.
190. Kennedy, *supra* note 176 at 961 [emphasis added].
191. *Ibid.*
192. Stiglitz, *supra* note 133.
193. *Ibid* at 5.
194. They "will obtain full payment on Argentina's pre-default obligations—both principle and cumulative interest on defaulted bonds—rather than payment of the (marked down) restructured debt" (*ibid* at 6).
195. *Ibid*.

debt restructuring".[196] Finally, Stiglitz argues that the decision "could imperil the IMF's and the World Bank's ability to perform essential functions"[197] and, contrary to the opinion of the judge in the case, will trigger a "sovereign debt flight" away from the US markets.[198]

In the epilogue to their book *The Three and a Half Minute Transaction*, Mitu Gulati and Robert Scott also discuss the wider ramifications of the *NML* litigation. Their discussion illustrates the way in which the commodification of debt actually plays out in literal markets. They begin with a discussion of Ecuador—which defaulted on two of its bonds (due 2012 and 2030) in late 2008 but continued to service a third set of bonds due in 2015. The country was in financial difficulties but could pay with oil revenues. The government argued that it was justified in defaulting on the first two bonds as these were issued illegitimately by the previous governments. Ecuador argued that the bonds "were lacking in requisite formalities" and challenged some standard features of the sovereign bonds "such as the acceptance of jurisdiction in New York and the waiver of sovereign immunity."[199] This led to a response by the affected creditor community and there was a discussion of whether they could use the *pari passu* clause to seize the payments made to the third group of bondholders. The creditors preferred the interpretation of the clause that had been accepted by the Belgian court in 2000 in *Elliot Associates*.[200] Gulati and Scott note that this interpretation, "which seemed outrageous in the context of the Peruvian payments on its restructured debt in 2000, seemed to make intuitive sense with respect to Ecuador in 2009."[201] Although this course of action did not actually transpire, the episode has significant implications as it indicates the wider resonance of the idea that bondholder enjoyment should be protected and compensated through enforcement litigation, whatever the cost to third parties. The authors then discuss the Eurozone crisis, in which the litigation outcome would come to underpin the official sector response to the Greek debt crisis. They note that "the EU/IMF rescue facility that was put in place in early 2010" had a *pari passu* clause, and was "a loan facility designed to establish the rules governing the loan granted by the Eurozone nations to Greece."[202] Importantly, it was "not a public

196. *Ibid*
197. *Ibid* at 14.
198. *Ibid* at 17.
199. Gulati & Scott, *supra* note 2 at 167.
200. *Supra* note 93.
201. *Ibid* at 168.
202. *Ibid* at 169.

bond issuance."[203] The authors note that the inclusion of the clause suggests that it "provides the kind of protection that the creditors in this instance—the various eurozone nations participating in the loan to Greece—desired."[204] Although the clause was incorporated, it was not clear what its meaning was—or indeed what kind of protection the official creditors were getting because of it. The wider use of the *pari passu* clause is evidence—albeit slight—that debt as a commodity form elides both literal and metaphorical markets.

C. THE NATURE OF LEGAL INDETERMINACY

Following from the preceding discussion, debt is viewed as a commodity in a manner that indicates that the enforcement decisions were consistent with neoclassical assumptions about the role of law in competitive markets. As discussed in the preceding section, "there are many possible specifications of a commodity regime and many possible specifications of a contract regime based on the idea of freedom."[205] It has been argued that the legal regime established by the New York courts is a response to debtor intransigence in a particular default episode. The wider implications of attempts to replicate or 'benchmark' this response as an enforcement template are disturbing. Debt enforcement decisions are particular to their context, but so is the legal fiction of debt as a commodity. This particularity is the nature of legal indeterminacy that marks adversarial litigation. As Duncan Kennedy puts it, "there is no single set of property and contract rules that will generate an efficient outcome in every case, no matter what other conditions of the economic system."[206]

Part III showed that a standard assumption in the metaphorical construction of property is that enforcement would increase welfare even if it is harsher on the debtor. This view was relied on to resist a formal framework for restructuring sovereign debt. The implicit assumption here is that common law enforcement decisions have what Kennedy describes as,

> a peculiar, almost sacred status as symbols of 'the efficient market solution …. They appear as a neutral background in everyone's interest (efficiency) that is constantly threatened by the more partial, political interest-group based or ideologically based initiatives of legislatures.[207]

203. *Ibid*.
204. *Ibid* at 170.
205. Kennedy, *supra* note 175 at 961.
206. *Ibid* at 963.
207. *Ibid* at 964.

My discussion of the sovereign debt litigation indicates such a move to fix the role of the law in sovereign debt markets. However, evidence from literal markets is consistent with Kennedy who argues that enforcement by common law courts is not "the efficient market solution to the problem of economic allocation; it was just one of many possible background regimes."[208] The NML enforcement template is thus a source of future legal uncertainty. Historical evidence indicates that there was never a common law enforcement template out there for "'a free market regime' that embodied the legal/economic requirements for efficient resource allocation."[209] The *NML* decision is not an exception to this trend. The outcome of that case reflects pressures on the courts to respond to debtor intransigence and offer remedies in the context of a wider fragmentation of the institutional configuration that so far has facilitated consensual debt workouts.

IV. CONCLUSION

Weidemaier argues, "Sovereign Bonds are treated like other contracts only when things are going well. An event of default triggers a conceptual shift in which political rather than legal concerns come to the fore."[210] This is true. On default, common law judges come to the fore with outcomes that are not confined to the four corners of a debt dispute.

Historically, on default, the enforcement of debt contracts has always justified assertions of public authority in sovereign debt markets. There is a long line of interventions that range from military action to further US foreign policy interests in nineteenth century Latin America[211] to the recent US federal court decisions to rein in what the courts considered a recalcitrant debtor. The difference this time is that this incipient, judge-mediated enforcement regime threatens consensual market driven debt workouts. This is significant as the burden of post-crisis adjustments is shifted onto the citizens of the debtor state

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208. *Ibid.*
209. *Ibid* at 965.
210. Weidemaier, *supra* note 11 at 147.
211. See Louis A Pérez & Deborah M Weissman, "Public Power and Private Purpose: Odious Debt and the Political Economy of Hegemony" (2007) 32 NC Cent L Rev 699; Emily Rosenberg, *Financial Missionaries to the World: The Politics and Culture of Dollar Diplomacy, 1900-1930* (Cambridge, Mass: Harvard University Press, 1999). Perez and Weissman provide a historical account of 19th century US government intervention that relied on debt obligations to widen its geopolitical influence in Latin America. Rosenberg provides a historical account of US intervention in Latin America that also relied on debt obligations and maps the creation of a cadre of financial administrators.

and, through bailouts, onto taxpayers whose contributions fund bailouts. The case law analysis developed here opens up a space for a discussion about the necessity of intervention by other branches of government to remove the pressures on judges to fill structural gaps in the fragmenting institutional configurations that have—thus far—sustained debt workouts.

"Judges" Lee Buchheit—a sovereign debt lawyer and legal expert—notes,

> are … ill-equipped and ill-positioned to decide how the discomfort of a financial crisis can be apportioned among the citizens of the debtor country and the various classes of its creditors. Judges can only hand down judgements saying that as a matter of law, the sovereign is bound. They cannot prescribe the nature or degree of the sacrifices that the sovereigns would be needed to impose on its other stakeholders in order to make those payments or to satisfy those judgements.

Is it time to circumscribe their enforcement role?