FOREIGN BONDHOLDERS PROTECTIVE ORGANIZATIONS

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THE unfortunate experience in recent years of the American holders of defaulted foreign bonds led to the passage by Congress on May 27, 1933, of the Corporation of Foreign Bondholders Act, as Title II of the Federal Securities Act.[1] It was designed to furnish a medium through which American bondholders could act jointly in the adjustment of their claims against defaulting governments or other foreign entities. The holders of the defaulted bonds of a foreign state occupy a peculiar position. They cannot sue in the bondholders' state, nor, even where foreign governments permit themselves to be sued, have they any effective remedy in the courts of the foreign country.[2] The diplomatic channel has been occasionally opened to them, but in most countries only on proof of discrimination against them as nationals of a particular country or on some evidence of denial of justice or bad faith, such as the diversion of security, or the repudiation of specific pledges or guaranties. Mere failure by reason of inability to pay is not alone deemed ipso jure, a violation of international law.[3] While unofficial good offices have often been extended by the governments of the bondholders in an effort to assist them in obtaining payment or adjustment of rightful claims, and while the line separating good offices from official representations is not so clearly defined as is often supposed, bondholders have had no assurance of legal protection either judicial or diplomatic. That fact has forced them to rely upon their own endeavors to effect an adjustment of their claims,[4] and they have learned

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1. P. L. No. 22, 73d Cong., 1st Sess. (1933) tit. II.

2. Disputes concerning the currency in which payment of the coupons may rightfully be demanded, have, it is true, been submitted by agreement of the parties to the Permanent Court. Judgments No. 14 and 15. But there is no recognized international tribunal or board of arbitration to which the legal and economic issues arising out of default may be referred.

3. For fuller treatment of this matter see Borchard, *International Loans and International Law* (1932) 26 PROC. AM. SOC. INT. LAW 135.

4. They have, however, one powerful and persuasive weapon at their command, in the fact that none of the leading European stock exchanges will grant a quotation to the new issues of a defaulting state. The keener the desire of the latter for fresh loans, therefore, the more eager will it be to come to terms with its creditors, and a large proportion of the agreements by which the numerous defaults of the past and present centuries have been terminated have in fact been followed by a re-entry of the outcast into foreign money markets almost as soon as the ban of exclusion was withdrawn.

that in union there is strength. The result has been the voluntary formation of protective committees, to which governments, as a matter of policy, have extended varying degrees of support, some taking more definite and affirmative action than others. The French and German Governments, for example, have shown themselves more ready to intervene officially in support of bondholders than has the British Government. In the Securities Act of 1933 it was made very clear that the Corporation of Foreign Bondholders was not to be deemed authorized to speak or act for the United States Government or the Department of State or to do anything to interfere with the activities of the Department of State in diplomatic or other negotiations.[5]

A governmental default is quite different from any other. The creditor cannot obtain judgment against and levy execution upon a debtor government, nor can he take over the management of its affairs. The functioning of the debtor government cannot be impaired, so that the creditor is perforce driven to negotiate and make such adjustments as he can. The default may be due to a variety of causes, such as war, depression, or financial mismanagement; new ones have been found in the current disorganization of world trade which has brought in its train various restrictions on foreign exchange, transfer moratoria, and other measures, the lifting of which often requires collateral negotiations with importers and others. In many defaults, moreover, several types of obligations are affected, some unsecured, others carrying varying classes and orders of security and priority, including debts, funded and floating, internal and external, tort and contract. Any reorganization must take account of the varying quality and character of these claims. The problem is one which has engaged the attention of many bondholders' committees and, because it lies at the root of most adjustments of conflicting claims, requires the fullest consideration. The negotiators, in order to effect an adjustment likely to endure, must also be able to comprehend the needs of the debtor country so that a restoration of impaired credit can be effected and a repetition of bankruptcy avoided. All this requires knowledge, skill, experience, objectivity, and statesmanship of a high order.[6]

Because single protective committees for a particular issue have often not had all the necessary qualifications, they have at times proved ineffective. Moreover, the conflicts of interest frequently prevailing among the holders of varying groups and series of bonds, and among other claim-

5. § 210.

6. Up to the present there has been no study of the history of governmental defaults to determine empirically the principles, legal or customary, if any, upon which the adjustment of these varying claims, in relation to one another, may be determined. Such a study is, however, now being prepared by the writers, with the aid of a grant made to Yale University for the purpose by the Carnegie Corporation.

ants, have brought about differences of policy which have been deleterious to all concerned. When they have sought governmental aid, these conflicts of interest have been hampering to successful efforts. When the issuing bankers form protective committees they are sometimes handicapped by a real or potential lack of disinterestedness or by an equivocal position between their client, the defaulting government, and the holders of the bonds.[7] They are rarely able to act promptly or on their own initiative, and cannot effect that cooperation with, or, on occasion, protection against foreign committees of similar character, which may be necessary. Thus, the interests of the bondholders, of the Foreign Office, and of the defaulting government combine to emphasize the importance of some central body through whom all parties can effectively deal.

The American Corporation of Foreign Bondholders, whose organization and function were provided for in considerable detail by the Act of 1933, was to consist of six directors appointed by the Federal Trade Commission for a term of years, and was given broad powers and privileges patterned after those believed to be exercised by the British and other national Corporations of Foreign Bondholders. Among its special features was a provision making any plan of adjustment worked out by the Corporation binding on all owners of deposited bonds, provided sixty per cent consented, and enabling the Corporation to levy a charge of one-fifth of one per cent of the face value of the bonds deposited.[8] They were, moreover, authorized to receive from any person, foundation, or agency of the United States subscriptions which in the discretion of the Corporation could be treated as repayable loans.[9] The Reconstruction Finance Corporation was authorized to lend up to $75,000 for its use.

The Act was not to take effect until the President so ordered.[10] The President has not yet acted and it appears unlikely that he will do so. What has been done is something quite different. A group of eighteen distinguished citizens, chosen from all walks of life, have been called together in Washington by the Departments of State and the Treasury to organize themselves into an American Foreign Bondholders Protective Committee designed, presumably, to carry out the general purposes of the Act of 1933. How far they will depart from the terms of that Act is still uncertain. It has been said that the State Department preferred an organization different from that contemplated in the Act of 1933 because it feared that the Board selected by the Federal Trade Commission might in the eyes of bondholders and foreign debtors have an official aspect—an inference which the Department desired to avoid, although

7. For a fuller discussion of this point, see Dulles, *The Protection of American Foreign Bondholders* (1932) 10 FOREIGN AFFAIRS 474, at 478 *et seq.*

8. §§ 204, 207.

9. § 208.

10. § 211.

the Act endeavored expressly to insure the independence of the Corporation and the absence of responsibilty on the part of the Government. Perhaps the experiences with the Department's requests of 1922 on issuing bankers that foreign bond issues be submitted to it for inspection on public grounds and the erroneous impression which gained some currency that the failure to object on political grounds constituted general approval of the loan had some bearing on the Administration's reluctance to carry out the terms of the Act.[11]

The British Corporation of Foreign Bondholders is the oldest and most important institution of the type now about to be set up in the United States. There have been few governmental defaults involving British bondholders which the Corporation has not been instrumental in settling. Its methods have thus stood the test of long experience and have justified themselves by their results. They have, moreover, been followed in their essentials elsewhere and especiall by the corresponding French organization—the Association Nationale des Porteurs Français de Valeurs Mobilières. Now while there may be no virtue in slavish adherence to precedents, it is often folly to disregard them, and, in the opinion of the writers, the highly successful methods of the Corporation, allowing for modifications necessitated by differences in American conditions, are likely to prove on the whole suitable for adoption in this country. At this time, therefore, it may be useful to describe in some detail the development, organization, and modus operandi of the Corporation, and to indicate the chief respects in which the French body differs in constitution and practice from its British exemplar.

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11. On March 3, 1922, the Department of State published an announcement of its desire to be informed by issuing bankers of all foreign loans intended to be floated in the United States. The announced purpose was not to pass on their business soundness, but on the public policy involved, e. g., not to approve loans on behalf of foreign governments or even companies of states which had not funded their debts to the United States, or on behalf of foreign government monopolies, or on behalf of purposes not approved by the United States, such as increase of armaments. The practical operation of these restrictions is discussed in Dulles, *Our Foreign Loan Policy* (1926) 5 FOREIGN AFFAIRS 33, and, in connection with the policies of other countries, in Edwards, *Government Control of Foreign Investments* (1928) 18 AM. ECON. REV. 684. While disclaiming the injection of business considerations, the impression nevertheless spread that the failure to object to the loan was not confined to political considerations and hence constituted general approval. In some cases, adverse economic considerations were suggested, for the Department of Commerce and the Treasury were consulted on these loans. Both before and after 1929, the Department of State was under attack in Congress and out for the adoption of a policy of loan control not expressly authorized by statute, a policy actually exercised by the governments of other countries exporting capital. When numerous loans went into default after 1929, and Senate investigations were begun, the Department of State suffered some embarrassment, because of erroneous implications attached to the Department's statement that it had no objection to the loan. If economic planning extends to the import and export trade, as seems possible, even more governmental control may in the future have to be extended to the export of capital.

II

Prior to the establishment of the Corporation of Foreign Bondholders, British holders of foreign bonds (and the same was, of course, true at that time of the relatively few bondholders of other nationalities) had no recognized means of organization for the protection of their interests. They were in many instances represented by committees which were either self-constituted or appointed by an informal meeting of holders of bonds which had gone into default; but there was in existence no institution whose object it was to represent the interests of the holders of foreign bonds in general, to represent their claims to the British Government, and to negotiate terms for the settlement of the default and the resumption of payment.

The need for such an organization was apparent, and at a general meeting of holders of foreign bonds convened in London on November 11, 1868, the following resolutions were unanimously adopted:[12]

"1. That in the opinion of this meeting, the formation of a Council for the purpose of watching over and protecting the interests of holders of foreign bonds is extremely necessary and desirable.

"2. That with the view of giving weight to its recommendations and a practical character to its policy, the Council should comprise some members of those eminent houses who have had experience in dealing with foreign governments."

In accordance with a third resolution a committee was appointed to prepare a general plan embodying rules and regulations for the proposed Council. The report of this committee was presented to a second general meeting on February 2, 1869, and obtained complete approval.[13]

The committee took the view that one of the main advantages of the Council would be that in negotiations with debtor states it would not be hampered as issuing houses had tended to be by a sense of divided loyalty. Whenever defaults have occurred, the committee stated, "contractors have found themselves in an embarrassing situation towards the Government and Bondholders, being under certain obligations to both. On such occasions the Council will be ready to act as mediator between the Foreign Government and the Bondholders, relieving thereby the contractor from his unpleasant and sometimes equivocal position." The Council, the committee recommended, should be composed of members of loan-contracting houses and of the stock exchange, together with private bondholders. The committee left it to the Council to determine the best method of financing the organization, but suggested that the necessary funds might be secured either:

12. London Times, Nov. 12, 1868.

13. *Id.* Feb. 2, 1869. The report of the Committee was published in pamphlet form, London, 1869. There is a copy in the library of the British Museum (8228d2).

(a) from fees for services rendered to bondholders, special committees, loan contractors, and foreign governments, supplemented perhaps by annual membership subscriptions entitling subscribers to copies of the Council's publications; or

(b) by raising a permanent fund large enough to yield an income sufficient to cover the running expenses of the Council.

After paying its way for three years chiefly by means of fees, the Council decided to establish a substantial capital fund by forming a Bondholders' Association of 1,000 members, each of whom was to subscribe for a 5 per cent bond of £100. The entire assets of the Association were to be the property of the members and to remain so even after all the bonds had been repaid. The income of the Association, to be derived from interest on the invested capital, from the contributions of bondholders, from fees, and from commissions on claims settled, would, the Council believed, be considerable, so that "besides rendering invaluable services to the public," the Association would be "not only self-supporting, but amply repay the members."[14] But without incorporation, the liability of the members would, it was realized, be unlimited. An application for incorporation by Royal Charter was refused,[15] while incorporation by Act of Parliament was found impracticable.[16] The Council thereupon decided to abandon the idea of a profit-making organization and, after considerable trouble and delay, succeeded in obtaining from the Board of Trade a license under Section 23 of the Companies Act of 1867[17] permitting the Association, as one formed not for the purposes of trade or profit, but for a public object, to be registered as a corporation and to enjoy limited liability without having the word "Limited" added to its title.[18]

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14. Circular issued by the Foreign Bondholders Association, London, 1872. A copy is in the library of the Council of Foreign Bondholders.

15. "It was proposed to incorporate the Association of Foreign Bondholders under limited liability by Royal Charter. Although Her Majesty's Government had resolved in 1856 not to exercise for the future the Royal prerogative of granting Royal Charters, it was believed that an exception would be made in favor of this institution, on account of its public importance.

"The petition was presented to Her Majesty, and referred to the Privy Council, but although several ministers were in favor of granting it, the Cabinet decided against it, being unwilling to establish a precedent." Report of the Council of Foreign Bondholders for 1872, at 7.

16. The difficulty was explained by the solicitors to the Council, in a letter to its chairman, as follows: "On one point, which was a *sine qua non,* viz., that the liability of the Members of the Corporation should be limited, we came to the conclusion that Parliament would not sanction such a condition, and after very careful search for precedents of any such conditions having ever been incorporated in a Private Bill, none could be found, and we are of opinion that such a condition would not be likely to be permitted by Parliament." *Id.* at 9.

17. 30 & 31 Vict. c. 131 (1867).

18. Report of the Council of the Corporation of Foreign Bondholders for 1873, at 6.

Upon its incorporation in August, 1873, under the designation of the "Corporation of Foreign Bondholders," the Association returned the contributions of those who were unwilling to remain members, now that there was no longer a prospect of profits,[19] while the bonds of the continuing members were redeemed as rapidly as the growing revenues of the Corporation permitted. The whole of the original capital fund was repaid by 1885,[20] but the subscribers, in accordance with the Articles of Association, retained their Certificates of Permanent Membership. These were transferable, the holder having the right of electing the members of the Council. As time passed, a considerable number of these certificates found their way into the hands of persons who were not "directly interested in foreign securities or in the work of the Corporation or the objects for which it was established."[21] Such holders looked with covetous eyes upon the substantial fund (amounting at the end of 1896 to about £100,000) which the Corporation had been able to build up and invest even after the repayment of the contributions of the permanent members. They clamored to have some part of this fund distributed among the certificate holders, although—as the Council was advised on the highest legal authority—any such distribution was absolutely precluded under the constitution of the Corporation.[22] As a further consequence of the acquisition by unsuitable individuals of a voice in the selection of the governing body, so critics of the Corporation alleged, the Council had come to include many members who had no knowledge at all of the type of business it had to transact.[23] Criticism of the Council was carried even further, and it was repeatedly accused during the eighties and nineties of serving limited interests at the expense of the bondholders.[24]

While no valid evidence was educed to show that the Council had in fact been influenced by any other considerations than the welfare of the bondholders, the Council decided that it would be wise to reconstitute

19. The sum of £60,280 was paid in by the Permanent Members of the Corporation. "The amount originally fixed was £100,000, but as the Council decided to allot only one Bond of £100 to every Member, the surplus subscriptions were returned to those who had not furnished a special nominee in respect of every £100 subscribed. To a number of subscribers, who had joined the Association for different objects than the protection of the rights and interests of the holders of Foreign Bonds, their subscriptions were likewise returned." *Id.* at 8.

20. Report of the Council of Foreign Bondholders for 1885, at 5.

21. Preamble to "An Act to Reconstitute the Corporation of Foreign Bondholders," 61 & 62 VICT. c. 149 (1898). Reprinted in Report of the Council of Foreign Bondholders for 1898-9.

22. Report of the Council of Foreign Bondholders for 1897, at 21. The legal opinion of Sir Farrer Herschell and Mr. Phipson Beale, O. C. (to whom the question was referred in 1883), is printed in extenso in the Report of the Council of Foreign Bondholders for 1893.

23. *The Corporation of Foreign Bondholders* (1897) 55 THE ECONOMIST 1624.

24. FEIS, EUROPE THE WORLD'S BANKER (1930) 113 n.

the Corporation so as to insure that it "should in the future more directly and exclusively represent the interests of the holders of foreign and other public securities" and also remove all danger of a diversion of its surplus funds to purposes other than the public objects for which it was constituted.[25] Such a reorganization could not be effected without the authority of Parliament. The necessary bill was successfully piloted through its various stages and became law on July 25, 1898, as the "Corporation of Foreign Bondholders Act."[26] This Act, therefore, is the present constitution of the Corporation, which is organized and operates in accordance with its provisions.[27]

While the Act gave the Corporation the status of a recognized quasi-public body, enlarged (though perhaps only on paper)[28] its objects and scope, and laid down new rules and regulations for the appointment of members of the Council and for the conduct of its proceedings, it effected no significant change in the policy and methods of the Corporation. The founders had made the initial mistake of attempting to establish the institution on a profit-making basis, but they quickly realized their error, and then proceeded to build wisely and well. Throughout the sixty odd years of its history the Corporation has followed much the same procedure in dealing with a default as it adopted from the outset.

III

The Council, or governing body, of the Corporation consists of twenty-one members, of whom six are nominated by the British Bankers' Association and six by the London Chamber of Commerce, while the remaining nine—of whom at least six must at the time of their election be bona fide holders of foreign bonds to the nominal amount of five thousand pounds—are co-opted by the Council as a whole. A body thus chosen is representative of the whole financial and commercial interests of the City as well as of the bondholders at large. The present Council includes directors of the Bank of England, the chairmen of the Big Five

25. Preamble to the Council of Foreign Bondholders Act of 1898, 1c.

26. Note 21, *supra*.

27. The Act (art. 10 and Second Schedule) required the Council to appropriate at least £2000 each year for the purchase, and subsequent cancellation of the Certificates of Permanent Membership. Holders of these certificates were invited to tender them for sale at a price not exceeding £100, the lowest tenders being accepted. The sum paid for these certificates averaged a little over £48 in the first redemption (May, 1899) and rose in later years to nearly par. The redemption was completed in May, 1919. Reports of the Council of Foreign Bondholders for the years 1898-9 to 1919.

28. The objects and scope of the Corporation are defined in art. 4 of the Act. By paragraph (a) of this article the Corporation is authorized "to watch over and protect the rights and interests of holders of public securities wherever issued but especially of foreign and colonial securities issued in the United Kingdom." In practice the Corporation has concerned itself solely with foreign securities.

joint-stock banks,[29] men of importance in commerce and industry or of considerable experience in public affairs.[30] The bondholding community is thus able to rest assured that, whenever the necessity unfortunately arises, its affairs will be handled by the Corporation with ability and good judgment, and that the financial guidance with which it is furnished will be both competent and disinterested.

The Council acts through various Bondholders' Committees, associated with it under the rules and regulations of the Corporation, of each of which the President and Vice-President of the Council are ex-officio members, and chairman and deputy-chairman respectively. When a default occurs many of the financial institutions, jobbers, and private individuals affected usually urge the Council to take action on their behalf.[31] As soon as it is clear that there is a demand for its services, the Council first investigates the extent of the British holding. If this is comparatively small, if the interest of the British bondholders is practically identical with that of the bondholders in other countries owning the bulk of the defaulted issues, and if the latter are strongly represented, as, for example, by a Committee of the Association Nationale, then the Council may take the view that it is unnecessary to have a separate British Committee. In such circumstances the Council will act on its own initiative without the advice of a Committee and use its influence to secure fair treatment for the minority interest it represents.

The Bondholders' Committees set up by the Council are more or less permanent, new members being appointed as required. When, therefore, the defaulting country is one whose financial delinquencies have on previous occasions been the concern of the Corporation, there is likely to be in existence the appropriate Committee to which the matter may be referred. Should there be no Committee and one be desired, the Council itself—as it has full authority to do—nominates the members. It may perhaps invite various banks and the issuing houses to make suggestions, and usually calls a conference of important bondholders to consider the proposed list of members, but it is not obliged to call a general meeting of bondholders to ratify its appointments. The Council is able to select Committees much more satisfactory than those which would be likely to result from the haphazard nomination and vote of a

29. These are, of course, commercial banks. According to the London Times of Nov. 22, 1918, representatives of the issuing houses are not eligible for membership on the Council. In this respect a significant departure has been made from the original plans for the Corporation which contemplated including such representatives in the Council. See p. 285, *supra*.

30. Seven members of the Council retire by rotation each year, but they are eligible for re-election.

31. For information on many aspects of the Corporation's procedure, communicated in interviews, thanks are expressed to the Secretary, Douglas Reid, Esq., and the Assistant Secretary, A. L. Philp, Esq.

large assembly. The members need not be bondholders; they are chosen solely on the basis of their general qualifications and special knowledge. The size of the Committee is determined in each case by the Council, but the membership is usually small and ranges at present from four (for Guatemala) to thirteen (for Greece).

The Committees are the expert advisers of the Council, not the attorneys of the bondholders. While the business of a Committee is to advise concerning the negotiation of a settlement of the default, it cannot conclude a binding agreement with the government concerned. The arrangements it advises are submitted to the Council, which, in turn, if it approves, recommends them for acceptance either to a general meeting of bondholders or by a reasoned communiqué to the press where such may seem adequate. There has in practice been no real dissension between the Council and any of the Committees. Harmony at all times is practically assured, since the two chief members of the Council sit on each Committee—and in some instances one or more other members also —while the Council, having itself selected the members of the Committee, has full confidence that any settlement which they advise is as fair and reasonable a one as it is possible to obtain. It may in fact be said that once an agreement has been recommended by a Committee, the assent of the Council tends to follow as a matter of course. In the final stage—the general meeting—the bondholders, too, throughout the history of the Corporation, have usually voted their accord, either unanimously or nearly so.

Such a general meeting is, however, only a convenient and easy method of giving bondholders the means of hearing explanations of an arrangement, discussing its pros and cons, and expressing their opinion with regard thereto. The majority cannot bind the minority, and even the vote of those who are in favor of the acceptance of the arrangement has no binding force. The real acceptance comes when the bondholders send in their securities to be stamped with the new conditions or exchanged for the new bonds, or when they encash the first coupon after the new arrangement. During the past three years of world-wide depression the Council has been obliged to agree, in respect of the external public debts of several countries, to a suspension of sinking fund, cessation of the transfer of part or the whole of the debt service from domestic into foreign currency, or to other arrangements for alleviating the burden of the debtor. These interim arrangements have rarely been submitted to a general meeting of bondholders, for, as the time, purpose and results of the meeting must be advertised all over the country, the reasoned communiqué recommending measures to deal with transitory conditions over a short period or by repetition over a series of short periods provides a less cumbrous and more elastic method.

Bondholders are not as a rule asked to deposit their bonds with the

Council when the latter undertakes to protect their interests. Apart from other considerations, where the British holding is very large, the mere space required to accommodate the securities would in itself constitute a considerable problem. The request for a deposit of bonds has been made in the rare cases where a government was attempting to profit through its own default by buying up its bonds at the resulting depressed price, or in circumstances under which the exact extent of the bondholders' interest represented by the Council had to be known. Such circumstances have arisen when it has been desirable to dispel doubts expressed by the defaulting state or foreign—and perhaps conflicting—financial interests as to the existence of a substantial British holding, or when litigation affecting the rights of the bondholders was contemplated, or when it was desired to give some one a power of attorney on their behalf. On depositing his securities the bondholder receives in exchange certificates for which the Stock Exchange may be asked to grant a quotation, thus making it possible for him to sell the equivalent of his holding in the market. The deposit agreement which he is required to sign is a simple and standard one, containing only five clauses.[32] These include a provision that "any Resolution passed by a General Meeting of

32. The Conditions of Deposit to which the bondholder is required to subscribe are as follows:

1. The Corporation of Foreign Bondholders is constituted the holder of the deposited Securities and is invested with all the powers of the actual owners thereof and in particular without limiting the generality of such powers is authorised to do any of the following things, that is to say:—

(a) To advance and support claims and enforce the rights of the Bondholders to property money or securities.
(b) To prosecute defend or compromise actions or other legal proceedings in relation to the said deposited securities.
(c) To appoint agents and delegate to them all or any of their powers.
(d) To negotiate compromises settlements conversion and exchange of securities or other arrangements and to complete and carry the same into effect.
(e) To send abroad for any purpose in relation to the matters aforesaid the Deposited Bonds or any coupons thereon present the same for payment exchange conversion or otherwise and receive give discharges for and hold or distribute any money or securities receivable in respect thereof.
(f) To give and sign any request consent direction or instruction and make any declarations and give any indemnities expedient for any purpose.
(g) Generally to act on behalf of the Certificate holders in any manner the Corporation may deem expedient in the interests of such holders.

2. No holder of Certificates issued in exchange for the deposited securities shall be entitled to claim re-delivery of such securities except on a general re-delivery to be made when deemed expedient by the Corporation.

3. The Corporation shall be responsible only for reasonable care in the custody and examination of the deposited securities but not further or otherwise.

4. The deposit is made subject to the condition that any Resolution passed by a General Meeting of the Certificate holders convened by the Corporation and held in the manner provided by its Rules and Regulations shall be valid and binding on all Certificate holders. The Corporation will not conclude any settlement or compromise until authorised by Resolution of a General Meeting.

5. After the conclusion of a settlement or compromise the Corporation reserves the right subject to the same authorisation to reimburse itself by deduction or otherwise from any cash or securities resulting therefrom such expenses or charges or any parts thereof as may be incurred in furtherance of the above purposes and which are not recoverable from the Government of —— or other parties.

the Certificate holders convened by the Corporation in the manner provided by its Rules and Regulations shall be valid and binding on all Certificate holders." Having deposited their securities the bondholders concerned are thus bound individually by the vote of a general meeting, whereas they are not so bound when no such deposit is required. Bondholders who have not by prior or subsequent lodgment of their bonds or in some other way consented to a new arrangement are not, however, bound by it. Theoretically they are entitled to retain intact the rights conferred upon them by their original bonds, but they have no effective means of enforcing these rights, with the result that once an arrangement has been accepted by the large majority of bondholders the small minority are practically obliged to come in, and in fact do so.

While negotiations are in progress for the settlement of a default, the bondholders may from time to time be informed of how matters are proceeding, but the Council tends to be spare with its communiqués, for these, if issued frequently, may provoke much ill-considered discussion or exacerbating criticism, and thus do more harm than good.

The original charter of the Corporation provided for three classes of members: permanent members and life members, who were to qualify by a single payment of £100 and £20 respectively, and subscribing members, who were to pay £2-2-0 per year. But the policy thus initiated of financing the Corporation in part by membership contributions was put into practice only for a short period and to a very limited extent. No steps were taken to invite the bondholding public at large to become life members or annual subscribers,[33] while the contributions of the permanent members—which were, in effect, loans—were all refunded, as already mentioned, by 1885. The Council defrays the expenses of its affiliated Bondholders' Committees, and recoups its outlay when a settlement is made, together with an additional sum for the general purposes of the Corporation, either from the state concerned or, to the extent to which this proves impossible, from the bondholders concerned. Apart from the cost of such negotiations the ordinary expenses of the Corporation amount to about £12,000 a year. Approximately two-thirds of this sum is met out of invested funds, which prior to the world crisis totalled about £200,000, and the Council looks forward to the day when it will not have to make any charge whatever to bondholders for its services. "In most cases, however, the expenses have been borne by the Governments concerned, and no charge has fallen on the bondholders."[34]

At the time of the first incorporation it was contemplated that the President and members of the Council should give their services gratuitously, and for the first seven or eight years they did so. But as the business operations of the Corporation increased it was no longer to be

33. Five life members were, however, acquired, but no subscribing members.

34. Preface to Annual Reports of the Corporation for 1932 and previous years.

expected that busy men of high standing and position would continue to act without remuneration, and in 1880 a modest scale of payment was adopted (though not until an opinion had been received from the Board of Trade that it saw no objection to such a course) which, with some slight modifications, was authorized under the reorganizing Act of 1898. The President receives £1,000, the Vice-President £500, and the other members of the Council £100 per annum. The duties of the President, in the words of the late Lord Avebury, who for twenty-five years acted in that capacity, "necessitate almost daily attention, frequent attendance at the meetings of the Council and of the twenty committees of foreign loans affiliated with it, constant communication with the Secretary and supervision of a large correspondence and of the daily work of the Council, involving most important and delicate negotiations and official communications with foreign states and others."[35] The members of the Bondholders' Committees are required by the terms of the incorporating statute to serve gratuitously. But the Council is authorized, when a settlement is arrived at and providing funds are available, to pay them as an honorarium a moderate fee for each attendance at the meetings of their Committee. No such fees are paid, however, to the President and Vice-President.

While the Corporation has the great advantage of operating under an excellent constitution, its past achievements and present influence must be ascribed in no small degree to the character and capacity of the men who have been chiefly responsible for the direction of its policy and the conduct of its activities. To the successive Presidents and Secretaries of the Corporation—and they have been few,[36] for a proud tradition of lifelong service has been built up—the foreign bondholding community in Great Britain owes a great debt. These officers necessarily play the leading rôle in the negotiation of the debt settlements, and had they been less conspicuous for integrity, ability, tact and good judgment, many defaults would have been far less satisfactorily adjusted.

IV

The Association Nationale des Porteurs Français de Valeurs Mobilières was founded in 1898 by the Paris Stock Exchange (Chambre Syndicale des Agents de Change) at the request of the French Minister of

35. Evidence of Sir John Lubbuck (afterwards Lord Avebury) before the Select Committee of the House of Commons on the Foreign Bondholders' Corporation Bill, quoted in Financial News, May 14, 1898.

36. The Secretary is the head of the small permanent staff of the Corporation. Since the foundation of the Corporation in 1868 there have been only 7 different Presidents and 4 Secretaries.

Finance. Its constitution[37] and practice[38] are very similar to those of the older British institution. It, too, embraces an executive council, a number of bondholders' committees, and a small permanent staff. The functions and powers of the members of the committees, their relationship to the Council and the bondholders, and the method by which they are selected are practically identical in the two organizations. Under French law, however, the members of the committees must be bondholders, while, on account of the great number of small holders of foreign bonds in France and their wide dispersion, general meetings of bondholders are seldom, if ever, called, even for the consideration of a proposed settlement. The bondholders signify their assent by encashment of the first coupon under the new arrangement. Before the war, acceptance by holders of about two-thirds of the French interest in the defaulted issues was required, but there has been no insistence since on such a proportion and even a bare majority might now be accepted. If only a minority of the coupons should be presented, the Association would probably instruct its Committee to reopen negotiations, but no such situation appears to have arisen. As in England, a deposit of bonds is required only in rare and corresponding circumstances. The Association also throws the burden of providing for the expenses of its bondholders committees upon the state whose default made the negotiations necessary, but, unlike the Corporation, its ordinary expenditure is financed partly out of annual contributions. The Stock Exchange is the chief contributor, but modest sums are also derived from subscribing and associate members, while a small subvention is also received from the state. The Council of the Association is a much smaller body than its English counterpart, being composed of only eight members.[39] At present two of these are representatives of the Stock Exchange and two of large commercial banks, one is an eminent professor of law, another a leading government engineer, and the remaining two a distinguished diplomat and a former high official in the Ministry of Finance.

Similar institutions for the protection of the foreign bondholder have been established in Belgium, Holland, and Germany, while in Italy and Switzerland this function is undertaken by the Association of Bankers.

V

The American Foreign Bondholders Protective Committee has come

37. The "Statuts" of the Association are printed in the Annuaire of the Association for 1915-1920.

38. For an explanation of the procedure of the Association, thanks are expressed to M. Barde, the Directeur.

39. The "Statuts" of the Association provide for 9 members, but for the past several years the Council has had only 8 members. The members are appointed for 6 years, but are subject to re-election.

into being at a time when an avalanche of foreign defaults require attention. It has the advantage of the experience acquired by the British Corporation, but has little experience of its own. Its large membership presents an analogy to the British, rather than the French, organization. Yet there is some evidence that the draftsmen of Title II of the Securities Act, in suggesting the modus operandi of the American Corporation of Foreign Bondholders, combined the French system of a small board of directors with the British example of operation through special committees,[40] which may or may not include members of the Council, other than the President and Vice-President. Whether the new Committee intends to follow that practice has not yet been announced. It may be inferred, however, that its announced policy of not asking the deposit of bonds and not financing its expenses from the bondholders implies that there is no present intention of dispensing with private bondholders' committees.[41] Whether this will prove a permanent policy cannot yet be surmised. But the relations established between the central Committee and the bondholders and their private committees are likely to constitute an important factor in the functioning of the new body. For example, it will be interesting to observe whether special committees will be established for each defaulted loan; whether the special committee will be composed partly of members of the central Committee and representatives of the holders of the bonds and, where there are several different issues involved, of representatives for each issue; whether the chairman of the central Committee will become an ex-officio member of all special committees; whether the members of the Committee, scattered as they are throughout the country, will all take an active part in administering its affairs; whether the central Committee will reserve

40. Section 204 of the Act provides: The board of directors may ". . . (3) Appoint committees from the directors of the Corporation and/or all other persons to represent holders of any class or classes of foreign securities which have defaulted in the payment either of principal or interest and determine and regulate the functions of such committees. The chairman and vice chairman of the board of directors shall be ex officio chairman and vice chairman of each committee." This would seem to add to the two British alternatives a third possible method of appointing committees, namely, exclusively from the membership of the board of directors. Query, was this intentional or inadvertent?

41. In England, the existence of the Corporation of Foreign Bondholders has not precluded the formation of independent committees. The interests of British holders of defaulted Peruvian bonds remained during the long negotiations of 1876 to 1890 in the hands of such a committee. When, in 1890, the federal government of Argentina proved unable to meet its foreign debt obligations, a committee of bankers dealt with the matter; on the three occasions on which the financial difficulties of the Brazilian Government necessitated the funding for a period of the service charges, the House of Rothschild itself concluded the arrangements; while a League Loans Committee has recently been constituted under other auspices than that of the Corporation. But such instances are few and can be accounted for by special circumstances.

to itself final review of the decisions of special committees or whether it will serve mainly as a liaison between private bondholders' committees or special committees, the Department of State and foreign entities in default. The number of experts the Committee employs and the character of its work may depend greatly upon the nature of the relationship it establishes with private committees, and the division of labor proposed.

Whether its functions, its modus operandi, and its relations to bondholders should be expressly set out in the Act or articles of incorporation or should be left flexible enough to be adjusted to the needs of each occasion is a question which deserves consideration. The specifications of the British Act of 1898, it may be noted, have not militated against a considerable flexibility in operation which has proved advantageous in numerous instances. The fact that the American Committee is a nonprofit association, that the bondholders have had little share in organizing it, and that it expects to function without cost to the bondholders, might possibly lessen its sense of responsibility and its effectiveness in arousing the confidence of the private interests concerned. Yet its freedom from any personal or special interest, its impartiality, and its independence may enhance its opportunity to serve usefully the divergent groups interested in its activities. The quasi-governmental auspices under which it has been created, its opportunity for ready access to governmental departments, and its detachment may enable it more effectively to protect the bondholders' interests and to become a source of authoritative information than could the private protective committees and ephemeral organizations to which bondholders have heretofore been ultimately remitted. The usefulness of the Committee should develop with its growing experience. It should normally become a clearing house for financial information concerning foreign countries and a repository of the many branches of knowledge upon which its special activity impinges. While it has not available the traditions and accumulated banking and financial experience upon which the British and French Corporations had to draw, there seems no reason to believe that the American Committee cannot become as effective an organization as the corresponding organizations in Great Britain, France, and other countries.