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Recalcitrant Creditors Against Debtor Nations, or How to Play Darts

Theodore Allegaert*

During the last decade and a half, the international financial system has had to cope with intermittent debt crises resulting from the over-extension of credit by Western banks and governments to less developed countries (LDCs).[1] Among many related developments during this time has been the advent and growth of a secondary market for sovereign debt, a market in which tranches of debt and related instruments are traded by and among financial institutions and others, usually at steep discounts from par or face value. The evolution of this market was a natural consequence of increases in the 1970s of private sector financing of sovereign debt and of the defaults and restructurings that followed. As in any "secondary" market, the sellers are often parties to original or primary transactions, seeking to cut losses and exit the market. Secondary buyers of sovereign debt instruments, on the other hand, tend to be speculators: they purchase the rights of the selling party hoping that the market's estimation of the likelihood of performance will rise over time and/or the debtor will actually perform to some extent beyond the discounted price paid.

The secondary purchasers of sovereign debt, who as a practical matter rarely acquire more than a small fraction of a country's total external debt,[2] are generally bound to the terms of the debt instruments in the same manner as the contracting parties.

* J.D. 1996, The University of Chicago. Law Clerk, United States District Court, Eastern District of Wisconsin, 1996-97. I thank Professors Kenneth Dam and Geoffrey Miller for their comments on earlier drafts.

1. This shorthand denotes a broader category than that of non-oil producing developing countries (NDOCs); because the debtor nations I refer to in this paper will in most cases be NDOCs, but not always, LDC is used here.

2. *See, e.g.*, Kenneth N. Gilpin, *Darts Clash with Brazil over Loans*, N.Y. TIMES, Oct. 23, 1993, at 37 (reporting that the Dart family, who bought an unusually large amount of Brazilian debt, held $1.4 billion of a $43.5 billion package of outstanding debt, which Brazil and other creditors sought to restructure); *see also* CIBC Bank and Trust Company (Cayman) Ltd. v. Banco Central do Brasil, 886 F. Supp. 1105, 1106 (S.D.N.Y. 1995) (ensuing action under the Foreign Sovereign Immunities Act).

Such terms typically include an undertaking to deal with other creditors in good faith, a clause requiring that all creditors be treated in pari passu and/or share any repayments pro-rata with other creditors, and sometimes a commitment to participate in any restructuring that a majority or super-majority of creditor banks may vote to implement. Interesting questions are raised, however, where the relevant agreement lacks this last ingredient, where the requisite majority is not reached, or where the agreement is ambiguous. In such cases dissenting creditors may feel no obligation to follow the lead of the major Western banks in negotiations to restructure sovereign commercial loans.[3] The purchasing bank might, for example, have a legitimate gripe about its treatment at the hands of the debtor and the large banks that negotiated the terms of a particular restructuring.[4] In another case, however, the purchaser might be a Cayman Islands "bank" that champertously bought with the intention of suing on its modest sub-tranche (which may happen to equal in value attachable commercial assets of the debtor country present in the forum of the lawsuit) and then dissolving without sharing the proceeds with other creditor banks. Can either or both sue on the debt in the face of an intervening restructuring? Can a court find a principled way of discerning between the legitimate complaint and the wholly speculative nuisance suit? Should a court even try?

This article examines the question of how a U.S. court should respond to an action by a secondary purchaser of LDC sovereign debt to enforce the obligation in toto. While this article seeks to answer the question for the United States (which is the forum most commonly specified in LDC loan agreements for litigation arising thereunder), the issues and arguments presented are for the most part applicable to similar suits in other IMF member nations, such as the United Kingdom. As will be discussed, the filing of such lawsuits typically constitutes an attempt by the purchaser to avoid acceding to debt restructurings which are either sought by the debtor or are already in place. Section I presents an overview of commercial sovereign loans, restructurings thereof, and describes U.S. policies in this area. Section II discusses the mechanics of the secondary mar-

3. *See* James B. Hurlock, *Advising Sovereign Clients on the Renegotiation of Their External Indebtedness*, 23 COLUM. J. TRANSNAT'L L. 29, 39 (1984).

4. Gilpin, *supra* note 2, at 37 ("The dispute, which has Citibank and several other big banks caught in the middle, centers on . . . loans . . . that Brazil . . . and its major commercial bank creditors have been painstakingly working to restructure . . . .").

ket for sovereign debt instruments and lawsuits by malcontent commercial purchasers in that market against LDCs, citing the well-publicized lawsuit by the Dart family against Brazil, among others. Section II posits that to permit such lawsuits to go forward presents a significant opportunity for abuse by unscrupulous plaintiffs and their lawyers, leading in turn to disruption in the efforts of less developed nations to renegotiate and restructure their international obligations in an orderly and consensual manner, the countering of which requires a critical reevaluation of existing law. Section III examines The Articles of Agreement of the International Monetary Fund[5] ("the Fund Agreement," also known as the Bretton Woods Treaty), focusing specifically on interpretive difficulties that courts, commentators and the IMF have faced in applying the treaty to legal problems.

Finally, Section IV argues that in order to counter nuisance suits in the sovereign debt context, the Bretton Woods Treaty should be read to bar a court from decreeing performance of sovereign debt obligations anytime the IMF is substantially involved in the affairs of the debtor nation. Section IV focuses on the different interpretations that courts and commentators have given to Article VIII, section 2(b) of the Fund Agreement and argues that this provision should, in certain circumstances, constitute a bar to the plaintiff who would challenge a debtor nation in court in the United States or another IMF member nation. First, because the debtor nation's exchange resources are directly affected by the performance of sovereign debt obligations, courts should consider such agreements to be "exchange contracts which involve the currency of" the debtor IMF member within the meaning of Article VIII, section 2(b). Second, a decision to restructure external debt, if taken with the involvement and approval of the IMF, should be deemed "exchange control regulations imposed . . . consistently with" the Fund Agreement. As elaborated in Section IV, this interpretation enables IMF-approved restructuring-*cum*-exchange-control-regulation to render pre-existing loans-*cum*-exchange-contracts unenforceable in court. This is because the latter (so characterized) are "contrary" to the former and are thus declared unenforceable by Article VIII, section 2(b). In these circumstances, and only these circumstances, dismissal of an enforcement action should follow.

The interpretation of the treaty proposed in Section IV is supported by ample authority and is a legitimate avenue

5. Articles of Agreement of the International Monetary Fund, Dec. 27, 1945, 60 Stat. 1401, 2 U.N.T.S. 39 [hereinafter Fund Agreement].

through which judges in the United States and other IMF member nations may render IMF-approved restructurings immune from collateral attack by minority creditors, a result which makes economic sense and which accords with evolving U.S. policies in this field. At the same time, however, the proposed interpretation and application of the Bretton Woods Treaty would leave in place the possibility of suits, including strike suits by speculative secondary purchasers. These suits may arise in any case where the debtor country has chosen for political or selfish reasons to "go it alone" with the help of its commercial creditors, whether by unwisely seeking to stay current in existing obligations through still more private borrowing or by pursuing other policies which the IMF would not sanction.[6] Section IV concludes that such a framework will give debtor nations a significant incentive to seek out the involvement of the IMF at earlier stages in the management of external debt problems than has historically been the case. I posit that this will promote the IMF's "firm supervisory" role in these matters, a role preferable to others it might play, including that of a world bankruptcy court.[7]

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6. Russia, for example, entered the international bond market in October 1996 with a $500 million global issue just as the IMF was withholding additional lending due to Russia's inability to meet its budget deficit target and its failure to reschedule other debt. *See, e.g.*, Carl Gewirtz, *From Russia, New Level of Debt*, INT'L HERALD TRIB., Nov. 18, 1996, at 14. Under the framework advanced here, such circumstances would entitle a holder of pre-existing Russian debt to refuse to accede to any proposed restructuring and to enforce the debt it owns in accordance with its original terms. Such a possibility would continue until the IMF re-endorses the economic policies of the debtor nation, which was exactly what happened to Russia a month later: Moscow took steps to stem corruption in its tax collection processes, and the IMF resumed disbursement of a multi-billion dollar loan. *See* Michael R. Gordon, *I.M.F. Resumes Paying Credit of $10.1 Billion to Russians*, N.Y. TIMES, Dec. 16, 1996, at A6. Now, any Russian restructuring of extant loans should be deemed "consistent with" the Bretton Woods Treaty (i.e., consistent with the IMF's views), which in turn renders original loans unenforceable in the court of any other IMF member nation.

7. *See, e.g.*, Bob Davis, *G-7 Summit Expected to Boost Support For Proposals to Help Insolvent Nations*, WALL ST. J., June 13, 1995, at A4 ("Under the bankruptcy plan [advocated by Professor Sachs, among others], the IMF would be authorized to halt debt payments from bankrupt nations, oversee new borrowing from the private market[,] approve a plan to pay off creditors . . . [and] could get out of the loan business altogether . . . . But the bankruptcy plan has big problems. Nations would have to be willing to surrender sovereign rights to the IMF."). *See generally* Note, *Procedural Guidelines for Renegotiating LDC Debt: An Analogy to Chapter 11 of the U.S. Bankruptcy Reform Act*, 21 VA. J. INT'L L. 305 (1981).

I. OVERVIEW OF COMMERCIAL LENDING TO SOVEREIGN STATES

A. HISTORICAL SUMMARY

Between World War II and the 1970's, the Bretton Woods System provided the framework for sovereign borrowing by developing countries. Under Bretton Woods, the IMF provided access to credit to allow developing countries to smooth over short term economic difficulties. The World Bank also provided funding for major development and infrastructure projects, and Western governments ("the Paris Club" led by the United States) provided funding for specific projects.[8] Under this arrangement, the credits extended to LDCs generally came with strings attached, and the amounts of funding available were limited. The IMF, for example, limited lending according to a formula derived from each member's quota (the annual sum paid into the Fund by members) and came increasingly to be guided by a policy of "conditionality."[9] The IMF would insist that borrowing countries implement measures to reduce trade imbalances, restrain domestic demand, limit public sector expenditures, and take other actions aimed at strengthening the financial positions of debtor nations.[10] For many years, the Bretton Woods System, with its emphasis on fixed exchange rates, worked tolerably well. In addition, because the setup was characterized by a structural bias in favor of under-lending, it provided a salutary check on LDCs' ever-increasing appetite for Western capital.[11]

In the 1960's, the Bretton Woods System began to weaken as the United States, with payment imbalances of its own, could no longer afford to maintain the par value currency system or the obligations the system placed on it as guarantor of world currency stability.[12] Once fixed exchange rates were jettisoned

8. *See, e.g.*, William N. Eskridge, Jr., Les Jeux Sont Faits: *Structural Origins of the International Debt Problem*, 25 VA. J. INT'L L. 281, 330 (1985).

9. ANDREAS F. LOWENFELD, THE INTERNATIONAL MONETARY SYSTEM 223 (2d ed. 1984).

10. *Id.*

11. Eskridge, *supra* note 8, at 330.

12. *Id.; see also* Joseph Gold, *Transformations of the International Monetary Fund*, 20 COLUM. J. TRANSNAT'L L. 227, 229 (1981). When the United States negotiated the Bretton Woods Treaty and undertook to buy and sell gold freely at $35 per ounce, it did so on the assumption that it would face a balance of payments surplus for the foreseeable future. *Id.* (attributing the failure of the par value system to its having imposed rigidity without fostering stability, precisely the opposite of what was intended).

in 1971, and the par value system formally met its demise in the 1977 Amendments to the IMF Articles of Agreement,[13] the IMF's approval of par value changes was no longer a relevant feature of the international financial system. As a result, countries were more free to maintain overvalued currencies and payment deficits. LDCs, in turn, sought ever larger foreign loans to finance these arrangements.[14]

In the late 1960s and early 1970s, these developments were accelerated by the failure of official international lenders to increase their available funds in step with inflation. Thus, while the IMF's contribution quotas for member states increased in absolute terms, the purchasing power of the Fund's assets declined overall in the face of inflation. There was also an unprecedented growth in the private banking system, fueled by increasing streams of petrodollar deposits by OPEC members, particularly at the offshore branches of U.S. banks.[15] The oil shocks of 1973 and 1979 increased the infusion of oil profits into the deposit accounts of Western banks, just as high oil prices were causing the economies of LDCs to recede. The end result was that LDCs needed and wanted to import unprecedented amounts of borrowed capital to sustain their ideology of growth.[16] Western banks, overflowing with petrodollars, were all too ready to lend to them.[17] The ready money of the Western banks, which generally came with no conditions attached, caused LDC governments to view conditioned aid from the IMF (and Paris Club lending conditioned on IMF involvement) as an unattractive and increasingly unnecessary option.

Thus, as Professor Lowenfeld notes, by 1976 almost half of the financing sought by LDCs came from private banks, up from

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13. Joseph Gold, *Book Review*, 24 VA. J. INT'L L. 729, 733 (1984).

14. THE FUTURE OF THE INTERNATIONAL MONETARY SYSTEM 2-4 (Tamir Agmon et al. eds., 1984).

15. These branches were opened in the face of U.S. regulation of foreign borrowing and investment through such devices as the Interest Equalization Tax of 1964, the Voluntary Credit Restraint Program of 1965, and other misguided efforts to limit overseas lending by U.S. banks and ameliorate balance of payments problems. Eskridge, *supra* note 8, at 331. These regulations spawned the eurodollar market, which permitted dollar-denominated deposits to be kept abroad and re-lent without being subject to minimum reserve or other U.S. banking regulations. The eurodollar market, in turn, may have hastened the demise of the Bretton Woods system. *See* KENNETH W. DAM, THE RULES OF THE GAME 186 (1982).

16. MICHAEL MOFFITT, THE WORLD'S MONEY: INTERNATIONAL BANKING FROM BRETTON WOODS TO THE BRINK OF INSOLVENCY 95-106 (1983).

17. *Id.* at 55-65.

a third only three years earlier.[18] That proportion continued to increase as OPEC deposits fostered a "bank lending rush."[19] By 1980, 70 per cent of total sovereign lending came from private banks.[20] Moreover, increased exports from LDCs, between the oil shocks at least, partially offset growth in their external debt, making the LDCs' situation appear more tenable than was actually the case.[21] The lending trend, described by some commentators as a "mania,"[22] continued until Mexico defaulted on its external debt in 1982. This triggered a debt crisis, with other Latin American countries such as Argentina and Brazil headed toward default. Since then, many LDC borrowers have had to restructure their external debts repeatedly, often with the IMF, the Bank for International Settlements, the United States, and other G-10 governments assisting with a range of palliatives (such as Brady reorganizations, discussed below).

To summarize, and reduce an avalanche of scholarly literature to a sound bite, commentators seem in accord that the debt crisis was caused by a mixture of (1) oil shocks, (2) a supply-side glut of deposit money in Western banks, (3) an ideology of growth on the part of LDCs, (4) a tendency of LDCs and Western banks to respond to capital shortages in LDCs with "new money" lending rather than suspension of payments or default, (5) poor policy responses by LDCs from 1979-82 (taken in lieu of IMF-imposed rationality), (6) and inadequate domestic U.S. regulation of foreign lending.[23] For present purposes, the removal of the IMF from the LDC management loop is most significant. It seems that in the formative stages of the Latin American debt crisis, the instincts of the players in the global money market were to prod debtor countries to devise *some* corrective fiscal and economic policies, but otherwise to let LDCs muddle through without taking on harsher, politically hard-to-swallow IMF pre-

18. LOWENFELD, *supra* note 9, at 223.

19. *Id.* at 230.

20. *A Nightmare of Debt: A Survey of International Banking*, ECONOMIST, Mar. 20, 1982, at 99.

21. Eskridge, *supra* note 8, at 342.

22. *Id.*

23. Not until 1983 did Congress respond with the International Lending Supervision Act. *See* 12 U.S.C. §§ 3901-12 (1994) [hereinafter ILSA]. Professor Lichtenstein suggested that, prior to ILSA, the policy of the United States and other Western governments was one of benign neglect, underpinned by a belief that increasing private sector lending would enhance export markets. Also, it seemed a reasonable assumption that bank regulators shared the bankers' view that sovereign nations "just don't go broke." *See* Cynthia C. Lichtenstein, *The U.S. Response to the International Debt Crisis: The International Lending Supervision Act of 1983*, 25 VA. J. INT'L L. 401, 402 (1985).

scriptions.[24] These inclinations produced disastrous results. In 1983, when private banks agreed to a package of new lending to Brazil and a rescheduling of existing loans on the condition that Brazil follow the IMF's program, Brazil was in such a bad state that compliance was politically impossible.[25] In the wake of that example and others, the inescapable conclusion was that future efforts should be made to ensure consultation with the IMF and implementation of its policies before borrower countries reach the crisis stage.[26] The framework proposed in this paper is intended to cause LDCs to do just that, or risk the embarrassment of having portions of their existing sovereign obligations enforced by speculative secondary purchasers in the courts of other nations.

B. RESTRUCTURINGS

In the wake of the Latin American debt crisis came a series of restructurings of the sovereign debts of developing countries, followed in many cases by restructurings of the restructurings, and much hand-wringing about how best to handle the problem of private LDC debt.[27] The players in this continuing saga include the debtor LDCs, Western banks (the London Club), the governments of creditor nations (the Paris Club) and multi-lateral organizations such as the IMF, the Bank for International Settlements, and the World Bank.[28] A variety of methods have been devised to stanch the trauma, most notably the "Brady Plan," devised in 1989 by Nicholas Brady when he was Secretary of the Treasury, and they have met with varying degrees of success. In broad overview these methods involve an admixture of debt forgiveness, drawing out of payment schedules, the issuance of long-maturity bonds, swaps of debt for equity in newly privatized state industries, and other means of balancing the limited ability of debtor nations to service external debt with the

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24. LOWENFELD, *supra* note 9, at 307 ("[T]he perception that fund conditionality is too severe, both in its performance targets and in its intrusiveness over domestic policies and priorities, . . . led Mexico, Brazil, and the others to approach the Fund only *in extremis*, when the political risk to the officials from doing so was clearly outweighed by the risks of all the alternatives.").

25. Eskridge, *supra* note 8, at 306.

26. *See, e.g.*, E. Walter Robichek, *The International Monetary Fund: An Arbiter in the Debt Restructuring Process*, 23 COLUM. J. TRANSNAT'L L. 143, 148 (1984) ("[E]xperts and observers have been searching for ways of dealing with this tardiness on the part of both creditors and debtors, many of them calling for an even closer relationship between the IMF and banks.").

27. *See supra* note 23 (discussing U.S. responses); *see also infra* Part I.C.

28. Hurlock, *supra* note 3, at 35.

desire of creditor institutions, especially private banks, to recoup some part of their losses in this market.

Significantly, debt agreements and subsequent restructuring agreements between LDCs and private banks generally include in their terms a broad waiver of sovereign immunity, a declaration establishing the governing law of the contract (commonly that of New York or England),[29] a provision for suits under the agreement in the courts of one or more countries (most often the United States) and procedural provisions to be applied in the event restructuring becomes necessary.[30] Despite all these boilerplate provisions, which seem necessary to get smaller members of loan syndicates on board, major creditors of LDCs do not attempt to enforce such agreements through the courts. The reasons follow from the adage "you cannot squeeze blood from a turnip." Thus, consensual renegotiation is the norm, even if it does not always go smoothly.[31]

The process begins when a country cannot service its debts according to existing agreements because its currency reserves are or may be jeopardized. The country will then take stock of its situation and set about formulating a renegotiation plan. While such plans often include private sector debtors located within LDCs and Paris Club creditors,[32] the focus here is on the approach LDC debtors generally take with respect to their London Club creditors. Within this category, the details, such as what sub-categories of debt (secured debt, private placements, precious metals contracts, etc.), what mix of principal and interest, and what maturities the debtor country will seek to renegotiate, are for the most part not important. It is assumed for present purposes that any renegotiation will seek to modify the obligations of an existing debt agreement, a subtranche of which the secondary buyer has purchased and would like to see performed according to its terms.

C. RELEVANT CLAUSES OF RESTRUCTURING PLANS

Renegotiation plans, like original debt agreements, will typically include a number of provisions that bind the fortunes of the secondary purchaser to that of its fellow creditors and are relevant to attempts made by secondary purchasers to enforce the obligations of the debtor through the courts. The following

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29. *Id.* at 39.
30. *Id.*
31. *Id.* at 44.
32. *Id.* at 34.

standard clauses are most significant here, as their presence or absence may guide a court in gauging the bona fide claims of a plaintiff creditor.

Cross default clauses link together the LDC's various creditors by making it "an event of default"[33] under an original agreement or a renegotiated agreement if the sovereign defaults on any other debt agreement to which it is a party. In such an event, creditors armed with cross default clauses will be entitled to declare a default, rendering all relevant loans subject to acceleration. These provisions are pressed upon debtor nations on the grounds that all creditors, including commercial creditors, should be treated in pari passu, notwithstanding that they may individually be party to multifarious agreements, which may or may not be in default. Significantly, renegotiated agreements will often exclude any failure to make payments to commercial creditors who are not party to the renegotiation from the scope of cross-default provisions. Such an exclusion may have the effect of coaxing reluctant but non-litigious creditors to sign on to the restructuring. As such small creditors will be aware, a troubled LDC will first default on obligations to creditors excluded from the scope of cross-default clauses. If such a default occurs, and to the extent the big banks have waived a cross-default clause in their attempts to induce recalcitrant smaller creditors to accede to an objectively unfair restructuring plan, a secondary purchaser may appear justified in using the courts to enforce its share of the LDC's debt. On the other side of the cross-default coin, each individual creditor theoretically retains the right not to participate in the consensual renegotiation and may indeed initiate litigation to enforce existing debt agreements.[34] The presence of sharing clauses, however, may still make it unattractive for an excluded creditor to sue in its own right.[35]

A sharing clause is an undertaking whereby each party to a debt agreement or renegotiation agrees to share any funds received from the debtor pro-rata with all other parties to the syndicate, or possibly all other commercial creditors of the LDC.[36] This will usually mean sharing with hundreds of banks leaving

33. *See id.* at 41.

34. *See* Derek Asiedu-Akrofi, *Sustaining Lender Commitment to Sovereign Debtors*, 30 COLUM. J. TRANSNAT'L L. 1, 13 (1992).

35. As to whether sharing clauses are effective means of countering nuisance suits by secondary purchasers, see *infra* Part II.D, discussing various devices employed to avoid the "sharing" mandated by the clause.

36. Such a case might arise where the same major London Club banks are involved in all or most of the LDC's commercial credits.

a tiny pro-rata fraction of the pie left in the hands of the originally receiving party. The clause will typically cover both voluntary payments by the debtor to the agent bank managing the loan (requiring the proceeds to be distributed by the agent) and proceeds from judicially imposed judgments. In the latter case a judgment creditor complying with the clause pays other banks their share or else purchases participations in the proceeds from them (which is effectively the same thing).[37] The motive behind these clauses is to ensure that no creditor receives more favorable treatment than others and to encourage creditors not to hold out from renegotiation. This goal is particularly applicable in situations where commercial creditors are fearful that the proceeds from new credits are being used to pay off pre-existing loans in a manner prejudicial to their interests.

Other common provisions are "required banks" clauses, which set forth a threshold percentage of banks required to take certain actions pursuant to an original or renegotiated debt agreement. The particular actions for which consent is required will vary, as will the percentage threshold for different actions.[38] These clauses typically require that a majority or super-majority[39] of all creditors agree to a renegotiation plan in order to bind non-consenting creditors to the new plan. As discussed below, a "required banks" clause was at the heart of the controversy between the Dart family and Brazil. [40]

D. U.S. POLICIES TOWARD SOVEREIGN DEBTORS AND RESTRUCTURINGS

This section presents U.S. responses to the debt crises of LDCs in order to show that the U.S. policies support cooperation and consensual action in the resolution of international debt problems. In all circumstances, these policies were made with the advice and approval of the IMF, and are germane to the argument made in Part IV.

37. Asiedu-Akrofi, *supra* note 34, at 14.

38. Hurlock, *supra* note 3, at 42.

39. *See, e.g.*, Philip J. Power, *Sovereign Debt: The Rise of the Secondary Market and Its Implications for Future Restructurings*, 64 FORDHAM L. REV. 2701, 2742-44 (1996) (describing supermajority vote requirements in syndicated loan agreements).

40. *See infra* notes 74-85 and accompanying text. In the early 1990s, Brazil engaged in a large buy-back of its own debt, such that it became its own majority creditor, and then proceeded to try to foist a renegotiation on the Darts. The Darts sued, claiming such action was an improper method of circumventing a required banks clause.

1. *International Lending Supervision Act of 1983 (ILSA)*

The first non-hortatory[41] U.S. response to the debt crisis was the International Lending Supervision Act of 1983 (ILSA),[42] which increased the U.S. quota in the IMF and directed the Comptroller of the Currency, the Federal Reserve, and the FDIC to promulgate regulations implementing the policies of their 1983 Joint Memorandum on the regulation of international lending.[43] One of the elements of the Joint Memorandum was a proposal that when a debtor country has been unable to service its debts for a protracted period of time, in specified circumstances creditor banks should be required to set aside loss reserves akin to ordinary loan loss reserves required by U.S. banking regulations.[44] For present purposes it is enough to note that ILSA exempts loans from the special reserve requirement where the debtor country is complying with the terms of an IMF-approved economic stabilization program. As noted, "[t]hese categories, which are used in bank supervisory agency evaluations of bank asset quality . . . , are remarkable in the emphasis which is put on IMF adjustment programs and on the existence of multi-bank rescheduling programs."[45] Thus, in setting up this scheme, Congress sought to devise a system that would motivate private lenders to restructure LDC debt and to ensure LDC compliance with IMF stabilization programs.[46] This is illustrative of the policy underlying the U.S. regulatory response to the debt crisis, which was to assume the soundness for accounting purposes of troubled loans to debtor countries that are within an IMF adjustment program, and presume the unsoundness of troubled loans that are not restructured and/or not within an IMF program.

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41. In response to an episode where U.S. commercial banks had made new money loans to Indonesia in violation of IMF conditions, Congress admonished U.S. banking regulators to be more diligent in policing inadvisable loans but did not include specific directions in, for example, the Bretton Woods Agreement Act Amendments of 1977. Lichtenstein, *supra* note 23, at 411.

42. Pub. L. No. 98-181, 97 Stat. 1278 (codified at 12 U.S.C. § 3901-12 (1994)).

43. *See Proposed Solutions to the International Debt Problems: Hearings on S. 502 and S. 695, Before the Senate Committee on Banking, Housing and Urban Affairs*, 98th Cong., 1st Sess. 25 (1983) (Joint Memorandum reprinted) [hereinafter Joint Memorandum].

44. Unlike normal loan loss reserves, ILSA-mandated reserves cannot count as capital. For further discussion of the technical workings of ILSA, *see* Troland S. Link, *The Value of Bank Assets Subject to Transfer Risk*, 23 COLUM. J. TRANSNAT'L L. 75, 77-80 (1984).

45. *Id.* at 79.

46. Lichtenstein, *supra* note 23, at 416.

2. International Debt Management Act of 1988 (Debt Management Act)

This piece of legislation formally recognized a policy in favor of restructuring and reduction of outstanding LDC debt, noting that "current approaches to the debt problem should not rely solely on new lending as a solution to the debt problem and should focus on other financing alternatives including a reduction in current debt service obligations."[47] As noted above, insolvent LDCs and their commercial creditors were generally inclined to arrange more loans in the hope that LDCs would "grow out of" situations of insolvency. Early on in the debt crisis, this had been the most politically palatable course of action for the debtors, as it permitted avoidance, or rather postponement, of the necessity of conferring with the IMF and taking its austere medicine. Moreover, as ILSA recognized, further lending enabled bankers to keep existing loans current on their financial statements. Against this backdrop, and recognizing that wholesale forgiveness would cause irreparable damage to LDC bank creditors,[48] and likely cause them to withdraw the market for new loans, the Debt Management Act further announced that it is "the policy of the United States that . . . it is necessary to broaden the range of options in dealing with the debt problem to include improved mechanisms to restructure existing debt."[49]

3. Support for East European Democracy Act of 1989 (SEED Act)

While scholarly commentary relating to the international debt crisis has for the most part focused on Latin American borrowers,[50] the situation faced by certain former Soviet bloc countries such as Poland and Hungary was similarly dire in the 1980s.[51] The economic problems of these countries became more topical as the decade wore on, as newly elected governments inherited the sovereign obligations of their communist predecessors, sought membership in the IMF, and further courted Western capital. Following Treasury Secretary Brady's lead (discussed below), the United States responded to these changes

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47. 22 U.S.C. § 5322 (1994).

48. Lichtenstein, *supra* note 23, at 414.

49. 22 U.S.C. § 5324 (1994).

50. Eskridge, *supra* note 8, at 283 (noting also that the debt figures for the Latin American borrowers were the most dramatic).

51. *See, e.g., Western Creditors to Meet with Poland on Its Official Debt*, WALL ST. J., Nov. 21, 1984, at 34 (reporting on Poland's negotiations with creditor governments to restructure $15 billion in debt).

with the SEED Act of 1989.[52] The SEED Act delineates a broad U.S. policy in favor of Poland and Hungary on a host of issues, among which are a lead role for the United States in "mobilizing . . . [the IMF] and . . . the World Bank group, to provide timely and appropriate resources to help Poland and Hungary."[53]

Regarding debt relief, the SEED Act provides first that the United States "shall urge all members of the 'Paris Club' of creditor governments . . . to adopt, and participate in, a generous and early rescheduling program."[54] Second, it provides that the United States shall coordinate with other governments "to facilitate a rescheduling and reduction of payments due on debt owed to [private] creditors in a manner consistent with the international debt policy announced by the Secretary of the Treasury on March 10, 1989."[55] The SEED Act authorized $200 million in cash stabilization assistance to Poland. In its current incarnation, the SEED Act refers to Poland and Hungary, but its legislative history indicates a general commitment to reform in Eastern Europe,[56] with IMF involvement a cornerstone of the process.[57]

4. *The Brady Plan*

In March 1989, Secretary of the Treasury Nicholas Brady announced a plan under which the United States government would throw its weight behind efforts to resolve the LDC debt problem, including plans for the securitization of LDC debt into marketable bonds of long maturity, backed in turn by U.S. treasury securities.[58] These came to be known as Brady Bonds. The plan constituted an official U.S. recognition that developing countries would never be able to repay their foreign debts in accordance with existing contractual commitments. The bold action taken by Secretary Brady sought to balance the inability of LDCs to pay in the near-to-medium term with the demands of commercial creditors that some substantial repayment occur eventually. As the Mexican monetary crisis of 1995 illustrates, the Brady scheme has not been a complete answer to all LDCs'

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52. Pub. L. No. 101-179 (1989) (codified at 22 U.S.C. § 5401-95 (1994)).
53. 22 U.S.C. § 5411(a)(1) (1994).
54. *Id.* § 5411(b)(2) (1994).
55. *Id.*
56. *See* H.R. REP. No. 101-278, at 744 (1989) ("the Committee believes that the United States has a strong national interest in supporting, consolidating, and furthering economic and political evolution in Eastern Europe").
57. 22 U.S.C. § 5401(c) (1994).
58. LEHMAN BROTHERS, BRADY BOND MARKET HANDBOOK 3 (1995).

economic problems, but it has in large measure smoothed over standoffs between LDCs and their commercial bank creditors.[59] In sum, the plan clarified U.S. support for the restructuring process and further emphasized the need for debt *reduction* as a means of spurring economic growth and additional lending further down the road.

5. *Summary*

The International Lending Supervision Act and the International Debt Management Act in general, and the Brady Plan and the SEED Act in particular, demonstrate that the policy of the United States is to support debtor governments to the extent they pursue political and economic policies which are consonant with IMF policies, including support for consensual sovereign debt restructurings. While these laws and their underlying policies evolved recently, they are unambiguous and, as argued below, they should be subject to judicial notice in litigation between debtor nations and their commercial creditors.

II. THE SECONDARY MARKET AND LAWSUITS ARISING THEREFROM

As commercial lending became the predominant source of imported capital for LDCs, sovereign debt began to trade at a discount in the 1980s, much like normal commercial debt instruments. In reactions to the cycle of crises LDCs had faced, many original lenders of LDCs sought to liquidate LDC debt paper for whatever the market would bear. This trend spawned and fostered an international secondary market, which has since grown rapidly.[60] The growth of this market has brought a number of positive effects. First, secondary trading allows the risks of LDC defaults to be transferred from a conservative regional U.S. bank[61] to assignees better able to bear the risk or even use it to their advantage. The market permits disaffected or risk-averse

59. *See, e.g.*, *Brazil to Begin Paying $8-Billion Interest Debt*, L.A. TIMES, Apr. 9, 1991, at D5 (reporting deal to pay $2 billion cash and $6 billion in bonds that ended a two year standoff with commercial lenders).

60. *See, e.g.*, *Review & Outlook: The Baker Plan Lives*, WALL ST. J., Apr. 6, 1989, at A13.

61. *See, e.g.*, Asiedu-Akrofi, *supra* note 34, at 3 ("Except for the large international banks [the prevalence of bank solidarity in syndicated lending] has now ended, and the underlying differences in exposure levels and business strategies are becoming important determinants of individual bank decisions . . . . Regional and small exposure banks are, for example, redirecting their lending activity toward traditional domestic and trade financing.").

institutions to get out of the unstable cycle of crises, reschedulings and, worst of all, involuntary lending as is often necessary to avoid meltdowns in the wake of crises.[62] Second, secondary market sales of LDC debt reduce undesirable retention of troubled and overvalued loans on bank balance sheets. The discounts from par in this market are often huge, and in some cases sovereign debt instruments have sold for pennies on the dollar.[63] This fact underscores the accounting concerns associated with keeping troubled sovereign loans on banks' balance sheets at full value. Third, the secondary market gives financial analysts an incentive to monitor and collect information about LDCs. The lack of such information was considered a problem for banks in the 1970s as banks, which were ill-equipped to assess LDCs' creditworthiness, tended to make LDC loans "blindly." Thus, while problems may arise where secondary purchasers of sovereign debt resort to the courts, the development of the secondary market has been of considerable benefit to the international financial system.

A. LAWSUITS BY SECONDARY PURCHASERS OF SOVEREIGN DEBT

A secondary buyer assumes the rights of its predecessor(s) in interest, including a legal right to receive principle and interest payments under the original agreement. Whether and when a buyer may sue in the face of a restructuring agreement and win special treatment for itself remains an open question.[64] Commentators acknowledge the possibility of legal action,[65] but research reveals few instances where this course of action has

62. *See id.* (noting that most regional U.S. banks cleared their portfolios of bad sovereign debt by selling at deep discounts into secondary market).

63. *See, e.g.*, Paul M. Sacks, *Let Banks Close the Value Gap: Secondary Markets Could Be Route Out of Latin Debt Crisis*, L.A. TIMES, May 22, 1987, Op. Ed. 2 (reporting that Sudan's debt traded at two cents on the dollar).

64. This question certainly could be asked with respect to original parties to debt agreements. The aim here, however, is to demonstrate that the inquiry is more applicable to secondary purchasers for reason of the smaller and hence more enforceable claims of secondary buyers, on the one hand, and the disinclination of foreign and regional U.S. banks to engage in litigation, on the other. Explanations for this latter attitude might include docility, ease of secondary sales as compared to the costs and uncertainty of litigation (especially in New York or London, which are normally specified in commercial debt agreements as the forums where the debtor consents to jurisdiction in litigation arising under such agreements), or a combination of these.

65. *See, e.g.*, Hurlock, *supra* note 3, at 44 ("Banks who choose not to sign the renegotiation agreement may make threats or commence legal action against the sovereign for repayment of their debt according to . . . the original loan documents.").

resulted in a trial and a published judicial opinion. Despite a paucity of authority, one commentator asserts that threats, litigation, and other coercive "tactics [by individual creditors] are much more common than might be expected and are practiced by a surprising range of institutions."[66] It should come as no surprise that such practices rarely result in litigated judgments and published case reports, since the recalcitrant creditor is interested only in a quick, strike-suit type settlement, and not in winning and enforcing a judgment in full. This dynamic makes settlement exceedingly likely.[67]

It is worth noting here that LDCs will normally have waived sovereign immunity and made themselves amenable to process under the terms of sovereign debt agreements.[68] Thus, while the enforceability of any plaintiff's judgment will be limited to certain commercial assets, the sovereign debtors, who in borrowing from banks are deemed to be acting in a commercial capacity, will in the majority of cases face enforcement actions in U.S. federal courts under the Foreign Sovereign Immunities Act,[69] or in the courts of other countries. Practical limitations

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66. Christine A. Bogdanowicz-Bindert, *The Role of Financial Advisors in Bank Debt Reschedulings,* 23 COLUM. J. TRANSNAT'L L. 49, 54 (1984); *see also, e.g.*, Weston Compagnie de Finance et d'Investissement, S.A. v. La Republica del Ecuador, 823 F. Supp. 1106, 1108 (S.D.N.Y. 1993) (suit by Swiss financial institution, a substantial part of the business of which involved the acquisition and trading of Latin American debt); Banque de Gestion Privee-Sib v. La Republica de Paraguay, 787 F. Supp. 53, 54 (S.D.N.Y. 1992).

67. Practical considerations may explain the dearth of published cases on point and give reason to think that a small number of published case reports provides no indication of the frequency with which these suits are brought. Certainly speculative purchasers (and their lawyers) are unlikely to litigate these cases vigorously in court and up through the appellate process, for an appellate precedent declaring that such lawsuits may (for whatever reason) not be maintained would be a disaster. Nor will defendant LDCs want to risk having an appeals court declare in a published opinion that these suits are proper because that would make plaintiffs' lawyers' threats to take such cases to trial more credible, necessitating higher settlement offers. Thus, both sides benefit from the uncertainty that shrouds this type of litigation, and the incentive to settle is very strong indeed. As noted elsewhere, such a dynamic seems to operate anytime plaintiffs' lawyers develop a novel or unusual type of nuisance suit. *See* Theodore Allegaert, Comment, *Derivative Actions By Policyholders on Behalf of Mutual Insurance Companies*, 63 U. CHI. L. REV. 1063, 1066 n.15 (1996).

68. *See* Hurlock, *supra* note 3, at 34; *see also infra* notes 159-68 and accompanying text (the doctrines of comity and the act of state are generally not applicable to suits to enforce sovereign debt).

69. 28 U.S.C. §§ 1602-11 (1994). The FSIA establishes federal subject matter and personal jurisdiction over foreign states where the sovereign is not entitled to immunity under sections 1605-07 or under any applicable international agreement. This includes instances where the sovereign has waived immunity expressly or by implication and where the sovereign has engaged in commercial

on the enforcement of judgments account for the fact that major London Club creditors generally do not view litigation as a worthwhile option.[70] Suits by "smaller" plaintiffs, however, are more credible: judgment will be more readily enforceable, since virtually any LDC will at any given time have a couple of million dollars' worth of commercial assets present in the United States which might be attached.

As to the frequency with which "smaller" plaintiffs resort to the courts, the evidence available is modest. Anecdotal evidence from conversations with lawyers in New York lends support to the assertion above that suits by secondary creditors are common.[71] One recent lawsuit reported in the British press involved a British Virgin Islands-registered investment company suing Vietnam's largest state-owned bank for repayment of a $1.5 million dollar portion of Vietnamese sovereign debt in the High Court in London.[72] The lawsuit hindered a proposed rescheduling of $800 million in Vietnamese debt owed to the London Club. Perhaps because the stakes were high, and the value of the claim comparatively low, the settlement reached was reportedly quite generous. This settlement in turn created worries among English bankers and lawyers that other non-London Club assignees of Vietnamese or other LDC debt would be encouraged to seek their own settlements through the courts.

activities, including commercial loans. *See* 28 U.S.C. § 1605(a)(1)-(2). This is in keeping with the "restrictive" view of sovereign immunity adopted by the State Department after World War II, under which foreign governments are not entitled to immunity for their actions.

70. *See* Eskridge, *supra* note 8, at 346 (noting that "only the property in [the United States] used for the commercial activity upon which the claim is based" may be attached). This in theory is limited to "the loan," but as a practical matter cross default clauses in the loan will enable the debt of state trading companies to be accelerated and their assets attached. One trader at CS First Boston with whom I spoke suggested that one of the factors which kept Peru honest in its dealing with creditors, despite its extreme political climate, was the fear that wholesale repudiation of its external debt obligations might result in the confiscation of its newly-nationalized oil tankers when they pulled into, for example, Galveston Harbor.

71. A "bank" or "financial institution" will virtually always be the plaintiff in this type of lawsuit. Before an assignment to a non-bank assignee will be accepted by the international agent, debt agreements by their terms usually require that the assignee agree to be bound by any restructuring agreed to by a lesser majority of commercial creditors than normally necessary to bind dissenting bank creditors.

72. *See* Jeremy Grant, *Offer Saves Vietnam Assets*, FIN. TIMES, Jan. 25, 1996, at 6.

Bankers fear such a state of affairs will further complicate London Club negotiations.[73]

B. *CIBC BANK*: THE DART LITIGATION

The controversy that brought the potential profitability of secondary purchases of LDC debt to the world's attention arose between Brazil and Florida's Dart family.[74] The Darts, of Styrofoam cup fame, instructed traders at Salomon Brothers (of which they own 5%) to begin buying Brazilian debt paper unobtrusively on the secondary market, which they then assigned to a specially created Cayman Islands "bank."[75] Within a year, after buying from creditor banks at prices between 25 and 40 cents on the dollar, the Cayman bank became the fourth largest single holder of Brazilian Debt. During this period the Darts had converted their holdings at face value into "capitalization bonds," the coupons of which were due to rise over the next six years. In 1993, however, Brazil cut a deal with Citibank and other large U.S. bank creditors to convert 35% of its outstanding debt, including the Darts' holdings, into other bonds at substantially less than face value. The Darts refused to accede to this and proceeded to engage Brazil in a "colossal game of chicken," the aim of which was to secure a deal for themselves substantially better than the arrangement agreed to by the big banks and finance ministry officials, but without going so far as to cause the restructuring to collapse.[76]

The Darts brought suit in federal court in New York a year later, seeking accelerated repayment of principal and interest on their bonds.[77] By that time, Brazil, acting through its central bank, had swapped $49 billion of debt for the discounted bonds which the Darts had spurned. In doing so, Brazil had become the holder of record for 95% of the debt issued under its 1988

73. *See id.*

74. *See* Gilpin, *supra* note 2, at 37; Kenneth N. Gilpin, *Dart Family Files Lawsuit to Nudge Brazilian Bank*, N.Y. TIMES, June 30, 1994, at D5; CIBC Bank and Trust Company (Cayman) Ltd. v. Banco Central do Brasil, 886 F. Supp. 1105 (S.D.N.Y. 1995) (denying defendant's motion to dismiss).

75. This maneuver was allegedly designed to avoid provisions in Brazil's 1988 debt agreement requiring that assignment to non-financial institutions be accompanied by an "Agreement to be Bound" to any restructuring. CIBC Bank, 886 F. Supp. at 1108. Brazil, in its motion for summary judgment, argued that this was improper. The court, while acknowledging that this argument "may yet prove to be correct," refused to accept it at the summary judgment stage. *Id.*

76. *See* Laurie P. Cohen, *Tug of War: Brazil Debt Deal Pits Nation and U.S. Banks Against Dart Family*, WALL ST. J., Nov. 30 1993, at A1.

77. Gilpin, *supra* note 74, at D5.

debt agreement. The Dart holdings were part of the remainder. The Darts' complaint alleged that Brazil's tactics relieved them of any obligation to be bound by the ensuing restructuring. In a motion for summary judgment, Brazil argued the contrary and asserted that the assignment from the Darts to their Cayman Islands bank was an improper attempt to circumvent the provisions in the 1988 debt agreement requiring non-bank assignees to go along with the restructuring. Judge Preska, noting that a ruling on the merits of either side's position required factual findings, denied the defendant's motion for summary judgment.[78] Subsequently, the two sides reached a settlement under which Brazil agreed to pay the Darts $25 million in cash and $52.3 million in bonds to cover past-due interest on the Darts' debt holdings, the market value of which increased substantially with the news that Brazil was on the verge of concluding negotiations with its creditors and resuming debt service.[79]

The Dart case is interesting in that it brought to light a type of controversy which is otherwise unlikely to be published in the press or in case reports. Indeed, as one trader noted, "[t]his kind of problem is not new, . . . but it usually occurs with smaller people. If the Darts had a smaller position, I think there would be an attempt to buy them out."[80] Thus, it appears that these "problems" can fairly be described as nuisance suits (or incipient ones, pre-filing): potential plaintiffs bring these actions not to litigate the merits and reap a full judgment, but rather for some quick settlement value over the price they paid for their rights. On that score, it is worth noting that Brazil had moved for summary judgment under New York's champerty statute,[81] citing the fact that the Darts' Cayman Islands bank had brought suit on its debt on the very first day possible after a contractually mandated post-assignment waiting period. As with the standing issue, Judge Preska held that champertous intent is a factual matter which could not be ruled on as a matter of law.[82]

The latter part of the federal court decision illustrates the toothlessness of champerty laws in the context of lawsuits by

78. CIBC Bank, 886 F. Supp. at 1111.

79. Gilpin, *supra* note 74, at D5.

80. Gilpin, *supra* note 2, at 37.

81. N.Y. JUD. LAW § 489 (McKinney 1995) (providing that "[n]o . . . corporation . . . shall . . . buy or take an assignment of . . . a bond [or other debt instrument], with the intent and for the purpose of bringing an action thereon").

82. CIBC Bank, 886 F. Supp. at 1111.

secondary purchasers of LDC debt.[83] As the Dart case suggests, such purchasers are usually fly-by-night offshore "banks" for whom an adverse finding of champertous intent will be of little practical consequence, even if the question were ever to get to a jury. Thus, a ruling on champerty puts the plaintiff out of court and once in a while costs the plaintiff the other side's attorney fees, but rarely if ever will the plaintiff be deprived of the ability to resell the debt paper and turn a profit. In sum, the ineffectiveness of champerty laws, coupled with the difficulty of winning summary judgment in cases involving complex contractual relationships, suggests the need for a novel approach by judges in the adjudication of such actions.

Beyond the practical difficulties in fending off these actions, this kind of litigation is inequitable and inconsistent with U.S. policy. In the Dart case, the United States filed an *amicus curiae* brief in support of Brazil, signed by officials from the Justice, Treasury, and State Departments, an unusual step for the United States to take in a civil dispute involving international debt agreements.[84] The U.S. government's brief stated flatly that

> [b]ecause the United States has a strong interest in encouraging the voluntary restructuring of sovereign debt . . . [it] does not wish to see a creditor use United States courts as a means of amending the terms of sovereign debt contracts [on the grounds that such action] would harm the process that has evolved to deal with sovereign debt problems.[85]

In light of the subsequent settlement, Judge Preska's refusal to grant summary judgment in the face of the government's opposition to the suit gives an even greater indication that a new approach is called for to enable judges to counter such lawsuits effectively when the equities of the situation support dismissal. Such an approach will be particularly desirable in suits by smaller holders seeking to be bought out at a premium, since the U.S. government would be less likely to go to the trouble of registering its opposition.

83. *See also* Banque de Gestion Privee-Sib v. La Republica de Paraguay, 787 F. Supp. at 56 ("whether assignee subsequently [to the assignment] forms an intent to sue . . . under the assignment is irrelevant for purposes of [New York's anti-champerty provision]").

84. Thomas T. Vogel, *U.S. Files Brief Supporting Brazil in Dart's Debt-Interest Suit*, WALL ST. J., Sept. 16, 1994, at B4.

85. *Id.*

III. THE FUND AGREEMENT

The Bretton Woods System and the IMF were created in 1945 by the Articles of Agreement of the International Monetary Fund, known as the Bretton Woods Treaty or the Fund Agreement.[86] The IMF is a multilateral institution providing balance of payments assistance to member nations and administering a system of rules designed to shape economic events in the international financial sphere.[87] The goals of the Fund are complex and not necessarily in harmony with each other in certain circumstances. Moreover, the role of the IMF in the international financial system has changed over the years, particularly with the demise of the par-value currency system in the 1970s and the creation of the Special Drawing Right, events which are not pertinent here. Despite competing goals and vast changes in the international financial system and the IMF's role, the first purpose of the Fund Agreement remains fixed: "to promote international monetary cooperation"[88] in order to promote the growth of world trade and foster stability in the financial sector. This section discusses some general difficulties that lawyers and judges have faced in interpreting the Fund Agreement and applying it to legal problems. The crux of the matter is that in interpreting the Fund Agreement and applying it to concrete cases, the "plain meaning" of the text is at best the tip of the interpretive iceberg.

A. THE DRAFTING OF THE FUND AGREEMENT

The preliminary groundwork for the Fund Agreement was largely performed during World War II by Harry Dexter White (of the United States) and Lord Keynes.[89] Their ideas and proposals for a post-war international monetary system differed in a number of respects, particularly their views on the desirability of exchange controls.[90] As Professor Dam has noted, this "conflict in ideologies [between the United States and United Kingdom] concerning the functions of economic policy and the role of the government in economic life complicated agreement on the

86. Fund Agreement, *supra* note 5, art. I(i).
87. DAM, *supra* note 15, at 115.
88. Fund Agreement, *supra* note 5, art. I(i).
89. John S. Williams, *Extraterritorial Enforcement of Exchange Control Regulations Under the International Monetary Fund Agreement*, 15 VA. J. INT'L L. 319, 322 (1975).
90. Keynes thought exchange controls, at least on capital movements, were beneficial and should be a permanent part of the post-war system. DAM, *supra* note 15, at 76.

details of postwar international monetary organization."[91] Thus, the drafting of the Fund Agreement was characterized by hard bargaining, compromise, and different levels of influence by the United States, United Kingdom and the other Bretton Woods delegations.[92] Inevitably, this process of drafting by nations with different views and agendas[93] resulted in ambiguity, contradiction, and at times opaqueness in the Articles of the Fund Agreement.[94] This is especially true from the vantage point of a non-expert.[95]

To take a germane example of such a contradiction, Article I of the Fund Agreement states that "foreign exchange restrictions which hamper the growth in world trade" are undesirable and should be eliminated.[96] Article VIII, however, provides for the maintenance of exchange controls in a number of circumstances, some to be valid during a transitional period and others permanently. Since exchange controls persist to this day, particularly with respect to capital transactions, Article VIII would appear to have trumped Article I. This could not have been known ex ante from the text of the Fund Agreement or its *travaux préparatoires*.[97]

The Fund Agreement left much to be worked out in the evolution of the new Bretton Woods System and to later interpretation of various provisions. As Sir Joseph Gold, the longtime general counsel to the IMF, states in his comprehensive treatment of the law of the Fund Agreement: "[t]he problem then will be to decide which purpose or purposes [of the Articles of the Fund Agreement] are to be given decisive weight in order to increase the likelihood that over time all the purposes of the fund can be realized."[98] Thus, in grappling with the Fund Agreement, it is almost always ill-advised and incorrect for courts to interpret the "plain meaning" of specific provisions of

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91. *Id.*

92. Williams, *supra* note 89, at 323.

93. *See* FREDERICK A. MANN, THE LEGAL ASPECT OF MONEY 383 n.39 (Clarendon Press 4th ed. 1982) ("The conference of 44 nations and about 200 delegates was an unusually rushed and confused affair. . . . The delegates believed they had covered a great field of intellectual and technical difficulty which many, it seems, later confessed not to have understood." (citing XXVI THE COLLECTED WORKS OF JOHN MAYNARD KEYNES 96-113 (1980))).

94. *Id.* ("The Articles of Agreement as a whole are . . . full of discrepancies and drafting obscurities . . . .").

95. DAM, *supra* note 15, at 85.

96. Fund Agreement, *supra* note 5, art. I(iv).

97. 2 JOSEPH GOLD, THE FUND AGREEMENT IN THE COURTS app. A at 437 (1982).

98. *Id.* at 3.

its text without considering expert commentary and available case precedent.

B. INTERPRETATION OF THE FUND AGREEMENT BY THE IMF

One issue of ongoing dispute is whether official IMF interpretations of the Fund Agreement are binding on the courts of member nations. Shortly after the implementation of the Fund Agreement, one commentator, Mr. Bernard Meyer, predicted that "[U.S.] courts will give conclusive effect in private litigation to Fund interpretations," despite the fact that the article providing for Fund determinations was not incorporated into U.S. domestic law by the Bretton Woods Agreement Act.[99] More recently, Sir Gold took the view that official IMF pronouncements are binding in advance on the courts of member nations, and he presented case law where courts appear to have considered themselves bound by the IMF's interpretation.[100] Still another commentator, Mr. Williams, challenged this view on the grounds that two of the U.S. cases Sir Gold cited were overruled on appeal.[101]

Dr. F.A. Mann, in *The Legal Aspect of Money*, asserted that "it is both the right and the duty of the courts to construe [provisions of the Articles], and . . . there is no justification for the opinion that 'in view of Article XIII of the Agreement,[102] it is undesirable for [courts] to express a view [on the subject].'"[103] Whatever differences there may be between Sir Gold, Dr. Mann and others on this issue, it appears that from the 1950s onward courts have not hesitated to make their own interpretations of

99. Bernard S. Meyer, *Recognition of Exchange Controls After the International Monetary Fund Agreement*, 62 YALE L.J. 867, 883 (1953) (Article XIII (as it then was) provided for official interpretations by the Board of Governors of the IMF). Under the Second Amendment to the Articles of Agreement, effective April 1, 1978, the provision for authoritative interpretation of the Articles was moved to Article XXIX. *See* GOLD, *supra* note 97, at xi. Mr. Meyer asserts that the fact that Article XIII was not given "the force of law" by Congress when it incorporated the Fund Agreement into domestic law is of small consequence, since the entire Fund Agreement, as a "congressional-executive agreement," would be the supreme law of the land. Meyer, *supra*, at 880.

100. GOLD, *supra* note 97, at 5-6.

101. Williams, *supra* note 89, at 331-32.

102. Now Article XXIX (*see supra* note 99).

103. MANN, *supra* note 93, at 383 (quoting Kahler v. Midland Bank, 1 All E.R. 811, 819 (1948)). A similar reluctance to interpret the Articles of Agreement was expressed contemporaneously with *Kahler* by an appellate court in New York. *See* Cermak v. Bata Akciova Spolecnost, 80 N.Y.S.2d 782, 785 (1948).

the Fund Agreement.[104] As a result, there is a notable lack of uniformity in judicial constructions of the Fund Agreement by the courts of various nations.[105]

From the mass of conflicting accounts and the abundance of cases interpreting the Fund Agreement, one commentator has reasonably concluded:

> a court may decide [for itself] whether or not an interpretation of the Fund Agreement is legally correct and therefore binding upon it, although an interpretation by the Board of Governors under Article XIII may be highly persuasive as to what the correct interpretation of such a provision should be. [Nevertheless,] a court is bound . . . only because it has determined *on its own* that its interpretation is legally correct.[106]

Thus, in cases involving the Fund Agreement brought in U.S. courts, existing and future IMF interpretations of the Fund Agreement may provide a sound basis for overruling prior judicial interpretations of relevant provisions, to the extent judges are willing lend decisive weight in considering such pronouncements.

C. INTERPRETATION OF THE FUND AGREEMENT BY COURTS

As a treaty, the Fund Agreement should be broadly construed and where necessary, re-construed to effect its underlying purpose, "to promote international monetary cooperation."[107] Treaties in general, and the Bretton Woods Treaty in particular, should not be construed in the same manner as domestic legislation. As one English judge has said, "[t]he language of an international convention . . . is neither couched in the conventional English legislative idiom nor designed to be construed exclusively by English judges."[108] Accordingly, a treaty should be interpreted "unconstrained by technical rules of English law, or by English legal precedent, but on broad princi-

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104. Williams, *supra* note 89, at 332 n.57.

105. *See infra* notes 107-115 and accompanying text.

106. Williams, *supra* note 89, at 330 (emphasis in original).

107. Fund Agreement, *supra* note 5, art. I(i); Williams, *supra* note 89, at 324-25. In regard to treaty construction by U.S. courts, *see, e.g.*, Air France v. Saks, 470 U.S. 392, 396 (1985) ("Treaties are construed more liberally than private agreements, and to ascertain their meaning we may look beyond the written words to the history of the treaty, the negotiations, and the practical construction adopted by the parties."); Maritime Ins. Co. v. Emery Air Freight Corp., 983 F.2d 437, 440 (2d Cir. 1993) ("when language is unclear, courts are enjoined to construe treaties more liberally than private agreements").

108. GOLD, *supra* note 97, at 5-6 n.5 (quoting Fothergill v. Monarch Airlines, 2 All E.R. 696, 706 (1980)).

ples of general acceptation."[109] The gist of these observations is no less applicable to other forums, especially common law forums such as the United States, where domestic legal precedent may stand in the way of the soundest interpretation of the treaty.

For example, if a given provision of the Fund Agreement was intended to provide a rule of uniform substantive law for all members, then it makes no sense for courts to evaluate a controversy only in light of legal conceptions which are peculiar to its forum.[110] If precedent is to be used, then the experience of the courts of other member nations whether common law or not ought to be as persuasive to a U.S. tribunal in this context as domestic precedents. Indeed, it is an open question whether stare decisis is properly applicable to interpretations of a complex and vaguely worded treaty where as here the economic framework within which the treaty operates may change over time.

Further along these lines, Sir Gold has observed that the uniformity and soundness of judicial treatments of the Fund Agreement have been limited by the tendency of lawyers to rely on domestic authorities in briefing issues before courts. Whether through neglect or inaccessibility of foreign materials, courts have often decided cases involving the Fund Agreement without the "full store of jurisprudence and critical material."[111] This has resulted in a measure of parochiality in the area of Fund Agreement jurisprudence. Whatever the exact explanation, the disinclination of courts to square their interpretations of the Fund Agreement with those of other members' courts has led them to treat the Fund Agreement as a domestic legal instrument, thus placing "more emphasis on verbal considerations than on purpose."[112]

From this it is reasonable to conclude that interpretation of the Fund Agreement should be an evolutionary process, subject to correction and re-evaluation in light of experience. This is easier said than done, however. As Sir Gold has noted:

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109. *Id.*

110. MANN, *supra* note 93, at 373-75. The situation described in the text might occur, for example, where a foreign-drafted exchange contract is construed by a common law court in light of common law conceptions (under conflict of law rules), even though the language of Article VIII of the Agreement, governing the enforceability of exchange contracts, presupposes that the proper law of the contract will govern.

111. GOLD, *supra* note 97, at 5.

112. *Id.* at 6.

> The growing awareness of the relevance of the Articles to certain legal problems that affect private parties has not always led to legal solutions that are fully compatible with the economics of the Articles. It should be a cardinal rule of interpretation that the solution of a legal problem involving the Articles should make maximum economic sense. This rule can be difficult to apply in some cases.[113]

For the future and as set forth in the next section, U.S. courts and lawyers briefing issues pertaining to the Fund Agreement should accept that foreign jurisprudence and foreign commentary are of no lesser value than domestic authorities. Their use may promote uniformity, tractability, and economic sense in the law of the international monetary system. Courts should also notice that the chaotic environment in which the Fund Agreement was drafted resulted in language that was in some measure a "historical accident."[114] This in turn should provide further impetus to look beyond the language of the treaty to its underlying core purpose, "to promote international monetary cooperation."[115]

IV. A NEW FRAMEWORK FOR ENFORCEMENT SUITS BY MALCONTENT COMMERCIAL CREDITORS OF LDCS

The IMF and the international monetary system are not coterminous, and much that goes on in the system occurs outside the purview of the IMF.[116] This section argues that Article VIII, section 2 of the Fund Agreement should be interpreted liberally in order to align the approach taken by U.S. courts in cases seeking enforcement of LDC debt agreements with IMF policies, especially since IMF policies are essentially congruent with those of the political branches of the U.S. government. This approach will foster and maintain IMF involvement in the economic arrangements of LDCs, while discouraging both unilateral repudiations and non-IMF-approved workouts by LDCs.

A. Interpretation and Application of Article VIII, Section 2(b) to Bar Suits by Commercial Creditors of LDCs

Article VIII, section 2(b) of the IMF Articles of Agreement provides that "[e]xchange contracts which involve the currency of any member and which are contrary to the exchange control

113. *Id.* at 3.
114. Meyer, *supra* note 99, at 889 (discussing Article VIII, § 2(b)).
115. MANN, *supra* note 93, at 384.
116. DAM, *supra* note 15, at 76.

regulations of that member maintained or imposed consistently with this agreement, shall be unenforceable in the territories of any member."[117] The "plain meaning" of this text is that certain contracts that are offensive to the exchange control regulations of an IMF member country (other than the one in which the forum is situated) cannot be enforced. The precise meaning and applicability of this provision, however, has been the subject of more litigation and more controversy among commentators than any other provision of the Fund Agreement,[118] and the meaning of virtually all of its terms has been disputed.[119] The IMF has provided clarification only on the question of whether Article VIII, section 2(b) was intended to override the public policy of the forum, which is now deemed to be the case.[120] As Sir Gold noted in 1982, "it will be obvious [from inquiry] . . . that the last word on the meaning of the provision has not been uttered by courts or authors."[121] This section evaluates some of the interpretive positions that courts and commentators have taken and

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117. Fund Agreement, *supra* note 5, art. VIII, § 2(b). This provision has the full force and effect of domestic law in the United States, 22 U.S.C.A. § 286(h) (1996), and in 50 IMF member countries as of 1980. *See* INTERNATIONAL MONETARY FUND 1980 ANNUAL REPORT 83, 122, table I.14 (1980).

118. GOLD, *supra* note 97, at 2.

119. *See, e.g.*, Williams, *supra* note 89, at 332.

120. The IMF has officially (though somewhat repetitively and unhelpfully) interpreted Article VIII section 2(b) as follows:

> Parties entering into exchange contracts involving the currency of any member of the Fund and contrary to exchange control regulations of that member which are maintained or imposed consistently with the Fund Agreement will not receive the assistance of the judicial or administrative authorities of other members in obtaining the performance of such contracts. That is to say, the obligations of such contracts will not be implemented by the . . . authorities of member countries, for example, by decreeing performance of the contracts or by awarding damages for their non-performance. . . .
>
> An obvious result of the foregoing undertaking is that if a party to an exchange contract of the kind referred to in Article VIII, section 2(b) seeks to enforce such a contract, the tribunal of the member country before which the proceedings are brought will not, on the ground that they are contrary to public policy (ordre public) of the forum, refuse recognition of the exchange control regulations of the other member which are maintained or imposed consistently with the Fund Agreement. It also follows that such contracts will be treated as unenforceable notwithstanding that under the private international law of the forum, the law under which the foreign exchange control regulations are maintained or imposed is not the law which governs the exchange contract or its performance.

National Advisory Council on International Monetary and Financial Problems, 14 Fed. Reg. 5208-09 (1949). On the *ordre public* issue, *accord* Perutz v. Bohemian Discount Bank in Liquidation, 304 N.Y. 533 (1953).

121. GOLD, *supra* note 97, at 2.

endeavors to demonstrate that Article VIII, section 2(b) is properly applicable to lawsuits brought by secondary purchasers of LDC debt. Although the interpretation advocated here is at odds with a number of extant U.S. precedents, it is submitted, that those precedents are either wrongly decided or are distinguishable from the type of case under scrutiny here.

1. LDC debt agreements should be deemed "exchange contracts which involve the currency" of member nations

The phrase "exchange contract" is nowhere defined in the Fund Agreement. In the fifty years since the Bretton Woods Treaty was drafted, courts and commentators have put forth different definitions of the phrase. Some have taken a "narrow" textual view, restricting the phrase to mean contracts for the exchange of one currency against another or one means of payment (such as gold) against another.[122] Others have adopted a "broad" definition of "exchange contracts," encompassing all contracts which affect a member country's exchange resources. This article argues in favor of the latter.

a. The "narrow" view of "exchange contracts" was incorrect from the start

Based on the text of the Bretton Woods Treaty, it might seem reasonable to limit the scope of Article VIII, section 2(b) to money-changing transactions. If correct, this would permit the courts of IMF member nations to hear, decide and decree performance in cases involving transactions in goods, barter agreements, and even more relevant here, agreements to borrow and repay a given currency, notwithstanding the effect such decrees will have on the exchange resources of other (defendant) IMF member nations.

The New York Court of Appeals was the first U.S. court to endorse (in dicta) the narrow view in *Banco do Brasil v. A.C. Israel Commodity Co.*[123] The plaintiff, an instrumentality of the government of Brazil, sought damages from a U.S. coffee importer who had contracted to pay a Brazilian coffee exporter cash for coffee received, rather than (some greater amount of) dollars to the Brazilian authorities, as required by Brazil's "forced sale" exchange control laws.[124] While basing its holding

122. Williams, *supra* note 89, at 333.
123. 12 N.Y.2d 371 (1963).
124. The exporter, in turn, would be able to sell these dollars on the black market for more cruzeiros than it would have received had the payment been

on other grounds, the court considered and disapproved the contention that the agreement was an "exchange contract" contrary to the exchange control regulations, stating:

> We are inclined to view an interpretation of subdivision (b) of section 2 that sweeps in all contracts affecting any members' exchange resources as doing considerable violence to the text of the section. It says 'involve the currency' of the country whose exchange controls are violated; not 'involve the exchange resources'.[125]

In approving the narrow view, the court cited a much-disputed article by Mr. Arthur Nussbaum[126] which argued that Article VIII, section 2(b) reaches only "transactions which have as their immediate object 'exchange', that is, international media of payment."[127] The difficulty inherent in this citation is that Mr. Nussbaum acknowledged that the meaning of "exchange contracts" is by no means self-explanatory, and he conceded that "national enactments on exchange control often invalidate unlicensed contracts not directly concerned with international media of payment."[128] Despite this acknowledgment, Mr. Nussbaum (warning that then totalitarian governments such as Poland and Czechoslovakia will "go to great lengths to extend their control") made the unsupported assertion that "[i]t cannot be the meaning of the Agreement that the other member countries have to carry out such policies."[129] This was a misguided observation even at the height of the Cold War for "such policies" would surely not have been "imposed consistently with" the Fund Agreement and therefore not within Article VIII, section 2(b). Also, Mr. Nussbaum's acknowledgment that countries had previously applied exchange control enactments to a range of contracts affirms the possibility that the drafters of the Fund Agreement had a broader meaning in mind.

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channeled through the government. Brazil's cause of action was premised on its contention that because the agreement violated Brazil's exchange control laws, Article VIII, section 2(b) provided a basis for recovery. The court stated that even if Article VIII were applicable, which it doubted, the obligation to withhold judicial assistance in enforcing the contract did not imply an obligation to impose tort penalties on the contracting party. *Id.* at 376-77.

125. *Id.* at 375-76.

126. *Id.* at 375 (citing Arthur Nussbaum, *Exchange Control and the International Monetary Fund*, 59 YALE L.J. 421, 426 (1950)).

127. Arthur Nussbaum, *Exchange Control and the International Monetary Fund*, 59 YALE L.J. 421, 426 (1950). For commentary taking issue with Mr. Nussbaum on this point, *see, e.g.*, Meyer, *supra* note 99, at 885-86; Williams, *supra* note 89, at 334-35.

128. Nussbaum, *supra* note 127, at 426.

129. *Id.* at 426-27.

A second problem with the *A.C. Israel* dicta is its concern with the violence that a broad definition would do to the text. This is misguided, since the text of the agreement is universally acknowledged to be less than letter-perfect. The text of Article VIII, section 2(b) has been described by Dr. Mann as "so unsatisfactory."[130] Even Mr. Nussbaum himself commented that he had little "confidence in the accuracy of the draft."[131] Thus, for all the reasons discussed above in Section III, anything approaching strict reliance on the text of the Fund Agreement, especially the text of Article VIII, section 2(b), is not an appropriate method of discerning its meaning. This was the mistake made by the *A.C. Israel* court and later courts adopting its dicta.

A.C. Israel was later cited by the New York Court of Appeals and other U.S. courts as authority for the application of the narrow view to a variety of contexts,[132] such as the "Cuban insurance cases" that arose after Fidel Castro withdrew Cuba from the IMF.[133] Yet, for all the citation of the opinion, there is ample reason to believe that Mr. Nussbaum and the *A.C. Israel* court and later judicial opinions relying on them were wrong.

Perturbingly for present purposes, the narrow view was adopted by Chief Judge Motley as one of several parts of the holding in *Libra Bank Ltd. v. Banco Nacional de Costa Rica S.A.*[134] This case involved an action by a commercial creditor in which it succeeded in enforcing an LDC loan after the government of Costa Rica repudiated its obligations to commercial creditors.[135] Chief Judge Motley's opinion did not acknowledge that the *A.C. Israel* language was dicta derived from the disputed view of a single commentator. Nor did it acknowledge that later opinions adopting the narrow view relied first and foremost on *A.C. Israel.* Nevertheless, because the action by

130. MANN, *supra* note 93, at 383.

131. Nussbaum, *supra* note 127, at 426.

132. *See, e.g.*, J. Zeevi & Sons, Ltd. v. Grindlays Bank (Uganda) Ltd., 37 N.Y.2d 220, 229 (1975) ("[irrevocable] letter of credit not an exchange contract") (citing *A.C. Israel*, 12 N.Y.2d at 375-76); *see also* John Sanderson & Co. (Wool) Pty., Ltd. v. Ludlow Jute Co., Ltd., 569 F.2d 696, 699 (1st Cir. 1988) (approving narrow interpretation of "exchange contract").

133. *See, e.g.*, Theye y Ajuria v Pan American Life Ins. Co., 161 So. 2d 70, 74 (La. 1964) ("a contract payable in . . . Louisiana in United States currency is not an exchange contract").

134. 570 F. Supp. 870 (S.D.N.Y. 1983).

135. *Id.* The number of reported U.S. cases which resulted in an LDC creditor winning a litigated judgment is small, probably due to the tendency of this type of case to settle. *See supra* notes 64-67 and accompanying text.

Costa Rica suspending external debt payments was taken without the involvement of the IMF, the result in *Libra Bank* is consistent with the framework advanced here.[136] Still, Chief Judge Motley's discussion of Article VIII, section 2(b) provides further support for the narrow definition of exchange contracts and, for a federal court in the Southern District of New York to apply the framework proposed in this article, that part of the *Libra Bank* decision will need to be reconsidered.[137] Expert authorities, such as Sir Gold, and decisions of courts in other IMF member nations, discussed next, compel the conclusion that Chief Judge Motley and the authorities she cited were incorrect in adopting the narrow view of "exchange contracts."[138]

b. The weight of authority favors a broad definition of exchange contracts, one which encompasses LDC commercial loans

The narrow view begs the interesting question of why the drafters of the Fund Agreement would protect controls on straight money-changing from interference by foreign courts, when other transactions could have an equally deleterious effect on a country whose currency reserves are in need of protection. Writing shortly after Mr. Nussbaum, Mr. Meyer rejected the narrow view, stating:

> The context of the agreement clearly demonstrates . . . that an 'exchange transaction' . . . covers a broad range of dealings. The fact that in a number of instances the Agreement contains language limiting the phrase to media transactions indicates that the drafters knew how to limit the phrase when they wanted to and bears out the conclusion that 'exchange transaction' is not limited to international media of payment.
>
> . . . The illogic of the contrary position, which would render media transactions unenforceable but would leave untouched the quantita-

136. *See infra* notes 162-68 and accompanying text for further discussion of *Libra Bank*.

137. Apparently the First Circuit and the Southern District of New York are the only federal courts that have had occasion to construe Article VIII, section 2(b). Thus, no other federal court is bound to follow the narrow interpretation of "exchange contracts."

138. *See also* Wilson, Smithett & Cope Ltd. v. Terruzzi, 1 Q.B. 683, 709 (C.A. 1976) (futures contract on the London Metal Exchange executed by Italian "gambler" in violation of Italian exchange control law not an exchange contract); MANN, *supra* note 93, at 388 ("The aim of Article VIII, section 2(b) is . . . to ensure a measure of respect for a member State's financial control. Furthermore, there exists a vast number of transactions which do not come within the Court of Appeal's definition . . . which, on account of their danger to the economy, a legislator is justified not only in prohibiting, but also in expecting to be shunned.").

> tively greater—and therefore more harmful—dealings in other forms of property and services, substantiates [this position].
>
> We are thus led to the conclusion that the term 'exchange contracts,' as used in Article VIII, section 2(b), means transactions having their bases in contract and involving exchange, whether of currency, property, or services.[139]

Writing on this point in 1964, Sir Gold, a leading authority on the IMF,[140] is unequivocal: "After the learned discussions of the last decade or more, [the narrow interpretation of 'exchange contracts'] can be taken seriously only if the normal scope of exchange control and the purpose of Article VIII, section 2(b) . . . are ignored."[141] Thus, notwithstanding the "plain meaning" of the words, "exchange contracts" means contracts which in any way affect a country's exchange resources so as to be liable to reduce them.[142] This definition has been adopted by a majority of commentators,[143] as well as courts in Germany, France, and Luxembourg.[144]

Once a court accepts the broad interpretation of the phrase "exchange contracts," a loan agreement between an LDC and a commercial creditor falls within the meaning of the term, even where the contract calls for disbursement and repayment of the loan in the same currency. The servicing of external debts will in all circumstances vitally affect the debtor country's foreign ex-

139. Meyer, *supra* note 99, at 885-87 (citing F.A. Mann, *Money in Public International Law*, 26 BRIT. Y.B. INT'L L. 259, 279 (1949)).

140. DAM, *supra* note 15, at xvi-xvii.

141. GOLD, *supra* note 97, at 11.

142. Joseph Gold, *"Exchange Contracts," Exchange Control, and the IMF Articles of Agreement: Some Animadversions on* Wilson, Smithett & Cope Ltd. v. Terruzzi, 33 INT'L & COMP. L.Q. 777, 787-89 (1984); *see also* MANN, *supra* note 93, at 385. Mann, taking the view presented in the text, states:

> This [interpretation] would appear to be in better harmony with the purpose of the Agreement and the true intentions of its authors to be gathered from it, but admittedly makes the word 'exchange' redundant . . . . So to disregard an important word may run counter to established principles of interpretation. Yet it is submitted that this objection, grave though it may be, is outweighed by the fact that no other interpretation would achieve the overriding purposes of the Agreement.

Id.

143. *See* Williams, *supra* note 89, at 344 ("Most contemporary authorities reject . . . the narrow construction and favor the broad interpretation.").

144. *See, e.g.*, Lessinger v. Mirau, 22 I.L.R. 725 (Schleswig-Holstein Ct. App. 1954) (dollar loan by one Austrian resident to another repayable in dollars was an 'exchange contract'); DeBoer, Widow Moojen v. Von Reichert, 51 REV. CRIT. DROIT INT'L PRIVE 67, 89 (1962) (contract for sale of shares in French Corporation by Dutch resident to a German in return for French Francs was an 'exchange contract' even though one single currency involved); Societe Filature et Tissage X. Jourdan v. Epoux Heynen Binter, 22 I.L.R. 727 (1956) (contract for sale of goods in exchange for currency is an exchange contract).

change resources. When an LDC repays a loan in dollars, the acquisition and release of those dollars necessarily reduces the LDC's exchange reserves. When low reserves jeopardize an LDC government's ability to manage current account problems, such a reduction may be utterly unacceptable. In sum, a sovereign loan agreement is a contract which necessarily contemplates exchange, and the performance of such a contract will always reduce the exchange resources of the debtor. In this light, the loan agreement by an LDC to borrow dollars and repay dollars necessarily "involve[s]" the currency of the LDC.[145]

2. *A decision to suspend debt service and/or seek restructuring of sovereign loan agreements should be deemed "exchange control regulation" within the meaning of Article VIII*

"Exchange control regulation" is not defined with legal precision in the Fund Agreement or in any decision of the Executive Directors of the IMF.[146] Sir Gold interprets the term to mean both restrictions on current payments for international transactions[147] and "such controls as are necessary to regulate international capital movements."[148] Dr. Mann defines the term as "enactments that control the movement of currency . . . for the purposes of protecting the financial resources of a country."[149] Concluding that a decision to suspend performance and seek restructuring of sovereign debt agreements is an "exchange control regulation" should not be controversial, for the impetus behind such government action is the defense of the debtor coun-

145. *See* MANN, *supra* note 93, at 391 ("The phrase 'which involve the currency' contemplates . . . not the denomination in a particular currency, but the financial area within which the transaction has economic effects. 'Currency' should be construed in the broad sense of economics rather than in a strictly legal sense.").

146. GOLD, *supra* note 97, at 13.

147. *Id.* at 125. Such restrictions may be imposed only with the approval of the Fund. *See* Articles of Agreement of the International Monetary Fund, art. VIII, § 2(a).

148. GOLD, *supra* note 97, at 125. These restrictions may be imposed by member governments without the approval of the Fund, according to Article IV, section 3. *See infra* note 157 and accompanying text.

149. MANN, THE LEGAL ASPECT OF MONEY 388 (5th ed. 1992). Williams similarly defines exchange controls to include any measure controlling "the transnational movement of currency, property or services for the purpose of protecting the financial resources of the controlling country." Williams, *supra* note 89, at 352.

try's currency through conservation of national resources.[150] It makes no difference whether the sovereign debtor imposes the restriction on itself or on private economic actors, since in either instance such restrictions constitute a species of "financial control" which Article VIII, section 2(b) aims to protect from scrutiny by the judicial authorities of other nations.[151] Whether such restrictions are imposed *consistently* with the Fund Agreement, however, is quite another matter and is addressed next.

3. *IMF involvement in the affairs of a debtor LDC should be necessary and sufficient for such LDC's debt restructuring to qualify as "exchange control regulation imposed consistently with" the Fund Agreement*

If a country is conducting its economic and monetary affairs with the approval of the IMF, then its debt restructuring-*cum*-exchange-control-regulation must be deemed consistent with the Fund Agreement. Where a particular LDC debt restructuring is endorsed by the fund, then *ipso facto*, the restructuring is "imposed consistently with" the Fund Agreement. Where the IMF is currently disbursing loans to the country in question, it will also be reasonable to conclude that such country's restructuring-*cum*-exchange control regulation is consistent with the Fund Agreement. It is hard to envision a situation where these conclusions would not hold, since presumably the IMF will neither lend money to countries of which it does not approve nor put its imprimatur on LDC debt workouts that are out of keeping with its charter.

In a situation where an IMF adjustment program is forthcoming, but the Fund has not yet approved an LDC's program, Article VIII, section 2(b) may still function to counter nuisance suits by small creditors. On this score, Mr. Williams asserted that "[w]hile express approval by the Fund of the regulations involved is unnecessary [to establish consistency of regulations with the Fund Agreement], the general character of the regulations must be authorized; insignificant inconsistencies will not

150. *See, e.g.*, Williams, *supra* note 89, at 356 ("[Ex]change control regulations to which Article VIII, section 2(b) applies are those . . . regulations genuinely concerned with the conservation of a country's economic resources and are directed to the financial aspect of an international transaction—whether current or capital transaction. Included are rules restricting the making of payments as well as exchange surrender regulations. Excluded are tariffs, trade restrictions . . . and legal tender laws.").

151. MANN, *supra* note 149, at 388.

be fatal."[152] This view allows judges discretion in evaluating a given debt restructuring for consistency with the Fund Agreement in cases where the IMF has not yet spoken.

While an IMF-approved restructuring ought to be presumed consistent with the Fund Agreement, the converse situation is more problematic. Whether a non-IMF-approved debt restructuring is inconsistent with the Fund Agreement requires inquiry into a further controversy, namely whether "exchange control regulation" encompasses restrictions on current cross-border transactions only, or whether, as Sir Gold asserts, it also encompasses restrictions on capital movements.[153] It is not wholly clear whether a sovereign loan agreement is a current or capital transaction, and research reveals no authority precisely on point. Article XIX(I), however, defines "payments for current transactions" as:

> [P]ayments which are not for the purpose of transferring capital [including], without limitation:
>
> (1) All payments due in connection with foreign trade, other current business, including services, and normal short-term banking and credit facilities;
>
> (2) Payments due as interest on loans and as net income from other investments;
>
> (3) Payments of moderate amount for amortization of loans or for depreciation of direct investments . . .
>
> The Fund may, after consultation with the members concerned, determine whether certain specific transactions are to be considered current transactions or capital transactions.[154]

This excerpt is not quite conclusive on the question of whether a sovereign loan is a current transaction, but the language suggests that payments of interest and principal due under sovereign loan agreements qualify as current payments, so long as

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152. Williams, *supra* note 89, at 360.

153. GOLD, *supra* note 97, at 79-81. Article VIII, section 2(a) provides that "no member shall, without the approval of the Fund, impose restrictions on the making of payments or transfers for current international transactions." Fund Agreement, *supra* note 5, art. VIII, § 2(a). Sir Gold asserted that the "control" phraseology of section 2(b) casts a wider net than the conditional right to regulate current payments provided by Article VIII, section 2(a), citing examples of "controls" which are not restrictions on payments, such as exchange surrender requirements. The uncertainty results from the following drafting inaccuracy: section 2, as originally drafted, pertained only to current transactions and that text became section 2(a). Section 2(b) was later added to the final version and, in Sir Gold's view, it applies to all controls, not merely restrictions on current payments. The addition of section 2(b) was made, however, without changing the heading of section 2, which still reads "Avoidance of Payments on Current Transactions." GOLD, *supra* note 97, at 85-86.

154. Fund Agreement, *supra* note 5, art. XIX(i).

"moderate"[155] in amount. From this it seems reasonable to assume that the agreements themselves are "current transactions." Moreover, taking these terms at face value—risks of textualism in this context duly noted—"capital transfers" would seem to connote more or less permanent relocations of capital, which does not adequately describe loan transactions. Noting the difficulty in making this distinction, Professor Dam reiterated that the examples in Article XIX are listed "without limitation."[156]

The distinction between current and capital transactions, which originated in accounting history,[157] is of significance to the framework proposed in this article because while Article VIII, section 2(a) requires fund approval for restrictions on current transactions, Article IV, section 3 leaves members free to impose restrictions on capital movements. Article VIII, section 2(b) can ensure that both are given effect. The difficulty is that consistency with the Fund Agreement depends in current transactions on fund approval, while *any* restriction on capital transfers is consistent with the Fund Agreement. As argued in Section IV, *infra*, the framework proposed here would allow for the possibility of nuisance suits by malcontent LDC creditors when a repudiation or restructuring occurs without the involvement of the IMF. In such a scheme, non IMF-approved restructurings, repudiations-*cum*-exchange-control-regulations should be deemed inconsistent with the Fund Agreement and therefore not within the reach of Article VIII, section 2(b). That assessment, however, requires that LDC loan agreements be deemed current transactions, since all restrictions on capital transfers are "imposed consistently" with the Fund Agreement, whether IMF-approved or not, per Article IV, section 3.

To the extent that LDC loan agreements do not self-evidently belong to one category or the other, and assuming that Article XIX does not fully answer the question, recourse should be had to "[p]roper analysis [of] the economic and accounting concepts and policies at stake."[158] It is submitted that the policy of promoting international monetary cooperation that undergirds the Fund Agreement militates in favor of viewing LDC loan agreements as current transactions so that they may be

155. One is entitled to wonder what yardstick "moderateness" is to be measured against; presumably sums which are very large in some contexts will nevertheless be moderate in the sovereign loan context.

156. DAM, *supra* note 15, at 100.

157. Williams, *supra* note 89, at 359.

158. *Id.*

held either consistent or inconsistent with the Fund Agreement for Article VIII purposes, depending on whether the IMF is involved in the particular restructuring.

4. *Summary*

Based on the foregoing discussion, Article VIII, section 2(b) of the Fund Agreement provides a basis whereby a sovereign debtor that has sought the involvement of the IMF in its debt problems may defend against lawsuits by recalcitrant creditors seeking to challenge a consensual restructuring. The rule of broad construction applicable to treaties, the overarching economic policies of the Fund Agreement, the indisputable inadequacies of the text, and the evolutionary process through which the meaning of the Agreement has come to be understood all support the proposed interpretation and application of the Fund Agreement to LDC debt litigation. To the extent that certain U.S. precedents have adopted the narrow definition of exchange contracts, and therefore pose an obstacle to the application of Article VIII, section 2(b) of the Fund Agreement as proposed here, a reconsideration is in order in light of the experience of courts of other IMF member nations and the unequivocal stance Sir Gold and other experts take on the issue. Moreover, courts should avail themselves of the opportunity to ascertain or actively seek out the IMF's views and accord them controlling weight so as to promote uniformity of interpretation and application of the Fund Agreement to this problem.

B. ARTICLE VIII, SECTION 2(b) SHOULD NOT APPLY IN CASES WHERE THE LDC HAS RESTRUCTURED EXTERNAL DEBT (OR OTHERWISE REPUDIATED ITS OBLIGATIONS) AND THE IMF IS EITHER NOT INVOLVED IN THE AFFAIRS OF THE DEBTOR NATION OR THE DEBTOR IS PURSUING POLICIES NOT CONSONANT WITH IMF ADVICE

As discussed in Section II, *supra*, secondary trading is a good thing. It serves the needs of creditor banks and encourages the collection of information on the creditworthiness of debtor nations. One may argue, as did the Darts in their case against Brazil, that any prohibition of suits by secondary purchasers to enforce LDC debt will depress prices, reduce open interest and thereby reduce liquidity in the market for LDC debt instruments, to the detriment of all concerned. One plausible answer to this concern is that in the absence of the possibility of quick nuisance suit payoffs, the price discovery for LDC debt will more

accurately reflect the likelihood that the LDC will actually pay its debts. This would be preferable to a situation where the market prices of LDC debt impound less relevant information, including, for example, noise as to the value of attachable commercial assets which are present in the putative forum.

Still, the proposed framework would leave undisturbed the possibility of plaintiff lawsuits, including speculative lawsuits by secondary purchasers of LDC debt, as a way of giving LDCs an incentive to seek the involvement of the IMF at earlier stages of their external debt problems than was the case in the 1970s and early 1980s. In this way, secondary purchasers and the plaintiff's bar may actually serve the international financial system by prodding LDCs to check the urge to handle debt problems by "going it alone" with London Club creditors through new lending and less stringent austerity measures than the IMF would prescribe. A few million-dollar judgments handed down by U.S. courts would bring a proud or profligate LDC government into the IMF fold more effectively than pressures from other sources. There is, moreover, little that LDCs can do contractually to avoid enforcement suits. No Western creditors will lend without a waiver of sovereign immunity and consent to service of process. While sharing clauses may align the interests of the troubled LDC and major creditors, it appears that offshore banking entities are teflon-coated against such clauses, since they exist to collect and then evaporate without sharing the booty. The framework proposed here seeks to find a silver lining in what is certainly a dark cloud.

There are instructive precedents on point. For example, in *Allied Bank International v. Banco Credito Agricola di Cartago*,[159] the Second Circuit held that in the wake of a unilateral repudiation by Costa Rica of its external debts and subsequent negotiation of a refinancing agreement, a single creditor, after refusing to participate in the refinancing agreement, could recover on its sub-tranche of debt. The court reversed its prior holding[160] after the United States filed a brief stating that

159. 757 F.2d 516 (2d Cir. 1985).

160. *See* 566 F. Supp. 1440 (S.D.N.Y. 1983). The affirmance of dismissal in the first *Allied Bank* case was based on principles of comity and was done in the mistaken belief that the Costa Rican decrees were consistent with U.S. policy. It is worth noting that the doctrine of comity might in certain circumstances achieve the same result as the Article VIII-based framework proposed here. It is, however, a slippery concept:

> Comity is a recognition which one nation extends within its own territory to the . . . acts of another. It is not a rule of law, but one of practice, convenience and expediency. Although more than mere courtesy

"Costa Rica's attempted unilateral restructuring of private obligations . . . was inconsistent with [the IMF-guided] system of international cooperation and negotiation and thus inconsistent with United States policy."[161] This result is in complete accord with the framework proposed here.

The result in *Libra Bank*[162] is consistent with this paper, except insofar as it adopts the narrow view of exchange contracts. In granting the plaintiff's motion for summary judgment, Chief Judge Motley made four basic holdings. First, the act of state doctrine did not shield a Costa Rican government decree suspending performance of commercial debt agreements from judicial scrutiny by a U.S. court even where the agreement provided an express waiver of sovereign immunity.[163] Second,

> and accommodation, comity does not achieve the force of an imperative or obligation. . . . Comity should be withheld only when its acceptance would be contrary or prejudicial to the interest of the nation being called on to give it effect.

Somportex Ltd v. Philadelphia Chewing Gum Corp., 453 F.2d 435, 440 (3d Cir. 1971).

By contrast, Article VIII, section 2(b) of the Fund Agreement does provide a rule of law and, furthermore, prohibits members from refusing to give effect to the exchange control regulations on the grounds that doing so would be contrary to the *ordre public* of the forum. *See* MANN, *supra* note 93, at 375.

161. 757 F.2d at 519.

162. *See supra* notes 134-38 and accompanying text.

163. This article does not take issue with this aspect of the *Libra Bank* holding and, indeed, is in agreement that the act of state doctrine, under which courts will not examine the acts of a foreign state done within its own territory so as to avoid vexing the conduct of diplomatic relations with that country, is inapplicable. This doctrine is essentially irrelevant to lawsuits to enforce commercial debt obligations payable outside the LDC (as all or most are). Thus, since the terms of the debt agreement in *Libra Bank* track the paradigm case discussed above in Part II, the following language in Chief Judge Motley's opinion is applicable to those LDC debt agreements within the scope of this paper:

> [W]here a foreign government contracts to repay a debt [in dollars] in New York City, consents to the jurisdiction of our courts, waives its sovereign immunity with respect to legal proceedings concerning that debt, and continues to maintain considerable assets in this nation, it can hardly be said that this court's judgment shall frustrate the foreign state's reasonable expectation of dominion over the legal rights involved so as to vex our amicable relations with that foreign nation. [Thus the] exercise of [this court's] judicial power is appropriate [and] fully consistent with the proper distribution of functions . . . between the 'judicial and political branches of the government on matters bearing on foreign affairs' . . . .

570 F. Supp at 884.

> [A]rgument based on the Bretton Woods Agreement is . . . distinct from . . . arguments based upon the act of state doctrine . . . . The argument that the nonenforcement of the loan agreement is dictated by a positive law . . . is entirely distinct from the argument that a doctrine of judicial abstention bars review of the decrees. . . . A commentator has also ar-

under the narrow interpretation of the phrase "exchange contracts," Article VIII, section 2(b) of the Fund Agreement did not bar judgment in favor of the plaintiff.[164] Third, even if section 2(b) did apply, the "defendant has submitted no authority for its view that a contract, valid and enforceable when made, may be rendered unenforceable by an intervening currency regulation."[165] Fourth, Costa Rica did not make an adequate showing that its decrees were consistent with the Fund Agreement.[166] The court was correct on the first point, the second point should be overruled, as noted. The third point is misguided, since there is ample authority to support the position that Article VIII, section 2(b) applies to the time performance is sought and not merely to the time the contract is made.[167] The fourth point accords with other authorities that favor placing the burden of showing consistency with the Fund Agreement on the defendant who relies on Article VIII, section 2(b).[168] In other cases similar to *Libra Bank*, where the defendant can make no such showing due to a lack of IMF involvement in its affairs, non-performance of its debt obligations would not be deemed consistent with the Fund Agreement, and an enforcement suit would lie under the proposed framework.

C. Differential Treatment of Plaintiff Suits Through Application of Article VIII Tracks Judicially Noticeable U.S. Policies

The briefs filed by the United States in *CIBC Bank* (the Dart case) and *Allied Bank* confirm that the policy of the United States is to encourage consensual and fiscally responsible solutions to LDC debt problems and to discourage obduracy and unilateralism on the part of both LDC debtors and their creditors. These policies are further confirmed by the texts and legislative histories of the International Lending Supervision and SEED Acts.

Ironically, despite the clarity with which these policies have been articulated, courts are hamstrung in that they may not

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gued that Article VIII, section 2(b) supersedes the act of state doctrine."

Id. at 896-97 n.1 (citing Williams, *supra* note 89, at 387-94).

164. *Id.* at 900.

165. *Id.*

166. *Id.* at 901.

167. *See, e.g.*, Perutz, 304 N.Y. at 533; *see also* Williams, *supra* note 89, at 364.

168. *See, e.g.*, GOLD, *supra* note 97, at 334.

freely take notice of and respond to such policies when applying Article VIII, section 2(b) of the Fund Agreement. The reason is that in making the Fund Agreement part of its domestic law, a member nation and its judiciary undertake not to refuse recognition of another member's exchange control regulations on the ground that such controls are contrary to the public policy (*ordre public*) of the forum.[169] In aligning the response of U.S. courts to LDC debt enforcement suits with the policies of the IMF, the proposed co-opt of Article VIII, section 2(b) of the Fund Agreement will lead to judicial outcomes that track evolving U.S. policies in this field.

D. DIFFERENTIAL TREATMENT OF PLAINTIFF SUITS MAINTAINS THE TRADITIONAL SUPERVISORY ROLE OF THE IMF WHILE ENCOURAGING LDCS TO DEAL WITH DEBT PROBLEMS EARLY.

While further exegesis on the role of the IMF is beyond the scope of this paper, it is worth noting that implementation of this framework as a means of dealing with LDC debt problems and related litigation may be preferable to radical alteration of the IMF's role in the international system, such as the proposed "bankruptcy model" which the IMF has recently been encouraged to pursue.[170] The bankruptcy model would in practice require insolvent LDCs to relinquish large measures of sovereign control, such as will likely never be politically palatable for a sitting government. Indeed, the inclination of LDCs to view the politically humiliating severity of IMF adjustment programs as a last resort, as did Peru in 1976 and Mexico in 1979-82, will presumably always be a factor. Moreover, an IMF with expansive bankruptcy court powers will be less accountable to its constituent members and less transparent in its activities.[171] These considerations counsel in favor of less expansive changes in the IMF's role.

The framework proposed here can be a valuable element in forestalling the need for an IMF bankruptcy scheme. The framework makes constructive use of the waiver of sovereign

169. MANN, *supra* note 93, at 375 (citations omitted).

170. *See, e.g.*, George Graham, *IMF Crisis Plan Draws on Mexican Lesson*, FIN. TIMES, Oct. 2, 1995, at 8 ("Some countries have argued that the IMF should consider building . . . a sort of international bankruptcy court, where sovereign debtors could negotiate orderly debt workouts with their creditors.").

171. *See* George P. Schultz, Stigler Lecture, The University of Chicago (Apr. 9, 1996) (increases in the overt power of international financial institutions result in proportional decreases in the accountability of such institutions).

immunity that is a part of every LDC commercial debt agreement and leverages it to the benefit of the London Club *and* LDCs. Once courts apply this framework to a fair number of live controversies and the word gets out, LDCs will have incentive to avoid unilateral repudiations of their obligations, on the one hand, and be encouraged to seek out the IMF early in their efforts to manage external debt problems, on the other, without forcing LDCs to relinquish more sovereign control than they do currently.

CONCLUSION

Suits by obdurate private LDC creditors, especially speculative secondary purchasers, will be increasingly common and troubling in the wake of the Darts' success. Small numbers of creditors will essentially seek to free ride off the losses of major creditors by getting in the way of restructuring efforts between LDCs and their commercial creditors. As this paper has demonstrated, courts faced with such actions may discourage rank profiteering, enhance the supervisory role of the IMF, and reach results which are in accord with U.S. policies by applying Article VIII, section 2(b) of the Fund Agreement in the manner proposed here. The aim is simply to weed out cases against LDCs that are managing their affairs in accord with IMF policies.

The framework espoused in this paper would maintain the IMF's latitude in recommending the most efficacious adjustments and at the same time, would leave LDC governments more able to justify IMF-prescribed belt tightening by pointing to the clear necessity of avoiding suits by malcontent creditors. In this way, application of Article VIII, section 2(b) of the Fund Agreement to enforcement suits by creditors will encourage global cooperation and, hopefully, reduce "the dynamic instability inherent in the game as currently played."[172]

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172. *See* B. J. Cohen, *LDC Debt: Towards a Genuinely Cooperative Solution*, *in* THE FUTURE OF THE INTERNATIONAL MONETARY SYSTEM 174, 191 (Hamouda et al. eds., 1990) (advocating a new "International Debt Restructuring Agency," possibly within the IMF, and presenting arguments both for and against the interposition of a "new player in a game where the old players already know all the rules").