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The Anomalous Lack of an International Bankruptcy Court

By
Charles Seavey*

I. INTRODUCTION

It is universally agreed that bankruptcy courts, in use since Roman times and employed in most domestic legal systems, minimize waste while granting worthy debtors a fresh start. Why is it that, in the year 2006, this proven judicial mechanism has yet to be established for sovereign nations, as recommended by Adam Smith himself?¹ This paper describes two key impediments that have prevented the establishment of a sovereign bankruptcy court: (i) the conflicts-of-interest of creditor and debtor state representatives; and (ii) the voting and political structures of the International Monetary Fund, the World Bank, and the Paris Club.

II. DEVELOPMENT OF THE SOVEREIGN DEBT RESTRUCTURING REGIME

“Property” is a term that is particularly socially-constructed. That is, the word no longer relates to its plain meaning, but instead to abstractions that have evolved over time and that are loosely based on that meaning. These abstractions have proven powerful. Rousseau considered the modern concept of alienable property owned by a single person the “founding myth” of modern civilization.² Before modern civilization, and in many indigenous societies to this day,

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1. “When it becomes necessary for a state to declare itself bankrupt, in the same manner as when it becomes necessary for an individual to do so, a fair, open, and avowed bankruptcy is always the measure which is both the least dishonourable to the debtor, and least hurtful to the creditor.” ADAM SMITH, *THE WEALTH OF NATIONS* 468 (Cannan ed., Methuen and Co. 2000) (1776).

2. CHARLES LIPSON, *STANDING GUARD: PROTECTING FOREIGN CAPITAL IN THE*

property was “owned” by the tribe, the community, or the Crown—not by individuals. Communal ownership only made sense when the community, the tribe or the people occupied and used the property. It was their territory, where they lived. The colonialist notion, far-removed, is that a legal person has a right to own property in a territory divorced from the colonialist’s community. This concept of property, which would have seemed abstract in a previous era, has become dominant over the last few hundred years, so much so that to disavow the colonialist notion would now seem illogical or heretical.

The modern notion of property first gained acceptance with advanced ships and navigation, as well as increased imbalances in military power, leading to a period of discovery, colonization and economic imperialism by rich Western states. Charles Lipson notes:

A central feature of all law, domestic and international, is the rationalization and maintenance of social relations, including, most significantly, property relations. The most effective legal systems do this with the least coercion, stimulating support for some political claims and hiding others from public view.³

Such rationalization took (and takes) place in a variety of forms, falling along a spectrum of imperial effort. At one end of this spectrum is colonization, the most coercive and expensive option for the rationalization and maintenance of social and property relations. Colonization was deemed necessary by Western powers in the early days of colonialism, where the perceived legal backwardness of the local populations required physical occupation in order to achieve economic exploitation.⁴

Later, the imperial powers discovered that they could avoid the expense of physical occupation, with its “causal link [to] investment security,”⁵ by resorting to only occasional armed intervention and indirect coercion through the “rule of law” and property rights. In Latin America a result similar to overt colonialism was achieved in this way through a combination of periodic armed intervention⁶ and co-option of the local elites to enforce the property rights of foreign investors. Even better than employing mixed panels of colonial and native judges (in order to provide some local participation in government and some expertise on local law),⁷ Latin American native judges could be relied upon, by themselves, to enforce the rights of the creditor states.

Thus, there existed in Latin America a remarkably pure example of what Professor David Caron describes as rule *through* law.⁸ As Martin Shapiro de-

NINETEENTH AND TWENTIETH CENTURIES 3 (1985).

3. *Id.* at 55. It is interesting, and perhaps internally inconsistent, that Lipson adopts the idea that property relations are the “most significant” social relations while simultaneously noting that the “West’s” emphasis on property relations is self-serving.

4. *Id.* at 16-17.

5. *Id.* at 149.

6. *Id.* at 54. Platt has discovered at least 40 examples of British armed intervention in Latin America between 1820 and 1914.

7. MARTIN M. SHAPIRO, *COURTS: A COMPARATIVE AND POLITICAL ANALYSIS* 59 (1981).

8. David D. Caron, *Towards a Political Theory of International Courts and Tribunals*, 24 *BERKELEY J. INT’L L.* 401, 406 (2006) (referencing Shapiro, Note 7, *supra*, pp. 17-20).

scribes it:

[S]o long as a judge acts to impose preexisting rules on the disputants, he is importing an element of social control. Or to put the matter differently, he is importing a third set of interests, whatever interests are *embodied in those rules*, to be adjudicated along with the interests of those two parties. (emphasis added).

Latin American judges adopted the rules of foreign states to the benefit of the foreign creditor states. Direct appointment of judges by the imperial power was unnecessary.

Thereafter, the Western powers found that they could move even further down the spectrum of imperial effort by creating international bodies that had as their goals free trade and the encouragement of foreign investment. In 1889, the US convened the first Inter-American Conference.⁹ The first Hague Conference was convened in 1899, followed by the bombardment and blockading of Venezuela by Britain, Germany and Italy to demand satisfaction of claims, including bond defaults.¹⁰ In the 1920s, the League of Nations held economic conferences, culminating with an attempt in 1929 to codify international property rights.¹¹ Then, in the wake of World War II, the victorious powers at the Bretton Woods Conference in 1944, after years of planning and negotiation between the US and Britain, created the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD), also known as the World Bank. In 1956, an informal group of creditor nations now known as the Paris Club held its first meeting. The constellation of the IMF, the World Bank, and the Paris Club has since become the principal locus of the international community's "sovereign debt restructuring" activities,¹² which are the subject of this paper.

III.

THE PROBLEM: THE ABSENCE OF A SOVEREIGN BANKRUPTCY COURT

The debt-restructuring functions of this constellation of the IMF, the World Bank, and the Paris Club have fallen far short of an ordered and predictable bankruptcy regime. Such regimes, as they have developed in domestic legal systems, have three goals in common:

- 1) They avoid the "run for the assets" and "run for the courthouse" problems that arise when multiple creditors have claims to a debtor's assets;
- 2) They enforce the payment of claims according to priority; and
- 3) They mandate the cancellation of all or most unpaid claims following

9. LIPSON *supra* note 2, at 58.

10. *Id.* at 73.

11. *Id.* at 75.

12. "Sovereign debt restructuring" is the euphemism adopted in academic and policy discussions on this topic, a phrase that rhetorically preserves the principle of *pacta sunt servanda*. To the extent that debt discharge is ever acknowledged in such discussion, it is generally termed "debt forgiveness." The term "debt repudiation" almost never appears in the literature.

bankruptcy in order to give the debtor a fresh start.¹³

Thomas Jackson reduces these three goals to what he describes as the two first principles of bankruptcy law:

- 1) Maximize efficiency by minimizing “conversion” or transaction costs in the bankruptcy process; and
- Provide some debtors with a fresh start.¹⁴

The way Jackson looks at it, the crafter of a bankruptcy regime first decides on the second item, a mechanism for deciding on whether or to what degree to grant a “fresh start” to various debtors. In the United States, for example, debtors are divided into classes and a fresh start is supplied according to class. A true fresh start, complete discharge, is granted to individuals with an income below the median income in their state. A less-generous fresh start is provided to more prosperous individuals. No discharge is granted to corporations.¹⁵

Whatever the mechanism, by answering the fresh-start question the crafter slices off a percentage of a various debtor’s total liabilities as “dischargeable,” with the balance “exempt-from-discharge.” Having made this determination, the crafter then turns to what Jackson calls the “core” goal of bankruptcy law; namely, maximizing the efficiency of the “conversion” process in order to leave the creditors as whole as possible.¹⁶ Efficiency is maximized by preventing wasteful conduct by the parties, especially the creditors, such as seizing assets that prevent the accumulation of income by the debtor, free-riding, holdout litigation, delay, and the like. *For their own benefit*, creditors acquiesce to an ordered bankruptcy process that arrives at a reasonably fair (as between creditors), swift, and utility-maximizing plan for repaying the debtor’s exempt-from-discharge liabilities as fully as possible.

In a sovereign context, creditors would ideally work with a debtor state as it approached bankruptcy in order to help the debtor state avoid bankruptcy, or to maximize their returns in a bankruptcy proceeding. But herein lies the problem: what should a rational creditor do if what will happen to the state following its bankruptcy is an unknown because the “bankruptcy” process is chaotic? Under such circumstances, it would be a fool’s game to bet on the outcome of a bankruptcy proceeding. The rational choice would be to hold out on the staunchest possible terms, even as the sovereign descends into bankruptcy. This tendency on the part of creditors in turn increases the probability of suicidal default. Such is the sovereign bankruptcy process as it exists today.

13. Patrick Bolton, *Toward a Statutory Approach to Sovereign Debt Restructuring: Lessons From Corporate Bankruptcy Practice Around the World*, IMF Working Paper WP/03/13 18 (Jan. 2003).

14. THOMAS JACKSON, *THE LOGIC AND LIMITS OF BANKRUPTCY LAW* 2-5 (1986).

15. Jeffrey D. Sachs, *Resolving the Debt Crises of Low-Income Countries*, in *BROOKINGS PAPERS ON ECONOMIC ACTIVITY* 2002:1 22-23, 27 (William C. Brainard & George L. Perry eds., 2002). In a sovereign context, Jeffrey Sachs suggests a case-by-case resolution of the fresh start question by an independent panel, perhaps under the auspices of the IMF. The panel would analyze the sustainability of the state’s debts in the context of its “business plan” and financial projections and decide what percentage of the debts were to be canceled.

16. JACKSON, *supra* note 14, at 5.

A. Sovereign Problem 1: Inadequate, Arbitrary Provision of Fresh Starts

The international community has in recent decades evolved non-judicial mechanisms for “sovereign debt restructuring,” such as the Highly Indebted Poor Countries Initiative (HIPC), the increasingly generous “Restructuring Terms” of the Paris Club,¹⁷ and recent debt forgiveness discussions/commitments by western leaders in the context of the Millennium Development Goals. The international community has, in other words, developed *ad hoc* mechanisms for providing something of a fresh start to debtors. However, the *ad hoc* nature of these acts has led to arbitrary inconsistencies among the degrees of debt relief offered to various nations.

For example, based in large part on the diplomatic efforts of special envoy James Baker III, the US has been successful in convincing the nineteen members of the Paris Club to agree to forgive eighty percent of debts owed to them by Iraq. On November 21, 2004, Jean-Pierre Jouyet, Paris Club president, said that the agreement urged by the US foresaw eighty per-cent of Iraq’s debts to the Paris Club being canceled in three stages: thirty per-cent immediately, a further thirty per-cent in 2005, and twenty per-cent in 2008.¹⁸

The arguments made by Mr. Baker in securing this accord apparently centered on the concept of “odious debts,” that is, debt proceeds misused by a previous government, specifically that of Saddam Hussein, for purposes other than the benefit of the people and territory of the state. These arguments contrast with decades of US assertion that sovereign debt agreements are binding under international law, regardless of the use of proceeds (*pacta sunt servanda*). As this news became public, one newspaper noted: “Some developing country policymakers and debt-relief campaign groups have contrasted the generous and swift relief being considered for Iraq with slow progress in reducing the debt of highly indebted African economies.”¹⁹ Meanwhile, sub-Saharan Africa has foreign debts of \$201 billion,²⁰ developing countries worldwide had almost \$1.25 trillion in external long-term debt at the end of 2003,²¹ and developing-country debt service is over \$179 billion per year.²² In Malawi, for example, one of the world’s poorest nations, twenty-one percent of government revenue is devoted to debt payments, approximately as much as Malawi spends on education, health, science, and technology combined.²³

17. Sachs, *supra* note 15, at 20.

18. Ralph Atkins & Andrew Balls, *Snow Praises Berlin for Iraq Debt Pact at G20 Summit*, FINANCIAL TIMES, Nov. 20, 2004, at 7.

19. *Id.*

20. ATKINS & BALLS, *supra* note 18.

21. U.N. Conference on Trade and Development, *Handbook of Statistics*, <http://www.unctad.org/Templates/Page.asp?intItemID=1914&lang=1> (last visited Mar. 1, 2006).

22. *Id.*

23. Warren Vieth, *Stubborn Debt Burden Spurs Search for New Ideas: On Eve of World Bank and IMF Talks, Activists Call on Rich Nations to Honor Pledges of Relief and Even Write Off Third World Obligations*, L.A. TIMES, Apr. 23, 2004, at 11. One could argue that a difference between Iraq and Malawi is that in the former case a dictatorial regime has been removed, whereas in the latter it remains in power. The relevance of this logical distinction is somewhat undermined by a

Apart from the special criteria that apparently surrounded Iraq's debt forgiveness, normal fresh-start mechanisms generally center around IMF "surveillance," the linchpin of informal debt relief. The focuses of IMF surveillance are macroeconomic and fiscal "reforms," which either increase the likelihood of debt repayment or benefit creditor-nation exporters and corporations.²⁴ No attention is placed on whether debt proceeds, undertaken on behalf of the people and territory, are actually being used on their behalf.

Similarly diffuse, the Heavily Indebted Poor Countries (HIPC) Initiative, jointly launched by the IMF and the World Bank in 1996, is based on a nation's total outstanding debt relative to exports and GDP, as opposed to ratios of debt service expenses to government revenues.²⁵ Turning back to Malawi, for example, the twenty-one percent of government revenue devoted to debt payments is the amount required *after* HIPC relief. Such debt service burdens, coupled with a general decrease in foreign aid since the 1990s, create what Jeffrey Sachs describes as a "poverty trap" in low-income countries.²⁶ Because the economic output of these nations added to foreign aid and then minus debt service is insufficient to maintain a subsistence level of income, the nations suffer a negative savings rate. That is, they are forced to cannibalize their income-producing capital stock, ensuring a decline in economic output and a decline in capital-labor ratios.²⁷ As a result, "requiring an IMF program has been an absorbing state: once in the IMF's clutches, it has been almost impossible to escape."²⁸

The significance of the Iraq write-down, for the purposes of this article, is less its irony than how it was achieved. The agreement was deliberately negotiated on an informal basis, and not even by a current US government official. The reasoning behind the agreement was not memorialized in any public document that carries value as precedent. The agreement, like the workings of institutions such as the Paris Club, was achieved in a manner kept outside the judicial or official realm. Denied such special treatment, Malawi soldiers on, its people unable to feed their children²⁹ even as the country cannibalizes its capital base due to a negative savings rate.

B. Problem 2: Failure to Maximize Conversion for Creditors

This *ad hoc* sovereign bankruptcy system is even more notable for its fail-

comparison of the generosity of the international community to post-Hussein Iraq relative to post-dictatorship Indonesia and the Philippines.

24. I.M.F., *IMF Surveillance: A Factsheet* (Sept. 2005), <http://imf.org/external/np/exr/facts/surv.htm>.

25. I.M.F., *Debt Relief Under the Heavily Indebted Poor Countries (HIPC) Initiative* (Sept. 2004), <http://www.imf.org/external/np/exr/facts/hipc.htm>.

26. Sachs, *supra* note 15, at 5.

27. *Id.* at 5-10.

28. *Id.* at 18. Sachs further notes that "[i]n 1978, there were 22 countries in IMF lending programs. By 1996 that figure had reached 75, and as of 2001, 63. Dozens of these countries have experienced nearly a quarter century of continuous IMF lending."

29. Craig Timberg, *Drought Magnifies Hunger, Suffering of Children in Malawi: Rural Village Tracks Malnutrition's Toll on Young*, WASH. POST, Nov. 4, 2005, at A1.

ure to maximize the efficiency of the “conversion” process, what Jackson describes as the core purpose of bankruptcy law. Argentina’s recent default, for example, involved more than 90 different bond issues and countless direct foreign investment disputes. With no mechanism in place to order these competing claims fairly, Argentina’s default resulted in a rush to exit from Argentina’s own debt, massive economic dislocation within Argentina (reducing its ability to repay), a cloud of litigation (notably holdout litigation), and years of delay.

In holdout litigation, a creditor (typically a hedge fund) buys up a significant portion of a bond issue and then, even if a restructuring settlement has been achieved with seventy or ninety percent of the bondholders, holds out by aggressively litigating their rights in the jurisdiction that was the choice of law for the bonds, usually New York. They hope to achieve a more favorable settlement than the rest of the bondholders even if it delays a global settlement for years, as has been the case with Argentina. At the same time, debtors have become more sophisticated and willing to litigate. However, as one Argentine official stated: “Forget litigation. It is useless The world has changed. Just over a decade ago, we had state-owned companies with assets all over the place that investors would have been able to target. The only thing left today are embassies and they are protected.”³⁰ The current system and the clouds of litigation it creates can be viewed as benefiting only lawyers.

Had a sovereign bankruptcy mechanism been in place to handle Argentina’s default, Argentina’s economic dislocation would have been minimized by a stay on litigation and debt service, as well as the infusion of new “priority” (debtor-in-possession) financing. Moreover, creditors would have been repaid more quickly and in an amount far greater than the roughly thirty five cents-on-the-dollar that they received pursuant to Argentina’s unilateral offer. The details could vary, but such a sovereign bankruptcy process would broadly consist of Argentina, after default, seeking in good faith temporary shelter in a court. The court would impose a stay on legal action as well as interest and principal repayments on Argentina’s debt. Then the court would, according to preexisting rules, sort out and prioritize various creditors’ claims against Argentina and propose a plan to which any party could object before it was adopted. After considering objections, the court would then set out a repayment and reorganization plan that would be binding on all parties.

As Professor David Caron points out in the introduction to this volume, a state’s expectation that it will most often appear before a given international court and tribunal (IC&T) as a claimant or a respondent will often drive its choice to back the creation of the IC&T.³¹ In Argentina, we have a situation where both claimant and respondent would benefit from the efficient solution described in the previous paragraph. Most participants in the debate over a sov-

30. Adam Thomson, *Stirring Up Talk of Legal Action: Adam Thomson Assesses How Effective Litigation Might Be for Argentina’s Frustrated Creditors*, FINANCIAL TIMES, Oct. 1, 2004, at 7.

31. Caron, *supra* note 8 at 415-16.

foreign bankruptcy court, with a few exceptions,³² agree with the notion that creating such a court would result in more equitable sovereign fresh starts while creating massive new efficiencies in the conversion process. We now turn to the conflicts of interest and historical forces that may be at work in the international community's failure to establish such a court.

IV. THE CONFLICTS OF INTEREST OF CREDITOR AND DEBTOR STATE REPRESENTATIVES

Common sense and international law distinguish between state representatives and the state. State representatives make up government and conduct international affairs, but they are not the state.³³ The state is the people and territory. For example, in the Vienna Convention on the Law of Treaties, if the expression by a State of "consent to be bound by a treaty has been procured through the corruption of its *representative* directly or indirectly by a negotiating State . . . [the State] may invoke such corruption as invalidating its consent to be bound by the treaty" (emphasis added).³⁴ International courts and tribunals are necessarily created by state representatives with limited tenure. These representatives, in choosing to create or not create a given IC&T, are driven by concerns unique to the circumstances of the incumbent political regime.³⁵ As such, state representatives exhibit two characteristics that may interfere with their ability to make reliable decisions about a given IC&T based upon an objective assessment of whether launching or not launching would maximize the utility of the com-

32. Two such exceptions are an industry group, the International Primary Market Association (IPMA) and the academic Nouriel Roubini.

Robert Gray, the chairman of the IPMA, states that "the IMF ha[s] produced no empirical evidence [of] . . . an inherent collective action problem among private sector creditors in sovereign debt restructuring that precludes agreement between them." Robert Gray, *Collective Action Clauses: The Way Forward* 4 (Feb. 2004), http://www.law.georgetown.edu/international/documents/Gray_000.pdf. This is an assertion of credibility similar to the chairman of an association of energy companies stating that there is no empirical evidence precluding the nonexistence of global warming. Nouriel Roubini states on his blog: "The current system of unilateral debt exchanges works and it should not be changed as it is not broken. All previous debt restructuring deals were done without negotiations between the debtor and its creditors. In a typical deal—Pakistan, Ukraine, Ecuador, Uruguay and now Argentina—the debtor never negotiates: it hires a legal advisor and a financial advisor who do some extensive market soundings—not negotiations—to figure out which deal is acceptable to a large fraction of creditors. Then, when the homework is done, the country makes an exchange offer, that is, a take-it-or-leave-it debt exchange. And in all cases before Argentina, 99% of creditors accepted the offer and there were very few holdouts. Argentina behaved in the same fair way: it did its market soundings and then made an exchange offer. Yes, some extra info sharing and consultation by Argentina with its creditors would have been nice and fair but it would have not changed the substance of the eventual deal." Nouriel Roubini, *The Successful End of the Argentine Debt Restructuring Saga* . . . (Mar. 2005), <http://www.rgemonitor.com/blog/roubini/91192>.

33. JAMES R. FOX, *DICTIONARY OF INTERNATIONAL AND COMPARATIVE LAW* 306 (3^d ed. 2003). A state is "a group of people permanently occupying a fixed territory and having common laws, government and the capability of conducting international affairs."

34. Vienna Convention on the Law of Treaties between States and International Organizations or Between International Organizations, May 22, 1969, art. 50, 1155 U.N.T.S. 331.

35. Caron, *supra* note 8 at 415-16.

munity of nations. First, state representatives are political actors; they are not necessarily motivated by the goals of a given IC&T as stated in its constitutive instrument.³⁶ Second, they are temporally-limited actors. In both respects, they are conflicted actors.

A. State Representatives are Temporally-Limited Actors

Jeffrey Sachs answers the question of why no sovereign bankruptcy court exists with the observation that, at any given starting date for a rational sovereign bankruptcy process, existing creditors will likely suffer a capital loss due to a more even-handed provision of a fresh start to debtors.³⁷ To put it in economic parlance, Sachs implies that even though the long-run utility of the creditor states will be maximized through the creation of an efficient sovereign bankruptcy system, state representatives avoid this rational choice either because: (i) their state's current creditors will suffer a disproportionate amount of the existing-creditor losses; or (ii) regardless of whether their state will suffer disproportionately relative to other creditor states, their interests are politically aligned with their state's current creditors as opposed to its future creditors.

With respect to the first possibility, it is true that the position of states as creditors shifts over time. For example, in 1914, 68% of Latin American external public debt was from Britain,³⁸ and 47% of private foreign investments in Latin America were from Britain.³⁹ The corresponding percentages in 1914 of US investment were far lower: 4% and 18% respectively.⁴⁰ In the years 1961-1967, by contrast, US investment constituted 61% of foreign direct investment flows from the thirteen major industrial countries.⁴¹ The corresponding percentage for Britain at that point was nine percent.⁴² Accordingly, if the starting date for a sovereign bankruptcy mechanism had been 1914, Britain would have suffered disproportionately. If the starting date had been 1967, the US would have suffered disproportionately. Such shifting burdens among states that have effective veto power over the establishment of a judicial mechanism make its approval less likely at any given point in time.

Second, at the starting date of the mechanism, the current constituencies of the creditor state representatives, and the state treasuries themselves, will likely see the efficiency gains from an improved conversion process more than canceled out by the accompanying fresh-start provisions. In contrast, future creditors will likely gain, on balance, from the new system due to increased effi-

36. *Id.*

37. Jeffrey Sachs, *The Roadblock to a Sovereign Bankruptcy Law*, 23 CATO J. 5 (Spring/Summer 2003).

38. U.N. Department of Economic and Social Affairs, Economic Commission for Latin America, *External Financing in Latin America* 16 (1965).

39. *Id.* at 17.

40. *Id.* at 16-17.

41. O.E.C.D., *International Investment and Multinational Enterprises: Recent International Direct Investment Trends* 40, table 3 (1981).

42. *Id.*

ciency of conversion and the disciplining effect of a sovereign bankruptcy mechanism on their investment decisions. Further, creditors will gain from improved behavior by sovereign debtors in their use of proceeds, which would be under closer scrutiny under the new system.

Debtor-state representatives face a similar conflict. Their primary goal with respect to their state's finances is to maximize, at least during their tenure, the difference between current account inflows and outflows. The expense of servicing existing debts generally forms a relatively minor part of outflows, whereas new borrowings could dwarf those outflows. A debtor-state representative's concern is therefore that the provision of a fresh start would be more than offset by a decrease in new investment. In the short-term, a fresh start is less valuable than continued foreign investment.

B. State Representatives are Political, Self-Interested Actors

These conflicts between the *status quo* and a sovereign bankruptcy regime are strongest, with respect to both creditor and debtor state representatives, when then debts being extended and assumed are to some degree odious. A debt is odious if the proceeds of the debt were not used for the benefit of the population and territory burdened by it,⁴³ a test used in the Versailles Treaty of June 28, 1919.⁴⁴

The ability of governments to use sovereign debt proceeds in an odious manner is virtually unlimited under the current system. Indeed, the current system imposes no checks or balances on the use of the money raised through sovereign debt agreements. This omission, and the malfeasance that it enables on the part of both creditors and borrowing government officials, is a major flaw in the current system of sovereign borrowing. Far from the detailed business plan that Sachs would require as part of a sovereign bankruptcy proceeding, the descriptions of the use of proceeds in most sovereign debt instruments are remarkably non-specific. For example, the "Use of Proceeds" section of a recent prospectus for an offering of \$12.6 billion in sovereign debt by the Republic of Argentina of states in full: "Unless otherwise specified in a prospectus supplement, the Government will use any net proceeds from the sale of securities offered by this prospectus for the general purposes of the government of Argentina."⁴⁵

In an 189-page prospectus, this single sentence is the extent of Argentina's disclosure regarding use of proceeds. How the proceeds will in fact used by the government of Argentina for its "general purposes," with no further elaboration,

43. D.P O'CONNELL, STATE SUCCESSION IN MUNICIPAL AND INTERNATIONAL LAW 460 (1967).

44. Treaty of Versailles, June 28, 1919, art. 296, 225 Parry 188, 2 Bevans 235, 13 AMER. J. INT'L L. SUPP. 151, 385 (year).

45. *Debt securities Registration Statement Filed by the Republic of Argentina with the Securities and Exchange Commission*, 5 (July 2, 2004), <http://www.sec.gov/Archives/edgar/data/914021/000095012304008163/y98698svb.htm>.

will be monitored by the government itself.

One solution to this ambiguity would be to require that Argentina's borrowing take the form of project finance: Five billion dollars for this power plant, one billion dollars for that highway. An intermediate solution would be for the document to show at least *some indication what the money is for*. Absent such a declaration, Argentina will nevertheless be under IMF "surveillance," but such surveillance does not focus on spending but instead focuses on macroeconomic issues such as exchange rates, deficits, inflation, and trade. According to the IMF:

Exchange rate, monetary and fiscal policies remain at the center of IMF surveillance "Article IV consultations," as IMF surveillance discussions are known, usually take place once a year. IMF economists visit the member country to gather information and hold discussions with government and central bank officials, and often private investors and labor representatives, members of parliament, and civil society organizations. Upon its return, the mission submits a report to the IMF's Executive Board for discussion. The Board's views are subsequently summarized and transmitted to the country's authorities.⁴⁶

Astonishingly, no element of Article IV consultations is devoted to tracking the use of the proceeds of specific sovereign debt offerings; in these consultations the IMF never asks the question, "So what did you actually do with that \$12.6 billion?"

In contrast, the use-of-proceeds statements of developed-country corporations are far more detailed than those of sovereigns. These statements are made in the prospectus itself or in other filings, press releases, analyst conference calls and meetings, or other disclosures. The corporation's subsequent adherence to its planned use of proceeds is then enforced through internal controls and external monitoring by a fleet of analysts, investors, and credit-rating agencies.

Proposals such as Sachs' and the SDRM would move sovereigns closer to the transparency and disclosures required of public corporations, which would in turn reduce or penalize the provision of odious debts. Perhaps unsurprisingly, the transparency requirements of the SDRM were among the provisions most hotly contested when the members of the IMF debated the idea in 2002-03.

Under the current system, creditors of sovereigns benefit from the lack of transparency and scrutiny because no one inquires into implicit or explicit tying arrangements that might have accompanied the funds. They also avoid objective scrutiny of whether it makes sense for the sovereign to assume the debt in the first place; that is, whether the additional capital can be used in a manner that increases economic output sufficiently to justify future debt service expenses. Debtor state representatives likewise benefit from a lack of scrutiny because it frees them to potentially use a portion of the funds for the consumption or aggrandizement of themselves, families, and friends.⁴⁷

46. *IMF Surveillance: A Factsheet*, *supra* note 24.

47. John Perkins puts all of this more darkly. He states that his role as an international economic consultant was, first, to "justify huge international loans" to developing countries that would "funnel money back" to US engineering and construction companies, and, second, to "bankrupt the

Thus, to the extent that international lending tends to produce odious debts at the expense of the peoples and territories on whose behalf the debts are assumed, both creditor and debtor state representatives stand to lose from a sovereign bankruptcy mechanism that would impose greater discipline and transparency. Similarly, state representatives, in assenting to an IC&T, are not necessarily motivated by the goals of a given IC&T stated in its constitutive instrument.⁴⁸ Furthermore, state representatives may also be conflicted by political and economic motivations specific to themselves and a subset of the constituencies that they represent.

V.

IMPEDIMENTS CREATED BY THE STRUCTURES OF THE IMF, THE WORLD BANK, AND THE PARIS CLUB

As Professor Caron notes, IC&Ts are often created by the community, not by parties.⁴⁹ The community is *a priori* concerned with the interests of the community in the resolution of a given class of disputes, and not necessarily in the interests of particular parties or the outcomes of particular disputes.⁵⁰ However, a community can define and organize itself in various ways, and these choices of definition and organization, particularly with respect to voting rights, affect how the “community” expresses its interests. We now turn to the political process through which a community of nations defined and organized itself in creating the IMF, the World Bank, and the Paris Club.

A. The IMF

In 1940, Britain stood isolated against German military onslaught. Britain’s armaments and food were being depleted at an alarming rate. In December 1940, President Roosevelt submitted to Congress a “Lend-Lease” program that would provide support to Britain and was greeted in London “with immense relief and gratitude.”⁵¹ During the following months and years, the US supplied Britain with temporary aid as Britain anxiously awaited Lend-Lease’s passage by Congress. During that period, in May 1941, the US initiated discussion with Britain regarding post-war economic policy.⁵² In response, the British and Lord

countries” (after the US companies had been paid) “so that they would be forever beholden to their creditors, and so they would present easy targets when we needed favors, including military bases, UN votes, or access to oil and other natural resources The unspoken aspect of every one of these projects was that they were intended to create large profits for the contractors, and to make a handful of wealthy and influential families in the receiving countries very happy, while assuring the long-term financial dependence [of the state] . . . *The larger the loan, the better*” (emphasis added). JOHN PERKINS, CONFESSIONS OF AN ECONOMIC HIT MAN 15-16 (2004).

48. Caron, *supra* note 8 at 414-15.

49. *Id.* at 415-16

50. *Id.*

51. ARMAND VAN DORMAEL, BRETTON WOODS: BIRTH OF A MONETARY SYSTEM 13 (1978).

52. *Id.* at 21.

Maynard Keynes responded with the latest draft of their post-war economic order that, according to Dean Acheson, “provided merely that lend-lease should be extended; that the British should return what was practicable for them to return; that no obligation should be created; and that they would be glad to talk about other matters.”⁵³

In reply, on July 28, Acheson handed Keynes a draft regarding what Britain could supply to the US as “consideration” for its generosity, stating in Article VII:

The terms and conditions upon which the United Kingdom receives defense aid from the United States of America and the benefits to be received by the United States of America in return therefor, as finally determined, shall be such as not to burden commerce between the two countries but to promote mutually advantageous economic relations between them and the betterment of world-wide economic relations; they shall provide against discrimination in either the United States of America or the United Kingdom against the importation of any product originating in the other country; and they shall provide for the formulation of measures for the achievement of these ends.⁵⁴

Keynes asked Acheson if Article VII in fact contained requirements regarding “imperial preferences” and “exchange and trade controls.”⁵⁵ Acheson acknowledged that it did. According to Acheson, Keynes thereupon “burst into a speech” that the agreement would “require an imperial conference” and “saddled upon the future an ironclad formula from the Nineteenth Century.”⁵⁶

In the next few months Keynes sketched out “an ideal scheme [for an International Clearing Union] which would preserve the advantages of an international means of payment universally acceptable, whilst avoiding those features of the old system which did the damage.”⁵⁷ Keynes’s ideas were self-described as “utopian” and “of the spirit of bold innovation,”⁵⁸ and were also borne of Britain’s position relative to the US under the circumstances. Britain at the time had close to zero foreign reserves, was a net-importer, and was being torn apart by war. In contrast, the US economic position was like that of China today: a massive net-exporter with an extraordinary level of foreign reserves. Keynes’ utopian proposals were perhaps motivated by principle and also perhaps the best Britain could hope for under the circumstances.

Meanwhile, US Treasury Department economist Harry White, Keynes’ intellectual counterpart in the US, developed a scheme for a “United Nations Stabilization Fund and a Bank for Reconstruction of the United and Associated Nations.”⁵⁹ Keynes finished the fourth draft of his Clearing Union proposal in February 1942,⁶⁰ and White finished the first draft of his proposal on May 8,

53. *Id.* at 22.

54. *Id.* at 22.

55. *Id.* at 22.

56. *Id.* at 22-23.

57. *Id.* at 34.

58. *Id.* at 34.

59. *Id.* at 51.

60. *Id.* at 48.

1942.⁶¹

In October 1942, US Treasury Secretary Robert Morgenthau and White traveled to Britain, where a meeting was held regarding the competing proposals. According to a participant in the meeting:

The exchange of views was left almost wholly to Keynes and White There was a substantial area of agreement but there were also sharp differences Differences arose on the voting system and other points. Finally Keynes argued for direct negotiations between the U.S. and U.K. alone or possibly with the Dominions and the Soviet Union added, while White maintained that this would create suspicion of an Anglo-Saxon financial ‘gang-up.’ Keynes heatedly argued that, the subject matter being complicated, it was essential that the U.S. and U.K. should work out a plan themselves, invite the Russians, in order to allay suspicion, and perhaps the Dominions and French, to join, and then set it up and invite the rest of the world to join⁶²

By March 1943, the US and Britain had prepared a draft regarding a “Stabilization Fund for the United and Associated Nations and an International Bank for Reconstruction and Development,” which was then shared with Russia and China. In June 1943, the US hosted a meeting to further discuss the plan that was attended by representatives of 12 nations, which resulted in another draft.⁶³ The Bretton Woods Conference was ultimately convened in July 1944. Representatives of 44 nations accepted the invitation of the US to attend the Conference.

Throughout the Conference, White and a small group of technical advisers kept absolute control over the text of the articles to be included in the agreement. Virtually all other important decisions, such as decisions over the allocation of quotas (voting rights), were made behind closed doors by negotiations between the American delegation, led by Morgenthau, and the foreign delegation involved.⁶⁴ At the end of the Conference, the Articles of Agreement of the IMF and the Articles of Agreement of the IBRD were presented for ratification by member governments.

The Articles granted voting rights to the Original Members of the IMF and the IBRD based upon quotas effectively determined by the US delegation.⁶⁵ The US, Britain, and the Union of Soviet Socialist Republics received the largest quotas, measuring \$2.75 billion, \$1.3 billion, and \$1.2 billion, respectively (by an agreement preceding the conference, the quota of the US and the entire British Commonwealth would be equal).⁶⁶ The remaining forty one nations re-

61. *Id.* at 51.

62. *Id.* at 62-63.

63. I.M.F., *Bretton Woods Conference Collection: Bretton Woods Conference Files*, <http://www.imf.org/external/np/arc/eng/fa/BWC/s4.htm>. The 12 nations were Belgium, Bolivia, Canada, Czechoslovakia, Ecuador, France, the Netherlands, Norway, Philippines, Poland, the United Kingdom, and the US. By the spring of 1944, the “Joint Statement of Experts on the International Monetary Fund” was published simultaneously in eight consulting countries, reporting the views of these nations.

64. VAN DORMAEL, *supra* note 51, at 179.

65. *Id.* at 182-83.

66. Articles of Agreement of the I.M.F., adopted at the United Nations Monetary and Finan-

ceived quotas ranging from between \$500,000 and \$550 million, with twenty nine of the forty one states receiving quotas of less than \$100 million.⁶⁷ The quotas of "Other Members" not invited or not present at the Conference, but that later joined the IMF, were to be determined by the IMF Board of Governors,⁶⁸ which would in turn consist of one representative from each current IMF member, each voting in an amount roughly corresponding to the state's quota.⁶⁹ Any change in quotas would require an eighty-five percent majority of the total voting power.⁷⁰

The IMF now includes 184 members. Currently, the (approximate) voting rights of the US (17%), Japan (6%), Germany (6%), Britain (5%), France (5%), Saudi Arabia (3%), Canada (3%), Italy (3%), Russia (3%), China (3%), and Belgium (2%),⁷¹ are together sufficient to establish a majority in any Board of Governor decision. The voting rights of the US alone are sufficient to veto any decision, such as a change in quotas, which requires an eighty-five percent super-majority. Similarly, the US can effectively veto any amendment to the Articles of Agreement, which would require a sixty percent majority of members having eighty-five percent of the total voting power of the IMF.⁷²

B. The IBRD

The IBRD/World Bank was set up parallel to the IMF. The Original Members were the Original Members of the IMF⁷³ and the size of their subscriptions and voting rights paralleled those of the IMF.⁷⁴ Like the IMF, the admission of Other Members and the size of their Subscriptions and corresponding voting rights is decided by the current members.⁷⁵ The relative member voting rights of the four organizations that constitute the World Bank Group (the IBRD, the International Finance Corporation, the International Development Association, and the Multilateral Investment Guarantee Agency) also roughly parallel those of the IMF.⁷⁶ In other words, they grant majority control to a relatively small group of rich nations, with by far the largest voting power (ranging from 13.92% at the International Development Association to 23.65% at the International Fi-

cial Conference, Dec. 27, 1945, Schedule A, 2 U.N.T.S. 39.

67. *Id.*

68. *Id.* art. II, sec. 2.

69. *Id.* art. XII, sec. 2(e).

70. *Id.* art. III, sec. 2.

71. I.M.F., *IMF Members' Quotas and Voting Power, and IMF Board of Governors* (Nov. 7, 2005) <http://www.imf.org/external/np/sec/memdir/members.htm>.

72. Articles of Agreement of the I.M.F., *supra* note 66, at art. XXVIII(a).

73. I.B.R.D. Articles of Agreement, art. II, sec. 1(a) (Feb. 16, 1989), <http://web.worldbank.org/WBSITE/EXTERNAL/EXTABOUTUS/ORGANIZATION/BODEXT/0,contentMDK:20049557~menuPK:64020046~pagePK:64020054~piPK:64020408~theSitePK:278036,00.html>.

74. The World Bank, *Voting Powers*, <http://web.worldbank.org/WBSITE/EXTERNAL/EXTABOUTUS/ORGANIZATION/BODEXT/0,contentMDK:50004947~menuPK:64020035~pagePK:64020054~piPK:64020408~theSitePK:278036,00.html> (last visited Mar. 1, 2006).

75. I.B.R.D. Articles of Agreement, *supra* note 66, art. II, sec. 1(b).

76. World Bank, *Voting Powers*, *supra* note 74.

nance Corporation) going to the US.⁷⁷

C. The Paris Club

The Paris Club describes itself as a “non-institution,” “an informal group of official creditors whose role is to find coordinated and sustainable solutions to the payment difficulties experienced by debtor nations.”⁷⁸ It has brokered 399 creditor agreements involving 82 debtor nations since inception.⁷⁹ The Paris Club’s Agreed Minutes are a “recommendation” to the participating parties.⁸⁰ They are not put on record. Instead, the Paris Club deliberately operates outside the realm of formal international or national law. The Paris Club’s stated restructuring terms for low-income countries have dramatically changed at least five times since 1988,⁸¹ without a consistent normative basis.

D. Green Rooms and IC&Ts

Courts and tribunals are not desirable to a given party if they dilute their ability to dominate other parties. When a given institutional structure *already* creates domination or a disproportionate power for some parties over others, and when the dominant parties simultaneously control whether or not the institution creates an IC&T, that institution is unlikely to create an IC&T. Other papers in this volume echo this assertion. Those papers variously discuss the failure to open any investigation into the air campaign in Yugoslavia,⁸² the unequal effects of the World Trade Organization (WTO) dispute resolution mechanism on developing countries,⁸³ the premature termination of the Yugoslavia and Rwanda war crimes tribunals,⁸⁴ and the failure to include dispute resolution procedures in the North American Free Trade Agreement (NAFTA).⁸⁵ These myriad failures and omissions, like the failure to create an international bankruptcy court, were not oversights. Rather, they stemmed from powerful states’

77. *Id.*

78. The Paris Club, *Description of the Paris Club*, <http://www.clubdeparis.org/en/presentation/presentation.php?BATCH=B01WP01> (last visited Mar. 1, 2006).

79. *Id.*

80. The Paris Club, *Definitions*, <http://www.clubdeparis.org/en/presentation/presentation.php?BATCH=B04WP02#1> (last visited Mar. 1, 2006).

81. Sachs, *supra* note 15, at 20-21. Such changes include the Toronto Terms (1988), the London Terms (1991), the Naples Terms (1994), the Lyon Terms (1996), and the Cologne Terms (1999).

82. Anne-Sophie Massa, *NATO’s Intervention in Kosovo and the Decision of the Prosecutor of the International Criminal Tribunal for the Former Yugoslavia Not to Investigate: An Abusive Exercise of Prosecutorial Discretion?*, 24 BERKELEY J. INT.’L L. 610 (2006).

83. Leah Granger, *Retaliation under World Trade Organization (WTO) Dispute Settlement System and its Relatively Different and Unequal Effects on Developing Countries*, 24 BERKELEY J. INT.’L L. 521 (2006).

84. Laura Bingham, *Strategy or Process? Closing the International Criminal Tribunals for the Former Yugoslavia and Rwanda*, 24 BERKELEY J. INT.’L L. 687 (2006).

85. Jennifer A. Heindl, *Toward a History of NAFTA’s Chapter Eleven*, 24 BERKELEY J. INT.’L L. 672 (2006).

perception of their interests coupled with their effective or statutory dominance over the institution in question.

If the game is fixed for certain parties in the very voting structure of an institution, why should the favored parties ratify an independent tribunal to question the institution's decisions? An institution that favors certain parties over the rest in its voting structure is unlikely to spawn an independent IC&T.

Similarly, unequal voting power makes the emergence of new IC&Ts at those institutions unlikely. This reality became starkly clear when Anne Krueger, soon after joining the IMF as its new First Deputy Managing Director (at the invitation of Managing Director Horst Köhler) in September 2001, proposed a Sovereign Debt Restructuring Mechanism (SDRM) that would have effectively created a sovereign bankruptcy court under the auspices of the IMF. Krueger's idea was to set up an "orderly framework"⁸⁶ within the IMF "legally ringfenced" from the IMF Executive Board⁸⁷ that would adjudicate sovereign bankruptcies.⁸⁸ Krueger's initial proposal, *A New Approach to Sovereign Debt Restructuring*, was met with criticism.⁸⁹ She then offered an extensively-revised version.⁹⁰ The revised proposal was still not acceptable to IMF leadership. Finally, a further revised proposal was formally considered and rejected by the IMF Executive Board in 2003.⁹¹ The adoption of the latter proposal was supported by seventy percent of the membership of the IMF,⁹² but implementation of the SDRM would have involved amendment of the IMF Articles of Agreement, which requires a sixty percent majority of members having eighty five percent of the total voting power of the IMF Board of Governors. Because the US prefers collective action clauses,⁹³ as opposed to the SDRM, amend-

86. I.M.F., *Transcript of a Teleconference on Sovereign Debt Restructuring Mechanism with Washington-based Journalists and First Deputy Managing Director, Anne Krueger* (Apr. 1, 2002) <http://www.imf.org/external/np/tr/2002/tr020401.htm>. ("QUESTION: Do you have any model in your head or any sort of existing model of how the judicial panel might work? Is it going to be based on a sort of WTO model or World Bank dispute model or what? MS. KRUEGER: Well, it could be any of those or it could actually be something from the International Court of Justice, whereby you have these judges who are called in for particular cases, and so you have—well, as WTO does, too—we don't have a model in mind, but I think the idea is that there would be a panel that could be called in as these cases arose.")

87. Anne O. Krueger, *To Make Sovereign Debt Restructuring Smoother, Not To Dictate the Terms*, LE MONDE ECONOMIE, Feb. 18, 2002, <http://www.imf.org/external/np/vc/2002/021802.htm>.

88. Anne O. Krueger, *A New Approach To Sovereign Debt Restructuring*, I.M.F., Apr. 2002.

89. GROUP OF THIRTY, WORKING GROUP REPORT: KEY ISSUES IN SOVEREIGN DEBT RESTRUCTURING 7 (2002).

90. *Id.*

91. I.M.F., *Proposals for a Sovereign Debt Restructuring Mechanism (SDRM)* (Jan. 2003), <http://imf.org/external/np/exr/facts/sdrm.htm>. The mechanism, based upon best practices in domestic bankruptcy law, would have allowed a defaulting sovereign and a qualified majority of creditors to reach an agreement that would then be made binding on all creditors, deterred disruptive litigation, protected creditor interests, and excluded a specified amount of new financing from the restructuring.

92. Gray, *supra* note 32, at 1 n.1.

93. John B. Taylor, *Sovereign Debt Restructuring: A U.S. Perspective, Remarks at the Conference on Sovereign Debt Workouts: Hopes and Hazards*, Institute for International Economics (Apr. 2, 2002), <http://www.ustreas.gov/press/releases/po2056.htm>.

ment of the Articles has been impossible because the US holds seventeen percent of the voting power at the IMF.

The proposal was, according to at least one report, also opposed by a few debtor states because they believed it would raise the price of credit due to increased creditor discipline, increased ease of restructuring, and a corresponding decrease in bailouts.⁹⁴ It was likewise opposed by some debtor advocates because it would place control of the mechanism permanently into the hands of the IMF. As Ann Pettifor, a director of Jubilee 2000,⁹⁵ stated at an IMF forum:

[U]nder the rule of law, wherever you have the rule of law, it is not appropriate to be judged in one's own court. And under the sovereign debt restructuring mechanism, the IMF, both as a major creditor in her own right but also the agent of creditors, is the judge effectively in the court of the SDRM.

We believe that this process is being driven by institutional self-interest because the sovereign debt restructuring mechanism would enhance the role of the Fund and would enshrine the international role of the Fund in law.⁹⁶

The IMF, with its colonialist provenance and undemocratic voting structure, has yet to receive the imprimatur of being a truly representative international body. Pettifor worries that giving the IMF jurisdiction over a sovereign bankruptcy court would grant it such credibility.

Indeed, as Pettifor suggests, the status in international law of the IMF, the World Bank and the Paris Club are unclear. The Yearbook of the United Nations for 1946-47 mentions that the question of an agreement between the United Nations and the IBRD clarifying the relationship of one to the other had, at the request of the IBRD, been postponed (apparently indefinitely). Similarly, the US effectively required that the location of the headquarters of the IMF and the World Bank be located in Washington, D.C., despite the strong objection of Keynes. Keynes preferred New York for four reasons:

- (1) the Fund and bank should appear international and independent;
- (2) no single government should be in a position to influence unduly the directors and the staff;
- (3) there were technical advantages in being located in New York, which was the financial centre of the United States; and
- (4) co-operation with the Economic and Social Council would be easier.⁹⁷

The formal title of the Bretton Woods conference was the United Nations Monetary and Financial Conference. The question that Krueger and Pettifor are currently concerned with is whether, at the creation of the Bretton Woods institutions, the international community effectively ceded jurisdiction over the in-

94. Hal S. Scott, *A Bankruptcy Procedure for Sovereign Debtors?*, 50 (Sep. 2003), <http://www.law.harvard.edu/programs/pifs/pdfs/hscottsovereigndebt.pdf>.

95. See generally The Jubilee Debt Campaign, <http://www.jubileedebtcampaign.org.uk/?lid=280> (last visited Mar. 1, 2006).

96. Transcript of an IMF Economic Forum, *A New Approach to Sovereign Debt Restructuring: An IMF Proposal*, Comments of Ann Pettifor, Programme Coordinator, Jubilee Research (Jan. 22, 2003), <http://www.imf.org/external/np/tr/2003/tr030122.htm>.

97. VAN DORMAEL, *supra* note 51, at 294.

ternational economic matters to the IMF and World Bank,⁹⁸ and whether these institutions, designed by two states, now in reality comprise the ‘international order’ for economic affairs.⁹⁹

E. The “Big Man” Problem

The IMF, World Bank and Paris Club do not make it clear what their rules are to begin with. Their ever-changing approaches to resolving sovereign defaults often lack coherence or consistency, or sometimes even a rational basis. For example, the latest approach, the Heavily Indebted Poor Countries (HIPC) Initiative, jointly launched by the IMF and the World Bank in 1996, is based on a nation’s total outstanding debt relative to exports and GDP, instead of ratios of debt service expenses to government revenues.¹⁰⁰ The HIPC criteria thereby penalize countries with: (i) low government tax revenues relative to exports or GDP; and/or (ii) high debt service relative to total outstanding debt. These criteria, which focus on a country’s balance sheet as opposed to its cash flows, have been repeatedly criticized by economists and debt-relief advocates.¹⁰¹

Given this lack of logic in rule-making, as well as their self-appointment, the IMF, the World Bank, and the Paris Club can at best be said to operate in the mediatory continuum¹⁰² in a role analogous to the “big man,” the Papuan owner of many pigs, as described by Shapiro in his book.¹⁰³ In Shapiro’s account, the Papuan disputants

do not expect [the big man] to be neutral in the sense of having no interests of his own. Indeed the bigger he is, the broader is likely to be the web of his interlocking social and economic interests. The requirement of mutual consent allows the Papuans, like modern corporations in search of an arbitrator, to settle on a third who will not see his interests, whatever they may be, as parallel to those of one but not the other of the parties.¹⁰⁴

The idea is that the big man, because of his wealth and position, is above bribery, and that placing him in the position of arbiter of disputes between those be-

98. “The memories of the economic, political, and social turbulence of the 1930s and the enormous suffering as well as the cost associated with its unfortunate aftermath, the Second World War, provided the impetus for establishing an order in the community of nations that would prevent the recurrence of such painful episodes. On the international front, the efforts that underpinned this order led to the creation of the United Nations and its numerous specialized agencies. In the economic area, the order was based on a framework laid out and agreed upon at the Bretton Woods Conference, which established the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD), also known as the World Bank (emphasis added).” I.M.F., *The Unique Nature of the Responsibilities of the IMF*, <http://www.imf.org/external/pubs/ft/pam/pam46/pam46int.htm>.

99. *Id.*

100. I.M.F. Fact Sheet, *Debt Relief Under the Heavily Indebted Poor Countries (HIPC) Initiative* (Sept. 2004), <http://www.imf.org/external/np/exr/facts/hipc.htm>.

101. For a summary of these critiques, see NANCY BIRDSALL & JOHN WILLIAMSON, *DELIVERING ON DEBT RELIEF* 33 (2002).

102. See generally SHAPIRO, *supra* note 7, at 8-17.

103. *Id.* at 6.

104. *Id.* at 18.

low him on the social and economic ladder reduces the likelihood of corruption of the judicial process.

The quota/subscription voting systems of the IMF and World Bank similarly derive from big-man logic. As an IMF Factsheet puts it, “quotas . . . broadly reflect each country’s economic size.”¹⁰⁵ Because IMF/World Bank members consented to membership (though the same cannot be said for the Paris Club), they could be said to have consented to the big nations’ mediation of their disputes, despite the fact that the organizations’ voting structures would seem to preclude true independence from “the party that receives the more favorable outcome”¹⁰⁶

However, a larger problem in applying the big-man analogy to these organizations is that it is difficult to say that their members consented to the norms enforced by the IMF, World Bank or the Paris Club. It could be argued that poor countries turn to the big man because he “knows more of the law and custom, because he has the economic, political, or social power to enforce his judgment, or because his success or high position is taken as an indication of his skill and intelligence at resolving disputes.”¹⁰⁷ It is not possible, however, to argue that poor countries are consenting to a detailed preexisting rule (even in an abstract sense) for in this instance the big man’s rules have been ever-changing without anchor in a clear set of norms.

A final impediment to the establishment of a sovereign bankruptcy court created by the structures of the IMF, World Bank, and Paris Club, is the very fact that creditor nations, by dint of history, find themselves in the role of the big man. They are naturally loath to dilute that position for two reasons. First, an international bankruptcy court would take away their power to respond to different situations in different ways, and they want to preserve that power because they feel it suits their interests. Second, even if such a bankruptcy court in and of itself were to appeal to the creditor nations, its creation could set a precedent that would open the door to the creation or strengthening of other independent international judicial institutions. The creation of an independent mechanism that circumvents *ad hoc* institutions threatens a slippery slope down from the unique position of control in which history has placed the big men over the international economic order. For example, in the latest efforts to avoid such a slippery slope, US United Nations Ambassador John Bolton is seeking to expand the influence of “principal budget contributors” over the United Nations through various “reform[s],” including reversion to past practice on the Security Council where the five permanent members—the US, Britain, Russia, China and France—reach agreement amongst themselves before bringing a proposal before

105. I.M.F., *The IMF at a Glance*, <http://www.imf.org/external/np/exr/facts/glance.htm> (last visited Mar. 1, 2006).

106. SHAPIRO, *supra* note 7, at 16. “So long as the [mediator] exercises any independent influence over the outcome, he must demonstrate his independence of the party who achieves the more favorable outcome if he is to achieve the consent of the less favored.”

107. SHAPIRO, *supra* note 7, at 6.

the wider membership.¹⁰⁸

VI. CONCLUSION

After World War II, the major economic powers formulated a new “international economic order” that allocated voting rights in the new order according to the size of states’ economies. In so doing, they effectively adopted a “big man” theory of conflict resolution for economic matters. This mode of organization, with the implicit veto power that it grants to various states and the incentives it creates for the big man to prevent decentralization of his authority, has frustrated the creation of an independent body or process to coordinate the sovereign default process.

Added to this impediment are factors stemming from the somewhat unique nature, relative to most treaties, of sovereign debt agreements. The debtor state receives the benefit immediately, while the burden falls on future governments or generations. Conversely, at the start date of an independent body or process to equitably and efficiently coordinate sovereign bankruptcies and provide fresh starts, the burden would fall on existing creditors, with only future creditors likely to benefit on balance from improved efficiency and coordination. These differences between the present and the future create conflicts of interest between state representatives and the long-term interests of the people and territory that they represent. In addition, both creditor and debtor state representatives suffer from perverse incentives created by a degree of corruption, in the form of odious and tied debts, which characterize the *status quo*. Because the state representatives, or powerful constituencies to whom they are beholden, benefit from such corruption, creditor and debtor state representatives are again conflicted when it comes to the question of creating an institution that would eliminate it.

As a result, the current self-declared political authority for international economic matters, institutionalized in the Bretton Woods bodies, has avoided the emergence of a sovereign bankruptcy court. It has employed three of the four tactics as listed by Shapiro that centralized political authorities use in various mixes to respond to courts that make laws that run counter to the centralized authority’s interests:

First, they can yield and in the process become more decentralized. Second, they can systematically withdraw from the legally defined competence of the judiciary all matters of political interest to themselves. Third, they may intervene at will to pull particular cases out of the courts and into their own hands. Fourth, they can create systems of judicial recruitment, training, organization, and promotion that ensure that the judge will be relatively neutral as between two purely private parties but will be the absolutely faithful servant of the regime on all legal matters

108. Mark Turner, *US Calls Urgent UN Meeting Amid Concern Over Reforms*, FINANCIAL TIMES, Nov. 17, 2005, at 11.

touching its interests.¹⁰⁹

Here, the centralized political authority has pro-actively employed the second tactic by preventing the creation of a sovereign bankruptcy court in the first place. We also see tactics three and four at work (to the extent that the workings of those institutions can be said to be quasi-judicial or systematic). Iraq's debt, for example, was not forgiven pursuant to the HIPC process, but by informal negotiations conducted outside the institution. And to the extent that IMF and World Bank staff occasionally exercise quasi-judicial independence in their assessments and decisions, that independence is tethered by the voting mechanisms of the institutions.

Recall, for example, Anne Krueger's recent unsuccessful multi-year campaign to establish an SDRM within the IMF. Her failed attempt demonstrates once and for all that the non-emergence of a sovereign bankruptcy court in the last half-century has not been an oversight. Instead, this failure has been, as Jeffrey Sachs puts it, a charade,¹¹⁰ a deliberate choice that has its roots in: (i) history; (ii) issues unique to sovereign debt; and (iii) the choices the "community" made in structuring itself. Problems (i) and (ii) could have been overcome, as Krueger's near-success demonstrates. But in the end, problem (iii), the voting structure that the "community" chose in organizing itself, has been intractable.

The community can only make rational choices regarding modes of conflict resolution if it organizes itself in a way that motivates rational choices. In a community that has adopted the big-man theory, no matter how attractive independent conflict resolution might be for a given class of disputes, the big man will be loath to start down the slippery slope of allowing his position to be diluted. Avoiding the creation of IC&Ts preserves the big man's freedom to maneuver. A system that relies on *ad hoc* mechanisms for dealing with issues arising from sovereign debt preserves the power of the big man.

109. SHAPIRO, *supra* note 7, at 32.

110. Speaking on the eve of a summit of the heads of state of the African Union on July 5, 2004, economist Jeffrey Sachs, special economic adviser to UN Secretary General Kofi Annan, said: "The time has come to end this charade. The debts are unaffordable. If they won't cancel the debts I would suggest obstruction; you do it yourselves." *Economist Advises on African Debt*, ASSOCIATED PRESS, July 5, 2004.