Recent Trends and Debates on the International Financial System

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1. Introduction

The East Asian crisis has triggered a massive literature – both theoretical and empirical -- on the need for a new international financial architecture. A paper by Akyuz (2000) listed the elements of the required changes in the international financial system: a) improved standards and transparency; b) sound financial regulation and supervision; c) more flexible exchange rate regimes; d) improved surveillance of national policies; e) management and regulation of the capital account; f) provision of international liquidity without eroding confidence; g) orderly debt workouts during liquidity and insolvency crises.

The theoretical and empirical bases for the above elements can be categorized into two: a) inadequacies and wrong policies in countries affected by financial crises; and b) inadequacies and systemic risks inherent in the world financial system. The first set of factors view financial crises as being caused by the countries themselves, and therefore requires strong changes in the policies and institutions of these debtor countries. These factors include: 1) a mistaken fixed exchange rate regime, 2) moral hazard problems involving 'over-borrowing' by debtor countries arising from implicit guarantees for their debts, 3) lack of sound financial regulation and supervision, 4) lack of transparency and accountability, corruption and 'crony capitalism'. These factors would require the first four elements mentioned in the Akyuz (2000) paper.

The second set of factors relate to systemic risks and inadequacies in the world financial markets that require interventions or new international arrangements. These include: 1) herding, 'panic' and self-fulfilling behavior, 2) contagion effects, 3) multiple equilibrium problems resulting in liquidity problems becoming insolvency crises. These factors require state interventions and new arrangements in the international financial markets comprising the last three elements listed in Akyuz (2000) paper.

Six years after the crisis, much have been done in the realm of the first four elements through country stabilization and structural adjustment programs for the International Monetary Fund (IMF) and the World Bank (WB). What have been clearly inadequate are the improvements and changes in the global financial arrangements that would tackle the systemic risks and international financial market inadequacies. Thus, financial crises in the developing world continue unabated as can be seen in the recent crises in Turkey, Argentina and Moldavia.

The clear reason for the current scenario was the Bretton Woods Institutions' (BWIs) penchant to concentrate on the country's inadequacies and mistakes, and the need for proper punishment in the tradition of the time inconsistency problem in the rational expectations literature of macroeconomic theory.

But, recently, the IMF had been singing a different tune. In the past two years, it has been designing a Sovereign Debt Restructuring Mechanism (SDRM), and, more recently,

[1] I am indebted to Jurgen Kaiser for providing me many materials (including his own papers) for this research. All mistakes are my own.

following up on the G-10's call for collective action clauses (CAC) in sovereign debt bonds. Finally in March 2003, the logical underpinnings of these initiatives were laid bare. In a paper by Prasad, Rogoff, Wei and Kose (2003), the IMF acknowledged that: 1) there is no evidence that financial and capital account liberalization leads developing countries to higher economic growth and development, 2) there is some evidence that financial and capital account liberalization leads to more volatility in consumption in developing countries. They, however, go on to talk about other important factors that determine the outcome – mainly governance and institutions, a sort of hedging in case they have to revert to blaming domestic country factors for the undesired results. More direct were the official statements of IMF First Deputy Managing Director Anne Krueger (2003) in an address to the Harvard University Business School's Finance Club. After stating that: "Stronger economic and financial policies have been combined with improving the environment for private sector decision taking in ways that should facilitate the assessment and management of risk….[and] allowing countries to reap the potential gains from globalization, while minimizing the likelihood, and potential severity, of crises," she makes a strong about-face: "*But we must recognize that despite best efforts at prevention, crises will occur.*" This is the clearest statement by an IMF official supporting the systemic risk arguments on the causes of financial crises. Of course Kreuger made this statement because she was promoting the SDRM process being pushed by the IMF.

After being severely criticized by private international creditors, the SDRM of the IMF was shot down by the US and by some emerging market countries themselves during the Spring Meeting of the BWIs in April 2003.[2] What remains is the dubious call for collective action clauses, which have very limited possibilities, as we shall see.

In another front, attempts to provide alternative sources of liquidity funds during crises of confidence were given some glimmer of hope when the US-rejected Japanese proposal for an Asian Monetary Fund during the Asian crisis seemed initially poised in 2001 to make a possible comeback with the currency swap arrangements in the East Asian region (ASEAN plus 3 – ASEAN countries plus Japan, China and South Korea). The initiative, however, was dealt a serious blow when differences erupted between Japan, which wanted IMF involvement and conditionality in the swap arrangements, and Malaysia, which vehemently objected to this. Lately, however, Thai Prime Minister Thaksin was able to convince the 18 members of the Asia Cooperation Dialogue in June 2003 to set up a regional $ 1 Asian Bond Fund and proceed with the development of an Asian Bond Market that would pave the way for a regional bond market that utilizes surplus capital for development and staving off crises in the region.

The above two cases demonstrate how difficult it is to effect a change in the international financial architecture in the current setting, but that there are existing attempts and moves to try to address the problems.

This paper discusses the latest trends, debates and issues involved in the latest initiatives and proposals on debt workouts: codes of good conduct (CGC), collective action clauses (CAC) and country insolvency proposals. It concludes that the potential for their success is very unlikely without very bold and innovative moves. This is especially true given the current failures in institutionalizing debt workout arrangements and without adequate initiatives in the provision of liquidity funds (sans confidence-damaging and recessionary

[2] Commercial creditors also oppose the SDRM initiative. The SDRM was not the only victim of the Spring 2003 Meeting of the BWIs. The International Financial Facility (IFF), proposed by Chancellor of Exchequer of the United Kingdom (Mr. Gordon Brown), which aimed to increase official development assistance by donor countries, was also shot down by the United States.

conditionalities) and without strong initiatives to concretize and make explicit sovereigns' rights to institute capital controls.

2. Debt Workouts

When debt workouts, debt standstill agreements and debt rollovers were proposed as a result of the East Asian crisis, one main concern was to prevent a liquidity problem degenerating into an insolvency crisis (see Akyuz (2000)). A temporary standstill on debt servicing was needed to stop accelerated payments demanded by creditors and "an asset-grab race" during crises of confidence and liquidity. Debt rollovers and liquidity funds (sans the traditional IMF-type of conditionalities) would directly address the liquidity problem, and debt workouts and restructuring would complement the debt standstill arrangement and restore confidence to the system, and ensure that the required new money would go to social insurance, development financing and fiscal stimulus so direly needed during crises of confidence. This was part and parcel of the call to correct the current pro-cyclical policies that reinforce and aggravate recessions during periods of crises of confidence towards a counter-cyclical one that provides funds and economic stimuli during periods of illiquidity and low confidence.

In Sept. 1998, when the East Asian crisis was still going on, Canada proposed an Emergency Standstill Clause to be mandated by IMF members and to be invoked during times of liquidity crises. Akyuz (2000) also invoked Chapter 11 of the US Bankruptcy Code in the context of a liquidity rather than insolvency problem since it was "designed primarily to address financial restructuring rather than liquidation." In the current moves by the IMF for SDRM and CACs, this objective is not so clear. The documents state that the initiative was to deal with 'unsustainable debt', which may be interpreted as closer to insolvency and an ex-post situation when the country is already in deep financial crisis as a result of currency runs and losses of confidence.

The fact that the IMF had refused then to take responsibility for calling an emergency standstill, and instead had left it to the difficult process of negotiation between creditors and debtor (outside IMF-programs), is indicative of the difficulties in designing international financial arrangements in favor of developing countries, as opposed to the current trend of favoring powerful international creditors.

A second important difference between the earlier vision of debt workouts and the ones being proposed today by the IMF and by the developed countries is the fact that the earlier call had the obvious point of view of saving a country from financial and economic distress. The current initiatives by the IMF and the developed countries (G-7 or G-10) on SDRM and/or CACs center on collective action problems among creditors and focus much on creditors' rights. This is indicative of the power balance in the current initiatives. The current plans for SDRM, CACs and voluntary codes of good conduct (CGCs) depend critically on the acquiescence and agreement of the majority of creditors. One can therefore infer the outcome of such initiatives. In order for these initiatives to benefit debtor countries, there has to be an implicit assumption that there is a common objective function for the debtor and the creditors in aggregate, so that the problem is to rein in the 'rogue' or 'vulture' creditors. This may be true if everybody maintains a medium and long run view where the creditors as a whole would benefit if the debtor country doesn't become insolvent.

Another variant of the collective action problem is that, left on their own, each creditor will opt for holding out against debt restructuring, which, if collectively done, may result in the country defaulting and unable to pay all its debts, to the detriment of all creditors. Thus the common good of the creditors may be to undertake and cooperate in debt restructuring.

But the literature of 'herd mentality', 'self-fulfilling prophecy' and the revival of Chapter 12 of Keynes' classic book all point to the shift in objective function during uncertain and pessimistic periods. The objective of the creditors and investors during crises of confidence would be to 'get out as fast as you can with as much as you can.' The collective action problem here is not getting a big majority of creditors to tame the few 'rogue' creditors, or getting the majority to decide among themselves to go against their gut-feeling of 'jumping ship'. The problem is how to institute some arm-twisting and *involuntary* mechanisms to force a standstill and an agreement. This of course is possible only: 1) if the debtor country has sufficient power to force a standstill and debt workout, 2) if some powerful third party force a standstill and debt workout, 3) if there are institutional mechanisms and arrangements that call for automatic standstill or debt rollovers or debt workouts during exceptional circumstances defined clearly. This is part of the real change in the international financial architecture that is needed as a result of the numerous financial crises in the past.

In the most successful debt workout during the Asian crisis, the South Korean government strongly and aggressively ordered the chaebols and their creditors in early 1998 (just a couple of months after it was hit by a financial crisis) to undertake a debt workout arrangement, called the Restructuring Accord. The scheme, done outside the IMF program and hailed as one of the reasons for Korea's early recovery from the crisis, worked partly because of the following components:

a) For each chaebol restructuring, a 'lead bank' – the one most exposed to the chaebol -- took charge of the Council of Creditor Financial Institutions tasked with negotiating with the chaebol in its financial restructuring. The 'lead bank' of course had the biggest stake and highest desire to keep the company solvent and performing.
b) A Corporate Restructuring Coordinating Committee whose members were designated by the major banks arbitrated differences among chaebol creditors and provided technical support.
c) The Accord imposed a freeze on all creditor enforcement action as soon as the Creditor Council was formed.

The Accord also succeeded because the major creditors were local Korean banks and so the government was able to exert influence on both creditors and debtors. South Korea was fortunate that the chaebols during the crisis owed around $500 billion to the Korean banking sector and only $25 billion to foreign banks and bond creditors. This was unlike the case of Thailand and Indonesia. In this respect, the Korean experience is a case against complete financial and capital account liberalization. The foreign creditors were also held at bay by pressures from the US Treasury. Thus the first two elements of debtor country strength and third party intervention were present in the Korean debt accord.

Most countries do not have the strength and clout of the South Korean government and do not hold strong sway over the United States. Many countries also are more exposed to foreign creditors. Thus, successful workout arrangements would critically depend on having pre-crisis international arrangements on debt standstills and debt rollovers.

It is in this context that we review the current initiatives in the areas of CGC, CAC and SDRM.

2.1 CGC, CAC and SDRM

The various complementary elements required for debt workouts from the IMF perspective consist of: 1) a voluntary code of good conduct (CGC) agreement between the debtors and creditors on matters concerning sovereign debts; 2) collective action clauses (CAC) in sovereign bonds that give statutory and legal international framework for the CGC to be carried out: The CAC would enable the creditors of that sovereign bond, through a pre-determined level of majority vote among them, to effect a debt standstill and debt restructuring agreement with the debtor country for during exceptional circumstances. However, most sovereign bonds in the past and present, as well as most foreign bank lending, do not have CACs. Thus, there is a need to *aggregate* external debts of a country and create a mechanism of arbitration between the country debtor and the bulk of its overall creditors -- and among the creditors themselves -- that will deal with the country's external debts comprehensively. This would be: 3) the comprehensive debt restructuring framework, which is the IMF's SDRM.

2.2 Codes of Good Conduct (CGCs)

The most interesting CGC that has come out from conventional sources is that from the Banque de France. It is much closer to the original intent of the debt workout proposals based on the East Asian crisis, and a lot more reasonable from the perspective of debtor nations than the CGCs coming from the Institute of International Finance (IIF) and other international financial associations, which concentrate on strong conditionalities, transparency of the sovereign country, information access and creditors' rights and very little and very nebulous creditors' obligations and responsibilities (see EMCA, IIF et al (2003))[3].

Jubilee 2000 views the Banque de France CGC proposal positively (Kaiser (2003a)). The positive aspects of the proposal are examined, but the enormous limitations and obstacles to the adoption of the proposal point to the inherent problem of relying on voluntary mechanisms and hoping for 'good faith' among commercial creditors to internalize the concerns of debtor countries.

The Banque de France proposal includes the following codes of good conduct, lifted from their document (Banque de France (2003)):

- ***"An early engagement with creditors*** before and when debt-servicing problems arise, whatever their nature.
- ***A fair information sharing*** among all interested parties. The CGC should specify which information is to be provided to stakeholders for them to make an informed assessment of the debtor's financial condition.

[3] Roubini and Setser (2003) had said that the proposed code of conduct of the international private financial players (EMCA, IIF et al (2003)) is "long on requirements for the debtor and short on credible commitments by creditors. In effect, it is a very extensive code of debtor conduct to be enforced by IMF conditionality."

- ***A fair representation of creditors***. The organisation of this representation should be based as much as possible on existing or agreed modalities, such as those included in Collective Action Clauses (e.g. majority clauses).
- ***An expeditious and cooperative process***, possibly resorting to instruments and techniques aimed at accelerating the renegotiation process and at discouraging "holdout creditors" (e.g. a voluntary stay on litigation).
- ***A comparable treatment among creditors***. This implies agreeing on the scope of the debt to be renegotiated and on specific voting procedures to be used across a large range of situations.
- ***Fair burden sharing*** between the debtor and its creditors.
- ***Negotiating in good faith*** from all participants. Procedures will be defined ex-ante to achieve this aim (e.g. mediator or arbitrator, etc.).
- ***The debtor's financial situation should be preserved***. A number of avenues could be explored (concerted rollover; status of new money; concerted standstill, etc.).
- ***Restoring, as soon as possible, debt sustainability*** should be the ultimate objective of debt re-negotiation. The IMF program and its debt sustainability analysis will provide the various parties involved with the background information to work out a sustainable solution."

"The Code of Good Conduct is intended to address a whole range of debt re-negotiation situations. Three illustrative scenarios are presented in the paper:

- In a first scenario ("**alleviating tensions on a sustainable debt")** characterised by a sustainable debt over the medium-term, a country faces short-term financial tensions and there are increasing expectations that the situation could deteriorate further. In order to prevent an unsustainable debt dynamic from developing, pro-active debt management or debt re-negotiation might be contemplated by the debtor. In this context, creditors and debtors could usefully implement several principles of the CGC.

- In a second scenario ("**re-negotiating unsustainable debts, while "remaining current")** characterised by an unsustainable debt, the debtor triggers a debt re-negotiation process, while still being able to service debt payments. An IMF program aiming at restoring debt sustainability over the medium term is designed. The principles and best practices of the CGC are expected to provide a comprehensive framework which would allow debtor and creditors to renegotiate expeditiously new terms and conditions, before the situation of the debtor deteriorates further.

- In a third scenario ("**renegotiating unsustainable debt under a payment standstill")** characterised by an unsustainable debt and temporary payments standstill, the main objective of the CGC is to reduce the risk of a non-cooperative debt restructuring process. Its implementation aims at ensuring debtor's good faith and a fair burden sharing among participants. The combination of an IMF adjustment program and lending into arrears is to be used as a critical instrument to reduce the severity of the crisis and ensure a fair implementation of the CGC, including the good faith criterion."

"Three categories of stakeholders should be involved in the design of the CGC:

- Representatives from the different categories of public and private creditors as well as other market participants or rating agencies;
- Sovereign issuers, notably emerging markets;
- The IMF which should act as a catalyst in designing the CGC, in coordination with other relevant organisations (e.g. the World Bank, BIS, FSF, etc.). "

Kaiser (2003a) gives us the positive elements of the Banque de France proposal or what he calls the Trichet[4] proposal:

- "The proposal acknowledges *that the borderline between debt sustainability and debt unsustainability is all but clear.* It does not build on pre-defined criteria and definitions, but foresees a high degree of flexibility, which would allow negotiators to tailor a solution to the particular needs of the debtor country.
- The CGC would also mandate a comprehensive solution, including all pre-cut-off-date debt. It is interesting to note that no reference is made to any preferred creditor status of any individual creditor or group of creditors.
- The principle to restore debt sustainability as soon as possible implies that *the creditors accept the principle that an agreement that would not restore debt sustainability is not viable and therefore that the net present value of their asset cannot be guaranteed. (p.11)* This seems to indicate some readiness to turn away from the eternal "too little, too late reschedulings" of the Paris Club – even if the basic prerequisite for a realistic assessment of what debt sustainability actually is – namely the independence of the one who assesses – is not considered. To make sure that … the most stubborn bondholder will understand the signs of the time, Trichet states explicitly: *Similarly, creditors should recognise that the debt restructuring might require a writing down of their claims. (p.10)*
- Under "negotiation in good faith" Trichet is the first creditor to acknowledge the overwhelming importance of neutral decision making, when under "best practices" he suggests: *To prevent mutual suspicion, a third party could be designated to act as a mediator or an arbitrator (p.10).*"

It is clear that the Banque de France CGC has the concern of the debtor countries in mind when it wants to quickly *avert* debt unsustainability (with 'an early engagement'). It also points to the involvement of debtor countries as critical for the process. The three scenarios obviously include the situation where liquidity problems might degenerate into insolvency crises (the first two scenarios) and contrasts sharply with the financial players' concern of restructuring already unsustainable debts.

Kaiser (2003a) states that the Banque de France position mirrors the position of some other central banks in Europe. In this regard, the proposal may have some influence on creditors from these countries, if the central banks use some pressure and persuasion on the private financial institutions in their countries and on their own government. However, a critical country – the United States – has consistently taken the side of the private creditors in resisting sovereign debt restructuring or debt reduction on the grounds of moral hazard and creditors' rights (as what had happened in its rejection of the IMF's SDRM). Most likely, other countries (such as Japan) will follow the US behavior. Thus, for the adoption of the CGC, debtor countries would have to unite – together with the friendly European countries and their central banks – to pressure the creditors to agree to the CGC by threat of undertaking loan transactions only with complying creditors. We shall discuss this in the last section of the paper. The major flaw therefore of the Banque de France is in hoping that the private creditors will voluntarily adopt the CGC, or in hoping that selected European central banks or governments can convince the formidable

[4] Jean-Claude Trichet was the Governor of the Banque de France when the proposal was made. He is now head of the European Central Bank.

coalition of the US, Japan and private creditors in giving in to the more lenient terms in the CGC for the debtor countries.

The Banque de France proposal also correctly predicts that the CGC will work only if complemented by Paris Club debt agreements and liquidity flows from the IMF, given that these are the only major institutions providing official debt restructuring and emergency liquidity funds, respectively. Again a basic flaw here is that, given that the CGC is largely aimed at confidence-building during crises of liquidity and confidence, the role of Paris Club members and the IMF in imposing stringent conditionality of fiscal and monetary austerity, high interest rates and blanket bank and firm closures – all proven to have aggravated the economic and financial crises and deepened economic uncertainties in various countries -- should be addressed, if confidence-building is to fully succeed.

2.3 Collective Action Clauses (CACs)

The voluntary CGC, if generally agreed upon, needs statutory mechanisms to be realized. If the Banque de France proposal, or another acceptable CGC, was generally adopted, the code could be explicitly enshrined in the sovereign bond contracts with the exceptional circumstances defined carefully. However, since there is no consensus yet on a CGC, and no strong desire for creditors to legally bind themselves to a strong CGC that might dilute their 'creditors' rights', the furthest the private creditors are willing to go (see IIF website) would be to allow collective action clauses in sovereign bond contracts.

These CACs would allow, through a pre-determined level of majority and representation of creditors to call for: 1) Majority restructuring clauses: a qualified majority can bind all creditors of the sovereign bond issue to the financial terms of a financial restructuring of the sovereign debt; 2) Majority enforcement clauses: limitations on enforcing accelerated claims of particular creditors by requiring: a) a vote by a minimum percentage of creditors to be able to accelerate their claims during debt workouts, and b) a pre-specified majority can reverse such acceleration; 3) Exit consents: This allows bondholders to agree to amend, through a pre-determined majority creditors' vote, changes in non-payment terms of the bonds from which they are exiting and impairs the bonds left in the hands of holdouts.

Most bonds carry the less important second component of limiting accelerated claims by certain creditors during defaults or debt standstills. This is standard practice with the usual sovereign bonds governed by either New York or English law. Most sovereign bonds do not have the first and more important component of the CAC since most bonds are being governed by New York law, which does not carry these clauses, while the less frequent ones being governed by English law do have. The New York law, however, usually does contain exit consent clauses.

Last March 2003, Mexico was able to issue, for the first time, a $1 billion bond issue under the New York law with CACs comprising both majority restructuring and majority enforcement provisions. This followed a G-10 Working Group report recommending CACs in sovereign bonds in September 2002, and an IIF (and financial industry) draft CAC proposal issued in February 2003. Table 1 reproduces a table from the IMF (2003) paper on CAC, summarizing the differences in provisions under English law, New York law, G-10 recommendations, financial industry proposal and the recent Mexican bond issue. An analysis of the table reveals the following points:

1) The financial industry draft requires an unreasonable 90% of creditor consent (based on outstanding principal, and not based on votes in a duly constituted meeting) for financial restructuring and debt standstill. This is because it requires 85% vote for changes to terms of payment, but any opposing camp comprising more than 10% of the outstanding principal would have veto power. This means that at least 90% of the creditors should agree with the changes in the terms of payment. As the IMF paper correctly states, this defeats the purpose of CACs. This 10% veto power of a small minority also allows 'vulture' creditors to demand repayments and destroy constructive debt workouts. What is clear is that the IIF and financial industry members are reluctant to have quick and timely standstill and debt restructuring agreements with the debtor country. Their required 75% of creditors' vote to reverse an acceleration of particular creditors' claims during default also points to their preference for less restrictions on individual creditor's behavior. The IIF's interpretation of 'vote' is based on outstanding principal, rather than the English law practice of votes cast at a duly convened meeting.

2) The IIF draft of requiring the debtor country to provide information requested by 5% of creditors also puts too much restriction (not currently existing) on the debtor country. The debtor country can be sued if it cannot provide information demanded by the 5% of creditors, especially information that it is legally bound to keep in confidentiality or information that is hard to get. The country has to prove in a foreign court that the information requested is 'unreasonable'. Furthermore, non-compliance would mean technically a default for the debtor country and a crisis of confidence may be triggered.

3) The closest thing to arbitration being proposed in the CAC process is the 'engagement' provision. The G-10 proposal recommends the adoption of the English law practice of establishing a trust structure where the trustee can act as bondholder representative for the life of the bond. The G-10 proposal also alternatively recommends a two-third majority vote to appoint at any time a representative for the bondholders in negotiation with the issuer (the debtor country) or other creditors. The engagement provision is also seen as a deterrent to litigations after a default and during a restructuring process. The G-10 proposal implies a bondholder committee (with representatives from each bond issue) that cuts across different broad issues to negotiate with the issuer and individual or groups of creditors. Thus the G-10 proposal has some sort of aggregation, which is discussed later.

   The industry draft rejects a trust structure and instead allows a simple majority of creditors to form a bondholder committee – one for each bond issue. The industry members do not believe in the aggregation of representatives into one bondholder representative committee (for all the bonds) to negotiate with the debtor country after default and restructuring. Representatives of the individual committees are voted by a simple majority of creditors, but 25% of creditors would have veto power. Furthermore the debtor country will pay all legal, financial, administrative and other fees and expenses of the committee of the particular bond issue. This complicated provision is simply a roundabout way of rejecting an arbitration and negotiating process which may dilute individual creditor's rights.

   All other proposals, including the latest Mexican bond, do not have engagement provisions.

4) The documents of CAC, especially the IMF and IIF drafts, refer to the CAC process as a response to a post-default restructuring process. There is no clear indication to trying to avert debt unsustainability or reducing the dangers of insolvency crises.

5) The industry draft frowns on *exit consents* – changes in non-payment terms that effectively dilutes creditors' rights of the holdouts. The industry draft would require unanimous approval for any *exit consents* that deprives creditors of important enforcement rights (e.g. waiver of sovereign immunity and change in governing law).

One problem with CACs is that since the majority of past and current sovereign bonds do not have CACs, even if all new bonds would start to include these clauses, it will take more than ten years for sufficient aggregation of bonds that would allow debt standstills and restructuring during crises. Plans to convert the past and existing non-CAC bonds to CAC bonds (e.g. the J.P. Morgan Proposal) are not feasible (see Kreuger (2003)). Convincing creditors to accept the more reasonable G-10 version of CAC for new bond issues is already extremely difficult enough that one cannot imagine them allowing all existing non-CAC bonds to be converted to ones with the proper CACs.

Successful aggregation or exchange of bonds into other types of bonds that allow restructuring, or successful use of exit consents in debt restructuring so far is limited to small countries (Ecuador, Uruguay, Moldova) with relatively small debts vis-à-vis other countries, and only after some period of negotiation once extreme debt unsustainability is evident. It is obvious that international creditors will not allow such ease for larger sovereign debtors (e.g. Argentina, Brazil, Russia, Indonesia, Pakistan).

But the more inherent problem of CAC is that its premise of collective action problem among creditors and a conflict between the common interest of creditors in the aggregate and debtor countries, on one hand, and rogue or holdout creditors on the other, is fundamentally erroneous. Thus even if aggregation is achieved, creditors in the aggregate, during periods of crises of confidence and liquidity, hold short-run perspectives and want quick exits, accelerated payments, stoppage of debt rollovers and minimum exposure to the country or countries at risk. The industry resistance to diluting creditors' rights during these crises periods, which we had just analyzed, further confirms this behavior. Their interest in the aggregate usually clashes with the interest of debtor countries during crises. The latter aims to minimize capital flight, maintain liquidity and provide funds for counter-cyclical, social insurance and development needs during the difficult and risky periods. One does not effect internalization of the objective function of debtor countries by solidifying the ranks of the creditors. On the contrary, one needs to solidify the ranks of the debtor countries so that they can negotiate with some clout during these difficult times.

Thus the empirical results speak for themselves. Significant debt restructuring is allowed only to very small countries, those who are obviously unable to pay their sovereign debts. But larger and more populous countries, with larger debts, are only given debt rescheduling, not allowed sufficient aggregation of bonds, and not given significant debt relief and debt reduction, even if it is obvious that their debts are unsustainable in the medium and long run.

2.4 The Sovereign Debt Restructuring Mechanism (SDRM)

2.4.1 The IMF SDRM Proposal

The benchmark of the SDRM and any insolvency arrangement proposal would naturally be the IMF proposal. The scheme is sketched below (summarized from IMF (2003c)):

I. Eligible claims would be claims by creditors included in the SDRM *except*:
   1. claims governed by domestic law and the domestic courts,
   2. claims that are secured or collateralized,
   3. claims held by international and multilateral organizations.

   A related problem is whether to include official bilateral creditors' debts in the restructuring, which the IMF proposal doesn't resolve. If they are included, the IMF proposed that they be placed in a separate class from commercial creditors. The two classes of creditors will receive different terms but approval by the required majority in both groups would be needed to legitimize the restructuring agreement.

II. A debtor member country of the IMF can activate the SDRM by claiming that its debt was unsustainable. A key question the IMF leaves unresolved is whether independent confirmation is required on the accuracy of this claim, and which entity would investigate and decide on this. There is a strong implicit assumption that the IMF will be strongly involved in this confirmation and verification process.

   The debtor will be required to provide relevant information regarding its indebtedness, including claims not to be restructured under the SDRM. Registration and verification of claims of indebtedness takes place and the Sovereign Debt Dispute Resolution Forum (SDDRF) resolves disputes arising from this verification process.

   Activation would not automatically suspend creditors' rights, including those holding out on the restructuring. However, to prevent 'rogue creditor' behavior, the amounts recovered by these creditors through litigation "would be deducted from its residual claim…in a manner that neutralizes any benefits of such litigation vis-à-vis other creditors." The IMF proposal also opens the option, upon approval of the majority of creditors (those subject to the restructuring), for the SDDRF to "enjoin specific enforcement actions in circumstances where such enforcement could undermine the restructuring process."

III. To encourage early participation of creditors in restructuring processes, a representative creditors' committee would be created to address problems and disagreements between debtor and creditors, and among creditors. Disputes on the representation of the committee would again be resolved by the SDDRF. The debtor country would bear the costs associated with the operation of the committee. Disputes concerning these costs would also be arbitrated by the SDDRF.

IV. Creditor approval of restructuring or priority financing proposals would require 75% of the outstanding principal of the registered and verified claims.

Alternatively an unspecified majority vote of the creditors can terminate the SDRM after the verification process.

The restructuring or priority financing agreement, once approved and passed with votes certified by the SDDRF, becomes binding on all registered creditors and creditors notified about the restructuring of their debts but failed to register.

False information, non-transparency, non-cooperation or inappropriate use of SDRM by the sovereign debtor will be punished under the Articles of Agreement of the IMF, including access to financial lending and lending into arrears (LIA).

V. The SDRM would end with the certification of the restructuring agreement by the SDDRF. As mentioned earlier, an unspecified majority of creditors can vote to end the SDRM on the grounds that activation of the SDRM was not justified. Alternatively, the sovereign can at any time terminate the SDRM, although unspecified disincentives should be imposed to prevent abuse of the mechanism. The SDDRF also can terminate the proceedings without a restructuring agreement on an unspecified basis of determination of lack of reasonable prospect for a restructuring agreement.

VI. The selection of the members of SDDRF would follow the following process:

i. The Managing Director of the IMF, upon advice by professional associations and other international organizations, designate a selection panel with 7 to 11 members.
ii. The selection panel identifies 12 to 16 candidates to form the members of a pool of judges. The nomination process would be an open one.
iii. Once selected by the panel, the pool of judges is approved by the Board of Governors. A President of the SDDRF will be selected.
iv. When the SDRM is activated, four judges from the pool would be impaneled by the President of the SDDRF. One would be responsible for making initial determinations. The remaining three would constitute an appeals panel.

The powers of the SDDRF would have no authority to challenge decisions of the Executive Board or make determinations on issues relating to the sustainability of the sovereign's debt.

The functions of the SDDRF are:

i. notification of creditors, registration of claims and administration of the voting process
ii. resolving disputes due to: i) claims verification, ii) the voting process and disqualification of certain creditors, iii) the representation and operations in the creditors' committee. The SDDRF will be *reactive*: it cannot initiate investigations regarding potential abuses but will merely adjudicate allegations of abuse brought by a party. It can request evidence but has no subpoena powers
iii. if need be, issuance of an order that would require a court outside the sovereign's territory to stay specific enforcement actions based on debtor's and creditors' approval.

VII. The SDRM and SDDRF can be established with an amendment of the IMF's Articles, which requires acceptance by three-fifths of the members with 85% voting power. Since the amendment will involve establishing new treaty obligations, most countries will need legislative authorization.

2.4.2 Critique of and Alternative Proposals to the IMF's SDRM

There are some positive points to the IMF initiative. The most important is the clear departure from old solutions to financial crises for developing countries which usually comprise liquidity funds in exchange for: 1) stabilization and austere policies that only deepen recession and the crisis of confidence, 2) financial reforms which may include counterproductive cures such as closure of banks and unrealistic privatization of banks during illiquid and confidence-less periods, 3) debt reschedulings and restructuring with the Paris Club members that usually come 'too little, too late', and tied to the stabilization conditionality. The move is closer to (but still far from) what has been termed 'a new international financial architecture', which implies an international arrangement to solving crises, rather than country-specific, and oftentimes, country-punishing solutions to financial and debt crises. The motivation is clearly a move from the first set of old factors blaming countries for financial crises (discussed in the beginning of the paper) to a more enlightened acceptance of 'market failures' and inherent systemic risks of the international financial markets. Kreuger (2003), in her address to the Harvard Business Club, clearly states that the object of SDRM is to *avert* debt unsustainability, and has in mind reducing the risks during liquidity and confidence crises.

Kaiser (2003d) lists the other positive points:

1. The protection of the debtor's sovereignty and its exclusive right to initiate the SDRM process;
2. The flexible-enough framework of the process with ad-hoc panels or committees;
3. An arbitration process where the sovereign debtor can dispute claims and demands of the creditors.

However, the IMF's SDRM proposal has been criticized by civil society organizations (CSOs) for being inadequate and weak. Some of the criticisms and alternative proposals are being posed by Kaiser (2002, 2003d), Pettifor and Raffer (2003) and Palley (2002, 2003) representing civil society groups (Erlassjahr, Jubilee Research, and Open Society Institute[5] respectively), and AFRODAD. Some of the alternative proposals for sovereign debt restructuring actually predate the IMF proposal (e.g. the proposal of Raffer (1990)). Their most serious criticisms, accompanied by their counter-proposals are:

1. The IMF roles in the proposed SDRM process, explicit in the selection of the arbitration panel members and implicit in determining debt sustainability of the sovereign debtor, are inappropriate given that the IMF itself is a creditor of the sovereign debtor and may not be an impartial stakeholder. The veto power of the IMF's Board of Governors on the arbitration panel composition is especially objectionable. Debt sustainability and the economic and social conditions of the country should be determined by an independent entity rather than the IMF. The CSOs would prefer that a more neutral body, such as the United Nations, take the lead in the selection of the arbitration panel.

[5] The Open Society Institute is associated with George Soros.

2. The power of the arbitration panel (the SDDRF) is too weak. Its role is only to try to settle disagreements on procedural and claims issues, but the final decisions for restructuring and standstill still need the consent of the majority of the creditors. The CSOs prefer a more courtroom situation, where the debtor and the creditors present their sides, and a neutral pool of judges will decide the final outcome.
3. Related to the above is the CSOs' preference to follow the US Chapter 9 Bankruptcy Law for municipalities and local governments rather than Chapter 11 for corporations. The Chapter 9 clauses allow relevant stakeholders (e.g. taxpayers, social service recipients) affected by debt payments and debt restructuring to be heard and to affect the final outcome. One important offshoot of this proposal is that 'odious' or 'illegal' debts made by corrupt, illegitimate or tyrannical regimes may be questioned by relevant stakeholders and their repayment presented for repudiation.
4. The SDRM process of the IMF is ambivalent about covering official bilateral debts and explicitly excludes multilateral debts. For a comprehensive treatment of the external debt, these elements should be included. The exception always given to multilateral loans is being questioned. Palley (2003) even suggests that including multilateral loans in the debt restructuring and standstill would tackle the moral hazard problem associated with IMF bailouts. Other critics (AFRODAD and Kaiser (2002)) even want to include domestic debt in the proceedings[6]. This is of course controversial. Although it is obvious that the domestic debt burden should be included in any debt sustainability analysis, including domestic debt in the coverage of the SDRM might adversely affect the immediate and day-to-day domestic borrowing capacity of the sovereign government, especially with respect to treasury bills and bonds. There are also different legal jurisdictions (international laws and domestic laws) that have to be resolved when both external and domestic debts are included in one debt restructuring.
5. It is obvious from the IMF concept of debt sustainability (see Kreuger (2002)) that benchmarks and targets of debt sustainability indicators, such as debt to GDP, debt to exports, and debt to government revenue ratios do not incorporate a rigorous assessment of the needed caps in debt service so that funds can be released to achieve the Millennium Development Goals (MDG) of halving poverty and accelerating social and human development in developing nations (see Kaiser (2003b)). One of the objectives, of course, for sovereign debt restructuring and for a 'new international financial architecture' is for developing countries to prioritize their expenditures from available foreign exchange and government revenues for development needs as well as human and social needs of the country, instead of the automatic prioritization of debt payments. This is exactly one of the main criticisms of the debt sustainability analysis (DSA) of the HIPC Initiative. Thus there is much room for coming up with a more MDG-oriented DSA and concept of debt sustainability that nets out from foreign exchange and government revenue bases the estimated financing needs for economic and social development.
6. The IMF's SDRM has been criticized also for being too concerned with creditors' rights. The consultation process is also criticized to have been more focused on creditors with very little consultations with sovereign debtors and civil society organizations (CSOs) – see Pettifor and Raffer (2003). Despite

[6] This is similar to criticisms of the HIPC Initiative, which does not include domestic debt in both the debt coverage and debt sustainability analysis.

the IMF's attempts to win over the creditors and financial industry players, the latter have rejected the SDRM process outright. Perhaps initiatives by the United Nations or the United Nations Development Group (UNDG) organizing debtor countries to consolidate a sovereign debt restructuring proposal – and consulting with creditors, CSOs and multilateral institutions – may yield better results.

2.4.3 Resistance of Creditors

It would also be interesting to find out the official and not-so-official reasons for the private creditors' rejection of the SDRM proposal of the IMF. A document prepared by the industry players, including IIF and Emerging Markets Trade Association (EMTA et al (2002)), lists their major official objections:

i. "The SDRM rests on the false premise that there is an inherent collective action problem among private sector creditors in sovereign debt restructuring that precludes agreement. In fact, not one restructuring has been prevented from moving ahead by the actions of holdout creditors…as evidenced by the spontaneous formation of bondholder committees in the cases of Argentina, Ecuador, Ivory Coast and Russia.

ii. Implementation of an SDRM would render collective action clauses meaningless by overriding, in advance, the clauses' intended operation with a statutory mechanism.

iii. Am SDRM and associated exchange controls that could affect international credit lines, create incentives that could themselves precipitate a crisis as creditors act defensively at the first sign of a problem and advance the rundown of short-term exposures and even accelerating long-term exposure.

iv. The analogy between an SDRM and private sector bankruptcy legislation is fundamentally flawed: private companies are subject to jurisdiction of the bankruptcy tribunal. Even under an SDRM the sovereign debtor would inherently not be subject to the appropriate checks and balances that legitimize and make a bankruptcy regime fair and defective.

v. The SDRM would force cases that may appear unsustainable, such as Brazil in 1999, toward long, costly, comprehensive restructurings, when informal, more surgical solutions might restore market access and growth at a much earlier stage. Paradoxically, the SDRM could shift more of a country's financing requirements to the official sector.

vi. Using debt sustainability as a trigger for the SDRM is fundamentally flawed. While the IMF has a useful role to play as an agent of adjustment, its role as de facto judge of debt sustainability presents major problems due to the acknowledged complexity of the task and the Fund's vested interest as a creditor.

vii. Despite its complex voting arrangements, the SDRM does not in fact resolve the problem of aggregation across different classes of debt, which is one of its principal goals. The private sector believes the issue of aggregation can be better – and more simply – addressed through greater transparency during the restructuring process.

viii. Capital markets are built on the fundamental principle of enforceability of contracts. By making 'structured' default – without the appropriate checks and balances such a regime normally includes – an alternative to policy adjustment, as SDRM represents a radical departure from this fundamental principle."

The first and last points are probably the most important and true reasons for the private sector objection to SDRM. It is clear that the private creditors do not feel there is a collective action problem and intervening in the capital market processes – reducing their individual creditors' rights -- will not be to their aggregate and collective interest. By the creditors' own behavior, the IMF's theoretical basis for SDRM is fundamentally flawed.

Kaiser (2003b) also reports that the Legal Department of the IMF thinks that the private creditors feared the IMF would use the SDRM as an instrument to withdraw from the large bail-out packages. This is very interesting since it brings the moral hazard focus of IMF rescue packages on bail-out of creditors rather than on the traditional complaint of bail-out of debtor countries (who, after all, will have to pay back the emergency loan funds at market interest rates).

3. What Next for a New International Financial Architecture?

3.1 Improving Debt Workout Mechanisms

Most emerging market countries were lukewarm or rejected outright the IMF's SDRM proposal. This springs clearly from their fear of being stigmatized as 'bankrupt' or 'insolvent', which will affect their short-run, medium-run and long-run access to credit lines. Kaiser (2003c) is correct, however, in pointing out that a good sovereign debt restructuring and debt workout arrangement should result in more, rather than less, debt sustainability for the sovereign debtor, and should improve their credit standing. But, because of the lack of country ownership of the SDRM proposal and lack of country consultation, most countries believe the financial industry players' threat that the arrangement will lead to more capital flight and less access to credits (the third and fifth arguments of the industry players' position listed previously). This fear is not unwarranted especially if the financial creditors are unified and the sovereign debtors are not. Credit agencies and domestic partners of the international financial players can cause crises of confidence (even if debt should be sustainable with the orderly workouts) by creating panic and self-fulfilling prophecies. The developing countries also do not have good arbitration experiences in the WTO-instigated arbitration of trade disputes. It is clear that sufficient bargaining and negotiating power of the sovereign debtors over the arrangements and their ownership of the proposal are key elements missing in the IMF SDRM proposal. For developing countries to clearly benefit from institutionalized debt workout arrangements, the following will have to be achieved:

1. Developing countries will have to be united in proposing: 1) a code of good conduct (CGC) for creditors and debtors; and 2) the process, content and circumstances of automatic debt standstills and workout arrangements, where the CGC is made statutory. The UN Development Group (UNDG) members, especially UNCTAD and UNDP, can facilitate this process. CSOs can also give technical, financial and lobbying support. There may be some differences in the financial needs and processes of low-income countries and LDCs (Least Developed Countries) compared to middle-income and emerging market countries. The main difference may be the fact that middle-income and emerging markets might have the advantage of getting more capital inflows, and the disadvantage of getting more volatilities and exposure to commercial creditors, which are usually more difficult to negotiate with during crisis situations. But the essential processes of debt standstills and debt restructuring with bilateral, multilateral and commercial creditors should be essentially similar. All in all, a common framework for a

voluntary code of good conduct and a statutory mechanism for automatic debt standstills and debt workouts during crises of liquidity or solvency (with interests of all types of developing countries accounted for) should be agreed upon among a significant number of developing countries. There may be different mechanisms and processes proposed depending whether the situation is a problem of temporary illiquidity, or real insolvency and unsustainable debt conditions. In the aftermath of the latest High Level General Assembly Dialogue on Financing for Development held in October 2003, the UN Department of Economic and Social Affairs had been tasked with coming up with viable proposals for sovereign debt restructuring.

2. Once a common framework and mechanism is proposed, the developing countries, together with allied international agencies (e.g. UNDG, concerned CSOs) should negotiate strongly and determinedly with the creditors and multilateral agencies. It should be made clear that, with sufficient unity among developing countries, boycotts of uncooperative creditors and preferential treatment of cooperative ones, will always be a very likely option for the sovereign debtors.

3. There has to be clear and strong acceptance of the procedures proposed from all stakeholders – particularly the commercial, official and multilateral creditors – to ensure that the debt workout arrangements will not be sabotaged by powerful financial players and big powerful countries.

The above will definitely take a while to achieve.

3.2 Other Vital Components of a New International Financial Architecture: Tackling the Systemic Risks During Financial Crises

But balancing the power play in debt standstill and workout arrangements is just part of the big gap in a new international financial architecture more conducive to the needs of developing nations. Debt standstill and workout arrangements, possibly long drawn, are not sufficient to stave off financial crises and currency runs or hasten the return to normalcy during financial crises.

Systemic risks related to capital flow movements, which lead to crises in confidence, financial malaise, and currency runs usually involve sudden changes in economic mood, from one of optimism to extreme pessimism to downright panic. A debt workout arrangement with a proper arbitration mechanism, even if properly and justly implemented, will take precious time. There will be negotiations, disagreements and arbitration among different types of creditors, and then negotiations and arbitration between creditors as a group and the sovereign debtor. Meanwhile, something has to be done to stop the deterioration in confidence and sudden rush for financial assets to leave the country.

Because the systemic risk associated with countries that have opened up their financial and capital accounts can be viewed in terms of 'market failure' and the absence of contingent markets as well as 'insurance' mechanisms during currency runs and capital reversals, two things are immediately necessary: 1) a mechanism to regulate the capital flows going in and out of the country; 2) the availability of international liquidity funds as sort of potential insurance against massive illiquidity arising from sudden financial outflows and stoppage of traditional credit lines.

3.3 International and Multilateral Acceptance of Capital Controls

As will be discussed more fully in other papers of the volume, the systemic risk associated with financial crises require capital controls, both during times of optimism and boom and during times of pessimism, currency runs, speculative attacks and stoppage of credit.[7] Although many countries have undertaken and are undertaking successful capital controls, usually quietly and without fanfare, it is required that capital controls be generally accepted by the powerful multilateral institutions and international financial markets as a standard practice and sovereign right of developing countries. This would allow all developing countries, large and small, powerful and not, to undertake regulation of capital flows without being stigmatized and punished by the multilateral institutions and global markets. The IMF paper by Rogoff et al acknowledging adverse effects of financial and capital account liberalization should provide the push for the Bretton Woods Institutions to reverse the (often forced) financial and capital account liberalization of many developing nations.

3.4 Availability of International Liquidity Funds Minus Stringent Conditionalities

As mentioned above, the availability of international liquidity funds acts as insurance during financial runs and crises and help reduce the systemic risk of self-fulfilling prophecies and multiple equilibria situations. Speculative attacks against the currency and stoppage of credit lines can be reduced immensely if liquid funds are reasonably available to countries affected by contagion and crises of confidence. The problem is that the IMF had, in past financial crises, taken this role, but imposed unreasonable pro-cyclical conditionalities that aggravate the crises and further instill losses in confidence. These conditionalities include:

a) Severe fiscal austerity that: i) reduce social and economic spending at a time of recessionary tendencies; ii) reduce confidence even more since the unreasonably tight fiscal targets are seen to be unachievable due to the decline of fiscal resources during recessionary periods, depreciation of currency and credit tightness, and so the country most likely will fail the IMF program.

b) Exceedingly high interest rates and monetary tightness to stave off currency speculation and inflationary tendencies, but instead: i) bring the recessionary tendencies to actual fruition by creating a credit crunch; ii) cause the deterioration of financial balance sheets and bring the financial and banking sector closer to distress.

c) Unnecessary and harmful punishment of alleged wrongdoers in of alleged wrongdoers. The view that domestic players are mostly to blame for the crisis has led to closure of banks that led directly to bank runs and extreme aggravation of the financial sector.

d) Pushing trade and financial liberalization, privatization and deregulation when the domestic economy is weakest. These policies, of course, cannot be successful if imposed when the country is in crisis, the financial sector dislocated and investors' confidence is nil.

These measures aggravate the pro-cyclical nature of policies during crises wherein low confidence and downturns are met with further confidence erosion and cutbacks in

[7] Most analysts would put more weight and importance on more preventive capital control of massive short-term speculative inflows during times of optimism and boom since it will be harder to impose capital control on capital outflows during times of speculative attacks and financial panic.

economic and fiscal stimuli. This ensures that the crises become very deep and long-drawn.

Thus the need for a new international financial architecture requires: i) a fundamental change in IMF conditionality; and/or ii) alternative sources of liquid funds with reasonable conditionalities to stave off a country's degeneration into insolvency during crises of confidence. It is left to future papers and research on how the above will be achieved.

Exceptional financing by the IMF during financial crises is usually accompanied by debt rescheduling and debt restructuring by Paris Club creditors. If the conditionalities are significantly improved, the Paris Club debt rescheduling and restructuring will be most helpful in restoring confidence, and in allowing badly needed liquid funds to go into social safety nets, vital public spending and public investments to pump-prime the economy back into a healthy condition.

Availability of liquidity fund with more reasonable conditionalities is very important in the necessary switch towards counter-cyclical policies to address financial crises and economic recession in developing countries.

3.5 Interlinking the Three Components

It must be emphasized that the three components are critically needed and linked. First capital controls reduce the potential size and extent of the crisis by reducing the amount of financial and capital flows. This eventually translates to a smaller level of required liquidity funds as well as debt restructuring (if at all).

Also integrally linked are the two other components. Both international liquidity funds and debt workouts reduce the net outflow of precious foreign exchange and funds that may lead to sovereign insolvency. In times of real crises and recession, debt standstills and workout arrangements ensure that the needed funds provided by multilateral and bilateral institutions go to social and economic spending for the country in order to resuscitate the economy and to provide social safety nets during the crisis. A clear policy that the international funds will largely *not* go to debt payments is the best way to ensure creditors' cooperation in debt workouts and debt restructuring arrangements, including the vulture and holdout creditors. It should be made clear that international creditors will *not* get any automatic bailout.

There is a controversy as to whether international liquidity funds, on one hand, and debt standstills and workout arrangements, on the other, should be substitutes or complements.[8] The view in this paper is that, as long as international funds are *not* targeted towards debt payments but to crucial non-debt budgetary and balance of payments support, then the two are complementary. Making them substitutes may expose the developing country to high risk wherein a long drawn-out debt workout negotiation process, without current liquidity funding, will lead to default, insolvency and prolonged economic and financial collapse. At the same time, debt standstills, through workout arrangements and Paris Club debt restructuring, help in ensuring that the liquidity funds will not go to debt payments.

[8] In the parlance of bankruptcy and insolvency proceedings, a sovereign debtor's access to international liquidity funds and additional borrowing while debt restructuring (akin to bankruptcy proceedings) is going on is called 'debtor-in-possession financing, or, alternatively, granting a 'seniority' status to debt contracted after a bankruptcy petition is filed.

Table 1: Existing and Proposed Collective Action Clauses

PROVISIONS	ENGLISH LAW GOVERNED BONDS	NEW YORK LAW GOVERNED BONDS	G-10 RECOMMEDATIONS	INDUSTRY ASSOCIATIONS DRAFT	MEXICAN BONDS GOVERNED BY NEW YORK LAW
Amendment of key terms, including payment terms	• Voting thresholds 75% based on votes cast at duly convened meeting. Quorum requirement for meeting 75% for first meeting; 25% for adjourned meeting.	• Voting threshold: unanimous consent	• Voting thresholds: 75% based on either outstanding principal or duly convened meeting.	• Voting thresholds: based on outstanding principal 85% for key terms unless more than 10% object; unanimous consent for governing law, submission to jurisdiction, waiver of sovereign immunity and service of process; and 75% for other terms.	• Voting thresholds: based on outstanding principal; 75% for key terms (including governing law and submission to jurisdiction)
Exclusion from CAC	• Excluded bonds: bonds held by or on behalf of the issuer	• Excluded bonds: bonds owned directly or indirectly by issuer.	• Excluded bonds: bonds owned or controlled directly or indirectly, by or on behalf of the issuer or any of its agencies for instrumentalities.	• Excluded bonds: bonds owned or controlled, directly or indirectly, by or on behalf of the issuer or any of its agencies or instrumentalities.	• Excluded bonds: bonds owned directly or indirectly by Mexico or any of its public sector instrumentalities.
Acceleration and De-acceleration of	• Acceleration: trustee has	• Acceleration typica	• Acceleration trustee has discretion,	• Acceleration: 25%	• Acceleration: 25%

Individual Creditors' Claims	discretion, but is required at the request of typically 25%, to accelerate • De-acceleration: none but achieved through majority restructuring clauses.	lly 25% • De-acceleration typically more than 50%, but in some cases 75%	but is required at the request of 25% to accelerate • De-acceleration: 50-66⅔%	• De-acceleration: 75%	• De-acceleration more than 50%

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PROVISIONS	ENGLISH LAW GOVERNED BONDS	NEW YORK LAW GOVERNED BONDS	G-10 RECOMMEDATIONS	INDUSTRY ASSOCIATIONS DRAFT	MEXICAN BONDS GOVERNED BY NEW YORK LAW
Initiation of Proceedings	• Fiscal agency structure: any bondholder • Trust structure: trustee has discretion, but can be instructed by 25 percent, to initiate lawsuits • Pro rata distribution of recovery proceeds under trust structure.	• Any bondholder	• Recommend trust deed or similar legal structure • 75% to instruct the trustee to settle lawsuits	• Any bondholder for bonds governed by NY law; trust deed optional for English law bonds.	• None
Engagement Provision	• None	• None	• A bondholder representative be appointed for the life of the bond • 66⅔ to appoint at any time any person to represent all holders in negotiation with the issuer or other creditors	• Upon approval of more than 50%, a bondholder committee will be formed only after an event of default or announcement of the issuer's intention to restructure • A majority to appoint any creditor committee	• None

				representative unless more than 25% object • The issuer will pay any fees and expenses of the committee and its legal and financial advisors	
Information Provision	• None	• None	• A covenant requiring the issuer to provide certain specified information over the life of the bond and following an event of default	• Requiring the issuer to subscribe to the SDDS, publish rolling 12-month forecasts, and provide other information over the life of the bond • Requiring issuer to provide information reasonably requested by 5%of bondholders	• None

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