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The New Vulture Culture: Sovereign debt restructuring and trade and investment treaties

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Abstract

The global community still lacks a regime for sovereign debt restructuring. But it has often been overlooked that the definition of a covered investment within international trade and investment agreements often includes sovereign debt. There is thus increasing concern that international investment agreements may become a "court" for sovereign workouts by default. In this context, this paper analyzes the extent to which investment provisions in various treaties may hinder the ability of nations and private creditors to comprehensively negotiate sovereign debt restructurings when a debtor nation has defaulted or is close to default on its government debt. It is found that the treatment of sovereign debt varies considerably in terms of strength and applicability across the spectrum of the thousands of trade and investment treaties in the world economy. Most treaties may restrict the ability to restructure debt in the wake of a financial crisis. It is therefore concluded that these treaties could undermine the ability of nations to recover from financial crises and thus broaden the impact of such crises.

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Sovereign debt restructuring, trade and investment treaties, financial crisis

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The New Vulture Culture: Sovereign debt restructuring and trade and investment treaties[1]

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I. Introduction

Government borrowing has been a feature of the world economy since the founding of nation states and a cornerstone of the development process as well. However, developing country debt crises are also growing phenomena. Inevitably, with each financial crisis one or more nations find themselves restructuring or defaulting on their sovereign debt commitments.

Debt crises can be a function of government profligacy, unpredictable swings in global markets, or both. Although sovereign debt restructuring and default have been a constant feature of the global economy for centuries, the fact that there is no comprehensive and uniform regime for governing debt workouts has been seen as one of the most glaring gaps in the international financial architecture. The lack of a clear regime for restructuring has accentuated financial crises.

Does the incorporation of sovereign debt as a covered investment in some international investment agreements (IIAs)[2] hinder the ability of debtor nations and their creditors to workout their debt obligations in an efficient manner that facilitates economic development? This question has received relatively little attention in both the economic policy community focusing on financial crises and by the IIA community. The memory of the numerous defaults and restructurings in the 1990s, Argentina's restructuring after its crisis in 2001, and the current European crises have triggered a new wave of thinking regarding the interactions between financial crises and IIAs.

The central findings of this research are the following:

- Sovereign debt is often a covered investment under IIAs;
- Thus sovereign debt restructuring is seen as grounds for private bondholders to file arbitral claims under IIAs;
- Safeguards under IIAs are limited, particularly in the US IIAs. This means that it is not clear which measures provide for policy space for effective restructuring in times of crises; and
- If claims against sovereign debt restructuring become more widespread, they could threaten the regime for financial crisis recovery that is already very fragile.

En route to these conclusions, this paper provides an overview of the rationale for and the state of the current regime for sovereign debt rescheduling in the world economy and then analyzes the extent to which such a regime overlaps with investment provisions of international trade and investment treaties. Following this brief introduction is an overview of the importance of debt in economic development, sovereign debt crises, and the process of sovereign debt restructuring. Section three provides an initial analysis of the extent to which sovereign debt restructuring can be facilitated by IIAs. The final section summarizes the findings and provides suggestions regarding policy and future research.

II. Debt, Development and Financial Crises

This section of the paper provides a very brief overview of developing country debt problems and the current financial crisis. It also provides a critical review of the problems with the current regime for sovereign debt restructuring.

If managed appropriately, government borrowing can be an essential ingredient for economic development, and it has been for centuries. Many developing countries have a savings gap—they lack the savings to finance planned investment, and thus seek to fill such a gap with foreign resources. If the gap is not reversed over time, for example, if the ratio of exports to imports does not increase, the rate of the return on development projects fails to exceed the interest rate on the debt, or the nation's general stage of development does not equip it with the absorptive capacity to turn loans into successful income, then nations begin to see problems in servicing their debt.

Even when nations manage to circumvent such pitfalls, they could still spiral into a debt crisis—simply defined as the situation when a nation cannot (or is no longer willing to) service its debt. Contagion from other crises or herd-like bouts expressing a lack of investor confidence could prevent creditors from rolling over or increasing loans. Developing country debt is most often denominated in a foreign currency, so when interest rates rise or the value of the national currency falls (on its own or relative to its creditors), the cost of debt servicing can skyrocket. When left unchecked, debt markets are too often pro-cyclical—there is a lot of liquidity during boom times and thus nations tend to borrow, but liquidity dries up during recessions and can make it difficult for nations to rollover or increase debt (Minsky, 1986). Even nations with low budget deficits can quickly be affected as governments borrow to stimulate an economy during a recession but then experience slow growth and low tax revenue thereafter. These tensions are exacerbated for developing nations that are overly exposed to international financial markets. Any number of the factors discussed above could cause massive inflows of debt and large swings in outflows that can cause financial instability (Herman et al, 2010).

In a comprehensive new study, Reinhart and Rogoff (2009) finds that the threshold for external debt-to-GDP ratio at which nations have historically slipped into crisis has been 30-35 percent of GDP. Table 1 updates and expands upon Reinhart and Rogoff's list of nations that experienced a debt crisis between 1970 and 2009. The first column lists the nation in question, and the second lists the year(s) in which the nation experienced a debt default or restructuring, followed by column three that lists the debt-to-GDP ratio at the time of default. Two more columns are added to the original table. Column four lists the debt-to-GDP ratio during the fourth quarter of 2009. Although Reinhart and Rogoff (2009) finds the threshold to be 30-35 percent of GDP, Table 1 shows that on average, nations had ratios of more than 69 percent. For those same nations—nations that Reinhart and Rogoff refer to as 'serial defaulters' because they have a long history of default—the average debt-to-GDP ratio was 43.7 percent and thus over the threshold.

Table 1: External Debt and Bilateral Investment Treaties: Middle income countries (1970-2009)

	Year of default or restructuring	Ratio of external debt to GNP at the end of the year of default or restructuring	Ratio of external debt to GDP (Q4 2009)	No. of BITs as of 6/1/2009
Albania	1990	16.6%	38.6%	40
Argentina	1982	55.1%	38.0%	58
	2001	50.8%		
Bolivia	1980	92.5%	33.1%	22
Brazil	1983	50.1%	21.9%	14
Bulgaria	1990	57.1%	107.6%	67
Chile	1972	31.1%	54.5%	
	1983	96.4%		
Costa Rica	1981	136.9%	26.8%	20
Dominican Republic	1982	31.8%	23.0%	16
Ecuador	1984	68.2%	31.0%*	19
	2000	106.1%		
	2008	20.0%		
Egypt, Arab Rep.	1984	112.0%	17.7%	101
Guyana	1982	214.3%	70.6%	7
Honduras	1981	61.5%	19.6%	n.a.
Iran	1992	41.8%	n.a.	57
Iraq	1990	n.a.	n.a.	3
Jamaica	1978	48.5%	68.7%	16
Jordan	1989	179.5%	65.9%	46
Mexico	1982	46.7%	23.8%	27
Morocco	1983	87.0%	23.4%	58
Panama	1983	88.1%	36.1%*	20
Peru	1978	80.9%	29.0%	32
	1984	62.0%		
Philippines	1983	70.6%	38.9%	35
Poland	1981	n.a.	69.4%	62
Romania	1982	n.a.	70.2%	83
Russian Federation	1991	12.5%	40.5%	64
	1982	58.5%		
South Africa	1985	n.a.	32.5%	45
Trinidad and Tobago	1989	49.4%	n.a.	11
Turkey	1978	21.0%	49.1%	79
Uruguay	1983	63.7%	43.3%	28
Venezuela, R.B. de	1982	41.4%	n.a.	28
Yugoslavia	1983	n.a.	64.5%**	32
Average		**69.3%**	**43.7%**	**39**

Notes: n.a. not available. Reinhart and Rogoff reports debt stocks at the end of the period which biases the ratio of debt to GNP upward since defaults result in exchange rate depreciation.

*Uses third quarter data.

** Q4 2009 external debt is for Macedonia, former Yugoslavia.

Sources: Reinhart, Carmen M. and Kenneth S. Rogoff (2009), *This Time is Different*, Princeton University Press; UNCTAD Database <http://www.unctad.org/Templates/Page.asp?intItemID=2344&lang=1>, Accessed July 6, 2010; International Monetary Fund (2009a), World Economic Outlook Database, April 2009; and World Bank, Quarterly External Debt Statistics.

To foreshadow the main analysis of this paper, a last column is added, which sums the number of bilateral investment treaties (BITs) that each of those nations is party to. On average, nations prone to default are each party to 39 BITs. Many BITs (and free trade agreements or FTAs) 'cover' sovereign debt and leave open the possibility that creditors can file claims against nations to recoup the full value of their investment.

A recent study by the IMF found that twenty-eight of the poorest nations are now at high risk of debt crisis (IMF, 2009). Table 2 exhibits the frequently watched "cumulative probability of default" (CPD) report, listing the twenty five nations with the highest probability of default as of July 2010, and the BITs held by such nations (CPD, 2010). CPD quantifies the probability of a country being unable to honor its debt obligations. Venezuela tops the list with a 58 percent chance that it will default, followed by the infamous Greece and Argentina. It is comforting to note that no African countries—among the most highly indebted on earth—seem to be close to default at the time of writing. On average, of these top 25 nations with the highest likelihood of default, each is a signatory to 48 BITs.

Table 2: Global Rankings by Cumulative Probability of Default

Country	CPD (%)	No. of BITs as of 6/1/2009
Venezuela	58.4%	28
Greece	53.0%	43
Argentina	48.0%	58
Pakistan	39.0%	47
Ukraine	35.7%	62
Dubai	29.5%	34
Iraq	29.0%	3
Romania	25.4%	83
Portugal	23.6%	47
Latvia	23.5%	43
Iceland	23.2%	9
Bulgaria	22.5%	67
Hungary	21.5%	58
Ireland	20.8%	1
Spain	20.7%	74
Croatia	20.5%	58
Lebanon	20.5%	49
Dominican Republic	19.4%	16
Lithuania	18.2%	51
Vietnam	16.8%	52
Italy	15.5%	99
El Salvador	15.1%	24
Kazakhstan	14.9%	38
Egypt	14.4%	101
Guatemala	13.1%	18
Turkey	13.0%	79

Notes: CPD is Cumulative Probability of Default which measures the probability of a country not being able to service its debt obligations. The CPD figures provided in the table are calculated over a five year period unless otherwise stated.

CPD is calculated using proprietary credit data from CMA Datavision using industry standard model.

Sources: Global Sovereign Credit Risk Report, Q2 2010, July 2010; and UNCTAD Database <http://www.unctad.org/Templates/Page.asp?intItemID=2344&lang=1>, Accessed July 6, 2010.

Many countries, if not this time then the next time around, may need to reschedule, restructure, or even default on their debt. At present there exists no adequate forum for nations to workout their debt problems.

From Bailouts to Bail-ins?

Coordinated global bailouts have been part of the traditional response to prevent and mitigate debt crises. However, they receive a great deal of criticism because of their costliness and lack of effectiveness. In an attempt to prevent default, or to manage a recovery after such an event, nations are often granted 'bailouts' in the form of new loans and grants from international financial institutions. Chief among those institutions is the International Monetary Fund (IMF), but national governments and other institutions (such as the Paris Club) often pitch in as well.

Increasingly however, bailouts are seen as costly, unfair, providing the wrong incentives and lacking in effectiveness. The most costly bailout until recently was the $50 billion rescue package for Mexico's crisis in 1994. Once seen as an unthinkable bailout, it has become eclipsed by the staggering $1 trillion for Europe's current crisis. These bailouts are often quickly sent out of the country to pay creditors and seldom help the nation regain its economic footing. Moreover, there is a real question of fairness given that global taxpayers (through contributions to the IMF or their governments) are the ones footing the bill to foreign creditors. Critics also refer to the 'moral hazard' problem that can come with international bailouts. If global investors (and debtors) know that they will be bailed out, they will have the incentive to make evermore risky loans. Finally, the record on the effectiveness of bailouts is limited at best, with many nations taking years to recover, if at all (Eichengreen, 2003).

Sovereign debt restructuring (SDR) is increasingly seen as an alternative to bailouts. However, the international community views the SDR regime to be greatly lacking. Many go so far as to argue that the lack of such an adequate regime to restructure sovereign debt in a comprehensive, fair and rapid manner is among the most glaring gaps in the international financial architecture (Krueger 2002, Herman et al, 2010).

When a sovereign government is no longer willing or able to pay its debts, sovereign debt restructurings occur during what amounts to a formal change to debt contracts that is negotiated between creditors and debtors. SDRs (or "workouts") often take the form of reducing the face value of the debt, "swaps" where new bonds with lower interest rates and longer maturities are exchanged for the defaulted bonds, and so forth. Such workouts are usually highly discounted and result in a loss for bondholders. Losses or discounts are commonly referred to as "haircuts". The process is often referred to as a "bailin" because the participants are not 'out' side of the investment itself as the IMF, governments and taxpayers are during a bailout. Table 3 lists some of the major SDRs over the last 12 years according to the duration of the SDR negotiations, the total face value of the bonds under restructuring, the 'haircut' and the participation rate.

Table 3: Sovereign Debt Restructurings, 1998 to 2010

	Duration (m)	**Value (US billion)**	**Haircut (%)**	**Participation (%)**
Russia (1998-2000)	20	31.8	37.5	98
Ukraine (1998-2000)	3	3.3	0	95
Pakistan (1999)	10	0.6	0	95
Ecuador (2000)	12	6.8	40	97
Uruguay (2004)	1	5.4	0	93
Argentina				
2005	40	81.8	67	76
2010	60	18	75	66
Argentina total	***100***	***99.8***		***93***

Sources: Porzecanski (2005); (Dhillon et al., 2006); (Hornbeck, 2010)

It is held that a restructuring is deemed successful when 90% or more of bondholders participate in an offering that is no less than 50% of the net present value of the debt (Hornbeck, 2010). There are always some 'holdouts' during a restructuring, disgruntled investors who refuse to negotiate and demand the full value of their investment. These holdouts often file suits under the municipal laws that govern bond contracts in New York, London and beyond. There are also 'vulture funds', which purchase debt when it is of a very low value before or after a restructuring and then file suits to increase the value of their investment (Thomson and Runciman, 2006). In a new development, and the subject of this paper, holdout investors have filed claims under BITs and could potentially do so under numerous FTAs.

Despite some significant improvements, collective action problems and the lack of a uniform system continue to plague the SDR regime. SDRs are seen as strong alternatives to bailouts, at least in theory. Indeed, among the key rationale for efficient SDRs are the avoided costs of taxpayer-funded bailouts and of the moral hazard associated with bailouts. However, the nature of private debt has evolved over time. For most of the 20th century, private debt was issued by large commercial banks. In a restructuring it was relatively easy for governments and international institutions to put pressure on a small number of such banks in order to facilitate a restructuring. However, at the end of the century, private debt became dominated by bonds, which can be held by numerous investors. These bondholders can be dispersed across the globe and are hard to track down, thus making the restructuring process more complex (Eichengreen, 2003).

Perhaps the most significant concerns relate to collective action problems that arise during a negotiation. Although a swift and efficient settlement could make creditors, debtors and international institutions better off, there are complex incentives that make negotiations drag on for long durations and can favor one party over another. Table 2 shows that even the shortest recent SDR took one month. And of course Argentina's debt wasn't restructured until 2010—nine years of restructuring that still may not be over.

Eichengreen and Mody (2003) summarizes the ramifications of a long and cumbersome restructuring process:

> Governments that default on their debts must embark on lengthy and difficult negotiations. Lenders and borrowers, uncertain of one another's willingness to compromise, may engage in costly wars of attrition, delaying agreement on restructuring terms. Even if disagreements about the debtor's willingness and ability to pay are put to rest, dissenting creditors may continue to block agreement until they are bought out on favorable terms.
>
> In the interim, the creditors receive no interest, and the borrowing country loses access to international capital markets. The exchange rate may collapse, and banks with foreign-currency-denominated liabilities may suffer runs. To avert or delay this costly and disruptive crisis, the International Monetary Fund will come under intense pressure to intervene, provoking all the controversy that IMF intervention typically entails. Officials of the

> borrowing country, for their part, will go to great lengths to avoid seeing the country placed in this difficult situation. They may raise interest rates, run down their reserves and put their economy through a deflationary wringer, all at considerable cost to society (80).

In addition to these problems, long workouts can accentuate debt overhang whereby a nation spends so much time and effort servicing its debt that it cannot grow to its full potential (Rogoff and Zettelmeyer, 2002).

These costs could be significantly reduced with a swift and orderly SDR process. A swift negotiation with standstills on payments and other measures to buffer a "rush to exit" in related assets would make all parties better off. Ironically, collective action problems get in the way.

It is in the interest of private creditors to support a regime that would prevent all creditors from rushing to exit given that such a run would jeopardize the collective value of the asset and keep a debtor solvent enough to pay debts. However, individual creditors have an incentive to quickly exit before other creditors do and still other investors may also holdout from negotiating until they are sure that the behavior of free riders that rush to exit is under control (Hagan, 2005; Helleiner, 2008). Of course it is in the debtors' interest to restructure debt in a manner that allows the nation to service its debt burden and begin to recover. Yet debtors have been reluctant to support a regime because they fear that the nation might be seen as more willing to default, resulting in a lack of general investor confidence in the country and a subsequent drain of investment (Helleiner, 2009).

The proliferation of recent SDRs led to a near consensus that the SDR regime was in need of repair. By the turn of the century, the international community was both fed up with IMF bailouts and frustrated with the SDR process. In 2001, Anne Krueger, a well-known US economist who had just taken the helm as the Deputy Managing Director of the IMF proposed a "Sovereign Debt Restructuring Mechanism" (SDRM). The SDRM was to be a new global mechanism analogous to bankruptcy courts for private creditors (known as Chapter 11 in the US). The argument for the SDRM was that it would minimize the need for major taxpayer and IMF bailouts to private creditors and reduce the moral hazard problem.

The main features of the SDRM (outlined in Table 4) were:

- a payments standstill on bonds and capital controls, all to be monitored by the IMF;
- a stay on litigation altogether or at least the requirement of a supermajority (75 percent) approval of stays on litigation;
- a process to prioritize some loans over others and for new loans to be made by the IMF and others; and
- a supermajority among all bondholders, regardless of a particular bond issue, would be all that is needed to accept the terms of the restructuring (Hagan, 2005).

Table 4: Varieties of Debt Workouts

Chapter 11	standstills	supermajority voting litigation stay	preferred status for new money	court supervision
SDRM	standstills capital controls	supermajority voting litigation stay	preferred status for new money	neutral agency plus IMF program
CACs		supermajority voting		representation clauses
Result	unilateral standstills capital controls	CAC (supermajority voting) ICSID	unilateral	Bond swaps/exchanges

Source: author's adaption from (Miller, 2002), and (Herman et al., 2010)

The SDRM was vehemently opposed by private creditors, the US government and even some creditor nations. As Helleiner (2009) and Setser (2010) explain, the US government did not want to grant the IMF so much power and did not want to engage in dollar diplomacy across the world. Private creditors argued that the status quo was not a bad one. Although there was a theoretical discussion of the collective action problem just described, creditors noted that no restructuring had been held up due to litigation. Some debtors were concerned that they would not receive any more IMF support, and were concerned that they would be scorned by private investors in the market place.

US Deputy Treasury Secretary John Taylor proposed an alternative that has ended up becoming widely accepted. Taylor proposed a more market-based "contractual" approach, whereby bonds themselves would have collective action clauses within their contracts. Most bonds issued from London at the time included such clauses, but most US bonds did not. The key features of collective action clauses (CACs) are that they have:

- a *collective representation* component, whereby a bondholders' meeting can take place such that creditors exchange views and discuss the default/restructuring;
- *a minumum enforcement* component, whereby 25 percent of the bondholders must agree that litigation can be taken; and
- *a majority restructuring* component, which enables a 75 percent supermajority of bondholders to bind all holders within the same bond issue to the terms of restructuring.

This idea has really taken off and at this point CACs are found in more than 90 percent of newly issued bonds in the United States (Helleiner, 2009).

Although CACs are a significant improvement, they are still seen as lacking by many observers. First, bondholders can be globally dispersed, as opposed to the day when a handful of major banks could be rounded up. Many bonds are also sold on secondary markets, making it even more difficult to "call a vote." Second, for some bond issues it may be easy for holdouts to purchase a 75 percent majority for a vote and neutralize the collective action component of the issue. In other words, it may not be very difficult to prevent 75 percent of the bondholders from accepting a restructuring, and/or to prevent just 25 percent of bondholders from voting to move to litigation. Third, and even more problematic is what is called the 'aggregation problem.' CACs only cover individual bond issues but have no effect on the holders of other issues. Restructurings increasingly involve multiple bond issuances and CAC provisions do not hold for collective action across multiple issuances (the SDRM would have allowed for such a mechanism) (Hagan, 2005). To be clear, CACs cover a single bond issuance. Consider, for example, a 10 month bond issued by country X in 2008. Country X may issue a 15 year bond in 2009, with a CAC as well. Often however, when a nation restructures its debt, it restructures multiple bond issuances. While CACs work within a particular bond issue, they do not cover multiple bonds. If bondholders of some issues refuse a government's offer, they may have to be paid in full. Moreover, a debtor may have fewer resources to share with other issue-holders, who may then reject its restructuring offer (Eichengreen and Mody, 2003, 80).

The most recent restructuring has occurred in Argentina, culminating in 2010. A short synopsis of the Argentine case is featured in Box 1. There have been holdouts in Argentina's restructurings, some of whom have gone to the International Center for the Settlement of Investment Disputes (ICSID) under a BIT.

Box 1:

Argentina: Crisis, Default, Restructuring and the ICSID

In June 2010, Argentina may have completed the most controversial sovereign default in history. Argentina restructured $100 billion of debt three times between 2001 and 2010.

During the 1990s, Argentina was seen as the poster child of the Washington Consensus. In addition to major privatization programs, trade and investment liberalization, and a general reduction of the state's role in economic affairs, Argentina enacted a "convertibility plan" that laid the foundation for the crisis. In a nutshell, the convertibility plan guaranteed a one-to-one convertibility of the peso to the US dollar and capped the ability of the nation to print domestic currency at the level of US dollars held in reserve (Blustein, 2005). To carry out the plan, fiscal and monetary policy had to be tight because the government could not expand money supply to fill budget gaps—thus leaving austerity or borrowing as the only options for preserving the system.

The plan got off to a positive start but convertibility and an open capital account left the nation vulnerable to external shocks. When the crises of the late 1990s in Asia and Russia spread to Brazil and led to a depreciation of the Brazilian real, Argentina was faced with competitors with weaker currencies—in an environment of a rising dollar, falling commodity prices, and a retreat from emerging market investment. Rather than warning Argentina of its eroding position, the IMF continued to support Argentina's policies (Damill, Frenkel, and Rapetti, 2010). The debate rages on regarding the relative importance of each of these factors, but it is clear that by 2001 the Argentine economy ran out of steam and the country defaulted in January 2002. GDP fell by 10 percent that year and poverty doubled.

For years, new policy-makers in Argentina attempted to negotiate a restructuring under the supervision of the IMF. By 2004 Argentina decided to take a different route. Argentina announced that it would open a one time bond exchange and passed domestic legislation that it would never hold a future swap with a better offer. In January 2005, the country opened an exchange on over $100 billion in principal and interest on a diverse number of bond issuances whereby the bondholders were to receive a 67 percent haircut. In the end it restructured just over $62 billion with a 76 percent participation rate (24 percent holdouts).

Holdouts and some observers of the restructuring were furious, going so far to call Argentina a "rogue creditor" (Porzecanski, 2005). Some holdouts, among them numerous vulture funds, took the litigation route in the United States, where 158 suits have been filed (Hornbeck, 2010).

For the first time ever, a number of those holdouts filed claims under IIAs to the International Center for the Settlement of Investment Disputes (ICSID). In September 2006, about 180,000 Argentine bondholders filed a claim under the Italy-Argentina BIT for approximately $4.3 billion. The creditors claimed that the Argentine restructuring was tantamount to expropriation and violated fair and equitable treatment standards under the treaty (Waibel, 2007).

Argentina was still left with a significant debt load and was short of the 90 percent threshold for the restructuring to be seen as successful such that the rest of the holdouts could essentially be ignored. Argentina launched another take-it-or-leave-it exchange from May-June of 2010 for $18 billion of its debt—offering a staggering 75 percent haircut under the same rationale as in 2005, despite experiencing a recent boom (Porzecanski, 2010). As was the case with the 2005 swap, the bonds were exchanged for bonds with CACs and that are linked to GDP—the bonds pay out more when the economy is growing fast, and less during slower times. 66% of the bondholders ($12.1 billion) tendered. $6.2 billion worth of bondholders will continue to litigate either through domestic courts or through the ICSID. It does appear however that some of the Italian bondholders who have filed an ICSID claim did indeed tender, though $1.2 billion or more remain with their ICSID claim (IMF, 2010; Hornbeck, 2010). Nevertheless, the two swaps together now amount to 92% of bondholders' tendering, what is normally seen as successful enough for Argentina to move on. Do the ICSID cases change this?

The recent case with Argentina reveals that the regime for SDR remains far from adequate. Argentina was shunned by international capital markets for almost nine years during the process, and creditors took heavy haircuts. It was costly to all involved, except for perhaps the patient bondholders who have turned to the ICSID. To this issue we now turn.

III. Sovereign Debt Restructuring and International Investment Agreements

This section of the paper examines the extent to which various trade and investment agreements grant developing nations the policy space to restructure sovereign debt in a comprehensive, just and efficient manner. Significant inconsistency is found regarding the coverage of sovereign debt in various trade and investment regimes. When sovereign debt is covered in a treaty however, a number of relevant questions arise.

The scope, coverage and jurisdiction of IIAs vary widely (Salacuse, 2010). To what extent is sovereign debt covered and under what provisions might an investor have grounds to file a claim because of restructuring? The following areas are discussed in this section: jurisdiction, umbrella clauses, national treatment, fair and equitable treatment, expropriation, transfers and safeguards. Each of these areas will be briefly discussed in turn.

Jurisdiction

Many IIAs treat "any kind of asset" as a covered investment and therefore include sovereign bonds. More recent treaties explicitly list bonds as covered by the treaty. That said, there are numerous treaties that do not include sovereign debt as well.[3] Other treaties do not include portfolio investment at all.[4] Increasingly however, sovereign bonds are included in IIAs. This leads to two concerns that are addressed in this subsection: the increasing coverage of sovereign debt in IIAs and the extent to which CACs provide protection under IIAs.

In terms of general jurisdiction and coverage, an arbitration claim against sovereign debt restructuring depends on several issues: whether the tribunal finds that it has jurisdiction, which requires an *investment* to have been made; and *consent* by the sovereign party or a claim based on the investment agreement itself. In terms of jurisdiction, the consent of the sovereign party is governed by the investment agreement.

This is where the "definitions" provisions of IIAs come in. If an agreement clearly includes bonds and other debt instruments as covered investments, then the country has consented to jurisdiction for those claims. By extension, then, any limitation within the BIT to those claims (such as the annexes on safeguards and the general exclusion in NAFTA of sovereign debt claims discussed later) is a limitation on consent (Cross 2006). Analysis of BITs and FTAs for this paper reveals that almost all of the agreements by major capital exporters from industrialized nations include "any kind of asset" as covered investments and thus likely cover sovereign bonds. Some treaties, such as the North American Free Trade Agreement (NAFTA), the majority of Peru's IIAs and some others (such as the Australia-Chile FTA) exclude or safeguard sovereign debt.

It appears that CACs do not provide adequate protection for sovereign debtors in the context of IIAs. On the surface, CACs would appear to prevent holdouts of sovereign bonds and vulture funds from filing claims under IIAs. Yet even if the bondholders of a particular issuance voted against litigation through a minority clause or agreed to the terms of a restructuring under a majority clause, such actions under a CAC would *not* prevent an investor from filing an arbitral claim. According to Waibel (2007), CACs cover contractual rights of enforcement under municipal laws and are not designed to deal with treaty claims. Thus even if a CAC was deployed, holdout bondholders could file a treaty claim arguing that the terms of a treaty have been violated. This leads Waibel to say that "ICSID arbitration could blow a hole in the international community's collective action policy" (Waibel, 2007, 715). Waibel expands:

> The prima facie limited coverage of CACs—their failure to include arbitration—opens up a new window of opportunity for holdout litigation. The importance of this potential loophole for sovereign debt markets cannot be overemphasized. Consider the following scenario.
>
> ICSID tribunals could conceivably hear treaty claims concerning sovereign bonds despite the legitimate exercise of CACs, which would become ineffective in binding nonparticipating creditors. If CACs were to leave treaty claims untouched, then they would bar only contractual causes of action originating in the bond contract. Bondholders might be able to obtain compensation even though the contractually prescribed majority of bondholders accepted the sovereign debt restructuring. Recourse to ICSID arbitration could thus create a legal gap in the international community's collective action policy (Waibel, 2007, 736).

Furthermore, bondholders could "treaty shop" and file claims under treaties where it may be more certain that a bondholder will win jurisdiction (Wells, 2010). Waibel (2011) has pointed out that a large number of sovereign bonds are traded on secondary markets and nationality can literally change in a matter of minutes, accentuating the ability of a bondholder to "shop" for favorable treaties.

Umbrella Clauses

Umbrella clauses, when they appear in IIAs, are intended to "impose an international treaty obligation on host countries that requires them to respect obligations they have entered into with respect to investments protected by the treaty. This places such obligations under the "umbrella" of international law, not just the domestic law that would otherwise apply exclusively." (Salacuse, 2010, 275). Thus a host state has the responsibility to respect its treaty obligations in addition to, or even despite the fact, that the same obligations may also be governed by domestic laws and contracts. This makes the host state subject to the jurisdiction of investor-state arbitration. Therefore, contractual approaches to SDR such as CACs could be interpreted as being within the scope of an IIA, via an umbrella clause. Even if a bond issuance with a CAC has had a bondholders' meeting whereby a supermajority has agreed to accept the restructuring and if there was no minimum enforcement vote of 25 percent of bondholders to litigate, under an umbrella clause holdouts may still be able to resort to investor-state arbitration.

National Treatment

National treatment implies that foreign investors are treated no less favorable than their domestic counterparts. Domestic investors have been treated differently under some restructurings with considerable economic justification, and could thus trigger claims under IIAs. Put simply, a national treatment claim could occur when a foreign bondholder receives different terms during a restructuring than do domestic holders.

Economists who specialize in mitigating financial crises agree that there are numerous circumstances when domestic investors should be given a priority over foreign creditors. As countries liberalize their capital accounts, the line between external and domestic debt becomes blurred. In years past it was relatively easy to delineate between external and domestic debt. In a nutshell, external debt was issued in foreign currency and was held by foreigners and domestic debt was denominated in local currency and held by residents. Under a liberalized capital account, foreign investors may invest in domestic debt and domestic residents may purchase foreign debt. Indeed, domestic financial institutions and residents held close to half of Argentina's debt that was restructured between 2001 and 2010. Economists and prominent legal scholars alike conclude that "the ability to treat domestic and foreign creditors differently is a necessary policy option for governments in a financial crisis" (Gelpern and Setser, 2004, 796).

The economic (and political) rationale for treating domestic and foreign investors differently during a debt crisis is multi-pronged.

First, it is recognized that domestic investors are often hit by a "double-adjustment" during a crisis and restructuring. Domestic investors not only suffer the reduction in the value of their bonds through the restructuring, but they are also affected by the impact of post-crisis ramifications that could include slow growth, high unemployment, high interest rates and devaluation. On the other hand, foreign investors' commitments will be in their own currency and these investors will not be affected by the domestic effects because they are outside the country in question and are very unlikely to make continued investments in the host economy in the short-term (Caliari, 2009).

On a related note, prioritizing domestic debt may be in order so as to revive a domestic financial system, provide liquidity and manage risk during a recovery. Without such measures a banking crisis can ensue wherein massive outflows of foreign exchange and/or bank runs can occur. In both the Russian and Argentinean cases, domestic investors received more favorable treatment with this in mind (Panizza, 2010; Gorbunov, 2010; Gelpern and Setser, 2004; Blustein, 2005; IMF, 2002).

Politics also plays a key role. The support of important constituents and political groups is often essential for a recovery and reform effort to be successful. There is also a clear rationale to prioritize the citizenry through maintaining the ability of economic actors to pay wages, salaries, and pensions in order to maintain livelihoods, enable domestic demand and avoid mass protest (Gelpern and Setser, 2004; IMF, 2002).

Expropriation

Sovereign debt restructuring or default could be interpreted as constituting a direct or indirect expropriation. It is held that among the claims levied by Italian bondholders under the Italy-Argentina BIT is the alleged expropriation of their investments through restructuring. Expropriation is commonly defined and seen in IIAs as "wealth deprivation" where "substantial deprivation" occurs that could be *direct* where an investment is "taken" in the form of a title or physical seizure, or indirect whereby the title or physical nature of the investment is not changed, but its value may be diminished (OECD, 2004). Both defaults and restructuring obviously diminish the value of an asset, and under a "take-it-or-leave-it" swap arrangement a bondholder has the choice to either lose a bond altogether or to accept a new bond with a haircut. Tribunals often perform a "substantial deprivation" test to examine the level of diminished value in a restructuring, and would thus in this case be examining the size of the haircut in a bond exchange (Newcomb and Paradell, 2004).

Fair and Equitable Treatment

Most newer IIAs include a "fair and equitable treatment" (FET) clause that usually grants investors the rights to transparency, protection of investors' reasonable expectations, freedom from harassment and coercion, due process and good faith (Waibel, 2007). Legal scholars have expressed concern that restructuring in general and bond exchanges in particular can be seen as violations of FET.

Concern has been expressed that bond exchanges may violate FET in and of themselves, despite the fact that exchanges have become standard practice for restructurings. Waibel (2007) outlines a number of justifications for claiming that bond exchanges violate FET under IIAs. Waibel sees it as possible that exchanges could trigger allegations that the process lacks transparency and that it is coercive. In addition, the "take-it-or-leave-it" nature of exchanges could be seen as violating due process and not seen as being in good faith given that the government does not take part in serious restructuring negotiations. Finally, Waibel also sees restructuring as possibly considered as actionable because a restructuring may be seen as transforming the business environment or undermining the legal framework of the bonds themselves.

Transfers

The transfers clauses in IIAs increasingly require that all covered investments of participating parties be transferred "freely and without delay." Restructuring could potentially clash with transfer provisions at three levels. First, an outright default ceases the transfer of the bond in question and thus could be seen as a clear violation. Second, during the restructuring negotiations, presumably little transferring related to the bonds in question is occurring and could possibly be grounds for disgruntled investors to file (or threaten to file to speed negotiation) a claim. Third, under some of the proposals for the SDRM, the IMF or another body would hold a 'standstill' during the negotiations whereby the nation deploys temporary capital or currency controls during the negotiations. In one of the numerous cases against Argentina in the aftermath of its 2000–01 crisis, an ICSID tribunal ruled that a tax on outflows (a common form of capital control used during crisis by Malaysia as well) was a violation of the transfers and expropriation clauses[5] (Salacuse, 2010).

Safeguards

To what extent might defaults and restructuring be protected under the various forms of safeguard clauses that can be found in many IIAs? Key safeguards that may provide cover are "essential security" provisions as well as special annexes in a handful of U.S. IIAs.

It may be possible that a nation can claim that actions taken during a financial crisis are measures needed to protect the 'essential security' of the nation. Language like Article 18 of the United States Model BIT is found in many treaties:

> ... to preclude a Party from applying measures that *it considers* necessary for the fulfilment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests (USTR, 2004).

The article does not mention economic crises per se, but "all tribunals that have considered the matter thus far have interpreted the rules broadly enough to include such crises" (Salacuse, 2010: 345). However, tribunals differ greatly over how grave the difficulties may be. In Argentina again, only one of three tribunals ruled that Argentina could not be held liable for actions it took to halt its crisis. A key matter is whether or not a measure by a nation to stem a crisis can be seen as "self-judging". In other words, can the host nation using the controls be the judge of whether or not the measure taken was necessary to protect its security. The language quoted above in the 2004 US Model BIT, which says "that *it* considers" is now seen as to mean that a measure is self judging (because of the "*it*"), but Argentina's BITs with the United States and others did not include such precise language at the time (Salacuse, 2010).[6]

In addition to self-judging, states often have to show there is a "necessity defense" in order to invoke essential security exception- a defence that is strictly delimited in customary international law. The word 'necessary' was also used in the BIT clause. As such Argentina and other nations facing crises will have to demonstrate that its measures were 'necessary' to address a threat to its essential security. Tribunals have to decide how much suffering and destitution a state is expected to tolerate in the welfare of its population and condition of its economy before one is prepared to conclude that it is necessary to intervene in spite of the state's obligations to foreign creditors, investors and so forth.

Annexes on Sovereign Debt Restructuring in US IIAs

Some of the recent IIAs negotiated by the United States clearly define sovereign bonds as covered investments and provide explicit guidelines for the interaction between SDR and certain IIAs. What is found in the US-Uruguay BIT, and in FTAs with Central America, Chile, Peru, and Colombia (pending) is a special annex on sovereign debt restructuring. Though the specific text of such an annex varies across the treaties, such provisions usually prohibit claims against 'negotiated debt restructuring', unless an investor holds that a restructuring violates national treatment (NT) or (MFN). Such treaties usually define "negotiated restructuring" as a restructuring where 75% of the bondholders have consented to a change in payment terms. If an investor does file a claim in the event of a restructuring that is not a "negotiated" one, s/he must honor a 'cooling off' period usually lasting 270 days before a claim may be filed. There is no cooling off period for a non-negotiated or negotiated restructuring that violates NT or MFN. The agreements with such provisions are contrasted in Table 5.

Table 5: Sovereign Debt Restructuring Annexes in Recent US IIAs

	US-Chile FTA 2003	**US-Uruguay BIT 2006**	**DR-CAFTA 2005**	**US-Peru FTA 2007**	**US-Colombia FTA Pending**
Definition of "investment"	Includes loans, bonds..	Includes loans, bonds..	Includes loans, bonds..	Includes loans, bonds..	Includes loans, bonds..
Safeguard for restructuring	Yes	Yes	Yes	Yes	Yes
NT & MFN exception to safeguard	Yes	Yes	Yes	Yes	Yes
"Negotiated" restructuring requirement	No	Yes	No	Yes	Yes
"Cooling off" period	No	For *non*-negotiated restructuring, except for violations of NT & MFN, 270 days	No	For *non*-negotiated restructuring, except for violations of NT & MFN, 270 days	For *non*-negotiated restructuring, except for violations of NT & MFN, 270 days

Note: DR-CAFTA refers to the US-Dominican Republic-Central America Free Trade Agreement

It should be noted that such annexes are not standard in US treaties after NAFTA (NAFTA excludes sovereign debt from the definition of investment altogether). Indeed, the US-Australia, US-South Korea (pending), US-Morocco, US-Oman, US-Panama and US-Singapore agreements included bonds and debt as covered investments, but do not include annexes for sovereign debt restructuring. The absence of such a safeguard in the US-South Korea agreement is striking given the fact that South Korea engaged in a historic restructuring of its sovereign debt following its financial crisis in the late 1990s (Blustein, 2001).

The US was initially very reluctant to include such annexes in its agreements. According to interviews with US negotiators for this report, the US does not initiate discussions regarding sovereign debt, but only responds to them when raised by negotiating partners. The US however sees SDR as not being much of a problem with IIAs at this point because of the emergence of CACs. The annexes on SDR are seen by the US as designed to raise the comfort level of trading partners' concerns.

The first nation to express concern over IIAs and SDRs was Chile, during the US-Chile FTA negotiations. The text of the resulting annex can be found in Box 2.

The second was the US-Uruguay BIT. According to Uruguay's chief negotiator who was interviewed for this paper, Uruguay was unaware of Chile's measures. The Uruguay BIT is the first to introduce the "negotiated restructuring" requirement and the "cooling off" period. The US-Chile FTA (and later the US-Dominican Republic-Central America Free Trade Agreement or DR-CAFTA) ban claims during a restructuring regardless of the type of restructuring except when a restructuring violates NT or MFN clauses; however, they do not refer to a "negotiated restructuring".

The negotiations with Uruguay took place in 2004, just months after Uruguay restructured its debt. Uruguayan negotiators wanted to make sure that the BIT recognized as lawful what Uruguay had just done and that, more importantly, allowed for that kind of flexibility should a similar circumstance arise in the future. According to interviews with negotiators, the US was strongly opposed to the idea at the beginning. This was a deal breaker for Uruguay. After a year of back and forth, the US finally came around. Uruguayan negotiators report that this was the toughest issue and the last one to be resolved.

To summarize, under the US agreements with Uruguay,Peru, and Colombia, any country can engage in a "negotiated restructuring" without being liable for the losses of foreign investors. Under these same agreements, however, *non*-negotiated restructuring is subject to claims as long as the investor waits 270 days (the same in each agreement) from the event before filing the claim.

Implicitly in the Uruguay BIT and more explicitly in the Peru and Colombia FTAs, NT and MFN claims may be brought regardless of whether the restructuring is negotiated and regardless of the cooling off period. In all these cases, the Annex excludes Articles 3 and 4 (NT and MFN) from its safeguard umbrella.

The DR-CAFTA resembles the Chile FTA much more closely. Like the above agreements, bonds and other debt instruments are considered covered investments under the agreement. Annex 10-A then specifies very clearly that sovereign debt restructuring is subject ONLY to Articles 10.3 (National Treatment) and 10.4 (MFN). The additional cooling off period does not seem to apply and there is no mention of "negotiated restructuring" as a prerequisite.

Box 2:

US-Chile FTA and DR-CAFTA

Annex 10-B

Public Debt

The rescheduling of the debts of Chile, or of its appropriate institutions owned or controlled through ownership interests by Chile, owed to the United States and the rescheduling of its debts owed to creditors in general are not subject to any provision of Section A other than Articles 10.2 and 10.3.

US-Peru & US-Colombia Free Trade Agreements

Annex 10-F

Public Debt

1. The Parties recognize that the purchase of debt issued by a Party entails commercial risk. For greater certainty, no award may be made in favor of a claimant for a claim under Article 10.16.1(a)(i)(A) or Article 10.16.1(b)(i)(A) with respect to default or non-payment of debt issued by a Party unless the claimant meets its burden of proving that such default or non-payment constitutes an uncompensated expropriation for purposes of Article 10.7.1 or a breach of any other obligation under Section A.

2. No claim that a restructuring of debt issued by a Party other than the United States breaches an obligation under Section A may be submitted to, or if already submitted continue in, arbitration under Section B if the restructuring is a negotiated restructuring at the time of submission, or becomes a negotiated restructuring after such submission, except for a claim that the restructuring violates Article 10.3 or 10.4.

3. Notwithstanding Article 10.16.3, and subject to paragraph 2 of this Annex, an investor of another Party may not submit a claim under Section B that a restructuring of debt issued by a Party other than the United States breaches an obligation under Section A (other than Article 10.3 or 10.4) unless 270 days have elapsed from the date of the events giving rise to the claim.

Limits of the US approach

These annexes can be seen as a step in the right direction given that parties to the agreement recognize that restructuring is a special case, yet they remain far from adequate for at least three reasons. First, as summarized in Box 3, CACs will not alleviate the possibility that bondholders will seek claims for restructuring. As indicated earlier, vulture funds and other holdouts can acquire a supermajority within a bond issuance and neutralize the bond issue and a 25 percent minority can still agree to litigate and arbitrate. Second, the definition of investment and the umbrella clauses allow for investor-state arbitration over treaty obligations regardless of whether such obligations are also covered by local law. Moreover, most restructurings are multi-issue restructurings and suffer from the aggregation problem described earlier. Again, collective action clauses only apply within a bond issue, not across multiple issues that are often bundled together in a restructuring.

Box 3:

Collective Action Clauses and IIAs: Three problems

1) Holdouts can acquire a supermajority within a bond issuance and neutralize the bond issue and a 25 percent minority can still agree to litigate and arbitrate.

2) ‘Definitions’ of investment and umbrella clauses allow for investor-state arbitration over treaty obligations regardless of whether such obligations are also covered by local law.

3) Many sovereign debt restructurings involve numerous bond issues and suffer from the agglomeration problem—collective action clauses do not apply across bond issuances, only within single bond issuances.

Secondly, economists and international financial institutions have repeatedly held that there are numerous circumstances when national treatment should be violated. Economic policy makers will often treat domestic bondholders and financial institutions differently during a crisis. Prioritizing domestic debt may be in order so as to revive a domestic financial system, provide liquidity and manage risk during a recovery (Gelpern and Setser, 2004, 796). Third, take-it-or-leave-it bond exchanges such as those that have occurred in Argentina would satisfy the 75 percent rule, but it is not clear that such swaps could justly be deemed as “negotiated”.

IV. Summary and Conclusion

This paper has shown that the regime for effective sovereign debt restructuring is very fragile and that the ability of holdout bondholders to use IIAs to reclaim the full value of their bonds could further undermine the development of an effective regime for sovereign debt restructuring.

Sovereign debt restructuring by definition changes the investment environment, reduces the value of an investment, allows a host government to 'take' back some of a loan, and often results in bonds held by domestic financial institutions and citizens being restructured differently than foreign bondholders. Therefore, when sovereign debt is defined and 'covered' by an IIA, numerous conflicts could arise between SDR and IIAs.

Argentina is thus far the only nation to be subject to IIA claims related to the nation's default and subsequent restructuring. Creative holdouts have sought ICSID claims because of that restructuring. As shown in Tables 1 and 2 of this paper, there are numerous nations that have a long history of default, which are experiencing debt-to-GDP ratios beyond what experts see as the threshold for triggering a debt crisis. If not immediately, at some point in the future debt default will certainly occur.

It now appears that investor-state claims through IIAs are now an avenue for holdout bondholders to attempt to claim the full value of their original investments. Such actions could accentuate collective action problems because private creditors may have a disincentive to vote to accept a restructuring, because those holders going to the ICSID have rushed to do so.

The Argentina situation is yet to be decided. Regardless of the decisions in those cases, international arbitral tribunals do not have a precedent as do many nation courts. For that reason, and because it has been strongly demonstrated that IIAs and SDR overlap, there remains a window for holdouts and vultures to take the international arbitration option through IIAs.

The United States is the only nation that includes explicit provisions regarding SDR in a small handful of its IIAs. While a step in the right direction, such provisions may prove to be inadequate in the event of an SDR. The annexes for SDR in the US IIAs do not permit SDR that violates national treatment, among other measures. It has long been held in the crisis management community that domestic interests need to be treated differently than foreign interests in response to a crisis, including in a restructuring. Such a spirit is clearly violated when US investors can resort to national treatment to file claims during a restructuring. Given that the United States is now the largest debtor nation and the value of that debt could drastically be affected in the event of a default or a stiff rise in interest rates, the US may be at a point when it too should reconsider how deep the coverage of sovereign debt in its IIAs should be.

The following is a handful of non-exclusive policy remedies that would enable IIAs to grant nations the policy space to conduct effective SDRs in the future:

- **Exclude sovereign debt from IIAs.** The exclusion of sovereign debt from "covered" investments under future treaties would relegate sovereign debt arbitration to national courts and to international financial bodies. Some IIAs already exclude sovereign debt, such as NAFTA and others. Argentina's new model BIT is reported to be moving in this direction as well.

- **Specify alternative choices of forum in bond contracts.** Clauses in bond contracts which note that conflicts over a particular bond must be exclusively decided in the national court that governs the bond issue could steer claims about SDR to other venues. The Permanent Court of Arbitration is currently working to devise sample language that may be to this effect.

- **Clarify that mitigating crises is "essential security".** It should be clarified that the Essential Security exceptions cover financial crises and that sovereign debt restructuring taken by host nations is 'self-judging' and of 'necessity'.

- **State-to-State dispute resolution for SDR and crisis-related instances** may be more prudent given that governments need to weigh a host of issues in such circumstances. States attempt to examine the economy-wide or public welfare effects of crises, whereas individual firms rationally look out for their own bottom line. Investor-state arbitration provision tips the cost-benefit upside down, giving power to the "losers" even when the gains to the winners of an orderly restructuring may far outweigh the costs to the losers.

This list of reforms is by no means a final one, nor is this paper the end of discussion on this subject. The global financial crisis that began in 2008 has triggered a discussion on the proper forums for preventing and mitigating financial crises. It is hoped that this paper contributes to that discussion.

Notes

[1] This paper draws on work conducted for UNCTAD's international investment agreements section. The author would like to thank Rachel Denae Thrasher and Elen Shrestha for valuable research assistance.

[2] "IIA" in this paper refers to any agreement with international investment provisions, therefore including both bi-lateral investment treaties (BITs) and free trade agreements (FTAs).

[3] Canada-Colombia FTA (2008), Article 838, footnote 11; Australia-Chile FTA (2008), Article 10.1(j)(iii); Azerbaijan-Croatia BIT (2007); Chile-Japan FTA (2007), Article 105. Recently revised model BITs of Colombia (2008) and Ghana (2009) exclude sovereign debt.

[4] Turkey Model BIT (2009), Article 1(1).

[5] *El Paso Energy Internacional Company vs. Argentina,* ICSID Case No ARB/03/15) Decision on Jurisdiction (27 April, 2006).

[6] *Continental Casualty vs. Argentina* dismissed most, but not all, of the claimant's claims on the basis of the essential security exception. The *Sempra Energy International v. the Argentine Republic* annulment panel annulled the Sempra award on the basis that it demonstrated a manifest excess of powers because, although it dealt with the issue of whether Argentina could justify its measures under customary international law it did not address whether the measures could be justified under the BIT security exception. The *CMS v. Argentina* annulment panel found a similar failing by the original tribunal to explain why it concluded that the essential security exception would not apply to the emergency measures in question, but declined to annul the award on the grounds that the failings did not rise to the level of a "manifest" excess of powers.

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