

## A Renewed Proposal for a Sovereign Debt Forum

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*This paper outlines a renewed proposal for a sovereign debt forum (SDF) that would provide a non-statutory neutral standing body to identify lessons from past episodes of sovereign debt distress, maintain information on sovereign debt, and assist in facilitating more predictable, transparent and timely treatments of sovereign debt during future episodes of distress.*

### **Background**

The recent experience with the Eurozone crisis and the restructuring of Greece's debt points to the ongoing need for further refinement of the international arrangements for the treatment of sovereign debt when servicing difficulties arise.

Voluntary restructurings undertaken in the 1990s and the early 2000s established a number of *de facto* norms and best practices for the treatment of sovereign debt to bilateral public creditors, multilateral institutions, bondholders, commercial creditors, secured creditors and trade-finance providers. Similarly, the discussion of the IMF's 2002 proposal to create a Sovereign Debt Restructuring Mechanism (SDRM) and efforts to include collective action clauses (CACs) in bond issuance provided an indication of the international community's shared appetite for the creation of a statutory approach to sovereign debt restructuring. Yet, the world lacks a standing body that can preserve the institutional memory of these episodes and, on the basis of the insights they have provided, facilitate smoother treatments of sovereign debt in the future by providing a venue for information discovery and negotiation.

The response to the present tensions in European debt markets, and the specter of further restructurings, makes plain the need for such a centre of expertise. The 2010 Deauville communiqué's call for the creation of a European SDRM elided over the difficulties that the IMF's SDRM proposal encountered some eight years prior. Important time was lost and uncertainties created during the gradual shift from this position and the eventual move to a protocol for the inclusion of CACs in future European sovereign bonds. Similarly, the organization of Greece's debt exchange was delayed by time needed to reach consensus on Greece's capacity to pay, a lack of clarity regarding the seniority of various public creditors and organizational challenges in aligning the interests of bondholders.

This paper outlines a renewed proposal for a sovereign debt forum (SDF) that would provide a standing body to identify lessons from past episodes of sovereign debt distress and assist in organizing better treatments of sovereign debt during future periods of servicing difficulties. The proposal builds on Richard Gitlin's 2003 proposal for an SDF and updates the proposal for present circumstances. An SDF may be seen as either an end in itself or a building block toward an eventual statutory SDRM. Either way, an SDF would fill an important gap by helping all constituencies in sovereign debt treatments reach agreement more efficiently and effectively.

This paper is intentionally parsimonious in its discussion: it is not intended to prescribe a particular structure or procedures for an SDF, but rather outline basic considerations that could catalyze sovereigns and their creditors to initiate discussions toward the creation of an SDF.

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## Core principles

**Non-statutory, non-institutional, un-codified.** The SDF would not be a multilateral institution: it would be a non-institution. It would not be created by statutory agreement, but rather by informal consensus. It would have no legal basis. Nevertheless, its work would be based on a number of agreed rules and principles to be outlined by its constituents and developed over time. This would facilitate open and informed decision making and more rapid conclusion of agreements on the appropriate responses to future episodes of sovereign debt distress. Existing precedents demonstrate the potential effectiveness of such an informal, rules-based standing body, but they also highlight the outstanding need for an inclusive venue with a balanced membership for the exchange of information and negotiation on treatments of sovereign debt.

**Fair, balanced and comprehensive representation.** Membership should be reasonably open and include all relevant constituents in the sovereign debt community: sovereigns, representatives of all forms of creditors, legal bodies, academics, et al. Standing member advisory groups would be encouraged to ensure constituents' interests can be represented quickly, fairly and clearly during times of debt distress.

**Stability, independence, neutrality and impartiality.** The SDF would require a small full-time standing staff of legal, financial and economic experts. It should be lean and minimalist in its construction. The SDF staff could be built through secondments from SDF members or *de novo* hires. The staff would be expected to act independently and impartially, with full detachment from any sponsoring institution. There are a number of options for financing the SDF's operations, *inter alia*: multi-year contributions from members; sale of IMF gold reserves; or a small fee assessed on bond issuers and/or purchasers. The SDF could be housed in a multilateral institution that is not itself a creditor (e.g., the BIS, which was originally charged with overseeing the resolution of international debt problems arising from German war reparations), in a major financial centre that would make meetings relatively easy for members to attend or in the capital of a country prepared to house the SDF at one of its governmental institutions.

**Comparability of treatment and fair burden sharing.** SDF members would commit to agree to processes that would ensure to the greatest extent possible comparability in the treatment of claims, limits on free riding, and follow-through on fair burden sharing. Advisory groups would be encouraged to review general procedures, specific negotiations and debt treatments to ensure that these principles are maintained in the face of potential collusion amongst subsets of constituents.

**Enhanced confidentiality and transparency.** SDF members would be expected to participate in its proceedings with an enhanced level of confidentiality in return for greater inter-member transparency. This would ensure support for and credibility in discussions of the debtor's macroeconomic programme, the adjustments the sovereign undertakes, the sovereign's capacity to pay, burden-sharing amongst creditors and the terms of any eventual debt treatment.

**Building on, but not bound by, precedent.** As a non-institution, the SDF's deliberations and eventual understandings would be recorded in minutes that would outline agreed actions and information. These minutes would have no legal standing and, hence, would never represent binding precedents. The SDF's nature would allow it to evolve rapidly and adjust to circumstance, while its professional staff would continue to inform SDF members of the lessons and insights of past experience.

**Subsidiarity.** No aspect of the SDF's work would be intended to replace, challenge or supersede the work of existing processes or institutions. For instance, SDF staff would not be charged to develop alternatives to members' analyses; instead, they would be tasked with reconciling competing data and analyses from the SDF's members in the discovery and negotiation process in order to help build balanced consensus on the needed adjustment and treatment of any relevant debt.

**Preservation of debtor's financial situation and quick return to sustainability.** All SDF procedures and actions should be designed with a view to preserving the financial situation of the sovereign under consideration and returning it to debt sustainability as quickly as possible.

### **Operating principles**

**Predictability.** SDF members should aim to design a collective, consistent process that would provide a standard template for the discussion of sovereign debt. This template would remove the guesswork that currently exists in initiating an open dialogue on a particular restructuring, but, as a non-statutory template, it would be applied flexibly on a case-by-case basis.

**Participation in a debt treatment.** Unless otherwise agreed, all relevant debt should be included in any restructuring in a manner that fairly represents each creditor group's position with respect to the sovereign. Cut-off dates on treatable debt may be considered to ensure that financing can continue to be provided to the debtor sovereign during discussions.

**Greater speed in execution.** By maintaining a standing body between episodes of sovereign debt distress, the SDF will enable the international system to respond to debtor and creditor needs more quickly than under the current *ad hoc* arrangements. Creditor and debtor representatives and advisory groups could be regularly updated and kept current. Structured processes could be initiated smoothly without reinventing the wheel for each distressed sovereign, while maintaining the flexibility to innovate on specific points.

**Enhanced data provision.** The SDF staff would assist in the rapid exchange of information amongst relevant parties following agreed protocols. SDF members may consider the creation of a standing debt registry to speed the identification of relevant interests in future debt discussions.

**Equal and concurrent information sharing.** All information would be shared amongst SDF members on an equal and concurrent basis given the commitment by members to strict confidentiality.

**Close consideration of financial-sector implications.** The Eurozone crisis has highlighted the close links between sovereigns and their banking systems. The SDF would highlight the implications of any possible debt treatment options for the financial sector.

**Voluntary stay of legal action.** SDF member creditors would agree to refrain from taking legal action or advancing any pending lawsuits during consideration of debt treatment provided the sovereign debtor is engaging in conduct, including good faith negotiations, consistent with membership in the SDF.

**Changes in bond documentation.** Consideration should be given to changing bond documentation, to the extent possible, to assist in implementation of the SDF's work, should this become necessary. This could include the insertion in bond documents of CACs requiring super majorities and by provisioning for the appointment of Trustees to assist in the early formation of committees prior to any default.

**Mediation.** The SDF may wish to consider involving nonbinding mediation and professional mediators in its standard processes to speed its work and ensure balanced outcomes.

**Retention of advisers.** SDF members would be empowered to retain professional legal, economic and financial advisers to support their participation and representation in the SDF on an equitable basis. SDF members could consider cross-subsidizing such technical assistance.

**Coordination with the Paris Club and other creditor committees.** The SDF would consult closely with existing representative and negotiating bodies the Paris Club and other creditor committees or representative bodies (e.g., the IIF) and share financial and economic analyses with regard to the sovereign debtor and possible debt treatments under consideration.

### **Next steps**

The creation of an SDF requires a small core of champions to advance its cause. A set of sovereigns, multilaterals, financial market participants, lawyers and economists would be ideally placed to advocate for an SDF. An SDF proposal could be advanced by members of the United Nations' General Assembly, the IMFC, the Financial Stability Board, the G20, the G24, the OECD and the IIF at the forthcoming regular meetings of these bodies—or through an invitation by Finance Minister(s) or Central Bank Governor(s) to an *ad hoc* stand-alone meeting of relevant parties.