Sovereign debt restructuring: UN takes a big step forward

By Bodo Ellmers (Eurodad)

The UN General Assembly has passed a landmark resolution that mandates the UN to create a "multilateral legal framework for sovereign debt restructuring". Promoted by the G77 countries and triggered by the aggressive vulture funds lawsuits against Argentina, this resolution could be a game changer for the way future debt crises are managed. First and foremost, it has shifted the forum for political debate away from the International Monetary Fund (IMF) towards the UN. However, shamefully the EU's vote was split over this crucial decision.

The path towards a real debt restructuring regime

It is certainly not news that the lack of a legal framework for sovereign debt restructuring – a state insolvency regime – has been a gaping hole in the international financial architecture. Prominent economists such as Joe Stiglitz, senior officials such as the IMF's former Deputy Director Anne O. Krueger and civil society campaigners have pointed again and again to this deficit.

However, governments from both debtor and creditor countries have so far been reluctant to put their political weight behind any meaningful initiative. The most relevant political commitment is probably the Monterrey Consensus' vague commitment to "consider" new debt workout mechanisms. The most relevant practical work, on the other hand, was the IMF's concept for a Sovereign Debt Restructuring Mechanism, which was shelved 11 years ago when it faced a political deadlock in the US and EU-dominated IMF Executive Board.

Never miss a good crisis

Remarkably, even the global financial crisis has not led to any meaningful political initiative by governments since 2008. It was civil society campaigns that kept the flame burning until the issue was picked up last year by the staff of international organisations, when the IMF issued a staff paper and the UN set up expert groups on new debt workout mechanisms at the UN Conference on Trade and Development (UNCTAD) and the UN Department of Economic and Social Affairs (DESA).

Then came the rather surreal vulture fund lawsuit of NML Capital vs Argentina at a provincial court in the US state of New York, and Judge Thomas Griesa's ruling to pay out the vultures in full. He interpreted the *pari passu* (equal treatment) clause in an extraordinary way and – probably as an unintended side-effect – kicked the whole contemporary sovereign debt restructuring non-regime into the dustbin.

Basically all the experts agree that debt restructurings as we knew them, which used to depend on the voluntary participation of creditors, simply don't work anymore if holdout creditors can achieve full payment through litigation. Restructuring decisions must be binding for all creditors and must be enforceable, hence the need for a multilateral legal framework.

Debtor countries drive the issue forward

Argentina's bold move of proposing a UN General Assembly (UNGA) Resolution – and successful mobilisation of the whole G77 as well as China to back this Resolution –

represents a long overdue political breakthrough. Finally, a critical mass of governments is willing to act. Most remarkably, while governance reform processes in the area of sovereign debt restructuring used to be dominated by creditor nations, or creditor-dominated institutions such as the IMF, debtor nations have now finally taken the driving seat. The Resolution was voted on yesterday, on 9 September 2014, and was passed with a large majority: 124 UN Member States voted in favour, 41 abstained, and only 11 voted against.

UN takes centre stage

When looking at the debate that took place around the vote, it becomes clear that any conflict was not so much about whether there should be a legal framework or not. Only the USA, one of the few 'no' voters, stated that this was counter-productive. For the other countries that spoke out, the question was more whether the UNGA should be mandated to take it on, or if this should be left to the IMF.

Developing countries made it clear that the UNGA, as the most inclusive forum, is the right place for political debate and decision-making to take place. Debt restructuring is simply too important to be left to the IMF, in whose board developing countries do not have a significant stake, and which, as a major creditor, would face an impossible conflict of interest.

All BRICS countries (Brazil, Russia, India, China and South Africa) voted in favour of the Resolution, another expression of their dissatisfaction with the stalled governance reform at the IMF. Of the five countries that have the largest share of voting rights and their own Executive Director at the IMF, four voted no (USA, Japan, Germany and the UK). The EU vote was split; the majority of European nations abstained. The EU speaker, Italy, stated the key reason for abstaining was that the G77 initiative was simply too rushed.

European governments' voting behaviour is shameful, as this continent is currently the most vulnerable to debt crises. As things stand, Europe is in most urgent need of a better state insolvency regime. However, at the next stages of this process, EU leaders will have the opportunity to engage constructively and to listen to their citizens. Ahead of the vote, a large coalition of European civil society organisations, including Eurodad, called on European governments to vote in favour of the Resolution. This might have helped to shift some European votes from 'no' to abstention.

The next steps

In any case, the G77's support was sufficient to help the Resolution pass. However, this represents just the beginning, not the end, of a process leading to a multilateral framework for sovereign debt restructurings. The next step will be that the UNGA decides on the modalities of the intergovernmental negotiations.

The character this new multilateral framework will take will be subject to political power plays in the future. For us as civil society organisations campaigning for just solutions to debt crises, it is key that a legal framework does not only make binding and enforceable decisions, but that it also reduces the human suffering that debt crises cause, and also addresses the question of illegitimate debts.

We therefore share the view of the UN Special Rapporteur on Debt and Human Rights that "*international human rights law should be considered applicable law in the context of debt restructurings*". On 25 September 2014, the UN Human Rights Council will vote on a

complementary resolution that places debt restructurings firmly in the context of human rights. We hope that Europe will take a more constructive position when it gets its second chance later this month.

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