Testimony of

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Examining Belt and Road: The Lending Practices of the People's Republic of China and Impact on the International Debt Architecture

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I. Chinese Lending in the Broader Context of Global Debt

Chairman Himes, Ranking Member Hill, and Members of the Subcommittee, thank you for the opportunity to testify on issues of Chinese lending practices and the international debt architecture.

To begin, I want to emphasize that the United States today *faces a turning point in the international framework* for dealing with sovereign debt problems. I say this for two reasons: First, government debt distress resulting from the pandemic is likely to be a multi-year issue. This means that the international community is currently paying closer attention to these problems than usual, and there may be greater appetite for putting in place necessary changes. Second, the global balance of economic power is likely to shift in the coming decades. The U.S. has been the central actor in international finance for over fifty years. This will not necessarily be the case forever. This means that the U.S. should act now to make sure that its values are reflected in lending and restructuring norms and practices going forward.

Much of my research focuses on problems associated with sovereign debt—the funds that countries borrow from other governments, from international organizations, and from private creditors—particularly when such debt becomes unsustainable or appears illegitimate. As such, the bulk of this written testimony details the financial challenges resulting from the pandemic, highlights emergency measures thus far, and argues for an explicitly multi-pronged approach to improving the global debt framework.

However, to introduce these broader issues, I want to emphasize three ways that Chinese lending practices fit into the story.

First, the problematic elements of Chinese lending practices—which are noted in the Hearing Memorandum and well-detailed in recent research by several of my fellow witnesses[1]—do not exist in a vacuum. These practices tend to reflect and amplify more general and endemic issues in the international debt arena, including: (i) a lack of transparency in loan amounts and terms; (ii) insufficient concern for whether debt actually benefits a country's underlying population, as opposed to its ruling elites and creditors; and (iii) a lack of comprehensive creditor participation. Chinese lending practices appear to take each of these defects to the extreme. Still, the best way to constrain problematic practices by *one* country or creditor is to establish norms and practices that are relevant to *all* countries or creditors. Otherwise, efforts to constrain particularly bad actors are unlikely to stick. This has been one of the key guiding principles of the post-World War II global order, and it remains essential. Therefore, any efforts to improve Chinese lending practices should be part of broader improvements to the international financial architecture.

Second, to the extent that the U.S. is concerned about China's increasing role in international capital flows, it needs to take steps now to cement American interests and values in international debt. These include transparency and accountability, public benefit, and collaborative and comprehensive participation in international efforts.

- This path, as with any long-term plan, begins with an initial step: The U.S. should start by committing to *support a swift, stable, and equitable recovery* from the pandemic, in both its public health and its financial dimensions. Such a commitment, made in conjunction with other countries and international organizations, will be essential to a full global economic recovery. It will also help to forestall follow-on consequences, such as political instability and disruptive migration patterns.
- In the medium-term, the U.S. should support the *implementation of widely-accepted sovereign lending and restructuring principles along multiple tracks*. This would include contract term improvements, domestic legislation within the U.S. and elsewhere, and international initiatives to support fair, comprehensive, and equitable restructurings. This matters regardless of whether creditors are private investors or government actors, especially when the line between these categories is starting to blur.
- To facilitate ongoing long-term progress, the U.S. should *consider the establishment of an independent authority* that could help coordinate improvements across these multiple tracks. Particularly given the potential of long-run changes in the global balance of power, an independent authority committed to broadly acknowledged principles of responsible lending, borrowing, and restructuring could be exceedingly helpful in the coming decades.

[1] Anna Gelpern et al., *How China Lends: A Rare Look into 100 Debt Contracts with Foreign Governments*, CENTER FOR GLOBAL DEVELOPMENT (March 2021).

My third and final introductory point involves corruption and the mismatched financial incentives present in a number of borrowing countries. Greater tolerance of corruption appears to be a problem in some Chinese lending contracts, and the decisions made by borrowing country ruling elites may not always reflect the interests of their citizens. Again, this issue implicates broader and longstanding dynamics in international finance. Right now, I believe it means two key things:

- First, debtor country elites may have made poor borrowing choices, but *we should not punish the populations* of those countries when dealing with the pandemic and the related sovereign debt crisis. While it makes sense to promote transparency and responsible lending now, these countries' populations will suffer the most from international financial inaction.
- Second, *U.S. and other international actors must take the lead in implementing and modeling new norms and practices*. It is sometimes said that debtor countries are primarily responsible for transparency and other reforms. But corrupt elites in these countries may prefer to foot drag, while the countries' citizens often do not have the information or the power to take action. Given the practical dynamics, power imbalances, and information asymmetries on the ground, more needs to be done by creditors—whether bilateral, multilateral, or private. As such, U.S. support for strong creditor-focused rules on transparency and responsible lending could, over time, help undermine the internal dynamics of corruption and misaligned incentives in sovereign borrowers.

Before continuing, I should note that meaningful support for principles like transparency, sustainability, public benefit, and comprehensive restructuring may not be fully embraced by all U.S. stakeholders. In particular, a number of private creditors that *also* have benefited from gaps in the international framework are American entities or affiliates. If the U.S. is serious about curbing problematic debt practices—such as those exhibited in Chinese lending contracts—it will have to make that commitment clear to domestic constituencies as well.

II. An Overview of the Remaining Arguments

The remainder of this written testimony focuses on the broader global architecture and proceeds in several steps.[2] I first note the country financial difficulties generated by the COVID-19 pandemic and the ways that national responses will likely have long-term financial impacts that make states more vulnerable to debt distress, particularly in the developing world. I also delineate how any restructuring efforts that might result from such distress would have to contend with longstanding problems in the international framework relevant to sovereign debt. These difficulties have become more complex in

[2] The following sections of my written testimony are based on a forthcoming essay, *The Time Has Come for Disaggregated Sovereign Bankruptcy*, EMORY BANKRUPTCY DEVELOPMENTS JOURNAL (2021). I thank the student editors of that journal, along with the participants at a related March 2021 workshop, for their feedback on previous versions of these arguments. These sections also draw on research conducted as part of a 2020 consultancy for the United Nations Conference on Trade and Development (UNCTAD) on constructing a post-COVID-19 international debt architecture.

recent years, as demonstrated by the Chinese lending practices at the center of this hearing.

I then mention several initiatives that have been put forward to address the pandemic-related financial crisis, formulated by policymakers and scholars to deal with problems already present or likely to emerge. These mechanisms should, if fully implemented, help to address countries' financial distress in the short-to-medium term, and they deserve strong Congressional support. However, mixed reaction to such proposals has made the existing gaps in the international financial architecture even more apparent. If anything, the recent crisis suggests that—in addition to short-term, emergency-focused proposals—the need for a more rational global debt restructuring platform remains. As such, the fact of the ongoing and fast-moving public health and economic situation does not mean that we should exclusively focus on emergency-level solutions. Indeed, it remains imperative to harness the crisis energy to move in the opposite direction—toward putting in place longer-term institutions that will be ready for the next crisis and, perhaps, make that next crisis less likely or less intense.

I further argue that the U.S. should support a policy framework in which multiple processes at varying levels simultaneously operationalize a shared set of sovereign debt resolution principles and commitments. Although numerous actors have called for a full-blown multilateral treaty-based restructuring regime, most famously the International Monetary Fund (IMF) in the early 2000s,[3] such proposals have thus far met with resistance. Improvements in market-based, contractually grounded solutions have taken some of the pressure off, but still leave many problems un- or under-addressed. Although the narrative of voluntary, market-based advancements *versus* 'involuntary' (or perhaps less voluntary) international statutory options offers a neatly binary conceptual package, it is well past time to abandon such overly simplistic framing—especially given the rise of mixed and hybrid creditor models, as in the Chinese lending examples. Improvements in the contractual realm, in the multilateral arena, and at the level of domestic legislation should be conceived of as complementary rather than competitive. Or, if these arenas may sometimes compete, we should understand this as the type of healthy competition that ultimately results in better outcomes; there is no need to champion one approach over another.

To be clear, the explicit embrace of a multi-pronged framework for implementing debt resolution principles does not suggest that any such framework should be disorganized or free-floating. Instead, I suggest that ideally the U.S. would also support the establishment of an international consultative body, purpose-built to recommend, coordinate, and facilitate steady, incremental progress in the architecture for dealing with sovereign debt across multiple vectors.[4] Instead of a full-blown multilateral body with

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[3] ANNE O. KRUEGER, IMF, A NEW APPROACH TO SOVEREIGN DEBT RESTRUCTURING 31 (2002), https://www.imf.org/external/pubs/ft/exrp/sdrm/eng/sdrm.pdf.

[4] In this, it echoes earlier and ongoing calls for a relatively modest but still internationally relevant forum. For example, the United Nations Conference on Trade and Development (UNCTAD) called for the development of an expert-based global debt authority in the first half of 2020; such a proposal, on which I have consulted, remains under development. In a somewhat similar vein, though more circumscribed, a

court-like adjudicative functions, a more pragmatically achievable and nimble organization could be proposed and implemented in order to serve as a focal point for ongoing activities designed to improve how the global community collectively deals with debt in the short, medium, and long term. Although any such organization may not be able to deal with the immediate financial fallout of the COVID-19 pandemic, advocates of more rational debt restructuring should not waste the sense of urgency present in the current crisis. We need to take steps now to adopt an infrastructure that would make future debt crises less severe and perhaps less likely—even when the spotlights are directed elsewhere.

(1) The COVID-19 pandemic and subsequent country responses have resulted in increased financial vulnerability and raised the risk of an international debt crisis.

Although the economic fallout of the COVID-19 pandemic has been well documented, several elements are especially important in thinking through its potential ramifications for international debtor-creditor relations. To begin with, factors that have led to decreased revenue and foreign exchange may have a lingering impact in the sovereign debt space. The drop in key export commodity prices for many countries has had a significant blow, along with the fall in global trade generally.[5] The near freeze in the international tourism industry dried up a key source of foreign exchange in certain regions.[6] And, for some countries, the significant decline in remittance flows from overseas workers, resulting from economic stagnation in remittance source countries, has constituted a significant hardship as well.[7] Given that many countries continue to denominate their external debt in foreign currency over which they have no control, these factors put together have meant that their capacity to service such debt has plummeted.

In addition, government expenditures have tended to rise steeply as a result of the pandemic, exacerbating the problems caused by the increased costs of international debt servicing, particularly in terms of certain local currencies.[8] The healthcare costs involved in addressing the crisis have been significant, especially where preventative measures

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recent G30 Report called for a consultative mechanism attached to the G20's Common Framework. G30, *Sovereign Debt and Financing for Recovery After the COVID-19 Shock: Next Steps to Build a Better Architecture* 3, 23 (May 2021).

[5] *See, e.g.,* Constantino Hevia & Andy Neumeyer, *A Perfect Storm: COVID-19 in Emerging Economies*, *in* COVID-19 IN DEVELOPING ECONOMIES 25, 25, 31 (Simeon Djankov & Ugo Panizza eds., 2020) (arguing that "developing countries will be harder hit by the pandemic than advanced economies").

[6] *See* Simeon Djankov & Ugo Panizza, *Developing Economies After COVID-19: An Introduction*, *in* COVID-19 IN DEVELOPING ECONOMIES, 8, 9 (2020) (stating that, throughout the COVID-19 pandemic, developing countries are facing "large negative economic shocks" linked, in part, to collapses in their respective tourist industries).

[7] *See* Hevia & Neumeyer, *supra*, at 25, 31 (discussing the negative economic impacts of COVID-19 in countries with emerging economies and arguing that a COVID-induced increase in unemployment in countries with advanced economies "will reduce immigrant remittances to their home countries").

[8] *See* Djankov & Panizza, *supra*, at 8, 20 (discussing how "local currency bonds issued by emerging market countries have been hit particularly hard by the Covid-19 pandemic" as government expenditures and debts continue to rise).

proved insufficient or failed to gain wide adherence.[9] Expenditures on unemployment have increased as many people struggled with pandemic-driven economic dislocation and turned to the state for assistance.[10] In countries with a significant reliance on global trade for key commodities, food security and related issues emerged as a real concern.[11] The World Bank estimated that 150 million people globally had been placed at risk of extreme poverty as a result of the pandemic, with global extreme poverty expected to rise for the first time in twenty years.[12]

Countries rightfully took measures to address this risk, and in some cases have turned to new debt as a cushion, leading to historically high public debt levels.[13] Particularly given low interest rates and increased liquidity, private entities have also partaken in the liquidity buffet, further fueling the massive rise in overall global debt levels.[14] Although such private entity debt does not directly impact sovereign state balance sheets, at least for now, in certain industries and for certain countries such debt may still end up as sovereign obligations if states are faced with the risk of struggling financial, infrastructure, or other systemic sectors down the line. In short, it is entirely understandable that countries and private actors alike have sought to mitigate the effects of the pandemic in any way possible. However, the aggregated impact of these national responses and private decisions may have long-term financial ramifications that make countries more vulnerable to debt distress.

It is important to point out that countries' (and individuals') exposure to pandemic-related challenges has been incredibly uneven, with World Bank President David Malpass warning of an "inequality pandemic" coming on the heels of the public health crisis.[15] States faced the crisis from different starting points, including in terms of basic economic

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[9] *See* Sarah M. Bartsch et al., *The Potential Health Care Costs and Resource Use Associated with COVID-19 in the United States*, 39 HEALTH AFFAIRS 927, 934 (2020) (discussing the causes and effects of health care spending in the United States during the COVID-19 pandemic).

[10] *See* David Laborde, Will Martin & Rob Vos, *Poverty and Food Insecurity Could Grow Dramatically as COVID-19 Spreads*, IFPRI BLOG: RESEARCH POST (Apr. 16, 2020), https://www.ifpri.org/blog/poverty-and-food-insecurity-could-grow-dramatically-covid-19-spreads (explaining how mandatory lockdowns and business closures caused unemployment to skyrocket around the world during the COVID-19 pandemic).

[11] *Id.*

[12] Press Release, World Bank, COVID-19 to Add as Many as 150 Million Extreme Poor by 2021 (Oct. 7, 2020), (available at https://www.worldbank.org/en/news/press-release/2020/10/07/covid-19-to-add-as-many-as-150-million-extreme-poor-by-2021#:~:text=The%20COVID%2D19%20pandemic%20is,severity%20of%20the%20economic%20contraction).

[13] *See* John Letzing, *Countries are Piling on Record Amounts of Debt Amid COVID-19. Here's What That Means*, WORLD ECON. FORUM (Nov. 5, 2020), https://www.weforum.org/agenda/2020/11/covid-19-has-countries-borrowing-money-just-about-as-quickly-as-they-can-print-it/.

[14] *See* Liz Capo McCormick et al., *The Covid-19 Pandemic Has Added $19.5 Trillion to Global Debt: Here Are Reasons to Be Grateful—and Worried*, BLOOMBERG, https://www.bloomberg.com/graphics/2021-coronavirus-global-debt/ (using data and charts to demonstrate how an increase in private debt that occurred in 2020 contributed to an overall rise in global debt amidst the COVID-19 pandemic).

[15] *See* David Malpass, President, World Bank Group, Speech at Frankfurt School of Finance and Management: Reversing the Inequality Pandemic (Oct. 5, 2020) (transcript available at https://www.worldbank.org/en/news/speech/2020/10/05/reversing-the-inequality-pandemic-speech-by-world-bank-group-president-david-malpass)

strength and healthcare capacity. Furthermore, countries had different external borrowing costs and levels of reliance on international transactions to begin with.[16] This meant, and continues to mean, that the long-term economic consequences of the COVID-19 pandemic, including the possibility of debt crises, will inevitably vary considerably across countries. Particularly for some, the risk of sovereign debt distress resulting from COVID-19 is real, and in certain situations already present, and it may prove long-lasting.[17]

(2) Long-term trends and the insufficiency of the existing sovereign debt architecture will compound the problems of any coming sovereign debt crisis.

What kind of financial architecture has been in place for dealing with debt crises when they appear and especially when they linger? While I discuss below the shorter-term international emergency measures taken and proposed in response to the pandemic, the background prognosis for longer-running crises is not especially encouraging. In particular, a brief review of the key challenges and recent trends underscores why debt crises and restructuring episodes may prove tenacious, especially once the headlines and emergency funds have moved on.

To begin with, the broad range of creditors, lending instruments, and local and international forums implicated in the sovereign arena has long fragmented this realm of debtor-creditor relations. Although official sector negotiations and private sector restructurings generally follow well-trodden pathways, with principles of comparability of treatment linking the two areas, issues of inequitable creditor outcomes and inconsistent legal interpretations remain. And recent trends have only exacerbated this fragmentation, particularly given the expanded range of creditors and financial instruments now implicated in sovereign debt. Whereas in the 1990s and through the early 2000s, sovereign bonds were by far the dominant private instrument, other forms of commercial lending have become more common, as have loans from hybrid public-private investors such as sovereign wealth funds and state-owned enterprises.[18] This fragmentation is further exacerbated by the steep increase since the Global Financial Crisis in developing countries' private indebtedness, which constitutes another important vulnerability and complication.[19] In addition, there has been a rise in collateralized lending,[20] central to Chinese loan contracts, in which creditors have recourse to specific assets in the event of nonpayment. Those assets thus may be removed from the general pool available to repay creditors in any broader restructuring. And, of course, among

[16] *See, e.g.,* Hevia & Neumeyer, *supra*, at 25, 31 (discussing the varying financial circumstances facing different countries before and during the COVID-19 pandemic).
[17] *See generally* Ben Parker, *The Debt Crisis Looming for Poor Countries*, THE NEW HUMANITARIAN (Oct. 8, 2020), https://www.thenewhumanitarian.org/analysis/2020/10/08/pandemic-debt-crisis-looms ("The World Bank and the IMF list Mozambique as one of eight countries in 'debt distress', while 28 others were considered at 'high risk' as of June.")
[18] For an overview of recent trends, see, for example, IMF, *The Evolution of Public Debt Vulnerabilities in Lower Income Economies*, IMF Policy Paper, Feb. 2020.
[19] U.N. Conf. Trade and Dev., Rep. on Financing a Global Green New Deal, at 74–83 (2019).
[20] *See, e.g.*, IMF and World Bank, *Collateralized Transactions: Key Considerations for Public Lenders and Borrowers*, January 24, 2020.

bilateral and semi-official creditors, a number of non-Paris Club creditor countries, especially China, have become dominant, particularly in certain regions. This has made it even more challenging to achieve a comprehensive restructuring agreement that includes all creditors and is likely to provide sufficient and long-lasting relief consistent with sustainable and equitable development. Overall, these shifts have resulted in a complex context for any post-pandemic debt restructuring to come.

Indeed, and perhaps unsurprisingly, the past debt restructurings that have emerged from this framework tend to be "too little, too late"—providing countries with tardy and insufficient relief that undermines their return to economic health. Sovereign borrower states often delay the decision to restructure due to a range of factors that may include lack of information, electoral concerns, and worries about financial contagion. Creditors' reluctance to face the possibility of losses, and the difficulty of dealing with collective action problems, mean that incentive problems exist on both sides. Creditors and international actors may also express moral hazard concerns in explaining resistance, and certain creditors have asserted that voluntary restructuring conflicts with their obligations to shareholders, investors, or regulators.[21] And, once a decision to restructure is made, insufficiently deep restructurings can result from overly optimistic growth forecasts or concerns about reputation. Although debt restructurings are almost inevitably difficult and politically tense, any perceptions that they are also non-transparent, inequitable, and illegitimate can intensify civil strife and thus make them even more disruptive. Such second-order disruption can exacerbate the distress already generated by the restructuring itself.[22]

Although progress toward more comprehensive and equitable restructuring has been made through both contractual developments and, in some cases, domestic legislative action, such progress remains highly incomplete. The International Capital Markets Association (ICMA) developed a model clause in 2014 that offers a menu of alternative voting procedures, including a "single limb" option under which a single aggregated vote can be taken across all applicable bonds.[23] Although the use of such clauses has become dominant (though not universal) in U.K. and New York law bonds, there has been no uptake in other geographical regions.[24] These other regions are admittedly currently far

[21] *See, e.g.*, Inst. for Int'l Fin., *Terms of Reference for Potential Private Sector Participation in the G20/Paris Club Debt Suspension Initiative* (May 28, 2020), https://www.iif.com/Portals/0/Files/content/Regulatory/Voluntary%20Private%20Sector%20Terms%20of%20Reference%20for%20DSSI_vf.pdf.

[22] For more on the challenge and potential benefit of legitimate restructurings, and on how 'legitimacy' might be understood in the sovereign debt context, see Odette Lienau, *The Challenge of Legitimacy in Sovereign Debt Restructuring*, 57 HARV. INT'L L. J., 151, 154–55 (2016).

[23] In addition, the model clause offers a clarification that *pari passu* language does not provide holdout creditors with ratable payment, which was at issue in the long-running Argentina litigation under New York Law. Natalie A. Turchi, *Restructuring a Sovereign Bond Pari Passu Work-Around: Can Holdout Creditors Ever Have Equal Treatment?*, 83 FORDHAM L. REV. 2171, 2208 (2015).

[24] IMF, *Fourth Progress Report on Inclusion of Enhanced Contractual Provisions in International Sovereign Bond Contracts*, 4–5 (Mar. 6, 2019), https://www.imf.org/en/Publications/Policy-Papers/Issues/2019/03/21/Fourth-Progress-Report-on-Inclusion-of-Enhanced-Contractual-Provisions-in-International-46671.

less significant in terms of bond issuances, but they do include financial centers likely to become more prominent over time. And although the outstanding global debt stock without these enhanced Collective Action Clauses (CACs) should decline over time, it remains substantial.[25]

In addition, part of the risk with contract-based innovations is that they may be undone in subsequent rounds of negotiation. Although the enhanced CACs seem well established, the August 2020 restructuring process for Argentina's bonds included a creditor proposal to leave out the enhanced CACs in the future restructured bonds.[26] In short, although contractually based progress certainly helps, it is hardly foolproof—particularly when coverage is incomplete, and when it is not backed up by complementary initiatives supporting collective action. In terms of statutory efforts, several jurisdictions, most notably the UK and Belgium, have passed domestic legislation designed to address holdout creditors and protect market infrastructure (such as payment systems) from collection efforts. However, this approach is hardly widespread. Overall, the background architecture available to deal with any post-pandemic sovereign debt crisis that might linger does not look especially promising.

(3) The U.S. should actively support and strengthen measures currently under discussion to deal with the immediate risk of financial crisis, while also looking beyond the short term.

In light of this unpromising background, a number of proposals have been taken up at the international level thus far. Unsurprisingly and appropriately, the key measures have tended to focus heavily on dealing with the immediate emergency rather than on efforts to prevent and ease the cycle of sovereign debt crises more generally. These projects have relieved some of the immediate pressure, and the U.S. should take the lead in strengthening and extending these international initiatives. However, these initiatives should also be understood as stepping stones to longer term efforts to improve the sovereign debt architecture.

The core crisis response has centered around the G20 Debt Service Suspension Initiative (DSSI), first proposed and adopted in April 2020 and currently extended until December 2021 and expanded through the G20's November 2020 announcement of the Common Framework for Debt Treatments beyond DSSI (Common Framework) for situations

[25] *Id.* at 7.
[26] *See, e.g.,* Joseph Stiglitz, Robert Howse & Anne-Marie Slaughter, *Sovereign Creditors Must Not Rewrite the Rules During the Pandemic*, PROJECT SYNDICATE (July 9, 2020), https://www.project-syndicate.org/commentary/argentina-sovereign-debt-rules-creditors-by-joseph-e-stiglitz-et-al-2020-07?barrier=accesspaylog#:~:text=Sovereign%20Creditors%20Must%20Not%20Rewrite%20the%20Rules%20During%20the%20Pandemic,-Jul%209%2C%202020&text=In%20the%20circumstances%20caused%20by,face%20risks%20of%20sovereign%20default; Lee Buchheit, Leland Goss & Brad Setser, Discussion at Virtual Panel: Collective Action Clauses: Argentina, Ecuador, and Their Future at the Official Monetary and Fin. Inst. Forum (Sept. 1, 2020), https://www.youtube.com/watch?v=w88s4aJmK_c (discussing CAC use in the recent restructurings of Ecuador and Argentina).

requiring more extensive workouts.[28] The basic DSSI approach allowed a range of Lower Income Countries (LICs) to request suspension of debt payments to bilateral official creditors (i.e. creditor countries). This did not restructure debt, but rather temporarily suspended payment, with interest accruing; it also did not include suspension of payments to private creditors or to official multilateral creditors like the IMF and World Bank. The Common Framework allows for restructuring in more extreme situations, but still applies only to the same limited set of countries—which is much narrower than the range of countries likely to face debt distress. It does mandate an IMF Program and, as an improvement, requires participating countries to request comparability of treatment from private creditors, although exceptions may still be possible.[29]

To further ease the stress on countries, the G20 economies have also recently agreed to a new allocation of IMF Special Drawing Rights (SDRs)—a key IMF mechanism for injecting liquidity into the global economy.[30] This could alleviate some of the pressure for struggling economies, and could also pave the way for the adoption of additional proposals to address countries' longer-run debt burdens, such as voluntary debt buybacks and debt swaps, perhaps through the establishment of new central credit facilities.[31] The current structure of SDR allocations means that they may not be sufficient or sufficiently targeted, given that they are currently distributed according to member country IMF voting shares. As such, further steps should be taken to recycle any allocations to where they will be most useful.[32] In short, although these initiatives deserve support, liquidity

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[28] G20, *supra*; *see also* FITCH RATINGS, THE G20 COMMON FRAMEWORK AND PRIVATE-SECTOR RESTRUCTURING (Feb. 16, 2021), https://www.fitchratings.com/research/sovereigns/g20-common-framework-private-sector-debt-restructuring-16-02-2021.

[29] G20, *supra*; FITCH RATINGS, *supra*.

[30] *See* Reuters Staff, *Big Economies Agree to Boost IMF Funding, Georgieva Says*, REUTERS (Mar. 3, 2021), https://www.reuters.com/article/africa-imf/update-2-big-economies-agree-to-boost-imf-funding-georgieva-says-idUSL5N2L056W. The last allocation of SDRs happened in 2009 in response to the Global Financial Crisis. For those seeking more general background, the IMF semi-regularly updates an SDR Q&A. IMF, *Questions and Answers on Special Drawing Rights* (Feb. 26, 2021), https://www.imf.org/en/About/FAQ/special-drawing-right.

[31] *See, e.g.*, Patrick Bolton et al., *How to Prevent a Sovereign Debt Disaster: A Relief Plan for Emerging Markets*, FOR. AFF. (June 4, 2020), https://www.foreignaffairs.com/articles/world/2020-06-04/how-prevent-sovereign-debt-disaster (recommending that debtor interest payments be routed to a central credit facility in which creditors could receive a stake; also discussed and elaborated in related publications); Matthew Fisher & Adnan Mazarei, *A Possible IMF Pandemic Support Facility for Emerging-Market Countries*, PETERSON INST. FOR INT'L ECON. 1, 1 (July 2020), https://www.piie.com/sites/default/files/documents/pb20-11.pdf (advocating the establishment of a specialized IMF Pandemic Support Facility); Hamid Rashid & Joseph Stiglitz, *Averting Catastrophic Debt Crisis in Developing Countries*, CTR. ECON. POL'Y RSCH. 1, 3 (2020), https://cepr.org/active/publications/policy_insights/viewpi.php?pino=104 (recommending a multilateral buyback facility that could be managed through the IMF's New Arrangements to Borrow function).

[32] *See, e.g.,* Hannah Wanjie Ryder & Gyude Moore, Commentary, *When Special Drawing Rights Aren't So Special*, PROJECT SYNDICATE (March 1, 2021), https://www.project-syndicate.org/commentary/how-sdrs-can-help-developing-countries-by-hannah-ryder-1-and-gyude-moore-2021-03. In her March 3, 2021 address to the G20, IMF Managing Director Kristalina Georgieva suggested ways to redirect the liquidity more to countries in need, and the ultimate IMF proposal for the allocation will presumably include some of these elements. Reuters Staff, *supra* note 35. The final allocation would then have to be approved by major states, most notably the United States, though Treasury Secretary Janet Yellen and other key officials

injections, temporary debt suspensions, and only tentative efforts at restructuring may not be enough to handle the scale of debt distress that countries face.

The last year has also highlighted the degree to which even urgent circumstances and emergency measures are unable to overcome the longstanding problems of the sovereign debt arena. The mixed participation of Chinese state-affiliated creditors in debt relief efforts is disheartening.[33] And the highly reluctant (or non-existent) participation of private creditors further means that countries will likely receive less restructuring than they need. Toward the beginning of the pandemic, private sector creditors were "called upon" to participate in debt suspensions in line with the DSSI, but declined to respond to the call despite the exigent pandemic situation.[34] The Institute for International Finance (IIF), a key international private creditor industry group, issued an unencouraging statement in May 2020 indicating that any private sector participation should be entirely voluntary, net present value neutral, and arranged on a creditor-by-creditor (or at least debt contract-by-debt contract) basis.[35] A September 2020 letter further emphasized commitment to market solutions, sanctity of contracts, resistance to top-down approaches, and the risks of losing private market access.[36] This stance means that public sector forbearance could indirectly support the ongoing repayment of non-participating private sector loans. The Common Framework's comparability of treatment requirement will help, and the U.S. should commit to implementing this requirement. Ensuring that private creditors, including those based in the U.S., fully participate in any debt restructuring may encourage official sector or state-affiliated creditors to participate in relief efforts themselves. Otherwise, these and similar collective action problems could undermine the ultimate scale of the relief, rendering it less ameliorative than the current situation warrants.[37]

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have signaled their support. Andrea Shalal & David Lawder, *Yellen Backs New Allocation of IMF's SDR Currency to Help Poor Nations*, REUTERS (Feb. 25, 2021), https://www.reuters.com/article/us-g20-usa/yellen-backs-new-allocation-of-imfs-sdr-currency-to-help-poor-nations-idUSKBN2AP1U0.

[33] *See* G30, *supra.*

[34] Andrea Shalal, *Pandemic Debt Relief Needs Private-Sector Involvement: IIF*, REUTERS (Apr. 9, 2020), https://www.reuters.com/article/us-health-coronavirus-debt-iif/pandemic-debt-relief-needs-private-sector-involvement-iif-idUSKCN21R2L6.

[35] Inst. for Int'l Fin., *Terms of Reference for Potential Private Sector Participation in the G20/Paris Club Debt Suspension Initiative* (May 28, 2020), https://www.iif.com/Portals/0/Files/content/Regulatory/Voluntary%20Private%20Sector%20Terms%20of%20Reference%20for%20DSSI_vf.pdf.

[36] Letter from Timothy Adams, IIF President and CEO, to Mohammed Al-Jadaan, Minister of Fin., Kingdom of Saudi Arabia (Sept. 22, 2020) (on file with author).

[37] For civil society group Eurodad's assessment of the first iteration of the DSSI, *see* IOLANDA FRESNILLO, THE G20 DEBT SERVICE SUSPENSION INITIATIVE: DRAINING OUT THE TITANIC WITH A BUCKET? 1, 2–23 (Oct. 14, 2020), https://d3n8a8pro7vhmx.cloudfront.net/eurodad/pages/768/attachments/original/1610355046/DSSI-briefing-final.pdf?1610355046. Eurodad and other civil society groups have held a similarly dim view of the 'Common Framework' extension. *See* Julia Ravenscroft, *Reaction to G20 Common Framework for Debt Treatments: Designed By and For Creditors*, EURODAD (Nov. 13, 2020), https://www.eurodad.org/reaction_to_g20_common_framework_for_debt_treatments_designed_by_and_for_creditors.

Setting aside the lukewarm reaction by some key actors to these initiatives, they are a start, and these and other circulating ideas deserve further consideration and extension. Unfortunately, one drawback of the thinking and writing inspired by any emergency is that the intensive discussion sometimes lasts only as long as the crisis itself. If past emergency experiences are any indication, not all of the worthy measures proposed will be taken up. The international policy and scholarly community may put aside these ideas once the current moment has passed, shelving them indefinitely on working paper websites or online article repositories.

(4) The U.S. should commit to a multi-level process for improving the international debt architecture in the long term.

Although the attention paid to immediate crisis alleviation is entirely understandable, the U.S. would be short-sighted to focus exclusively on emergency solutions. The problems of creditor free-riding and insufficient relief remain, even in a situation widely acknowledged to be urgent. Recent circumstances have also highlighted the increasing complexity of the sovereign debt area, relative to previous decades—the multiplicity of debt instruments, the varied institutional forms of investors, the geographical spread of creditors, and the lack of transparency in all the above. The well-known statement that one should "never waste a crisis" applies with full force to the current moment. Before the energy and attention dissipate, it makes sense to set the foundations to deal more proactively with the next international debt crisis, if not avert it altogether. In particular, the U.S. *should commit to a framework by which multiple processes at varying levels simultaneously support or instantiate a shared set of sovereign debt resolution principles and commitments*.

One threshold question that might arise here is: why work across multiple tracks? Would it not be better to recommit to a more centralized and maximalist restructuring framework, perhaps revitalizing proposals from an earlier era, at least to the extent that the willpower exists for such an endeavor? Or maybe more can be done with market-based solutions, given sufficient global attention? Perhaps. But one of the complications in the sovereign debt arena—as in so many areas of policymaking—is that the key problems, actors, and plausible solutions change over time. The Chinese mixed-form creditor entities and lending practices at the center of discussion today offer a good example of this dynamic. Such complexity and fluidity can make proposals that once seemed appropriate appear outdated farther down the line. They also suggest that the occasionally binary nature of discussions in sovereign debt policy-making—market-based advancements *versus* statutory options—should be set aside. Under the circumstances of complexity, fluidity, and uncertainty, which do not appear likely to change in the foreseeable future, it is hard to know which debt instruments or actors will be implicated and thus which approach will be needed at any given moment. In this world, multiplicity should perhaps be understood not as a defect or a compromised second-best but rather as a *virtue*.

If this is the case, what are the 'multiple processes at varying levels' and 'principles and commitments' that underpin such a vision? To begin with, the basic principles and

commitments in this arena should not be very controversial; there is no need to reinvent the wheel here. We need to improve the effectiveness, efficiency, and legitimacy of the sovereign debt market and of debt restructuring events. Supporting these overarching ideas, key sub-goals may include the promotion of preventive restructuring; encouraging comprehensive and equitable creditor participation; supporting realistic debt sustainability analysis; enabling standstills on litigation where appropriate; enhancing the transparency of sovereign debt obligations and restructurings; and improving markers and perceptions of sovereign debt legitimacy, among others.[38] To an important degree, the 'multiple processes at varying levels' also already exist, at least in part. The tools for instantiating core commitments might include contractual or market-based mechanisms, national or provincial legislation, international legal guidelines and principles, and measures that could be implemented by other international bodies, such as through UN Security Council Resolutions or IMF measures, or eventually perhaps a stand-alone statutory mechanism.

What could still exist more fully is a commitment to knitting these principles and processes together, particularly at a global scale, and to explicitly conceiving of them as complementary and deserving of simultaneous attention and support. Instead of deciding whether to press forward with market-based measures, alterations in domestic law, *or* international guidelines or semi-adjudicatory procedures, it may well be the case that greater progress will be made across all these tracks when they are pursued in parallel. To highlight one example worth remembering, it appears that, until the early 2000s, New York-based market actors were wary of incorporating even the most basic first-generation CACs into New York-law governed bonds, despite their longstanding and widespread use in UK-law bonds.[39] However, the possibility of a more muscular treaty-based mechanism for dealing with collective action problems, raised with the presentation of the IMF's Sovereign Debt Restructuring Mechanism (SDRM) proposal,[40] corresponded to renewed declarations of fealty to market-based solutions and a recommitment to updated contractual clauses. In this case, a perception of competition may have proved a virtuous instigation rather than a problem.

A more explicit and public shared commitment to fair principles and processes across multiple tracks could also have the benefit of making each of these steps appear less solitary, and thus might make them more likely. Statutorily-based domestic restructuring frameworks, such as for corporations, have become widespread internationally—and, indeed, at least some portion of the investors concerned about a more comprehensive (and less voluntary) restructuring system for sovereign debt nonetheless actively

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[38] These cross-cutting goals, and this document more generally, are in line with the 2015 UNGA Resolution establishing basic principles for sovereign debt restructuring as well as the April 2015 UNCTAD 'Roadmap' for Sovereign Debt Workouts. G.A. Res. 69/319 (Sept. 10, 2015); U.N. Conference on Trade and Development, Sovereign Debt Workouts: Going Forward 1, 3–5 (April 2015), https://unctad.org/system/files/official-document/gdsddf2015misc1_en.pdf. For more on what the elusive concept of 'legitimacy' might mean in the sovereign debt context, *see* Lienau, *supra* note 24, at 151–214.
[39] Mark Gugiatti & Anthony Richards, The Use of Collective Action Clauses in New York Law Bonds of Sovereign Borrowers 1, 1 (July 11, 2003) (unpublished manuscript) (on file with author).
[40] ANNE O. KRUEGER, IMF, A NEW APPROACH TO SOVEREIGN DEBT RESTRUCTURING 31 (2002), https://www.imf.org/external/pubs/ft/exrp/sdrm/eng/sdrm.pdf.

participate in domestic bankruptcy claims trading. Still, it can be difficult to act alone or as a first mover in the international arena. National or sub-national legislatures may not want to go out on a limb in embracing legislative innovations, and practitioners could find comfort in making changes as part of a broader community of actors moving in the same direction. Naming and sharing a collective project—even a project spread across multiple levels and processes—could help to spur on and facilitate that progressive movement.

(5) The U.S. should consider supporting the establishment of an independent international debt authority, which could coordinate ongoing improvements in line with widely-accepted lending and restructuring norms.

The deliberately multi-tiered approach proposed here could conceivably emerge from the natural patterns of international relations, perhaps catalyzed by a change of outlook. However, any such emergence would likely be painfully slow, less organized than ideal, and far from guaranteed. Instead, the U.S. should consider establishing *an internationally oriented body to recommend, coordinate, and facilitate steady, incremental progress in the architecture for dealing with sovereign debt*. Although any such institution obviously could not contend with the immediate financial fallout of the pandemic, it would nonetheless be a valuable outcome of the current moment.

This approach is closest in spirit to past recommendations for a semi-structured international framework—one that aims to improve coordination and strengthen shared principles and practices but still draws from institutional mechanisms already in existence. It echoes the possibility of an international debt authority floated in the first half of 2020[42] as well as earlier calls for a relatively modest but still internationally relevant forum.[43] To clarify, this coordinating authority would not be a full-blown multilateral organization with adjudicative functions along the lines of the IMF's earlier SDRM proposal.[44] Instead, a more modest institution could be established, perhaps even by a smaller number of states and supporters, to serve as a focal point for ongoing activities designed to improve how the global community collectively deals with debt in the short/emergency term, medium term, and long term. This authority would work toward operationalizing the substantive goals noted above in particular situations,

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[42] Alonso Soto, *New Global Body to Help with Debt Relief*, BLOOMBERG (April 22, 2020), https://www.bloomberg.com/news/articles/2020-04-22/un-to-call-for-new-global-body-to-help-with-debt-relief.

[43] One earlier proposal called for an even less formalized "Sovereign Debt Forum" more focused on research and prevention efforts and on bringing together creditors and debtors at an early stage, structured as a private, incorporated, non-profit organization. RICHARD GITLIN & BRETT HOUSE, CTR. INT'L GOV'T INNOVATION, A BLUEPRINT FOR A SOVEREIGN DEBT FORUM, (March 2014). An interdisciplinary, academically based research hub of the same name has been recently launched, which could serve as a partner in certain of the GDA's activities. An earlier UNCTAD Roadmap and Guide from 2015 also recommended, in broad strokes, an independent "Debt Workout Institution" along these lines that can be understood as a precursor to the proposal currently under development. The Roadmap suggested that a higher degree of legitimacy would result from a more coordinated multilateral establishment of any such body. U.N. Conference on Trade and Development, *supra* note 43, at 62–63.

[44] KRUEGER, *supra* note 45, at 31.

pushing forward and coordinating developments at the contractual level, domestic legislative level, and international level—either in establishing soft-law guidelines or in the development of more enforceable hard-law legislation.

As part of this larger mission, it could serve as an *idea generator and home for orphaned proposals*—worthy ideas formulated during a crisis (such as the present one) but then set aside as the international community shifts its focus to other problems in the news cycle. While higher-level attention is directed elsewhere, a dedicated debt institution could establish work streams to combine and then refine proposals in the same topic family—for example around domestic legislation to address collective action problems, support for debt transparency, protection of financial market infrastructure, or emergency standstills. If the authority were working on nationally-based but coordinated emergency standstill legislation, it might formulate and negotiate appropriate and shared triggers for emergency measures. It could formally endorse model laws, establish relationships with those actors that might be in a position to implement them, and have both the substance and the processes at the ready for when the moment is right. Furthermore, as part of its ongoing and incremental work, it could revisit and update past proposals and recommend their further consideration or adoption when appropriate.

As should be clear from the foregoing, part of this body's work would be to *identify, cultivate, and coordinate the cross-cutting tools, actors, and networks that might best achieve substantive goals*. Such actors and alliances could include national/provincial/supranational legislator groups; international and national associations centered around insolvency professionals and judges; creditor groups such as the IIF and ICMA; bond trustee institutions; market utilities such as payment clearing systems; UNCITRAL and other bodies active in legislative coordination; civil society organizations; and subject matter experts. Many others would, of course, be relevant depending on the goals, tools, and processes under consideration. To be sure, certain of these networks exist to some degree already, through fairly regular academic, policy, and interdisciplinary conferences. Still, they could be further formalized and extended, particularly to include actors and groupings important for progress in these arenas but not already deeply attentive to and involved in sovereign debt matters. Similarly, other international organizations undertake certain of these activities at various times, such as the IMF and UNCTAD, or even private creditor groups like the IIF. However, they can be limited by their broader missions, attentiveness to other issues, and concomitant political constraints. In some instances, existing organizations also may be considered insufficiently neutral due to their financial interests, affiliations, and positions in global economic and political relations—all of which may shift in the coming decades.

The proposed authority could also serve as a *natural institutional home for important debt-relevant proposals*. Indeed, one striking feature of the sovereign debt arena is the current absence of such a landing spot. An example of this is the occasional homelessness of initiatives that are widely acknowledged to be valuable, such as a truly global 'sovereign debt registry' to make core information more transparent and broadly accessible. The IMF would have been a natural location but declined, seemingly on the basis of political delicacies—and, indeed, its goals going forward could tie even more

deeply into changing sensitivities engendered by the shifting balance of global economic power. A private creditor organization would be less than ideal for such a registry, and indeed the IIF's own debt transparency principles are a step in the right direction but leave many key indicators out.[46] An academic institution is unlikely to carry sufficient weight, and of course the commitment of any academic institution alters with the make-up and interests of particular faculty members.[47] The Organization for Economic Cooperation and Development (OECD) has stepped up for now, launching an initiative to develop a data platform later this year. This could be promising but may prove insufficient, particularly given that it builds upon and does not purport to extend the IIF approach.[48] As such, a purpose-built international debt authority could serve as an informational hub or repository for accessible, comprehensive, and comprehensible sovereign debt-related information. This could include developing and maintaining databases for, for example, debt restructuring agreements, debt sustainability analyses, and of course a central sovereign debt registry, perhaps in conjunction with the OECD. Other valuable initiatives and proposals that may emerge down the line deserve a swifter and more secure positive response.

III. Conclusion: The U.S. should take the lead in the current crisis, and also not waste this moment to embed its values in a longer-term international architecture for dealing with sovereign debt.

While the ongoing economic crisis caused by the COVID-19 pandemic has generated important initiatives for addressing countries' financial distress—initiatives that deserve American support—it has also made even more apparent the ongoing gaps in the international financial architecture. These defects in the global debt framework are of a piece with the problematic elements of Chinese lending practices, which tend to take these insufficiencies to the extreme. In addition, the current crisis has highlighted the extent to which the international community pays closest attention to the sovereign debt infrastructure in situations of crisis—well past the ideal time to develop and implement necessary improvements. As part of the discussion of how to deal with the pandemic's financial fallout, the U.S. should explicitly support multi-tiered efforts across different jurisdictional spaces. Such an approach would not favor one mechanism over another and indeed would explicitly embrace the potentially complementary rather than competitive nature of progress along different tracks. It makes particular sense given that a single adjudicative mechanism remains politically unattainable and may not even be appropriate given the complexity of the current international debt market.

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[46] *See* Inst. for Int'l Fin., Voluntary Principles for Debt Transparency 1, 2–5 (June 10, 2019), https://www.iif.com/Portals/0/Files/Principles%20for%20Debt%20Transparency.pdf.

[47] The Euro-Mediterranean Economists Association has also launched a debt transparency platform advocating for a global sovereign debt registry. It is at an early stage and would likely benefit from broader support and perhaps a more explicit connection to other initiatives. DEBT TRANSPARENCY PLATFORM, https://dtransparency.org/ (last visited Mar. 28, 2021).

[48] OECD Debt Transparency Initiative, https://www.oecd.org/daf/fin/financial-markets/oecd-debt-transparency-initiative.htm (last visited May 17, 2021).

As part of this long-term project, the U.S. should consider supporting the development of a corollary institution. An international authority could act as a base and catalyst for developing and implementing incremental improvements to the sovereign debt arena across a range of levels and mechanisms, guided by a shared set of principles and commitments. Ideally debtors, creditors, and the international community writ large would eventually have a regularly updated menu of prepared options ready to be put into action whenever needed—even as we hope that the time of need never comes.