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Introduction

Chairman Barr, Ranking Member Moore, and Members of the Subcommittee, thank you for the opportunity to testify before you on the evolving role of the International Monetary Fund ("IMF" or the "Fund") in sovereign debt crises, and the implications of its involvement in Greece. In my research on sovereign debt management and financial crises, the IMF has emerged as a central element of the global crisis response and restructuring framework. It is fair to say that the Greek crisis has tested it like no other. The IMF has learned from this experience, and has adapted its policies in response to criticism—just as it had in the 1980s and 1990s—so that it remains an indispensable part of the sovereign debt restructuring regime today. I believe that a strong and independent IMF is very much in the U.S. interest and, on balance, in the interest of the citizens of crisis-stricken countries. Of course, there is scope for reform.

My testimony today will outline the sovereign debt restructuring context, focusing on the role of the IMF, summarize my view of recent restructuring experience, focusing on Greece, and offer reform suggestions.[*] Sovereign debt restructuring reform should have three objectives, addressing both the perennial flaws in the prevailing regime and new challenges to it. *First,* the reformed regime should achieve sustainable outcomes generally accepted as fair. It should deliver a fresh start for debtors and finality for creditors, and treat similarly situated debtors and creditors alike. *Second,* to that end, the restructuring process should be comprehensive and collective. *Third,* the sovereign debt restructuring regime should be intelligible and accountable to all stakeholders. While overnight transformation is not in the

[*] Portions of this testimony are based on my article, *Sovereign Debt: Now What?*, which appeared in a special issue of the Yale International Law Journal in 2016.

cards, even partial and incremental changes should be evaluated based on how well they advance the three objectives.

Sovereign debt restructuring reform is not all about the IMF, but it cannot happen without the IMF.

- With respect to the first objective, sustainability, the IMF has already moved to reform its approach to assessing countries' debt burdens, and to open up its methodology to outside scrutiny. In Europe, the IMF has been a force for good—despite its own repeated embarrassments—pushing EU authorities to be more realistic in their projections even in the face of political constraints. Nonetheless, I continue to believe that there is much to be gained from opening the sustainability debate further to competing views.
- As to the second objective, comprehensive and collective process, the IMF is literally the only institution in the world today with capacity to bring together diverse stakeholders in a sovereign debt crisis, including private and other official creditors. The Fund's lending policies are a source of considerable leverage in this area. I am especially gratified by the IMF's engagement with the changing role of official creditors in recent years. The position of the European Central Bank ("ECB") in the 2012 Greek debt restructuring, the still-dominant role of government creditors in Greece today, and a recent bondholder lawsuit against Ukraine, brought on Russia's behalf in London, all illustrate the magnitude of the enduring challenge.
- Finally, the IMF is ideally positioned to promote more transparency, intelligibility, and accountability in sovereign debt restructuring. It has the technical and political tools to secure consistent, comprehensive, and publicly accessible disclosure of debt restructuring results, including both legal and financial terms. There is simply no reason for this information, which is of utmost public importance, to be the exclusive province of academic sleuths (including many of my colleagues and dear friends) on whom we now rely.

The IMF is in a peculiar position today. Unless it receives a massive funding boost, it will stay small relative to the scale of global capital flows. Yet its knowledge, experience, and political clout remain far in excess of its financial might. The IMF's role in Greece today is a case in point. This is precious capital. It is in everyone's interest to protect and fortify it for the crises to come.

I. The Sovereign Debt Context

A. *No Fresh Start, Weak Enforcement*

When a government cannot pay its bills, it cannot file for bankruptcy. There is no court, no authoritative body to declare that a state is insolvent, to bring all the stakeholders together in a restructuring plan, or to shield its assets from seizure by opportunistic creditors while everyone works out a compromise to put the country on the road to recovery. To be sure, many governments are leery of bankruptcy: they do not want to submit to a binding process beyond their control.[1] But without bankruptcy, there is also no debt discharge, no fresh start as a matter of right. Sovereign debt is literally forever.

Governments do have the protection of sovereign immunity.[2] Most of the sovereign debtor's assets are inside its borders; those that are not, such as embassies and military bases, are shielded from seizure. Short of gunboats, there are few ways for creditors to make governments pay.[3] However, creditors can make life plenty difficult for sovereigns by trying to cut off their sources of funding and disrupting their international financial transactions.[4] This requires creditors to stick together, which is no small task without a bankruptcy backstop.

Sovereign borrowing and restructuring are a function of this tension: the debt is hard to enforce, but it never goes away. In practice, debt restructuring has come from bargaining between a government and its creditors. However, it often takes many years, and brings insufficient relief.

Lengthy debt crises bring deadweight losses (they are inefficient), but they also disproportionately hurt the poorest, least sophisticated debtors and creditors.[5] These ultimate stakeholders of any sovereign debt restructuring regime—citizens, taxpayers, bank depositors and pensioners—lose their livelihoods along with their faith in domestic and international institutions.[6] Governments lose their capacity to meet the basic human needs of their citizens and to safeguard their human rights.

1. *See, e.g.*, Sean Hagan, *Designing a Legal Framework to Restructure Sovereign Debt*, 36 GEO. J. INT'L L. 299, 346-47, 352, 391 n. 250 (2005); Jérôme Sgard, *How the IMF Did It—Sovereign Debt Restructuring Between 1970 and 1989*, 11 CAP. MKTS. L.J. 103 (2016).

2. For canonical accounts of the enforcement challenge and its implications, *see* Jonathan Eaton & Mark Gersovitz, *Debt with Potential Repudiation: Theoretical and Empirical Analysis*, 48 REV. ECON. STUDIES 289 (1981) (reputation); Jeremy Bulow & Kenneth Rogoff, *Sovereign Debt: Is to Forgive to Forget*, 79 AM. ECON. REV. 43 (1989) and Jeremy Bulow & Kenneth Rogoff, *A Constant Recontracting Model of Sovereign Debt*, 97 J. POLIT. ECON. 155 (1989) (enforcement); MICHAEL TOMZ, REPUTATION AND INTERNATIONAL COOPERATION: SOVEREIGN DEBT ACROSS THREE CENTURIES (2007) (reputation).

3. W. Mark C. Weidemaier, *Sovereign Immunity and Sovereign Debt*, 2014 U. ILL. L. REV. 67 (2014); Pierre-Hugues Verdier & Erik Voeten, *How Does Customary International Law Change? The Case of State Immunity*, 59 INT'L STUD. Q. 209 (2014).

4. *See* LEE C. BUCHHEIT ET AL., BROOKINGS INST., COMM. ON INT'L ECON. POL'Y & REFORM, REVISITING SOVEREIGN BANKRUPTCY (2013) (follow "Download the full report" hyperlink under "Download") [hereinafter REVISITING SOVEREIGN BANKRUPTCY].

5. *See, e.g.*, FEDERICO STURZENEGGER & JEROMIN ZETTELMEYER, DEBT DEFAULTS AND LESSONS FROM A DECADE OF CRISES 50-53 (2006) (summarizing economic literature on deadweight losses from sovereign debt default); Peter Fallon & Robert Lucas, *The Impact of Financial Crises on Labor Markets, Household Incomes, and Poverty: A Review of Evidence*, 17 WORLD BANK RES. OBSERVER 21, 21-45 (2002); 2 Jeffrey D. Sachs, *Introduction* to DEVELOPING COUNTRY DEBT AND ECONOMIC PERFORMANCE: COUNTRY STUDIES—ARGENTINA, BOLIVIA, BRAZIL, MEXICO 19-24 (Jeffrey D. Sachs ed., 1990) (describing the distributional effect of debt crises).

6. *Cf.* Armin von Bogdandy & Matthias Goldmann, *Sovereign Debt Restructurings as Exercises of International Public Authority: Towards a Decentralized Sovereign Insolvency Law*, *in* SOVEREIGN FINANCING AND INTERNATIONAL LAW: THE UNCTAD PRINCIPLES ON RESPONSIBLE SOVEREIGN LENDING AND BORROWING 39 (Carlos Espósito, Yuefen Li & Juan Pablo Bohoslavsky eds., 2013) (arguing that the effects of sovereign debt restructuring

B. The Sovereign Debt Restructuring Regime and the IMF, a Brief History

To structure bargaining without bankruptcy, a set of interlocking institutions and norms emerged late in the twentieth century. This informal regime has been anchored in institutions dominated by the Group of Seven (G-7) wealthy nations,[7] and has continued to evolve. All along, it drew criticism for failing to deliver enough relief or fair distribution; it prevailed nonetheless in good part because "[f]or 30 years sovereign debt restructurings have gotten done."[8] New patterns of capital flows and political realignments have challenged the sovereign debt restructuring regime from the moment it came together in the mid-1990s. Recent debt crises, including the crisis in Greece, have exposed more perennial failures and new shortcomings.

Changes in international trade and capital movements, the decline of absolute sovereign immunity, post-colonial and post-Soviet upheavals each periodically called for new debt management and restructuring tools, and forced the old ones to adapt. Growth in bilateral trade finance from the rubble of World War II created demand for coordination among government-to-government creditors. The Paris Club, a regular informal gathering of official bilateral creditors, was born in the 1950s.[9] The 1970s saw a spike in syndicated loans to poor and middle-income countries, made by banks in major financial centers. The crises and restructurings that followed in the 1980s required a mechanism to coordinate commercial banks. Bank advisory committees, or the London Club process, emerged in response.[10] G-7 finance officials were just backstage with moral suasion, funding and regulatory incentives, because the health of their financial systems depended on the success of the process: banks took nearly a decade to build up enough capital and reserves to absorb losses from debt reduction.[11] Meanwhile, sovereign debt kept growing.[12]

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fall on the public and should be governed by public law).

7. The Group of Seven (G-7) comprises Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States.

8. Lee C. Buchheit, *Sovereign Debt Restructurings: The Legal Context*, in SOVEREIGN RISK: A WORLD WITHOUT RISK-FREE ASSETS? BIS PAPERS NO. 72 107, 110 (July 2013), http://www.bis.org/publ/bppdf/bispap72.pdf. For evidence that debt relief comes too late and delivers too little relief, *see* Rodrigo Mariscal et al., *Sovereign Defaults: Has the Current System Resulted in Lasting (Re)Solutions?* (Escuela de Negocios: Universidad Torcuato Di Tella, Working Paper 03/2015, 2015); REVISITING SOVEREIGN BANKRUPTCY, *supra* note 4, at 5-14; Elena Duggar, *Sovereign Defaults Series: The Aftermath of Sovereign Defaults*, Moody's (Oct. 2013); Udaibir S. Das, Michael G. Papaioannou & Christoph Trebesch, *Sovereign Debt Restructurings 1950-2010: Literature Survey, Data, and Stylized Facts* (IMF, Working Paper No. WP/12/203, 2012).

9. THOMAS M. CALLAGHY, THE MISUNDERSTOOD ORIGINS OF THE PARIS CLUB (2008) (unpublished manuscript) (on file with author).

10. José Antonio Ocampo traces some of the same history, with an emphasis on the booms and busts in different forms of lending to sovereigns, but argues that the accretion of institutions to restructure sovereign debt to different creditors resulted in a "non-system." José Antonio Ocampo, *A Brief History of Sovereign Debt Resolution and a Proposal for a Multilateral Instrument*, in TOO LITTLE, TOO LATE: THE QUEST TO RESOLVE SOVEREIGN DEBT CRISES 189-195 (MARTIN GUZMAN, JOSÉ ANTONIO OCAMPO & JOSEPH E. STIGLITZ, EDS., 2016). *See also*, LEX RIEFFEL, RESTRUCTURING SOVEREIGN DEBT: THE CASE FOR AD-HOC MACHINERY 95-131 (2003) (describing the London Club process).

11. WILLIAM R. CLINE, INTERNATIONAL DEBT REEXAMINED 72-73 (1995) (describing changes in the financial position of banks and developing country debt stocks throughout the 1980s); Ocampo, *supra* note 10; RIEFFEL, *supra* note 10. *See also*, JOSEPH KRAFT, THE MEXICAN RESCUE (1984) (a journalistic account of the early days of the Third World Debt Crisis and the bank coordination process). For a description of sovereign debt restructuring as a three-party negotiation including the debtor, the creditor, and creditors' governments, *see* Jeremy Bulow & Kenneth Rogoff, *Multilateral Negotiations for Rescheduling Developing Country Debt: A Bargaining-Theoretic Framework*, 35 IMF STAFF PAPERS 644 (1988).

12. CLINE, *supra* note 11.

Starting in 1989, banks exchanged unpayable loans for tradable bonds at a discount. Developing countries reduced their debt to foreign banks by a third or more.[13] Bonds quickly eclipsed loans as the funding instrument of choice for sovereigns, as they had been in the late nineteenth and early twentieth centuries.[14] Defaults returned to the sovereign bond market in the late 1990s, and called for bondholder coordination.[15] Designing the right coordination machinery was a challenge because late twentieth-century bonds traded more widely and actively than their ancestors, and because modern-day bondholders did not normally have enduring ties to governments. Creditor committees, which had led bond restructuring negotiations a century earlier and commercial bank negotiations a decade earlier, have played a limited role in contemporary bond exchanges. For the most part in the late 1990s and early 2000s, debtors and their advisers drove distressed sovereign bond exchanges, which resembled new securities offerings more than the deals brokered by bank advisory committees or bondholder councils of yore.[16]

Chronically poor countries cut off from private markets borrowed instead from governments and multilateral institutions such as the IMF, the World Bank, and regional development banks. Many of the economic reform and development programs financed with foreign official credits failed to deliver thanks to some combination of bad design, bad implementation, and bad luck. By the late 1990s, some countries' debts had grown and their economies had deteriorated so much that stretching out repayments (rescheduling) and even substantial debt reduction by Paris Club creditors could not put them on a sustainable path: their debts would keep growing in perpetuity. In response to a global civil society campaign, the G-7 unveiled new dedicated debt relief programs, the Heavily Indebted Poor Countries (HIPC) initiative in 1996 and the Multilateral Debt Relief Initiative (MDRI) in 2005. Throughout the 1990s and into the 2000s, a mix of outside pressure, creditor country politics, new research and policy experience prompted a succession of program changes to deliver more relief in exchange for more reform. Multilateral debt of the world's poorest countries eventually would be cut for the first time alongside bilateral debt, with debt reduction tied to policy and governance conditionality.[17]

13. *See, e.g.*, Serkan Arslanalp & Peter Blair Henry, *Is Debt Relief Efficient?*, 60 J. Fin. 1017 (2005).

14. Ross Buckley, *The Facilitation of the Brady Plan: Emerging Markets Debt Trading From 1989 to 1993*, 21 FORDHAM INT'L L.J. 1802, 1804-18, 1820-22 (1997).

15. Udaibir S. Das, Michael G. Papaioannou & Christoph Trebesch, *Restructuring Sovereign Debt: Lessons from Recent History*, *in* FINANCIAL CRISES: CAUSES, CONSEQUENCES, AND POLICY RESPONSES 593 (Stijn Claessens et al. eds., 2014).

16. For accounts of bondholder committees in the nineteenth and early twentieth centuries, see Marc Flandreau, *Sovereign States, Bondholders Committees, and the London Stock Exchange in the Nineteenth Century (1827–68): New Facts and Old Fictions*, 29 OXFORD REV. ECON. POL. 668 (2013); and Rory Macmillan, *Towards a Sovereign Debt Work-out System*, 16 NW. J. INT'L L. & BUS. 57 (1995). On the development of contemporary sovereign bond restructuring practices, see NOURIEL ROUBINI & BRAD SETSER, BAILOUTS OR BAIL-INS? RESPONDING TO FINANCIAL CRISES IN EMERGING ECONOMIES (2004); STURZENEGGER & ZETTELMEYER, *supra* note 3; Ran Bi, Marcos Chamon & Jeromin Zettelmeyer, *The Problem that Wasn't: Coordination Failures in Sovereign Debt Restructurings* (IMF, Working Paper No. WP/11/265, 2011) Ugo Panizza, Federico Sturzenegger & Jeromin Zettelmeyer, *The Economics and Law of Sovereign Debt and Default*, 47 J. ECON. LIT. 651 (2009).

17. Technically, the debt was paid off on the debtors' behalf by donor countries. Martin A. Weiss, *The Multilateral Debt Relief Initiative*, CRS Report No. 22534 (Jun. 11, 2012), Martin A Weiss, *Debt Relief for Heavily Indebted Poor Countries: Issues for Congress*, CRS Report No. RL33073 (Apr. 18, 2006); NANCY BIRDSALL & JOHN WILLIAMSON, DELIVERING ON DEBT RELIEF: FROM IMF GOLD TO A NEW AID ARCHITECTURE (2002); IMF, *Factsheet: The Multilateral Debt Relief Initiative* (updated Sep. 17, 2015); IMF, *Factsheet: Debt Relief Under the Heavily*

Different fora, practices, and techniques—the Paris and London Clubs, bond exchanges, HIPC and MDRI—could be mixed and matched to suit particular debtors, creditors, and debt stocks. By the late 1990s, sovereign debt restructuring was the work of a reasonably integrated regime, even if it was not recognized as such.

The IMF established itself as the foundation of this restructuring regime beginning in the 1980s.[18] It delivered temporary liquidity for the debtor and used its lending instruments and policies to nudge disparate creditor groups to coordinate. By the turn of the century, this role was well-understood by a small core of repeat players: finance officials in debtor and creditor countries, staff and management at multilateral institutions, experts at credit rating agencies, big law and financial firms, and smaller, specialized investors.[19] A country that could not pay its debt first turned to the IMF, which typically offered financial support for up to three years, conditioned on economic reform.[20] The IMF indicated what budget savings the country could achieve, which implied a "financing gap" to be filled by new lending and debt relief from other creditors. By default, the IMF also became a gatekeeper: if the gap could not be filled, the program could not go forward. Without IMF funding, the country and its creditors faced the prospect of disorderly default.[21]

For debtors and creditors, there were few good alternatives to negotiation. Throughout the 1980s and 1990s, national courts chipped away at sovereign borrowers' defenses to paying their debts.[22] Yet most government property remained beyond creditors' reach, either safe inside debtors' borders or covered by still-potent central bank, military and diplomatic immunities.[23] Governments that could not or would not pay their foreign creditors had to choose between

Indebted Poor Countries (HIPC) Initiative (updated Sept. 17, 2015), http://www.imf.org/external/np/exr/facts/hipc.htm; Joshua Busby, *Is There a Constituency for Global Poverty? Jubilee 2000 and the Future of Development Advocacy*, *in* GLOBAL DEVELOPMENT 2.0: CAN PHILANTHROPISTS, THE PUBLIC AND THE POOR MAKE POVERTY HISTORY? 85 (Lael Brainard & Derek Chollet eds., 2008).

18. Sgard puts the start of this role for the IMF in the 1970s; it developed more fully during the Third World Debt Crisis in the 1980s. Sgard, *supra* note 1.

19. *See* Anna Gelpern & Mitu Gulati, *Public Symbol in Private Contract: A Case Study*, 84 WASH. U. L. REV. 1627 (2006) (an interview-based study of sovereign bond contract reform, describing different parts of the sovereign debt restructuring community); MITU GULATI & ROBERT E. SCOTT, THE 3 1/2 MINUTE TRANSACTION: BOILERPLATE AND THE LIMITS OF CONTRACT DESIGN (2012) (describing and interviewing lawyers in New York and London); *cf*. YVES DEZALAY & BRYANT G. GARTH, DEALING IN VIRTUE: INTERNATIONAL COMMERCIAL ARBITRATION AND THE CONSTRUCTION OF A TRANSNATIONAL LEGAL ORDER 10 (1996) (describing the tightly-knit international arbitration community).

20. Lee Buchheit, *The Role of the Official Sector in Sovereign Debt Workouts*, 6 CHI. J. INT'L L. 333 (2005).

21. *Id*. at 341-42. Buchheit points out that this IMF role was not well understood by the private sector. While this may have been true of the private sector in general or investor groups new to the sovereign debt restructuring scene, it was not true of insiders like him, who numbered in the dozens. *Supra* note 24. Ocampo argues that outright defaults in the interwar periods led to better economic outcomes for the borrowing countries than the managed restructuring process described here. Ocampo, *supra* note 10.

22. For U.S. jurisprudence, see, for example, *Argentina v. Weltover, Inc*., 504 U.S. 607 (1992) (U.S. courts have jurisdiction over domestic-law bonds payable in New York; debt issuance is commercial activity outside the scope of sovereign immunity); *Allied Bank Int'l v. Banco Credito Agricola de Cartago*, 757 F.2d 516 (2d Cir. 1985) (eliminating the Act of State Doctrine as a defense to sovereign default); and *Elliott Assocs. v. Banco de la Nacion*, 194 F.3d 363 (2d Cir. 1999) (effectively eliminating the champerty defense in sovereign debt).

23. The "ARA Libertad" Case (Argentina v. Ghana), Case No. 20, Order of Dec. 15, 2012, 12 ITLOS Rep. 332.

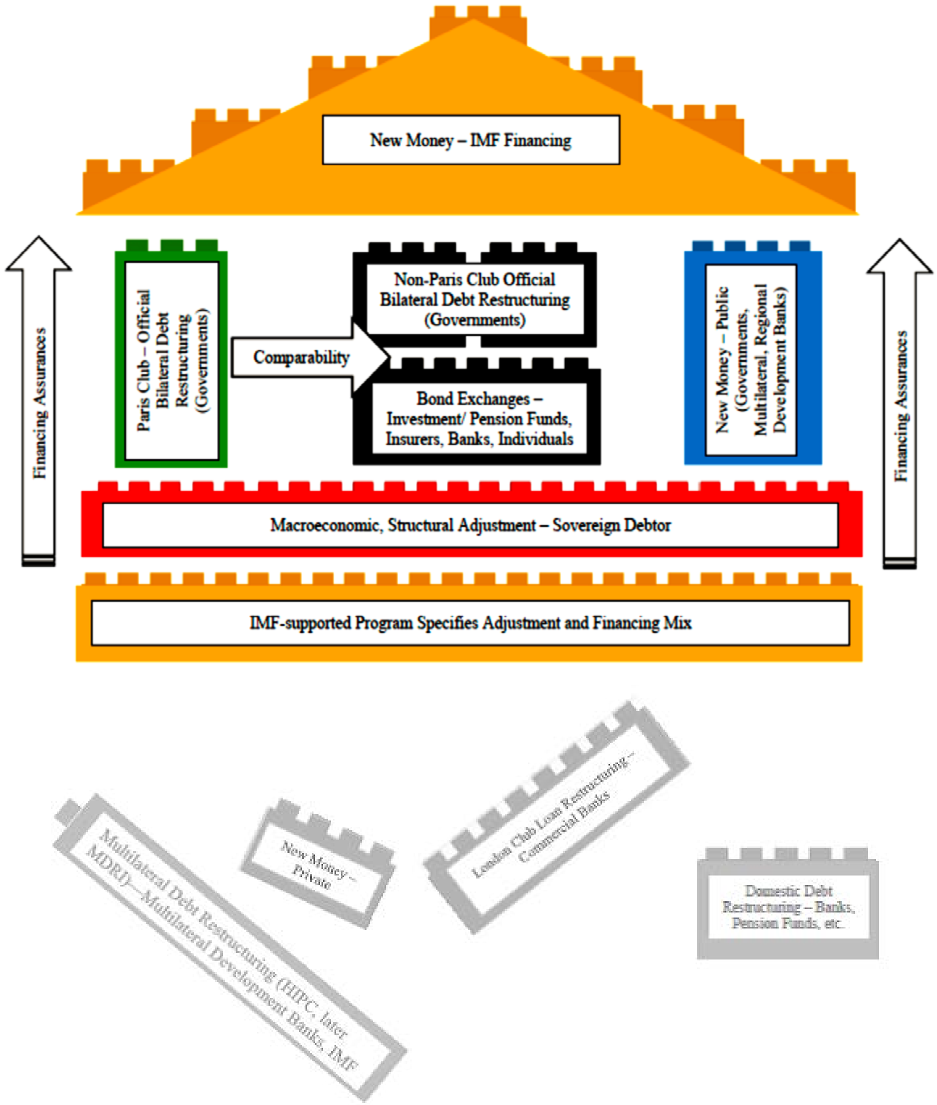
compromise and a lifetime of hiding assets and rerouting payments, which made it hard to pursue international trade and finance.[24] Meanwhile, creditors with judgments against sovereigns could spend years scouring the world for morsels of attachable property and hassling debtors into settlement. A scant few could play this game; hardly anyone else found it appealing.[25]

The sovereign debt restructuring regime at the turn of the century had features that helped it manage sovereign debt distress to survive in a world without statutory, court-supervised bankruptcy, robust contract enforcement, or strong shared norms. *First*, creditors with similar interests, legal entitlements and constraints stuck together; each group followed a distinct restructuring process reflecting its particular attributes and relationship with the debtor. *Second*, groups of creditors—official bilateral lenders, banks, and foreign bondholders—normally linked their own concessions to those of the other groups, and to the IMF program parameters. The Paris Club's insistence that sovereign debtors obtain "comparability of treatment" from other public and private creditors is perhaps the best-known example of such linkage. *Third*, the entire process was dominated by repeat players, a feature to which I return in more detail below. One might picture the regime in the late 1990s and early 2000s as a building assembled out of Lego blocks (Figure 1). Each block represents a different creditor group that might contribute debt relief or new financing. Different building blocks could be assembled based on an IMF-supported program design. The precise mix would depend on the sovereign's debt composition, and its political and financial constraints.

24. *Compare* stylized description of enforcement in Bulow & Rogoff, *Is to Forgive to Forget* and *A Constant Recontracting Model*, *supra* note 2.

25. For game-theoretic analysis of sovereign debt restructuring episodes, see, for example, VINOD K. AGGARWAL, DEBT GAMES: STRATEGIC INTERACTION IN INTERNATIONAL DEBT RESCHEDULING (1996).

Figure 1: The Sovereign Debt Restructuring Regime *circa* 2000



It is important to emphasize that the regime depicted in Figure 1 might have been informal, but it was far from chaotic. It delivered a measure of relief for debtors and impressive returns for creditors with no treaty, no statute, and no court in charge.[26] It was flexible enough to adapt to massive shifts in global politics and economics. It was also effective enough, and accepted generally enough—just enough—to preempt far-reaching alternatives that periodically sprouted up.[27]

26. Carmen M. Reinhart & Christoph Trebesch, *A Distant Mirror of Debt, Default, and Relief* (Univ. of Munich, Dep't of Econ., Discussion Paper No. 2014-49, 2014), https://epub.ub.uni-muenchen.de/21832/1/Distant_Mirror_October_27_2014.pdf; Carmen Reinhart & Christoph Trebesch, *Sovereign Debt Relief and its Aftermath*, 14 J. EUR. ECON. ASS'N 215 (2016) (debt relief figures); Michael Tomz & Mark Wright, *Empirical Research on Sovereign Debt and Default,* 2013 ANN. REV. ECON. 247; Christoph Klingen et al., *How Private Creditors Fared in Emerging Debt Markets, 1970-2000*, at 37 (IMF, Working Paper No. WP/04/13, 2004) (observing "sizable ex post premiums" for creditors of emerging market countries in the 1990s).

27. *See, e.g.*, Sgard, *supra* note 1; RIEFFEL, *supra* note 10, at 132-48 (describing the North-South Dialogue and the defeat of the International Debt Commission proposal in the 1970s); Hagan, *supra* note 1 (describing the rise and

Nonetheless, it is hard to explain the regime's durability by its outcomes alone. Restructurings came late, and often took a long time to complete.[28] They delivered short-term liquidity relief, but often did not address the underlying solvency problems.[29] Re-defaults followed within a few years of sovereign debt restructurings in nearly forty percent of the cases.[30] While causation is open to debate, some mix of ill-conceived and ill-timed relief, and bad policy, likely played a part.

The dominance of repeat players and institutions shaped by long-term political alliances may help make sense of the regime survival puzzle. Late twentieth century sovereign debt restructurings involved a relatively small and tight cohort of officials from a handful of countries and international organizations, a dozen or so big financial firms, and half a dozen law firms.[31] They had developed restructuring practices through trial and error, reacting to crises. They were also invested in these practices and controlled the institutions charged with their operation. Knowing the composition of and relationships among the creditor groups, the customary sequence of negotiations, the range of terms Paris Club creditors had accepted as "comparable," the habitual exclusion of certain informally "preferred" claims from burden-sharing[32] was (and still is) invaluable in a world without public bankruptcy. Such knowledge can confer status, gain a seat at the negotiating table, and even help fashion arguments for reform. Long-term investment in the regime and a measure of social cohesion among those "in the know" helped sustain it.[33]

On the other hand, the structure of the regime—let alone the logic behind it—was unintelligible to ordinary people, the ultimate debtors and creditors. Public debt was a matter for private ordering, both in the legal sense (contract) and in the practical sense (behind closed doors). The regime as a whole could hardly claim to be effective, fair, or legitimate in absolute terms, if only because so few saw it as a regime or agreed on a standard by which to judge it.[34] It might have delivered serviceable outcomes, but for most stakeholders, it was not worth fighting for.

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fall of the IMF's proposal for the Sovereign Debt Restructuring Mechanism (SDRM)).

28. *See, e.g.*, *supra* note 8 (multiple sources citing evidence of the "too little-too late" problem in sovereign debt restructuring).

29. *See, e.g.*, IMF, *The Fund's Lending Framework and Sovereign Debt – Annexes*, (June 2014), [hereinafter IMF Lending Framework Annexes].MF Lending Framework Annexes.

30. Duggar, *supra* note 8.

31. GULATI & SCOTT, *supra* note 24, at 59-61; Gelpern & Gulati, *supra* note 24, at 1634-36 (2006).

32. Exclusion from comparability and other burden-sharing mechanisms was tantamount to a grant of seniority ("preferred creditor status") for claims of identical legal rank. Short-term trade credits, interbank loans, and, until recently, multilateral debt, have enjoyed such informal preference—presumably based on other participants' collective judgment that it was in their interest to consent to informal subordination. *See* RUTSEL SILVESTRE J. MARTHA, *Ranking of Obligations, in* THE FINANCIAL OBLIGATION IN INTERNATIONAL LAW 479 (2015).

33. *Compare* this depiction and Pierre-Hugues Verdier, *The Political Economy of International Financial Regulation*, 88 Ind. L. Rev. 1405 (2013) (arguing that soft law and informal network governance in international financial regulation has empowered certain political actors to the detriment of financial stability).

34. Legitimacy here does not look solely or primarily to the authority of the parties or the restructuring forum, but rather to the terms of the debt and the restructuring process that produce it. *See* Marie Sudreau & Juan Pablo Bohoslavsky, *Sovereign Debt Governance, Legitimacy, and the Sustainable Development Goals: Examining the Principles on Responsible Sovereign Lending and Borrowing*, 24 WASH. INT'L L.J. 613 (2015); *cf.* the discussion of legitimacy above and in the text to ODETTE LIENAU, RETHINKING SOVEREIGN DEBT: POLITICS, REPUTATION, AND LEGITIMACY IN MODERN FINANCE (2014) (considering the function of sovereignty in sovereign debt).

C. A Changing Landscape, 2000-2010

Several trends, some of which date back to the 1990s, have threatened to undermine the sovereign debt restructuring regime pictured in Figure 1. I will focus on three of these trends. *First*, new creditors grew in importance. Countries such as China and Russia, as well as distressed bond funds and sovereign wealth funds,[35] among others, were not necessarily invested in the old restructuring processes and institutions. *Second*, cross-border capital mobility and government creditors' participation in the private capital markets eroded the boundaries of creditor groups, along with internal discipline and linkages among restructuring fora. *Third*, the vast scale of global capital flows made the IMF small by comparison, and put its central coordinating role in crisis management at risk.

The rise of new official bilateral lenders has received relatively little attention in the academic and policy debates, particularly when compared to the attention showered on distressed bond funds. In the 2000s, manufacturing and commodity exporters with large stores of government savings, most notably China and the Gulf states, began investing more of their foreign currency reserves in the emerging markets.[36] This trend accelerated after 2009, when interest rates dropped near zero in Europe and the United States post-crisis, and sent investors looking for higher returns elsewhere.[37] In parallel, China expanded its official bilateral lending to poor and middle income governments so dramatically that it eclipsed the original Paris Club lenders in some countries within a few years.[38]

New creditors contributed to the rise in complex forms of government-to-government lending that did not quite fit Paris Club reporting conventions. For example, Venezuela began borrowing from China against future oil sales in 2007; by 2015, oil payment advances from China

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35. "Sovereign wealth funds (SWFs) are special purpose investment funds or arrangements, owned by the general government. Created by the general government for macroeconomic purposes, SWFs hold, manage or administer assets to achieve financial objectives, and … [invest] in foreign financial assets." International Working Group of Sovereign Wealth Funds (IWG-SWF), *Generally Accepted Principles and Practices—Santiago Principles*, at 3 (Oct. 2008).

36. *See* IMF, *Market Developments and Issues*, Global Financial Stability Report 99 (April 2006), [hereinafter IMF GFSR April 2006]; *see, e.g.*, *Portfolio Overview*, ABU DHABI INV. AUTHORITY (ADIA), www.adia.ae/En/Investment/Portfolio.aspx (specifies 10-20% for government bonds and 15-25% for emerging markets). ADIA's total assets under management were estimated at $773 billion. Andrew Torchia, *Abu Dhabi fund ADIA Manages More of its Billions In-House*, REUTERS (June 2, 2015).

37. Serkan Arslanalp & Takahiro Tsuda, *Tracking Global Demand for Emerging Market Sovereign Debt* (IMF, Working Paper No. WP/14/39, 2014).

38. For example, China became Angola's largest creditor by 2014, holding 41% of its debt, followed by the United Kingdom with 27%. IMF, *Angola Staff Report for the 2014 Article IV Consultation*, Country Report No. 14/274, at 9 (Aug. 14, 2014). Some of China's exposure is secured by oil. Yun Sun, *China's Aid to Africa: Monster or Messiah?*, BROOKINGS (Feb. 2014). China's lending to Congo has grown rapidly since 2006, much of it effectively secured by oil proceeds that Congo is required to keep on deposit in China. China became the dominant creditor after Congo secured HIPC and MDRI relief from wealthy countries and multilateral institutions. IMF, *Republic of Congo Staff Report For the 2014 Article IV Consultation*, Country Report No. 14/272, at 9 (July 7, 2014); *see also* IMF, *Republic of Congo Staff Report for The 2014 Article IV Consultation—Debt Sustainability Analysis*, Country Report No. 14/272, at 2 (July 7, 2014) (China accounted for 63% of Congo's official bilateral debt and 15% of its overall external debt in 2010).

reportedly were among the scant few sources of external financing it had left. In mid-2016, Venezuela approached China for a debt restructuring by another name as more and more of its oil exports effectively functioned as debt repayments.[39] Angola was even worse off, with no spare export capacity left after making its debt payments in oil.[40]

Lending that combined features of trade, investment, development aid, and strategic alliance-building was not new, but the scale and the players were.[41] In the past, such complex, mixed-motive arrangements might have been settled quietly on the margins of Paris Club negotiations. Classifying the debt and finding a forum to renegotiate it is more of a challenge today, when both debtors and major creditors view the prevailing regime with suspicion, and are underrepresented in its institutions.[42]

Further complicating matters, government creditors could take advantage of bigger, deeper, more liquid international capital markets to sell their bilateral loans.[43] On the one hand, official creditors such as central banks and government reserve managers have long been important buyers of sovereign debt. Their market participation was viewed primarily through the lens of their monetary and exchange rate policy functions, and their extreme conservatism. However, it became increasingly apparent in the 2000s that central banks, reserve managers, and sovereign wealth funds were not uniformly risk-averse as bond investors; some made bets on the debts of troubled countries and actively managed their sovereign debt portfolios.[44]

Active bond trading benefited sovereign borrowers: it promoted information and price discovery, expanded the range of potential buyers, and saved borrowing costs over time. However, it also meant that the mix of public and private creditors behind a debt stock could change at any

39. Corina Pons, Alexandra Ulmer & Marianna Parraga, *Venezuela in Talks with China for Grace Period in Oil-for-Loans Deal*, REUTERS (Jun. 15, 2016).

40. Libby George, *Growing Chinese Debt Leaves Angola with Little Spare Oil*, REUTERS (Mar. 14, 2016).

41. The phenomenon of deliberately ambiguous financing forms is not new. For example, the United States financed South Vietnam's military with disguised agricultural credits during the Vietnam War. *See, e.g.*, Agreement between the Government of the United States of America and the Government of the Republic of Viet-Nam for Sales of Agricultural Commodities, 22 U.S.T. 1459, Sec. II.A.2 (June 28, 1971); Marian Nash (Leich), *Contemporary Practice of the United States Relating to International Law*, 91 AM. J. INT'L. L. 697, 705–06 (1997). Vietnam refused to repay the credits when it came to the Paris Club to restructure its debt in 1993. The difference is that the new creditors are not fully part of the institutions within which creditors negotiated how to deal with these ambiguities. For example, after the fall of Saddam Hussein, Iraq claimed that much of its "debt" to its Gulf neighbors was supposed to have been a grant, to help support Iraq in its war against Iran. Negotiations with Gulf countries, which were not part of the Paris Club, lasted for years after the Paris Club had agreed on near-total relief. MARTIN A. WEISS, CONG. RESEARCH SERV., RL33376, IRAQ'S DEBT RELIEF: PROCEDURE AND POTENTIAL IMPLICATIONS FOR INTERNATIONAL DEBT RELIEF 6 (2009).

42. *See, e.g.*, MARTIN A. WEISS, CONG. RESEARCH SERV., RS21482, THE PARIS CLUB AND INTERNATIONAL DEBT RELIEF 1 (2013) (China and Gulf states are not part of the Paris Club); NGAIRE WOODS, GOVERNING THE GLOBAL ECONOMY: STRENGTHENING MULTILATERAL INSTITUTIONS 2 (2008) (observing that China and Gulf states are underrepresented in the multilateral organizations, including the IMF and the World Bank).

43. *See, e.g.*, Thomas Laryea, Donegal v. Zambia *and the Persistent Debt Problems of Low-Income Countries*, 73 L. AND CONTEMP. PROBS. 193-200 (2010) (analyzing a lawsuit brought in English courts by a private offshore fund on contracts that originated with Romania's bilateral agricultural credits to Zambia. Romania sold the loans to a private investor and avoided restructuring them in the Paris Club); *see also*, Felipe Ossa, *Woolly Outcome for Aries*, ASSET SECURITIZATION REPORT (July 3, 2006) (reporting Germany's securitization of its export credit loans to the Russian government).

44. *See, e.g.*, IMF GFSR April 2006, *supra* note 36; Brad Setser, *Norway was against Iceland before it was for Iceland*, FOLLOW THE MONEY BLOG (May 17, 2008); Andres R. Martinez, *CIC Stops Buying Europe Government Debt on Crisis Concern*, BLOOMBERG (May 10, 2012).

time, so that not even the debtor could ever know for sure who held what debt.[45] This would present a challenge when trying to organize a restructuring.

While the mid-2000s were a period of rapid growth and relative calm in the sovereign debt markets, the IMF's ability to anchor a hypothetical crisis response[46] suffered from the growing gap between its resources and the scale of global capital flows. Figure 2 shows IMF lending capacity against the background of capital flows in and out of the euro area and developing countries between 1999 and 2006. At the end of 1999, with much of Asia, Brazil, and Russia still in crisis, the IMF could lend up to $86 billion of its own resources, and borrow an additional $47 billion from wealthy member governments.[47] Even after disbursing nearly $10 billion to Brazil, $5.6 billion to Russia, and $6.3 billion to Indonesia during its 1998-1999 financial year,[48] the IMF could backstop a respectable 35 percent of gross outflows from the developing world. By 2006, with large emerging market economies issuing bonds and repaying the IMF, it could lend up to $189 billion of its own resources—but that was only eleven percent of the $1,723.8 billion in outflows from the developing world.[49] Including $1,941.4 billion from the euro area in 2006 would put available IMF resources at five percent of the relevant capital outflows. Then again, no one had imagined in 2006 that the IMF would be disbursing $20.6 billion to Greece and $8.1 billion to Ireland in just four years.[50]

45. While their effect in sovereign debt markets is the subject of a heated debate, at least in theory, the rise of credit derivatives can further exacerbate the divergence between creditor incentives and their contractual claims. *See* Patrick Bolton & Martin Oehmke, *Credit Default Swaps and The Empty Creditor Problem*, 24 REV. FIN. STUD. 8 (2011); David Mengle, *The Empty Creditor Hypothesis*, ISDA RES. NOTES (2009); Skylar Brooks et al., *Identifying and Resolving Inter-Creditor and Debtor-Creditor Equity Issues in Sovereign Debt Restructuring*, CENTRE FOR INT'L GOVERNANCE INNOVATION (Jan. 12, 2015), https://www.cigionline.org/sites/default/files/pb_no53.pdf; Nikki Tait & David Oakley, *Brussels Gives Sovereign CDS Trading All-Clear*, FIN. TIMES (Dec. 6, 2010), http://www.ft.com/intl /cms/s/0/5be55b2a-016a-11e0-9b29-00144feab49a.html#axzz42Ye94mRb (reporting the results of a European Union inquiry into credit default swaps as a potential source of speculative pressure on sovereign debt prices).

46. PAUL BLUSTEIN, OFF BALANCE: THE TRAVAILS OF INSTITUTIONS THAT GOVERN THE GLOBAL FINANCIAL SYSTEM 1 (2013) (describing the IMF during this period of relative calm, and its efforts to prepare for a potential crisis).

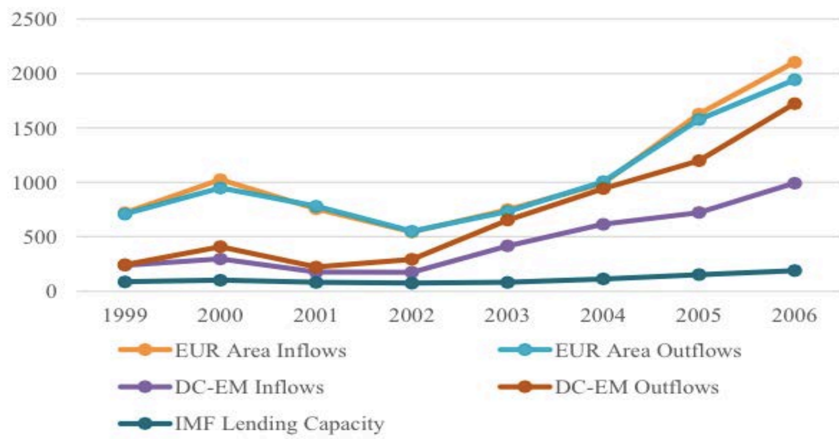
47. *IMF's Financial Resources and Liquidity Position, 1997-December 1999*, http://www.imf.org/external/np/tre/liquid/1999/1299.htm (Net Uncommitted Usable Resources).

48. IMF, *Report of the Executive Board for the Financial Year Ended April 30, 1999*, Annual Report 1999, at 100-101 (Apr. 1999). U.S. dollar amounts are based on SDR1=USD1.37.

49. IMF resources fared better compared to portfolio flows. In 2006, it could finance approximately 19 percent of combined euro area and developing country portfolio outflows. It could supplement this lending capacity in 2006 with $51 billion from borrowing arrangements with members. *IMF's Financial Resources and Liquidity Position, 2004 – December 2006* (One-year Forward Commitment Capacity, memorandum items for General Arrangements to Borrow and New Arrangements to Borrow); IMF, *Financial Market Turbulence: Causes, Consequences, and Policies*, Global Financial Stability Report 2007, Stat. App. Table 1, 136-37 (Oct. 2007) [hereinafter IMF GFSR October 2007]. Although portfolio flows are typically considered more volatile, the distinction between portfolio and other types of capital flows may be overstated. *See, e.g.*, UN Development Programme, Towards Human Resilience: Sustaining MDG Progress in an Age of Economic Uncertainty 86 (2011).

50. IMF, *Financial Operations and Transactions*, Annual Report 2011 App. Table II.4 (2011), U.S. dollar amounts are based on SDR1=USD1.62.

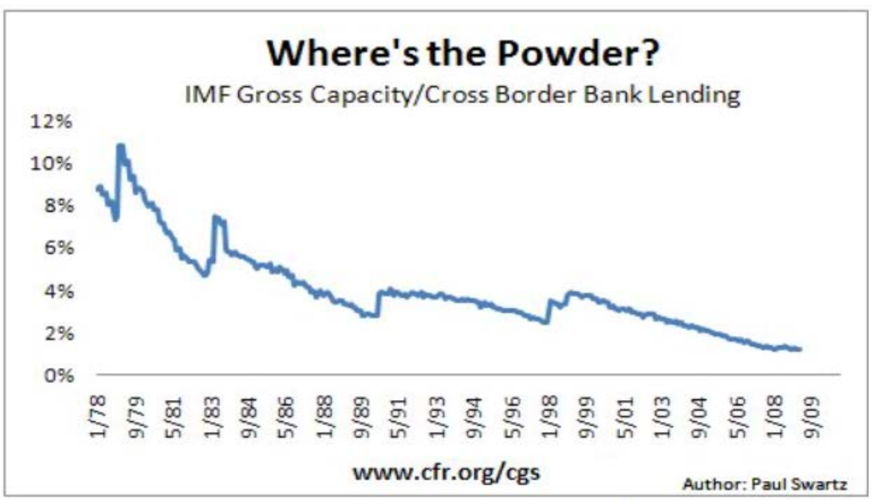
Figure 2:
Total Capital Inflows and Outflows, IMF Lending Capacity
Euro Area, Developing Countries and Emerging Markets
(USD billions)



Source: IMF [51]

Long-term decline of IMF lending capacity relative to cross-border bank lending, which can be prone to runs, paints a similar picture in Figure 3.

Figure 3:



Source: Council on Foreign Relations[94]

51. IMF GFSR October 2007, *supra* note 36; *IMF's Financial Resources and Liquidity Position, 1997-December 1999*, *supra* note 89; *IMF's Financial Resources and Liquidity Position, 2004 – December 2006*, *supra* note 91. Figures for IMF lending capacity exclude available borrowing arrangements, which stood at $47 billion in December 1999, and $51 billion in December 2006. *Id. See also*, *One-Year Forward Commitment Capacity*, *supra* note 87; MARKUS JAEGER, DEUTSCHE BANK RESEARCH, DOES THE IMF HAVE SUFFICIENT RESOURCES TO BAIL OUT THE EMERGING MARKETS? (2008) (market view of IMF capacity in light of the "explosion" in net private capital flows and potential future exposure).

To the extent the IMF's power to set restructuring parameters and nudge the process along depended on its unique ability to mobilize enough financing quickly to stop a run, stem contagion, and keep the distressed economy afloat during the workout, this power appeared to be at risk.[52]

The IMF's lopsided governance made matters worse. It reflected twentieth century compromises, with the G-7 and small European countries substantially overrepresented compared to the big emerging markets, whose voice and vote did not reflect the size and international importance of their economies.[53] Yet the incumbents showed few signs of either giving up control or investing in the IMF in the early and mid-2000s. As finance got bigger, powerful stakeholders spoke of the need to constrain the IMF as a source of "bailouts" and moral hazard.[54] Meanwhile, post-crisis countries, particularly in Asia, accumulated vast foreign exchange reserves and put in place regional arrangements that would allow them to bypass the IMF should misfortune strike again.[55]

Despite its outdated vote allocation, shrinking scale, self-insuring clients, and contested track record, the IMF remained indispensable in a debt crisis. It had the unique combination of institutional memory and analytical capacity, a record of past practice, a global membership, and a formal governance structure prescribed by treaty—which made its actions at least somewhat accessible and predictable. The IMF's role as distressed countries' gateway to external financing long made it a valuable lever for other actors; it rose in importance as other elements of the debt restructuring regime weakened. Public and private creditors sought to use IMF lending and arrears policies to gain leverage in restructuring negotiations. Sovereign borrowers cited IMF analysis and policy conditions to bolster their position *vis-à-vis* foreign and domestic constituents.[56] As it was called upon to fill more coordination gaps, the IMF was becoming both under-funded and overtaxed.

Weaker discipline among creditors was not all bad for the debtors, even if it threatened to prolong the restructuring process. Without tightly-knit creditor groups linked by cross-conditionality, sovereigns could play creditors off against one another. If private foreign investors

52. James M. Boughton, *The IMF as Just One Creditor: Who's in Charge When a Country Can't Pay?* CENTRE FOR INT'L GOVERNANCE INNOVATION 1 (Apr. 27, 2015); James M. Boughton et al., *IMF Lending Practices and Sovereign Debt Restructuring*, CENTRE FOR INT'L GOVERNANCE INNOVATION 4 (June 9, 2014).

53. *See, e.g.*, EDWIN M. TRUMAN, A STRATEGY FOR IMF REFORM (2006) (arguing for an overhaul in IMF governance and work program).

54. *See, e.g.*, JOHN B. TAYLOR, GLOBAL FINANCIAL WARRIORS: THE UNTOLD STORY OF INTERNATIONAL FINANCE IN THE POST-9/11 WORLD, at 98-110, 130-32 (2007), Hagan, *supra* note 1, at 345.

55. *See, e.g.*, Barry Eichengreen, *Commentary: A Blueprint for IMF Reform: More Than Just a Lender*, 10 INT'L FINANCE 153 (2007). The motives for reserve accumulation are a matter of debate, with authoritative commentary split between attributing it to self-insurance against crises and exchange rate management.

56. *See* IMF, *Access Policy in Capital Account Crises*, Policy Papers 18-26 (July 29, 2002); IMF, *The Fund's Lending Framework and Sovereign Debt—Preliminary Considerations*, Policy Papers 8-21 (May 22, 2014). *See also* Lee C. Buchheit & Rosa M. Lastra, *Lending into Arrears—A Policy Adrift*, 41 INT'L LAW. 939 (2007); JAMES M. BOUGHTON, THE SILENT REVOLUTION: THE INTERNATIONAL MONETARY FUND 1979-1989 (2001); NGAIRE WOODS, THE GLOBALIZERS: THE IMF, THE WORLD BANK AND THEIR BORROWERS (2006) (describing emerging markets officials using the IMF as a lever in domestic reform negotiations).

would not lend or restructure, a government might turn to an oil-rich neighbor; if IMF conditions seemed too onerous, it could try borrowing from domestic banks, or from China; if Paris Club relief were slow in coming, foreign bondholders might be persuaded to move first.[57]

The upshot of these developments was a restructuring regime that was losing sway over both debtors and creditors. The London Club had disappeared as bank loans gave way to bond financing; the Paris Club at risk of becoming a side show. The IMF was at risk of becoming "just one creditor" among many—and far from the biggest—anchoring a regime where other creditors could not be counted upon to cooperate.[58] In the background, national courts presided over isolated claims with no mandate to consider the overall debt picture, and had no way to compel the sovereign to follow their orders. Such a regime might be able to nudge willing parties to compromise, but was hardly fit to host mortal combat to come.

II. Greece in Context

In the article from which I draw in this testimony, I describe a series of crises between 2010 and 2015 that publicly exposed major flaws in the existing sovereign debt restructuring regime. Below I focus on Greece because, in my view, it presented the biggest challenge to the IMF's role in the regime—but also illustrates its potential. Early in the crisis, the IMF repeatedly failed to shape debt restructuring outcomes, tainting public perceptions of its analysis and lending decisions. Greece also demonstrated the toxic politics of government-to-government debt—reviving ugly stereotypes and stoking historical resentments—which threatened political compromises underpinning Europe's monetary union.[59]

The IMF, the European Commission, and the European Central Bank (ECB) launched a €110 billion ($145 billion) financing program for Greece on May 9, 2010. The IMF's contribution of €30 billion ($40 billion) to this "troika" package was by far the largest program in its history.[60] The program went ahead despite IMF staff concerns about public debt sustainability, and based on heroic assumptions about tax collection, privatization, unemployment, economic growth, and a speedy return to the capital markets.[61] Figure 4, drawn from the IMF's own ex-post evaluation of that program, illustrates.

57. Argentina, Ecuador, Nigeria and Venezuela all successfully deployed such strategies.

58. Boughton, *supra* note 52.

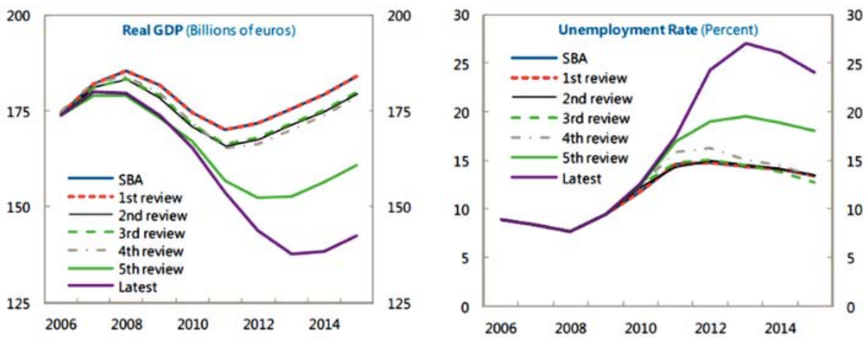
59. IMF, *Greece: Ex Post Evaluation of Exceptional Access under the 2010 Stand-By Arrangement*, Country Report No. 13 (June 2013) [hereinafter IMF Ex-Post Evaluation of SBA (Greece)].

60. Press Release, IMF, IMF Executive Board Approves €30 Billion Stand-By Arrangement for Greece, No. 10/187 (May 9, 2010); IMF Ex-Post Evaluation of SBA (Greece) *supra* note 59, at 9.

61. IMF Ex-Post Evaluation of SBA (Greece) *supra* note 59, at 8; *see also* WILLIAM R. CLINE, MANAGING THE EURO AREA DEBT CRISIS 185 (2014); David Keohane, *Greek Government Acquires More Realistic Crystal Ball*, FT ALPHAVILLE (Nov. 1, 2012) (citing IMF and market analysis of IMF forecasts).

Figure 4:
Evolution of IMF Program Projections for Greek GDP and Unemployment under the 2010-2012 IMF Stand-By Arrangement for Greece[62]

("SBA" reflects projections in the May 2010 IMF stand-by arrangement)



Early baseline projections had the debt ratio rising from 115 percent of Gross Domestic Product (GDP) in May 2010 above 150 percent in 2013, potentially reaching 220 percent in some stress scenarios.[63] The Fund's assumptions and program conditions were more sober than those of the European authorities before the IMF had been brought in. Moreover, IMF staff analysis, however rosy, was sufficiently pessimistic to warrant the conclusion that Greek debt could not be sustainable with "high probability" in the medium term.

This judgment about debt sustainability posed a problem under the IMF's policy barring large-scale lending to over-indebted countries. As the staff saw it, the IMF had two choices: condition its participation in the troika on Greek debt relief, or ask its Executive Board to approve a policy change. Less than two years after the failure of Lehman Brothers had brought global finance to the brink, fear of Greece turning into "another Lehman-type event" took debt restructuring off the table.[64]

The Lehman reference underscores the challenge of managing debt crises in large economies integrated in regional and global financial systems (the euro area is an extreme example). Neither the IMF nor the European Union was prepared to address contagion in 2010 with liquidity support for its likely victims. Although IMF members had agreed in 2009 to lend the Fund up to $576 billion,[65] its resources remained visibly inadequate to rescue large euro area

62. IMF Ex-Post Evaluation of SBA (Greece), *supra* note 59, at 13, 17, 25.

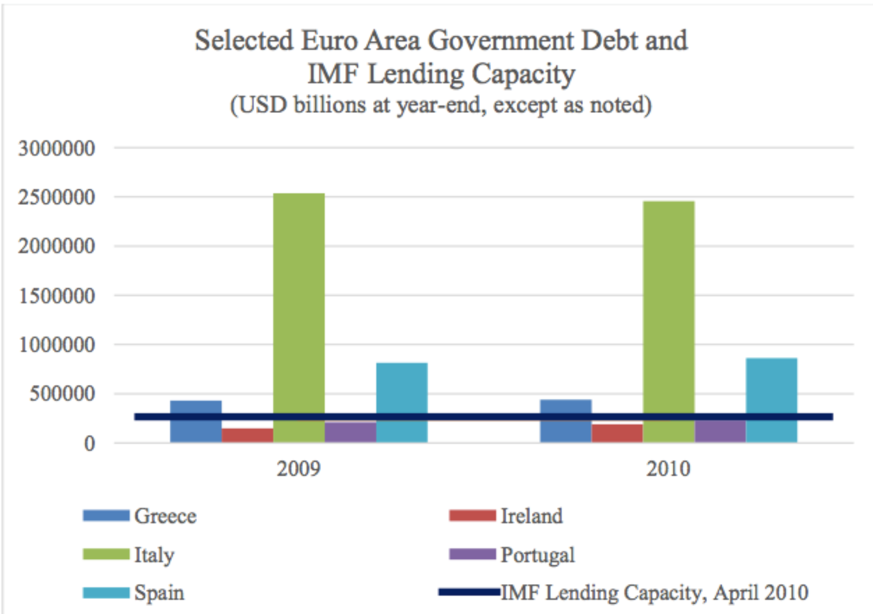
63. Paul Blustein, *Laid Low: The IMF, the Euro Zone and the First Rescue of Greece*, CENTRE FOR INT'L GOVERNANCE INNOVATION 2 (Apr. 7, 2015); IMF, *Greece: Preliminary Debt Sustainability Analysis—Updated Estimates and Further Considerations*, Country Report No. 16/130 1 (May 2016), [hereinafter IMF Preliminary Greek DSA May 2016] (citing public debt ratio of 115 percent of GDP, projected to top 150 percent despite policy adjustment); IMF Ex-Post Evaluation of SBA (Greece), *supra* note 59, at 16, 26-27 (citing initial projections for debt to peak at 154-156 percent of GDP in 2013, but continuing to rise above 220 percent under stress).

64. Blustein, *Laid Low*, *supra* note 63 at 27.

65. IMF ANNUAL REPORT FY2011 at 49 (tenfold expansion and activation of New Arrangements to Borrow (NAB) between November 2009 and April 2010); DOMENICO LOMBARDI & SARAH PURITZ MILSOM, THE BROOKINGS

economies, certainly not two or three at the same time. The IMF's lending capacity in April 2010, on the eve of its first Greek program, was $255.5 billion, counting supplemental borrowing of $253 billion.[66] In the next twelve months, it would approve nearly $210 billion in new commitments, including large, front-loaded programs for Greece and Ireland.[67] Spain and Italy, which looked shaky, were in a different category altogether. At the end of 2009, Spain had $815 billion in sovereign debt and Italy had $2.5 trillion, compared to Greece's $431 billion. In less than two years, foreign banks reduced their Italian government debt holdings by over $125 billion.[68]

Figure 5:



Sources: Eurostat, Board of Governors of the Federal Reserve System, IMF[69]

INSTITUTION, THE EURO-AREA CRISIS: WEIGHING OPTIONS FOR UNCONVENTIONAL IMF INTERVENTIONS 4 (Dec. 2011).

66. IMF's Financial Resources and Liquidity Position, 2008 – April 2010.

67. IMF ANNUAL REPORT FY2011, Appendix Table II.1: Arrangements Approved during Financial Years Ended April 30, 2002-2011, and Appendix Table II.4: Purchases and Loans from the IMF, Financial Year Ended April 30, 2011. SDR=USD1.61967. IMF Financial Activities -- Update April 28, 2011.

68. Approximately half of Italian government debt was held by non-residents, mostly in the euro area. INT'L MONETARY FUND, ITALY: SELECTED ISSUES, IMF Country Report No. 12/168 87-88 (Jul. 2012) (detailing Italian debt composition); IMF, *The Quest for Lasting Stability*, Global Financial Stability Report 19 (Apr. 2012) (Figure 2.6, showing a reduction of foreign bank holdings by €94 billion between Q1 2010 and Q3 2011). EUR=USD1.3449 at the end of Q3 2011. Board of Governors of the Federal Reserve System (US), U.S. / Euro Foreign Exchange Rate [DEXUSEU], (retrieved from FRED, Federal Reserve Bank of St. Louis, May 31, 2016); *see also* IMF, *Restoring Confidence and Progressing on Reforms*, Global Financial Stability Report 30 (Oct. 2012) (Figure 2.9, showing the exit of foreign private investors in Italian and Spanish government debt).

69. Eurostat, Government Consolidated Gross Debt by Components - Annual Data [tipsgo11], ("Government debt is defined as total gross debt at nominal value outstanding at the end of the year and consolidated between and within the sectors of general government."); Board of Governors of the Federal Reserve System (US), U.S. / Euro Foreign Exchange Rate [DEXUSEU], (retrieved from FRED, Federal Reserve Bank of St. Louis, May 31, 2016); *IMF's Financial Resources and Liquidity Position, 2008 – April 2010* (One-Year Forward Commitment Capacity).

If the crisis in Greece spread to Italy, contagion across the euro area, to the United Kingdom and the United States could bring back the darkest days of September 2008.[70] The euro area might have addressed the problem on its own—it had a powerful central bank, and strong economies at the core—but it was only beginning to develop the political consensus, legal and institutional tools against contagion.[71] When the risk of contagion topped the policy agenda, it was down to the IMF, which had crisis-fighting experience and resources on standby. In 2010, these resources were not enough to support new and potential IMF clients, which were vastly bigger than the old ones.

With no backstop in sight for large economies vulnerable to contagion from Greece, the IMF changed its lending policy. From May 2010, countries whose debts were not sustainable with high probability could avoid restructuring and still get large-scale IMF support, provided there was a high risk of "systemic international spillovers."[72] Greece then proceeded to borrow at least in part for the sake of broader financial stability—although Greece alone would be bound to repay.[73]

The IMF's failure to insist on debt relief for Greece in 2010 was not in itself a challenge to the old sovereign debt restructuring regime; it was the IMF's inability well into 2011 to force a restructuring once it became convinced that one was necessary, and despite the risk to its own resources.[74] Finance officials had always been wary of debtor moral hazard, hurting banks, spending tax money, and, more recently, undermining the "catalytic" effect of IMF lending on the debtor's access to the private capital markets.[75] The Lego house in Figure 1 did not require debt reduction *per se*, only some combination of new money, debt restructuring, and adjustment to fill the financing gap during the program period. Countries avoided restructuring in 21 out of 53 emerging market sovereign debt distress episodes identified by the IMF between 1980 and 2012.[76] Debt stock sustainability only became a formal condition for very large ("exceptional access") IMF programs in a policy introduced in 2002, as part of a campaign to limit bailouts and moral hazard.[77]

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70. IMF, *Italy: 2012 Article IV Consultation*, Country Report No. 12/167, at 12 (2012), https://www.imf.org/external/pubs/ft/scr/2012/cr12167.pdf. (Box 2: Italy – Spillovers from a Potential Intensification of the Euro Area Crisis, showing cross-border borrowing by Italian banks exceeding €1.4 trillion, primarily from Germany, France, and Austria, as well as elsewhere in the euro area, Eastern Europe and the United States).

71. IMF, *Euro Area Policies: 2015 Article IV Consultation—Press Release, Staff Report, and Statement by the Executive Director*, Country Report No. 15/204, at 5 (July 2015) [hereinafter, Euro Area Article IV Report 2015] (highlighting continuing risk of contagion from Greece despite new ECB tools).

72. *IMF Reforms Policy for Exceptional Access Lending*, IMF Survey, (Jan. 29, 2016).

73. *Supra* note 11-12 and accompanying text; *compare* lending to Greece to avoid a crisis elsewhere in Europe and lending to developing countries in the 1980s to avoid a banking crisis in New York and London, *supra* note 16 and accompanying text. The argument that Greece borrowed for lack of better tools to avoid contagion broadly is distinct from the argument that troika loans bailed out French and German banks. *See, e.g.*, Dan Davies, *2010 and All That—Relitigating the Greek Bailout (Part 1)*, BULL MKT. (Jul. 21, 2015) (considering accusations that the Greek rescue benefited German and French financial institutions).

74. *See* Ashoka Mody, *In Bad Faith*, BRUEGEL (July 2, 2015), http://bruegel.org/2015/07/in-bad-faith/ (arguing that the IMF acted in bad faith by letting debt relief be deferred while insisting, along with euro area governments, on crippling adjustment conditions in Greece).

75. IMF Lending Framework Annexes, *supra* note 29 at 9-20.

76. *Id*. at 28.

77. The new criterion was part of an effort to limit debtor and creditor moral hazard from IMF programs, instituted just as the global financial markets entered a period of relative calm. *Id*.; TAYLOR, *supra* note 54, at 119-21, 130-32 (2007).

There is no evidence that the 2002 policy made large programs any more exceptional, nor that it made debt restructuring more common—there were few crises to test it in the mid-2000s. However, for as long as the IMF remained a source of some and the gatekeeper for most external financing in crisis, the 2002 reform raised the stakes for IMF staff analysis of borrowers' debt sustainability. As the policy came to be interpreted, large-scale IMF programs would require deep debt restructuring unless that analysis showed sovereign debt to be sustainable "with high probability."[78] Private creditors became big consumers of the analysis, and tough critics of the methodology.

The IMF's capacity to leverage its analytical and financial resources to shape a country's recovery program had long anchored the sovereign debt restructuring regime. Greece exposed the limits of this role. IMF staff called for debt relief early in 2011; a bond restructuring came a year later, after more than $150 billion in private capital had fled the country and was replaced by public funds from the euro area and the IMF.[79]

After the bond restructuring in March 2012, discussed in more detail below, a new four-year Fund program brought more lending and projections that Greek debt would fall below 120 percent of GDP by 2020—even as domestic politics deteriorated and support for the program sank.[80] According to the IMF's own assessment in 2017, this program still suffered from implausibly rosy projections about political support for reform, market confidence and economic performance. However, IMF staff were markedly clearer in expressing their skepticism in the program documents[81] and, after a program overhaul in 2013, program assumptions drifted closer to reality (Figure 6).

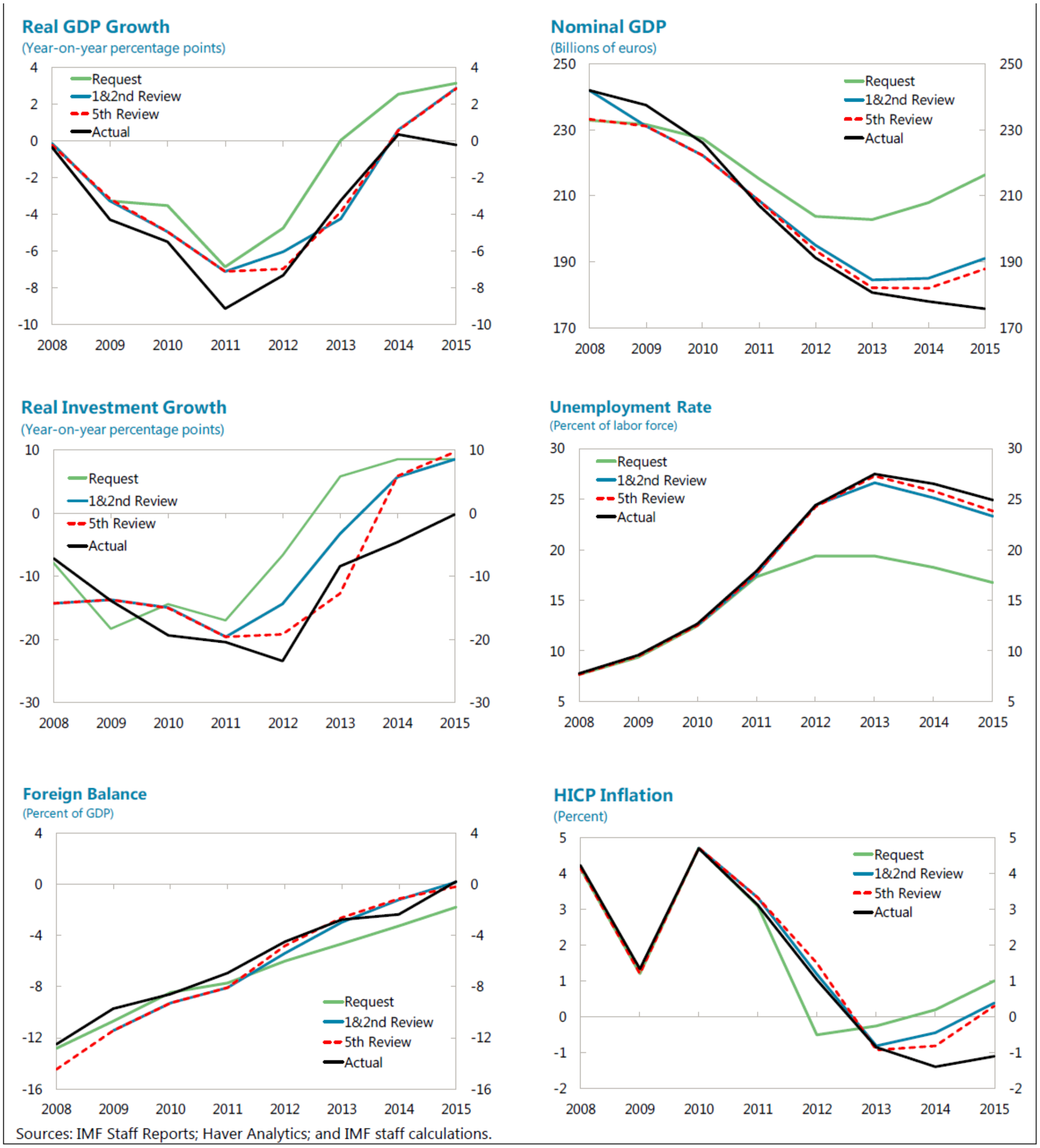
78. IMF Lending Framework Annexes, *supra* note 29.

79. IMF Ex-Post Evaluation of SBA (Greece), *supra* note 59, at 27; *see also* Matthew Higgins & Thomas Klitgaard, *The Balance of Payments Crisis in the Euro Area Periphery*, 20 CURRENT ISSUES ECON. & FINANCE, no. 2, 2014, at 7.

80. IMF exposure would remain essentially unchanged. Press Release, IMF, IMF Executive Board Approves €28 Billion Arrangement under Extended Fund Facility for Greece, No. 12/85 (Mar. 15, 2012).

81. IMF, *Greece: Ex Post Evaluation of Exceptional Access under the 2012 Extended Arrangement* No. 17/44 (Feb. 2017) [hereinafter IMF Ex-Post Evaluation of EFF (Greece)], at 1.

Figure 6:
Evolution of IMF Program Projections
under the 2012-2016 IMF Extended Fund Facility for Greece



Source: IMF[82]

Nonetheless, the program went off track in 2014. In July 2015, the debt stock neared 180

82. IMF Ex-Post Evaluation of EFF (Greece), *supra* note 81 at 18.

percent of GDP and the Greek banking system was on life support from the ECB, rationing cash withdrawals. A new government was in a standoff with the troika over a third IMF program, and the IMF was at odds with its troika partners over government-to-government debt relief. In the middle of an acute political crisis, Greece threatened to abandon the euro and delayed repayment of €1.55 billion ($1.73 billion) to the IMF . . . causing new anxiety for being "the first developed country to default" on the multilateral lender.[83]

The second IMF program never came back on track, and was abandoned in January 2016 in the face of continued political turmoil. After a brief drop in 2012, Greek debt-to-GDP ratio was back at 180 percent in early 2016, and has malingered there since. In May 2016, Euro area governments agreed to disburse €10.3 billion ($11.5 billion) in new loans, but the IMF held back on a new program: it would wait for "a clear, detailed Greek debt restructuring plan."[84] This was finally a principled position that might have produced better results had it come sooner.

IMF staff had a hard enough time negotiating Greek program parameters with euro area institutions when private investors' money was on the line; with euro area taxpayers as the dominant creditors, the political challenge was nearly insurmountable.[85] At the outset, program parameters had to be settled with euro area institutions first, leaving little room for Greek agency (or policy "ownership")[86] For their part, euro area leaders had left themselves limited scope to maneuver: after telling their citizens that EU treaties categorically barred public debt forgiveness, they had to choose between the prospect of outright default and a mix of transactional engineering, accounting gimmicks and wishful thinking about Greek citizens' tolerance for more austerity.[87] More bilateral financing was unpalatable, but default was still unthinkable for fear of financial and political contagion. The search for alternatives had produced six years of crippling economic decline and political upheaval.[88]

It was a foregone conclusion that the Paris Club would have no part in the Greek debt restructuring, even though it had been the preeminent forum for restructuring government-to-government debt, while the Greek debt stock looked more and more like those of the poorest countries in the Paris Club, cut off from private markets.[89] Nonetheless, Europe insisted on

83. *See, e.g.*, Reuters, *Greece Becomes the First Developed Country to Default on IMF Loan*, NEWSWEEK (July 1, 2015).

84. *Greece Bailout: IMF Queries Eurozone Debt Relief Deal,* BBC (May 25, 2016).

85. IMF Ex-Post Evaluation of SBA (Greece), *supra* note 59, at 21, 30-32.

86. On Greek program "ownership," see IMF Ex-Post Evaluation of SBA (Greece), *supra* note 59. *Compare* BLUSTEIN, *supra* note 54, *with* WOODS, *supra* note 99 (on economic reform and power dynamics between emerging market and multilateral officials).

87. *See, e.g.*, Ashoka Mody, *Wolfgang Schäuble, Debt Relief, and the Future of the Eurozone*, BRUEGEL (August 6, 2015); Paul Carrel, *Legal Gray Areas Give Scope for Greek Debt Relief If Europe Wants It*, REUTERS (July 9, 2015).

88. *See* Mody, *supra* note 87.

89. Both had triple-digit debt ratios and few private creditors. For example, at the end of 2012, after most of its privately held debt had been repaid or restructured, Greece had a debt-to-GDP ratio north of 150 percent and rising, while private creditors held approximately 20 percent of its debt; the rest was in the hands of other governments and the IMF. IMF Preliminary Greek DSA May 2016, *supra* note 63, at 4; *compare* debt composition figures cited in Jeromin Zettelmeyer, Christoph Trebesch & Mitu Gulati, *The Greek Debt Restructuring: An Autopsy*, 28 ECON. POL'Y

handling Greece as a family affair. To lighten its debt service burden, euro area governments quietly extended repayment term to between fifteen and forty years, and lowered interest rates to 1.2 percent on average for the moment; however, they stood firm against reducing principal claims.[90] This approach might have relieved near-term liquidity pressures, but was not enough to alter the debt trajectory, nor to stop government-to-government debt from fueling political fights that cast doubt over the viability of the monetary union.[91]

In contrast to the tortured path to official debt relief, the 2012 Greek bond restructuring was a brilliantly executed operation—on a technical level. Once it was launched, the deal was done, and done quickly. It covered a record-breaking stock of debt, approximately €200 billion ($260 billion), and reduced the private debt burden by over fifty percent.[92] The smooth execution was mostly attributable to the fact that more than ninety percent of the bonds were governed by Greek law and could be amended retroactively by statute.[93] The Greek Bondholder Act enabled the government to call a single vote of all its Greek-law bond holders, with quorum and voting thresholds set low at fifty percent and 66 2/3 percent, respectively, to ensure success.[94] The voting mechanism in Greek retroactive legislation was fundamentally unlike then-standard majority amendment provisions ("Collective Action Clauses," or "CACs") in sovereign bonds: the law was designed *ex post* to prevent individual bond series from dropping out and free-riding on the rest. CACs incorporated in contracts *ex ante* had always allowed some bonds to drop out. The single stock-wide vote legislated in Greece meant that either all or none of the bonds polled were bound to restructure.

Greece got much less benefit from the CACs already incorporated in its foreign-law bond contracts, which had been held up as a bulwark against free-riders in G-7 statements and G-10 reports since the mid-1990s.[95] As was customary at the time, CACs in Greek bond contracts governed by English and Swiss law applied only to individual bond series. Holdouts secured blocking positions in more than half of the series by number. The restructuring vote failed for approximately forty-four percent of foreign-law principal outstanding.[96] Private creditors holding

513 (2013) [hereinafter Greece Autopsy], *and* Liberia in 2007-2008, with 28 percent of the debt stock in the hands of commercial creditors, and an external debt-to-GDP ratio of 186 percent before debt relief. IMF, *Liberia: Enhanced Initiative for Heavily Indebted Poor Countries—Completion Point Document and Multilateral Debt Relief Initiative*, Country Report No. 10/192, at 32, 41 (July 2010).

90. IMF Preliminary Greek DSA May 2016, *supra* note 142, at 4-5 (arguing that substantial official debt relief to date is not enough to achieve sustainability); *see also* William R. Cline, *Policy Brief 15-12: From Populist Destabilization to Reform and Possible Debt Relief in Greece*, PETERSON INST. INT'L ECON. (Aug. 2015).

91. *See, e.g.*, Jason Hovet, *Czech President Floats Idea of Greece Paying Debts by Hosting Migrant Centers*, REUTERS (Andrew Bolton ed., Mar. 6, 2016); Yanis Varoufakis, *Germany Won't Spare Greek Pain—It Has an Interest in Breaking Us*, GUARDIAN (July 10, 2015).

92. Greece Autopsy, *supra* note 89, at 2.

93. Greece Autopsy, *supra* note 167. Retroactive legislation superimposed a majority voting mechanism on the entire stock of domestic-law bonds. Although it was enacted after consultations with creditors, it was in no way contractual – neither consensual nor market standard. The thresholds were designed to ensure that dissenting creditors would be outvoted by a combination of Greek and other euro area banks.

94. *Id.* at 11-12

95. *Id.* at 42.

96. Greece Autopsy, *supra* note 89.

€6.4 billion ($8.3 billion) in bonds kept their old bonds and have been paid on schedule since.[97]

The 2012 restructuring also caused controversy for excluding €56.7 billion ($73.7 billion) in bonds held by euro area institutions, primarily the ECB and national central banks in the euro area.[98] The ECB was Greece's largest bondholder and the biggest holdout. The exclusion of central bank holdings sent the signal that some official creditors would get paid first even when their contracts were identical to those of private creditors, and threatened to make official support synonymous with subordination in the eyes of such creditors.[99] To diffuse market fears that could undermine its emergency interventions, the ECB later promised that its new financing would be on equal footing (*pari passu*) with the debt owed to private creditors.[100] This promise has not been tested.

In sum, from the perspective of the evolving sovereign debt restructuring regime, the Greek experience between 2010 and 2016 implied that the IMF was weak, the Paris Club irrelevant, government creditors paralyzed by domestic politics, and issue-by-issue CACs mostly futile. It highlighted a peculiar structure of accountability in crisis management institutions, which allowed Greece to accumulate unpayable debt at least in part thanks to their own inability to stop contagion and manage domestic politics in creditor countries. Echoing the experience of developing countries in the 1980s, Greece took on more and more debt at least in part because the international financial architecture was unequipped to process its default.

Today, Greece has total debt of €326 billion ($364 billion), of which it owes €226 billion ($252 billion) to the ECB, the European Financial Stability Facility (EFSF) and its successor the European Stability Mechanism (ESM), and other governments in the euro area.[101] In other words, Greece's debt problem is overwhelmingly official, and therefore politically fraught. As noted earlier, much of the official debt has been restructured to lengthen maturities and reduce the interest rate, so that Greece's payments are relatively modest. However, the enormous stock of debt and the likelihood that it would not come down on its own in the foreseeable future can depress investor confidence, and dim recovery prospects further. Perhaps more importantly, given recent history, the large debt stock can severely undermine political support for reform and continue to serve as a source of political discord in the euro area.

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97. *Id*.

98. *Id*. at 15, 28.

99. In addition to the Eurosystem holdings, €350 million in bonds held by the European Investment Bank (EIB) were excluded from restructuring. *Id*. On the other hand, Greek bonds held by the Norwegian sovereign wealth fund were treated alongside privately held bonds, and restructured over its objections. Richard Milne, *Norway State Fund Sells Eurozone Debt*, FIN. TIMES (May 4, 2012).

100. Press Release, European Central Bank, Technical Features of Outright Monetary Transactions (Sept. 6, 2012) ("The Eurosystem intends to clarify in the legal act concerning Outright Monetary Transactions that it accepts the same (*pari passu*) treatment as private or other creditors with respect to bonds issued by euro area countries and purchased by the Eurosystem through Outright Monetary Transactions, in accordance with the terms of such bonds.").

101. Jeromin Zettelmeyer, Eike Kreplin, & Ugo Panizza, *Does Greece Need More Official Debt Relief? If So, How Much?*, Peterson Institute for International Economics Working Paper 17-6 (Apr. 2017) at 3.

On the bright side, the IMF's position in the troika arrangement has changed dramatically since the early days of the Greek program. After ending its last disbursing program in early 2016, the Fund has actively engaged in policy formulation and review, but has not resumed a financing program pending credible assurance of adequate debt relief by Greece's European partners. Meanwhile, the ESM has extended an €86 billion ($96 billion) program for Greece, covering the period from August 2015 to August 2018. As part of the program, euro area governments have insisted on IMF involvement to boost the credibility of policy design and performance review. In other words, for as long as it stands firm on its policy principles, the IMF may well have more policy clout now than it did in 2010, with less of a financial stake. This may be a temporary and idiosyncratic development, a function of recent history with IMF and euro area performance in the Greek crisis. Continued hopes for the IMF's return to a financing role, albeit a modest one, may have played a part. Nonetheless, it is a significant development. It shows that, while money is important, it is ultimately not the sole—or even the biggest—source of the IMF's leverage.

III. Exceptional Access Reform and Contagion

The IMF's involvement in Greece in 2010-2012 faced withering criticism from all quarters. Fund staff responded with a concerted effort to recapture policy initiative in debt restructuring beginning in 2013.[102] Most importantly, in January 2016, the Executive Board did away with the systemic risk exception that had allowed the IMF to lend to Greece and others despite its questionable debt profile.[103] It also expressly broadened the range of restructuring outcomes IMF staff could seek when a country's debt sustainability was in doubt, introducing a measure of flexibility in the 2002 lending policy as it had been interpreted.[104]

Under the new policy, a country whose debt sustainability is in the gray zone might be asked to secure its creditors' commitment to maintain their exposure as a condition of IMF support. Although the debt would not be paid on schedule, creditors would not necessarily suffer losses until and unless the analysis indicated that the debt was, in fact, unsustainable. However, public money would not finance massive payments to private creditors, as happened in Greece in 2010-2012. Similar conditions had been imposed on several occasions before 2002.

Had the revised policy been in place in 2010, it probably would not have changed the outcome in Greece. European authorities at the time resisted the notion of *any* change in the payment terms of EU member state debt, and, in the aftermath of Lehman, other governments agreed. The no-restructuring bridge was crossed with the 2012 Greek bond exchange. On balance, the new exceptional access policy should reduce pressure on IMF staff to produce optimistic debt

102. *See Sovereign Debt Restructuring—Recent Developments and Implications for the Fund's Legal and Policy Framework*, IMF (April 26, 2013) [hereinafter IMF 2013 Sovereign Debt Review].

103. Press Release, IMF, IMF Executive Board Approves Exceptional Access Lending Framework Reforms, No. 16/31 (Jan. 29, 2016).

104. *Id*.

projections in order to lend.

Nonetheless, he subject of contagion, which loomed large over the IMF's early lending to Greece and the erstwhile systemic risk exception, remains an important gap in the international policy framework. The IMF's revised access policy effectively tries to remove the Fund from the contagion calculus when the crisis country's debt is unsustainable. The policy approved in January 2016 suggests that, to stem contagion, other governments should finance a country like Greece bilaterally on below-market terms.[105]

Disclaiming responsibility for fighting contagion should help reduce political pressure on the IMF to lend to over-indebted countries—a good thing.[106] However, if this disclaimer is to have broad credibility, it is imperative for other parts of the global financial system to take on the task of addressing the risk of contagion.[107] In Europe, a response to contagion without the IMF is more plausible today than it might have been in 2010 or even 2012, since the euro area has developed an expanded toolbox to provide central bank liquidity and multilateral crisis financing, at least to the smaller economies.[108] However, if these tools, in Europe or elsewhere, prove to be inadequate relative to the scale of likely capital outflows, pressure on the IMF would return in the next crisis. As a membership organization with a crisis-fighting mandate, the IMF could find such pressure hard to resist, with further damage to its analysis and reputation.

IV. Lessons and Policy Recommendations

Sovereign debt restructuring has always been a flawed enterprise. It would be wrong to describe the 1980s and the 1990s as the halcyon days of debt relief and burden-sharing. Agreements took years to negotiate and failed to secure a durable exit from debt crises. There were endless iterations of piecemeal relief and painful adjustment. But by the end of the twentieth century, debt crises unfolded in a regime that had its own structure and customs, and exerted a measure of discipline over its constituents within an IMF-centered analytical framework, thanks to cohesion among similarly-situated creditors and linkages among public, private, domestic and external restructuring processes. The regime was surprisingly resilient: creditors could come and go, but the overall framework would change incrementally, in response to discrete problems. It was recognizable from crisis to crisis, and was familiar to a small core of specialists and repeat players. Nonetheless, it was unintelligible as a whole, and felt unaccountable to the lending and

105. Press Release, IMF, IMF Executive Board Approves Exceptional Access Lending Framework Reforms, No. 16/31 (Jan. 29, 2016) (reporting Board approval of the policy); IMF, *The Fund's Lending Framework and Sovereign Debt—Further Considerations*, Policy Paper (Apr. 9, 2015) (policy reform proposal). Going forward, this would mean a lot more bilateral rescue packages of the sort the United States had arranged for Mexico as a temporary measure to stem the 1990s Tequila crisis.

106. IMF, *The Fund's Lending Framework and Sovereign Debt—Further Considerations*, Policy Paper 10-11 (Apr. 9, 2015).

107. IMF, *The Fund's Lending Framework and Sovereign Debt—Further Considerations*, Policy Paper (Apr. 9, 2015)

108. Euro Area Article IV Report 2015, *supra* note 71

borrowing public.

The Greek crisis was one of a series of shocks that threw the regime into disarray. It was particularly damaging to the IMF. Having lost its preeminence as a lender, the Fund appeared to compromise its analysis under political pressure from a powerful subset of its shareholders. Meanwhile, debt fueled street protests and political crises. It was high time for reform.

Initiatives to reform the sovereign debt restructuring regime poured in from different corners of the sovereign debt universe. As noted earlier, the IMF launched a comprehensive review of sovereign debt restructuring in 2013, including proposals to reform its analysis and lending policies.[109] The U.N. General Assembly called for a multilateral sovereign debt restructuring framework in September 2014, and endorsed a set of "Basic Principles" for sovereign debt restructuring a year later.[110] The resolutions built on a multi-year work program at the U.N. Conference on Trade and Development (UNCTAD), which also produced a restructuring "roadmap" for sovereign debtors.[111] The International Capital Market Association (ICMA) proposed new contract reforms in August 2014, including stock-wide aggregated majority voting adapted from the 2012 Greek Bondholder Law. "Super-aggregated" CACs were a product of ICMA's collaboration with other industry bodies, large emerging market debtors, the IMF and official bilateral creditors. They have been adopted in the majority of new international sovereign bond issues—although outstanding stock without these terms remains high.[112]

Perhaps more than any other actor in the sovereign debt restructuring regime, the IMF has learned from the crisis, and has pursued meaningful reforms. I have already mentioned its initiatives with respect to debt sustainability analysis and large-scale lending, as well as its facilitation of bond contract reform. However, more remains to be done to achieve sustainable outcomes, a comprehensive and collective restructuring process, and an intelligible and accountable restructuring regime.

A. Sustainable Outcomes

The existing regime tends to approach debt sustainability as a fact, an ascertainable threshold: an economy's debt stock or debt service burden is either stable and payable, or doomed to keep growing. As noted earlier, this threshold can be hard to calculate with precision; however,

109. IMF 2013 Sovereign Debt Review, *supra* note 102.

110. Sixty-ninth General Assembly, 102nd Meeting (PM), Discussion of Draft Resolution on "Basic Principles on Sovereign Debt Restructuring Processes" (document A/69/L.84), September 10, 2015.

111. Report of UN Conf. on Trade and Dev., Sovereign Debt Workouts: Going Forward, Roadmap and Guide (Apr. 2015).

112. *Progress Report on Inclusion of Enhanced Contractual Provisions in International Sovereign Bond Contracts*, IMF, December 2016. The U.S. Treasury convened a working group for two years, culminating in ICMA's model clause proposal. *Collective Action Clauses*, INT'L CAP. MKT. ASS'N (August 2014); *see also* Anna Gelpern, Ben Heller & Brad Setser, *Count the Limbs: Designing Robust Aggregation Clauses in Sovereign Debt Contracts* (forthcoming in TOO LITTLE, TOO LATE: THE QUEST TO RESOLVE SOVEREIGN DEBT CRISES (Martin Guzman, José Antonio Ocampo & Joseph E. Stiglitz eds., 2016).

the basic idea is relatively straightforward.

It is generally understood, but less commonly discussed, that sustainability is also a political judgment about distribution of resources between debtors and creditors, and among different creditors with claims on the sovereign. A sovereign debtor allocates political capital, reform efforts and budget resources across a range of priorities that might include veterans' pensions, foreign bond payments, domestic bank bailouts, girls' education, and gold statues of military leaders. A government creditor chooses to lend its crisis-stricken neighbor billions of dollars to pay off its bonds, to wage war on a common enemy, to pursue economic reform, or some combination. In all cases, achieving sustainability requires political support from the government's domestic constituents and foreign creditors, since it implies loss distribution on a substantial scale.

Because they implicate sensitive political calculations, debt sustainability judgments expose IMF staff to political pressure, overt or implied. As the Greek case amply demonstrates, sustainability politics can threaten the IMF's credibility, and cast doubt on its impartiality. Crucially, sustainability judgments are at greater political risk when they are tied rigidly to lending policies. In a battle between emergency financing and analysis, analysis is likely to lose.

To reduce the political burden on the IMF while taking advantage of its staff expertise, it is important to build still-broader consensus around debt sustainability methodology, including the range of assumptions that might go into a model, and to harness independent analytical capacity outside the Fund, which could be mobilized in crisis and be accepted by the relevant constituents.

For example, sustainability determinations could be made by standing or *ad hoc* expert panels, drawn from agreed lists including market, civil society, and public sector representatives. Such panels may consider data and other input from IMF staff, peer governments, market and academic experts. A representative working group under the auspices of the IMF or another multilateral body can develop and periodically review the substantive methodology, and agree on rules for constituting panels. Panel determinations of sustainability need not be binding. However, debtors and creditors may wish to incorporate them by reference in their contracts and policies, to reduce uncertainty in the event of a crisis. In a more modest version of this proposal, the IMF would continue to follow its in-house debt sustainability analysis (DSA), but would account publicly for any material divergence between its own analysis and that of an independent panel.

IMF DSAs can and should continue to play an internal role at the Fund, for example, to assess the risk of a program to the IMF's own resources. This determination is distinct from whether a country should borrow or restructure, and on what terms—and would benefit from being made separately. Put differently, it is plausible for the IMF, the sovereign borrower, and its creditors to reach different conclusions about what is achievable and desirable, taking both politics and economics into account. Each may come to the table with different assessments and different normative priors. IMF staff may well decide that the sovereign's analysis does not add up. In that case, the IMF should not lend. If no other funding is available, the government may default or restructure; it may also continue to engage with the IMF to arrive at a consensus analysis. However, it is also possible that other financing sources would materialize, especially if the IMF is capacity constrained.[113] A key lesson of Greece is that abstaining from a program that might strain its analytical credibility can bolster the IMF's position in a more diverse field of creditors, and preserve its resources—perhaps even to fight contagion.

B. A Comprehensive, Collective Restructuring Process

Among the most sobering lessons from Greece concerns the role of government creditors in sovereign debt restructuring. In late twentieth-century restructurings, debtors came from low- and middle-income countries, while creditors came primarily from G-7 and OECD countries and had a stake in the Paris Club forum. With very rare exceptions, government-to-government debt tended to stay in the hands of the original creditor.

It would be imprudent to assume that the next sovereign debt crisis would continue to follow this pattern. Some of the biggest official bilateral creditors, including China, Russia, and the Gulf states, have no stake or a limited stake in the Paris Club process (although Russia is a member). After the Greek experience, it is safe to say that any debt problems of euro area countries would be entirely outside the club's purview.

On the other hand, more and more governments hold one another's bonds. As noted earlier, the ECB was the biggest holdout in the 2012 Greek restructuring. It has since stated that it considers itself bound to vote against a debt restructuring if CACs were invoked.[114] In a very different setting, Russia's sovereign wealth fund, which holds a $3 billion bond claim against Ukraine, remains the biggest holdout in that country's 2015 bond restructuring. In 2016, the bond trustee sued Ukraine on Russia's behalf in an English court. The court reaffirmed in March of this year that the bonds would be treated as ordinary commercial contracts, notwithstanding the extraordinary circumstances of the Russia-Ukraine conflict.

The rise of new creditors and forms of financing that mix trade, investment, and finance, elevates the importance of consistent accounting and reporting. If the trend continues, it will get harder and harder to categorize a debt contract as official, private, domestic, or external. Private financial industry groups, official creditors, including the IMF and members of the Paris Club, but

113. Boughton, *supra* note 52.

114. Opinion of Advocate General Cruz Villalón delivered on 14 January 2015, in Peter Gauweiler and Others v Deutscher Bundestag, Request for a preliminary ruling from the Bundesverfassungsgericht, at §235 ("Moreover, the ECB has stated in its written observations that, in the context of a restructuring subject to CACs, it will always vote against a full or partial waiver of its claims. In other words, the ECB will not actively contribute to bringing about a restructuring but will seek to recover in full the claim securitised on the bond. The fact that the ECB acts with a view to preserving its claim in full confirms that the aim of its conduct is not to grant a financial advantage to the debtor State but to ensure that the latter meets the obligation it has entered into.")

also the International Forum of Sovereign Wealth Funds,[115] would benefit from comparing notes on their respective accounting conventions and reporting requirements. Unless such groups cooperate in this apparently mundane task, creditors would be tempted to engage in a form of regulatory arbitrage, characterizing the same debt in multiple ways in order to free-ride on others' concessions.

The IMF recently reformed its policy on lending to countries that have stopped paying their government creditors, to bring it in closer alignment with its policy on sovereign arrears to private creditors.[116] This was a sensible change, arguably long overdue. However, more analytical and policy work remains to be done to ensure that all official and all private creditors contribute to resolving a sovereign debt crisis in a fair and meaningful way. In particular, it is important to account for governments and private creditors holding identical tradable bonds while their interests and sources of leverage over the sovereign debtor are very different. The experience in Greece and Ukraine suggest that creditors with fundamentally different incentives should not participate side by side in the same bond restructuring vote; however, there should be a credible way to account for their contribution to the country's recovery program. One way of addressing this problem in a bond restructuring would be to disenfranchise all bonds held by official creditors in a debt restructuring vote—or, at a minimum, to segregate them in a separate voting pool bound to make comparable concessions.[117]

Finally, much has been said already on the need to elaborate the IMF's approach to working with countries that are members of a monetary union. The fact that a sovereign debtor in a monetary union has limited agency, and that other stakeholders and decision makers may be beyond the purview of conventional IMF tools, is among the more painful and awkward lessons of Greece. The fact that a monetary union can, in effect, take some policy areas and sources of funding off the table is counter to the imperative of making the debt restructuring process collective and comprehensive. It also detracts from transparency and legitimacy.

C. An Intelligible and Accountable Regime

Sovereign debt restructuring experience must be accessible and intelligible to the public. Of all the items on my policy wish list, this is the easiest to implement, and likely to have a significant long-term impact.[118] It is also unglamorous.

It is simply wrong in this day and age that sovereign debt restructuring experience,

115. The International Forum of Sovereign Wealth Funds is a self-governing for sovereign wealth funds.
116. IMF, *Reforming the Fund's Policy on Non-toleration of Arrears to Official Creditors* (Dec. 2015)
117. As an alternative to separate classification or disenfranchisement, official creditors could also commit not to trade their debt, and not to enforce it in national courts. However, such a commitment may be politically hard for official creditors to make, and hard to enforce.
118. This proposal is already part of the UNCTAD Roadmap, *supra* note 111

including the most basic facts about legal and financial outcomes, is not easily accessible in the public domain. Instead, we rely on painstaking detective work of academic researchers and commercial databases. Any international organization, trade or civil society group can host a comprehensive, searchable public database of past restructurings, including financial and legal terms, the treatment of public, private, domestic and foreign claims, and any underlying assumptions—made available as soon as practicable after the agreement is finalized. The sovereign borrower should be responsible for supplying required information in standardized form within a prescribed period. At least basic summary terms should be available in English and in the language of the borrowing country. The requirement to disclose restructuring terms can be incorporated in standard form debt contracts, as well as in IMF and other institutional lending policies. Failure to deliver information within a reasonable period without a compelling justification could give rise to sanctions, including claw backs of restructuring concessions in extreme cases, such as fraud.

Of course, the IMF is ideally placed both to require and host such disclosure. However, if it does not, someone else should.

Conclusions

Sovereign debt crises are, by definition, systemic financial and political crises in the borrowing country. They could never be orderly or predictable in the strict sense. Sovereign debt restructurings in the late 20th and early 21st centuries have had a remarkable track record of operational success and substantive failure. Deals got done, but few debtors got timely and durable relief. The informal regime with the IMF at the core, which has dominated sovereign debt restructuring since the 1980s, has been under stress in recent years as a result of changes in international politics and international capital flows. The Greek crisis is a stark example of the continuing challenges to the regime.

Although the IMF's experience in Greece inarguably damaged its credibility, on balance, the Fund has been a force for good in Europe, and has demonstrably learned from its mistakes. It has undertaken welcome reforms in its lending policies and debt sustainability analysis, and, most recently, has shown that its analytical depth and crisis management experience remain indispensable even after it has stopped lending to Greece. The lesson is not that the IMF never needs the money, but that it always needs credibility—and that it has managed to recapture it in this case, despite the early setbacks. The IMF is the only international institution today capable of bringing together diverse stakeholders in a comprehensive debt restructuring framework, adapting quickly in a volatile and fast-changing world. It is in everyone's interest to bolster the IMF's hard-won credibility and independence and encourage continued reform.

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