

EMTA WEBINAR: PROPOSED NEW YORK STATE LEGISLATION RELATING TO SOVEREIGN DEBT

A Compendium

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Panel Discussion

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A bill has been introduced into the New York State Legislature that would affect sovereign bond restructurings, where the bonds at issue are governed by New York law.

While many sovereign bonds in Emerging Market countries contain collective-action clauses (CAC's) that require all creditors to be bound by the modifications agreed to by the majority of such creditors, other sovereign bond contracts lack the CAC's mechanism. The proposed NYS legislation would create an opt-in mechanism allowing sovereign debtors to replace existing contractual amendment provisions (including those based on ICMA recommendations) with a standard statutory cram-down mechanism.

This EMTA Webinar explored the ramifications of the proposed law, including its effects on the use of New York as the governing law (along with UK law) on new sovereign debt bond contracts, as well as the bill's prospects for being enacted into law.

A. Background

I. Origin of Model Law, Intent of New York State Bill and Summary of Opposing Viewpoints

Closely modeled on Duke University Law School’s Professor Steven Schwarcz’s 2017 Policy Brief [“A Model-law Approach to Restructuring Unsustainable Sovereign Debt”](#) (which itself is based on his more extensive 2016 paper [“Sovereign Debt Restructuring: A Model-Law Approach”](#)¹ (2016 Paper)), New York State Bill No. S6627 (see Annex A), introduced by New York State Senator Rivera on May 10, 2021, seeks to amend the NYS Banking Law by adding a new Article 7, with the legislative intent “to [p]rovide effective mechanisms for restructuring unsustainable sovereign and subnational debt so as to reduce the social costs of sovereign and subnational debt crises, systemic [and contagion] risk to the financial system [through defaults and otherwise], creditor uncertainty [which increases lending costs] and the need for sovereign and subnational debt bailouts, which are costly and create moral hazard”. As Professor Schwarcz states, [t]he ultimate goals are to restore the debtor-state to debt sustainability, so as to relieve the undue economic burden on the debtor-state’s citizens; to enable the debtor-state to pay its debts, thereby avoiding a default that might have systemic consequences...The United Nations and the International Monetary Fund [(IMF)] have attempted to propose treaties to enable...debt restructuring, but the political difficulties of reaching a worldwide consensus have stymied their efforts”².

¹ [Schwarcz’s] article argues that “a model-law approach to achieving that resolution framework should be legally, politically, and economically feasible. Because most sovereign debt contracts (if not governed by the debtor-state’s law) are governed by New York or English law, it would be sufficient if England and New York State – and it would be valuable if merely one of those jurisdictions – enact a model law”.

² Moreover, the Bretton Woods Committee’s Sovereign Debt Working Group’s April 2021 paper [“Sovereign Debt: A Critical Challenge”](#) states, “In addition to the broad protections that most sovereigns enjoy, several countries have recently considered or adopted legislation designed to further protect sovereign borrowers from so-called vulture (or holdout) creditors. To date, the United Kingdom, Belgium, and France have passed legislation to this effect:

The UK’s legislation is narrowly tailored, applying only to heavily indebted poor countries (HIPC) and limiting creditor recoveries to the level set by the HIPC Initiative (Debt Relief (Developing Countries) Act 2010, c.22, § 3). The Belgian law is much broader: it applies to all debtor countries regardless of the debtor nation’s wealth, and limits recoveries to the purchase price paid by the creditor (Loi Relative à la Lutte contre les Activités des Fonds Vautours, Moniteur Belge, September 9, 2015, 57357). The French law protects the assets of a country from seizure by a creditor that purchased a debt instrument in default or subject to a pending restructuring proposal if the country was recognized by the OECD as a recipient of official development assistance when the debt instrument was acquired, subject to certain other conditions (Loi n° 2016–1691, Relative à la Transparence, à la Lutte contre la Corruption et à la Modernisation de la Vie Économique, December 9, 2016, Article 60, https://www.legifrance.gouv.fr/loda/article_lc/LEGIARTI000033561959).

The Bill implements a new mechanism for restructuring plans by overriding existing contracts governed by NY law between sovereign debtors and creditors and imposing a collective action mechanism, in essence, significantly different to the aggregated collective action clauses (CAC's)³ proposed by the International Capital Market Association (ICMA)⁴ in 2014. For example, the aggregated CAC voting requires a 75% threshold to bind the rest of the outstanding debt to the new contract terms, whereas the Bill requires a two-thirds threshold, making a holdout veto more difficult.

The retroactive application of the new law is only one concern that was raised in the EMTA-sponsored panel discussion on May 4, 2021 via Zoom. Proponents of the proposed law claim that sovereign debt restructurings need such a new mechanism since, among other reasons, COVID will increase the number of sovereign defaults on the horizon as many countries attempt to deal with their falling economies; a more holistic approach is needed generally for restructurings to avoid holdout scenarios that would impede the process and delay debt relief. Proponents also use empirical evidence to show that the new law should reduce borrowing costs for sovereign issuers and that a more predictable process will increase debtor/creditor use of New York as the governing law in their contracts.

Opponents of the proposed law claim that the mechanism currently in place for sovereign debt restructurings is working well, especially since the advent of ICMA aggregated CAC's, and any statutory approach to this non-existent problem is inherently market-unfriendly and uncollaborative, may increase borrowing costs for sovereign issuers and will deter debtor/creditor use of New York as the governing law in their contracts (thus diminishing New York as one of the leading financial centers in the world) since the implementation of the Model Law is uncertain and ambiguous.

II. Key Provisions in the Bill⁵

A sovereign state can invoke Article 7 by filing a voluntary petition for relief with the “supervisory authority”, certifying that it seeks relief (and has not done so in the previous 10 years) to restructure claims⁶ that, absent such relief, would constitute an unsustainable

³ See EMTA's [Collective Action Clauses and Their Impact on the 2020 Argentina and Ecuador Restructurings - A Primer](#) (June 16, 2021).

⁴ See Annex B for ICMA's reactions to the Bill.

⁵ A detailed analysis of all the provisions in the Bill, coupled with observations on it, can be found in Clifford Chance's May 2021 Client Briefing [“Proposed Amendment to New York Banking Law Through New Article 7”](#) (Clifford Chance Client Briefing).

⁶ The 2016 Paper states that “the definition of a ‘claim’ is broadly defined and is not limited to bond debt or other debt instruments traded as securities and covers all payment claims against a debtor-state for monies borrowed or for the debtor-state's guarantee thereof. However, the debtor-state's internal operational debt claims, such as pension and retiree obligations, tax refunds, unpaid salaries to public employees, or social program payments, are not meant to be covered”. And see Section 2.1.1 of the Clifford Chance Client Briefing for observations on “claim”.

debt. Unless dismissed by such supervisory authority for lack of good faith, Article 7 would apply to the debtor state's New York law-governed contracts with its creditors (or to the state's contracts governed by other laws that have enacted a similar Article or recognized the Article).

Within 30 days of filing the petition for relief, the debtor state must notify its creditors of its intention to negotiate a plan for restructuring, and the "supervisory authority"⁷ will maintain a list of creditors for the purposes of verifying claims in connection with overseeing the creditor voting process. The "supervisory authority" (nominated by the NYS Senate Finance Committee) will also choose an independent body to conduct a comprehensive audit to ensure transparency, with costs borne by the debtor state.

Only debtor states can propose one or more restructuring plans at any time, specifying the proposed treatment of each class of claims, providing for the same treatment for each claim of a particular class (unless the holder of a claim agrees to a less favorable treatment), disclosing any claims not included in the plan's classes of claims, providing adequate means for the plan's implementation (including curing or waiving any defaults, changing the maturity dates, principal amount or interest rate or canceling or modifying any liens or encumbrances) and certifying that the debtor state's debt will become sustainable under such a plan.

A plan becomes effective and binding on the debtor state and its creditors when agreed to by each class of such creditors' claims (holding at least two-thirds in amount and more than one-half in number). Each class of claims will be equal in priority; however, equal claims need not all be included in the same class, and claims of governmental or multi-governmental entities will be classed separately. Creditors have 30 days to respond to the "supervisory authority" about the debtor state's plan to borrow new money, and, once approved by 75% of creditors who responded, these new loans under the plan will receive priority over other claims⁸.

To adjudicate disputes, a court of competent jurisdiction may appoint a referee or a special master to make recommendations to such court (a prior version of the Bill provided for arbitration by the rules of the International Centre for Settlement of Investment

⁷ The 2016 paper states that "the definition of 'supervisory authority' references a neutral international organization. This is likely to be one of the most controversial provisions since it currently is unclear what organization might qualify as truly neutral. Imperfect options might include, among other possibilities, a neutral committee of the IMF, the World Bank, or UNCITRAL, or even a court of the debtor-state. There are concerns, however, that existing organizations are too political or conflicted. However, no formal supervisory authority is needed to exercise discretion because disputes are adjudicated, and its main role is, in fact, ministerial: to fact-check information and to oversee the creditor voting process".

And see Sections B.V. and B.IV. below for a more fulsome panel discussion of this topic, as well as Section 2.2.3 of the Clifford Chance Client Briefing for observations on "supervisory authority".

⁸ As stated in the 2016 Paper, "[this] statutory mechanism can give such new-money lenders priority over existing creditors. To minimize the risk of "overinvestment," existing creditors [will] have notice and the opportunity to block the new lending if its amount is too high or its terms are inappropriate".

Disputes (ICSID), with the debtor state bearing such costs). Article 7 would take effect immediately (in contrast to its prior version of 180 days after enactment), and applies retroactively by overriding any contractual provisions between the debtor state and the creditors.

III. The Model Law's Justifications (as Stated in the Bill)

Encapsulating the primary concern of holdouts, the Bill references countries “mired in debt” they cannot pay and unable (unlike individuals and corporations) to use bankruptcy laws to restructure such unsustainable debt, being “forced to negotiate each of their debt contracts individually...The absence of a predictable, orderly, and rapid process for restructuring sovereign debt has created a ‘Wild Wild West’ system, hurting debtor nations, their citizens and their creditors, while also posing serious systemic threats to the international financial system...[A] few bad faith actors...are exploiting a void in {New York’s} legal system to engage in destabilizing and speculative behavior..., [which] jeopardizes the functioning of sovereign lending markets and the authority of New York State.

[Given that not all contracts contain CAC’s], [h]erein emerges one of the central challenges in sovereign debt restructuring...‘the holdout problem’-- a type of collective action problem where certain creditors, such as vulture funds [making ‘huge profits’ and ‘extracting ransom payments’, while people in those nations suffer famines, economic depression and austerity measures] that may have bought debt in the secondary market for a steep discount, sue to receive full payment by refusing to agree to a debt restructuring plan that proposes to change critical terms, even though the other debt holders consider the plan reasonable. These tactics delay the finalization of a restructuring plan, leading to inequities between creditors while posing severe consequences for debtor nations. Unsustainable debt burdens that are unresolved for a prolonged period of time can lead to sovereign nations losing access to the credit market, hampering the ability to provide for their population’s most basic needs”.

New York is “uniquely positioned” to aid the debt crisis and preserve its dominance by creating a framework to legally mandate supermajority voting that can bind dissenting creditors. This would give “struggling nations...the real prospect of equitably restructuring their debt to sustainable levels, thereby lowering sovereign borrowing costs and increasing creditor confidence by reducing uncertainty”.

On the retroactive application of the Bill to existing contracts, “any impairment would be a reasonable exercise of the state’s police powers to protect its economy[,] reducing the likelihood that a country-debt default could trigger a systemic collapse”. Moreover, “any impairment must be voluntarily agreed to by a ‘supermajority’ of creditors, [thus] preserv[ing] reasonable contractual expectations based on what creditors then realistically expect to receive as payment”. Realistically, therefore, any impairment would not be material.

The impassioned language concludes, “This is a financially powerful opportunity for New York. Never before has a U.S. state had the power to influence the international community to such an extent. Circumstances have given New York State the astonishing ability to make history by establishing an orderly sovereign debt resolution procedure under the rule of law. New York would benefit, and the world would benefit. This extraordinary opportunity is too important for the state to ignore”⁹.

IV. Highlighting Sustainability and the IMF

As noted in the 2016 Paper, a debtor-state’s petition for relief must include a certification that the debtor state “needs relief...to restructure claims that, absent such relief, would constitute unsustainable debt of the State”.

Schwarcz states that, “[a]lthough the debtor state itself would make the determination of debt sustainability, it should be guided by the best practices in making such a determination.

There does not yet, however, appear to be a universally accepted view of what constitutes debt sustainability for nations. Even the IMF framework¹⁰ for conducting debt sustainability analyses (DSAs) has been criticized for creating intercreditor inequities and for being ineffective in detecting sustainability problems”.

The Clifford Chance Client Briefing counters with, “Whilst not without question by private creditors on occasions, the work of the IMF on [DSAs] is a generally accepted significant

⁹ Clearly, opponents of the Bill agree that this unprecedented departure will most undoubtedly affect sovereign debt restructurings, albeit most negatively.

¹⁰ The Fund’s definition of debt sustainability is as follows: In general terms, public debt can be regarded as sustainable when the primary balance needed to at least stabilize debt under both the baseline and realistic shock scenarios is economically and politically feasible, such that the level of debt is consistent with an acceptably low rollover risk and with preserving potential growth at a satisfactory level.

The IMF recently refined its DSA for Market-Access Countries; [see https://www.imf.org/external/pubs/ft/dsa/mac.htm](https://www.imf.org/external/pubs/ft/dsa/mac.htm).

For the IMF’s 2013 paper on the importance of the DSA, [see https://www.imf.org/external/np/pp/eng/2013/042613.pdf](https://www.imf.org/external/np/pp/eng/2013/042613.pdf), some of which is reprinted here:

Because of the important role that the Fund’s determination of debt sustainability plays in lending and restructuring decisions, considerable effort has been made over the years to develop a framework for rigorous debt sustainability analysis (DSA). Rigorous DSAs are also a key tool in crisis prevention efforts. A DSA provides a thorough examination of the structure of debt and projections for debt burden indicators in baseline, alternative, and stress test scenarios over the medium term (generally understood to cover a period of five years). In particular, debt sustainability requires a judgment that the primary balance needed to stabilize debt under both the baseline and realistic shock scenarios is credible, i.e., economically and politically feasible, and the level of debt is consistent with an acceptably low rollover risk and with preserving potential growth at a satisfactory level. In the context of a Fund-supported program that involves debt restructuring, the DSA also plays the essential role of determining the envelope of financial resources that is available for debt service payments to official and private creditors by charting out the program’s medium-term paths for key macroeconomic, policy, and financing variables.

anchor to sovereign debt restructurings and evaluations as to the resulting amount of debt relief which may be sought”.

In its October 2020 paper [“The International Architecture for Resolving Sovereign Debt Involving Private-Sector Creditors—Recent Developments, Challenges, And Reform Options”](#) (IMF Paper), the IMF staff discusses the architecture for the resolution of sovereign debt problems involving private-sector creditors. An analysis of the Bill was not included in the IMF Paper since the Bill had not yet been introduced, but one can surmise that the IMF would be interested in understanding how the Bill may affect the IMF’s role in sovereign debt restructurings (including its DSA).

As the IMF Paper concludes, the existing contractual infrastructure has proven “largely effective”, with deals post-2014 closing at high creditor participation levels and shorter timeframes than those previous restructurings (1980’s-2014) that were the subject of the IMF’s analysis. Notwithstanding a few cases of litigation, the holdout problem has not been a substantial obstacle to private-sector debt resolution. The IMF paper acknowledges that there may be gaps in the existing architecture (e.g., there is still a large stock of outstanding international sovereign bonds without enhanced CAC’s, majority restructuring provisions similar to CACs are not used in loan documentation and changes to loan payment terms typically require unanimous consent from the lenders¹¹, with loans being increasingly used in low-income countries to obtain financing; the use of collateral that tends to complicate sovereign debt restructurings; and there is a need for more transparency¹²). It notes that targeted statutory approaches that have been adopted in certain countries (such as so called “vulture-fund” legislation) could be adopted more widely to address systemic crises such as the COVID-19 pandemic, but as a last resort and on a time-bound basis, and they should be carefully designed to limit the impact on creditors’ rights and avoid undermining the secondary market.

Given the conclusions of the IMF Paper, the potential impact of the NY legislation on bonds governed by NY and English law (and, also, other foreign laws), the interaction with other creditors (including the IMF, Paris Club and International Financial Institutions (IFI’s) generally) and the effect on the NY market must be carefully and comprehensively considered since the IMF is typically concerned about the overall international financial architecture, and any statutory approach should be carefully designed to limit the impact on creditors’ rights and avoid undermining the secondary market.

Moreover, the interaction between the Bill and the IMF’s debt policies (operational and otherwise, including the DSA, which determines the financing envelope and thus the quantum of debt relief that must be sought), the likelihood that NY courts will take the Bill into account, the effect of the Bill on negotiations between debtors and creditors, whether

¹¹ See the IMF Paper, in which Staff comment that the lack of majority restructuring provisions for payment terms in syndicated loans increase the potential complications in a restructuring where such debt is dominant; the G7 have also established a G7-Private Sector Debt Working Group to look at the issue.

¹² See the [G20 Operational Guidelines for Sustainable Finance](#) (March 2017) and the [IIF Debt Transparency Principles](#) (June 10, 2019).

debtors will likely avail themselves of the Bill, whether the *de facto* preferred creditor status of the IMF would be affected, whether their claims would be subject to the Bill if a sovereign chose to opt into it, how the retroactive interference with contractual rights would affect the market for NY law-governed sovereign bonds, and whether the Bill would have implications for future debt restructurings under the auspices of the Common Framework are all relevant and complex considerations that the IMF and others (including the US Treasury and the Federal Reserve Bank of New York) may wish to further analyze and discuss with the Bill sponsors.

It goes without saying that the sponsors of the Bill need to reach out and ascertain not just comments from the private sector and issuers, but also from regulatory bodies, lenders and IFI's¹³, for the financial stability, reliability, predictability and overall certainty of the markets (including financing costs beyond those related to an individual sovereign's economic status and the enforcement of contract law that undergird such markets) and future sovereign debt restructurings under international financial architecture that should be more properly vetted.

And finally, see the panel discussion on this topic below in Sections B.IV. and B.VI.

V. Certain Provisions Not in the Bill

The Bill omits certain provisions that one might otherwise associate with a legal framework for sovereign debt restructuring: (1) a stay of enforcement actions¹⁴, (2) a

¹³ Note that the Center for Popular Democracy and New York Communities for Change organizations state that "As a coalition, we have consulted with a number of stakeholders with varied expertise in the sovereign debt field. We have had consultations (and are continuing to have ongoing conversations) with a number of leading academics in the field, the official sector, bankruptcy judges, some of the top law firms representing both market participants and issuers, IFIs and other trade associations".

¹⁴ As noted in the 2016 Paper, "First, a stay does not appear to be critical to resolving sovereign debt problems. A debtor-state could unilaterally decide to suspend payments. And the main purpose of a stay, to prevent a grab race, is less significant in a sovereign debt context because creditors could only attempt to grab the State's relatively few assets located in other jurisdictions. Second, model laws are less likely than conventions to effectively impose enforcement stays. If a creditor's claim against a debtor-state is governed by the law of a jurisdiction that has enacted the Model Law, such creditor would theoretically be prejudiced in a grab race by other creditors of that state whose claims are governed by the law of a jurisdiction that has not enacted the Model Law. That creates perverse incentives for creditors to want to have their claims governed by the law of a jurisdiction that has not enacted the Model Law. Third, a stay could be costly, leading to litigation over its scope and duration and also possibly affecting non-bankruptcy incentives, thereby increasing sovereign financing costs".

The Clifford Chance Client Briefing counters with, "Activation of Article 7, through the filing of a petition may result in litigation, even in a pre-payment default scenario, as events of default and potential events of default would be occurring at this point. Litigation on contract claims may therefore occur almost simultaneously with activation".

cram-down alternative in the event one or more classes of claims fails to agree¹⁵ and (3) the formal creation of a creditors' committee¹⁶.

B. Summary of the Panel Discussion

I. Background and Latest Restructurings

Dennis Hranitzky (Quinn Emanuel Urquhart & Sullivan) moderated EMTA's panel discussion and provided the following background:

New or improved means of addressing solvency and liquidity crises among sovereigns have come into renewed focus in light of COVID, its drag on issuers' economies and the public health burdens it has imposed. In the last 15 months, the following initiatives have been either introduced or expanded upon: the Group of 20's (G20) Debt Service Suspension Initiative (DSSI) (which provide the world's poorest countries suspension of debt service to permit resources to be directed towards more pandemic-related services) and Common Framework for Debt Treatments beyond the DSSI, a flurry of activity emanating from the Bretton Woods working group, and this proposed sovereign restructuring regime for New York law-governed sovereign debt, which its proponents hope will be followed by a UK equivalent.

Hranitzky remarked that the expected sponsor of this proposed legislation, Senator Gustavo Rivera, is probably responding to his constituents' displeasure over how Puerto Rico's restructuring process under PROMESA has unfolded; although he notes that no Puerto Rican issuer would be eligible to invoke the law.

¹⁵ As noted in the 2016 Paper, "Although [the Bill] makes a debt-restructuring plan effective and binding on the debtor-state and its creditors when it has been submitted by the debtor-state and agreed to by each class of such creditors' claims designated in the plan, any such class of claims could stymie the plan's effectiveness by failing to agree. To overcome the possibility of one or more classes of claims unreasonably withholding consent to a plan, corporate debt-restructuring laws often provide for a cram-down power. The difficulties with applying cram down in a governmental debt restructuring context are in determining what governmental austerity measures and levels of taxation are reasonable, in order to assess whether the creditors are receiving all they can reasonably expect under the circumstances. At the very least, these determinations would be complex, fact-intensive, and highly politically sensitive. In the Chapter 9 context, federal bankruptcy courts make these determinations, yet the decisions are far from consistent. In the sovereign debtor-state context, however, there is as yet no suitable judicial venue for making such determinations. For these reasons, and also because including cram down at this nascent point in the model-law process could engender significant creditor opposition, the Model Law currently omits a cram-down power".

¹⁶ As noted in the 2016 paper, "An official creditors' committee does not appear to be necessary in a sovereign-debt-restructuring context because "the claims against a State are so large that many creditors, or at least a de facto committee of creditors chosen consensually, should find it economically feasible to participate in the restructuring process".

Also see Section B.V. of the panel discussion, where this topic is discussed.

Hranitzky notes that Professor Schwarcz identified a number of factors driving the need for the Bill: (i) court decisions in the UK regarding the illegality of exit consents, (ii) decisions of the federal courts in New York regarding the meaning and proper application of the *pari passu* clause in Argentina's 1990's era sovereign debt contracts and (iii) debt crises in Greece, Venezuela and other countries as highlighting the risks of an inadequate legal resolution framework for restructuring unsustainable sovereign debt.

However, since 2017, Hranitzky remarks that a comprehensive debt restructuring was completed in Argentina (as well as in some of its Provinces) where CAC's were successfully invoked; a comprehensive restructuring in Ecuador, also invoking CAC's, which survived a challenge in the New York courts was also completed; successful restructurings in several of the Argentinean provinces were concluded; improvements were made to the model *pari passu* clause developed by ICMA which, among other things, make a *pari passu* injunction based on bonds issued after 2015 impossible; and, at least in Zambia, Chinese lenders emerged as the main obstacle to forward movement in debt restructuring negotiations, which was one of the primary issues the Common Framework was intended to address.

II. Root Problem Meant to be Addressed by the Model Law

In Schwarcz's view, the main impediment to successful sovereign debt restructurings is that the existing legal resolution framework through a "contractual" approach¹⁷ – the use of CAC's¹⁸ – is insufficient and inadequate to solve the holdout problem, thus "hurting individual debtor nations and their citizens, as well as their creditors [, with a] sovereign debt default [possibly] pos[ing] a serious systemic threat to the international financial system". The Model Law is critically important because contractual CAC's don't always work, not all sovereign debt contracts have them¹⁹ (thus requiring unanimity to change repayment terms and enabling any party to the contract to act as a holdout), and, when they do, they do not contain aggregated CAC's that ICMA later introduced, which are fundamental to the Model Law (whereby all parties were deemed to agree to aggregated CAC's).

The existing supermajority CAC's may be at such a high percentage (e.g., 75%) that some creditors can purchase a small portion of the debt stock and veto and block an otherwise reasonable restructuring. The Model Law was meant to solve in a legislative

¹⁷ He stated in the 2016 Paper, "Even those who are not adherents of sovereign 'bankruptcy' believe that the status quo contractual approach is deeply dysfunctional and produces bad law". And, furthermore, "CAC's are not a substitute for pursuing a more systematic legal resolution framework for helping debtor-states to restructure unsustainable debt".

¹⁸ CAC's are clauses in debt contracts that enable a specified supermajority, such as 66-2/3% or 75%, of the contracting parties to amend the principal amount, interest rate, maturities, and other critical repayment terms.

¹⁹ He stated in the 2016 Paper, "[A] CAC ordinarily binds only the parties to the particular contract that includes it. The parties to any given sovereign debt contract therefore could act as holdouts in a debt restructuring plan that requires all of a debtor-state's debt issues to agree to the plan".

manner a market failure related to a contractual problem (the same problem ICMA addressed in its CAC paradigm), whereby a holdout creditor would extract a special deal by threat of a lawsuit (“hoping to receive more than their fair share of a settlement”) and/or stymieing other creditors’ ability to move forward with a consensual restructuring. As he notes in the 2016 Paper, “statutory supermajority aggregate voting is the tried-and-true method by which corporate insolvency law [such as Chapter 11 of the U.S. Bankruptcy Code] successfully, and equitably, addresses the holdout problem”.

Moreover, the Model Law would affect existing contracts that don’t have CAC provisions, and would solve the *pari passu* problem. The statute was not needed in the past because exchange offers were more “forced” (through moral suasion or otherwise) with a more limited creditor base reaching agreement. However, at present, restructurings are more voluntary in nature and legal issues have arisen that warrant more attention to solving this issue on a wider scale.

III. Reactions from Panelists

Ben Heller (HBK Investments), a member of the expert group convened by US Treasury staff on *pari passu* clauses and CAC’s and a veteran of sovereign restructurings going back at least to Peru in the late 1990’s, emphasized that the CAC design was guided by one extreme example -- one disruptive, contumacious debtor (Argentina) and one of the hardest creditors (Elliott Management). He noted that hard cases make bad law, and that the holdout problem was not a central one (although he admitted it was real and not a fantasy). Holdouts can usually be paid off as nuisances without jeopardizes a country’s economic program, and it’s unusual for that approach to unduly disrupt restructurings. The more efficient solution is to have more contracts include the ameliorative CAC provisions (which has already been happening through voluntary market restructurings). Possibly there may be room for statutory enhancements in other contexts where those with non-bond claims can threaten debt service on bonds, but there are very few cases where we have seen this kind of “bondholder-on-bondholder violence”.

Ian Clark (White & Case), who has participated on both sides of the debtor/creditor table, was more optimistic than Schwarcz that the current architecture was sufficient to absorb the holdout risk. In Argentina’s recent restructuring, where diverse creditors culminated in differing creditor committees with differing objectives, the high risk was anticipated that holdout creditors pursuing disparate interests would adversely affect the success of the restructuring, but that scenario did not come to pass. Instead, creditors (real money investors and secondary market participants) behaved responsibly, so he was not sure what the NY legislature was attempting to fix in such a dramatic way. The clarion call that a handful of vulture funds seeking to pursue aggressive agendas would hamper future restructurings was simply not the case, he posited. Instead, he viewed creditors as acting in a responsible manner when a restructuring was supported by the international community and/or underwritten by the IMF and other international financial institutions. Furthermore, there is no real evidence that the COVID threat, coupled with a low interest rate environment which has increased debt levels all across the EM sovereign world, have

not been adequately addressed by the DSSI, the Common Framework, ICMA CAC's and various other non-legislative initiatives.

Hranitzky seconded Clark's statements by pointing out that, while Hranitzky represented hedge funds in the Argentine context and Clark represented real money interests, they both worked constructively, with "no threat of violence" (reflected in the spirit of the hedge fund group) to the successful resolution of the restructuring, and that he was pleased that the predictions of a failed resolution due to the hedge fund group's participation did not come to pass.

Andrew Lowenthal (Managed Funds Association) speculated about what may be motivating the proposed law and what problem Senator Rivera was trying to solve, since Lowenthal did not believe it was to cure the problems of sovereign debt restructurings. He characterized the Bill's supporters as trying to fundamentally reshape the way in which capital markets operate (which characterization Schwarcz opposed; it was not a "complete redo") and change the role and participation of the secondary market and financial institutions in the weight of their ability to dictate outcomes against the needs of the citizenry. The belief that the isolated sovereign against the IMF, World Bank, G-20, hedge funds and other financial institutions cannot adequately protect its citizenry is at the core of why the supporters want to pass this law, regardless of the ability of creditors to work with their debtors to successfully restructure debt, a debate that is now taking place when, in fact, the market has been working very well. The increased "testing" of the capital markets derives from the notion that they are not working well enough to protect poor, limited resource sovereigns. He viewed the local political dynamics (which has increasingly had a Socialist bent) of pandering to constituencies that felt sympathy for the way the Puerto Rico bankruptcy regime played out, coupled with fervent affinity with the ills that have befallen Argentina and other EM countries during COVID and otherwise, as the real reasons behind Rivera's dogged pursuit of the Bill, which empowered NY political figures to carry out global decisions through the audit provisions of the Bill. This was an "arrow in the quiver to the larger testing going on". He remarked that Schwarcz's Model Law was being used for purposes unintended, much like an author, once his novel is in the public domain, doesn't control the way his words are used for various purposes and multiple agendas. The Bill, in Lowenthal's view, is not meant to be solution-oriented, but rather to trigger and prompt a broader conversation throughout DC and NY that may have other pending legislation against the creditor community.

IV. What are the Implications of the New York Legislature Legislatively Augmenting and Revising Sovereign Debt Agreements?

Hranitzky asked the fundamental question of what it means for New York's legislature to dip into the financial architecture of international relations, the implications for the market and existing sovereign contracts, as well as where the role of the IMF, Paris Club and others.

Heller addressed the proposed Bill's implications to the market by listing some of his predictions: (i) increased cost of credit, availability and higher spreads for sovereigns, (ii)

fracturing of the market into competing jurisdictions, thus fragmenting liquidity, and (iii) increased risk and uncertainty. He expounded by noting that the Bill was not, as Schwarcz suggested, just a legislative response similar to ICMA's contractual response with CAC's. While it may superficially look the same, ICMA's aggregated CAC's have additional protections, which have been stripped away by the Bill (see below for Clark's discussion of these deficiencies in the Bill) and, thus, may be subject to abuse in the Bill's implementation.

The audit mechanism in the Bill is unclear²⁰, and the reference to ICSID arbitration to resolve a pending default will result in too many delays in the restructuring process²¹.

Moreover, in Heller's view, the salient factor in why the Bill is not advisable has everything to do with process. The ICMA CAC's did not result in increased pricing for sovereigns that adopted them because the process to vet those CAC's was inclusive, comprehensive and collaborative, with issuers, debtors, the official sector and trade associations participating, with ample research, negotiation and education that made the market and issuers alike comfortable with the final net result, which was certain. In deep contrast, the proposed Bill did not solicit any input from, and was not at the behest of, sovereign issuers, creditors, the IMF, the Paris Club or any other institutional financial bodies with "skin in the game"²², and purports to override contracts. He warned that this Bill may be the first of many laws at the whim of a New York legislature that was, at the moment, "plagued by the political winds of Albany" with an anti-capitalist contingent. And, finally, he remarked that the higher costs involved for the foreseeable future may be an effect of the uncertainty with respect to the Bill's passing, regardless of whether it actually passes

²⁰ As further cautioned in the Clifford Chance Client Briefing, "The audit process contemplated would raise confidentiality considerations and be entirely dependent on the state providing historic as well as current documentation".

²¹ As noted above, the ICSID arbitration for resolution of disputes has been modified in the Bill to a court of competent jurisdiction appointing a referee or special master to make recommendations to the court, but this may also engender significant delays in the restructuring process.

²² As buttressed by the Clifford Chance Client Briefing, "It has become customary for there to be market consultations with varying degrees of formality in respect of proposed significant initiatives in the field of sovereign debt restructurings. A consultation process allows both a technical review and the evaluation of potential unintended consequences to be undertaken, for example, any pricing implications for new debt raisings following a new policy initiative, potentially affecting the debt sustainability of debtor countries through increased debt servicing costs or leading to loss of market access quicker than might otherwise have been the case. In very broad terms, historically, the US National Government position, where the debts owed by foreign sovereigns are unsustainable, has been to promote voluntary creditor participation through negotiation. Article 7 therefore strays into areas which may be regarded as beyond normal limits and, as a result, may raise separation of powers arguments by affected stakeholders.

Rating implications and the risk of accelerated sell offs have also been taken into consideration in developing policy in this area. The filing of a petition is likely to (a) be regarded as a negative event by rating agencies and (b) give rise to events of default or potential events of default in many types of debt arrangements".

or not, given the potential that some other form of the Bill may rear its ugly head in the future.

Clark addressed the problematic implications of the proposed Bill to the existing sovereign restructuring architecture, which includes not just issuers and bondholders but the Paris Club, the official sector and others. This new restructuring mechanism -- the introduction into New York law of a retroactive amendment to existing contractual CAC's -- at a very fundamental level calls into question the reliability of New York law in the future treatment of contract enforceability, is of major concern and opens a Pandora's Box of possible future changes to contract law. What both debtors and creditors appreciate in New York law is its respect for, and acceptance of, contractually agreed terms and, thus, its enforceability of those terms.

The significant procedural deficiencies in the collective action framework were corrected with ICMA's aggregated CAC's. In the single-limb CAC structure, a universally applicable condition of equal and fair treatment across the different members of the particular voting class is not a protection that is included in the NY legislation²³. He explained that, in the dual-limb CAC used in the Argentine and Ecuador contracts, the layer of protection was that a minimum of 50% of bondholders had to approve the restructuring plan, which prevented the previous abuse of behavior against minority bondholders. The Bill grossly simplifies and strips away these procedural rights that are in ICMA CAC's and have been used to balance interests of debtors and creditors in complex situations.

Clark echoed Heller's claim of uncertainty in how all this will affect debtor and creditor behavior in the negotiation process and otherwise, and he went further to add that this Bill may be very de-stabilizing and, in fact, undermine the goal of the legislation to aid issuers in distress to find consensual resolution with their creditors. He noted that the legislation could have been worse and more similar to the anti-vulture fund legislation seen in other jurisdictions that may affect enforceability of claims, but that was not sufficient reason to accept this proposed legislation that dramatically affects parties' contractual rights.

Hranitzky discussed the difficult legal implications of the Bill. He viewed the Bill as being preempted by federal law, and doubted that any US state legislature could ever enact a similar bill, given the foreign affairs implications. While not having any particular insight

²³ The Clifford Chance Client Briefing concurs with some additional observations, "The aggregate voting threshold in Section 305.5 contains no safeguards of the type used in single limb aggregated voting in the enhanced CAC's recommended as part of the Existing Architecture, most importantly the uniformly applicable safeguard in the enhanced CAC's requires existing holders to be offered the same terms or to select from an identical menu of options and the information covenant also therein requires the country to set out detailed economic and financial information, including a description of its policy reform and provisional macroeconomic outlook no later than any proposal to revise payment terms.

Most sovereign debt restructurings requiring voting from creditors proceed on the basis that trading is effectively frozen whilst the voting process is being conducted through blocking instructions to the clearing and settlement systems. These types of operational aspects are not addressed".

into US Treasury's thinking on the topic, he doubted that it would view the proposed law as advancing the foreign affairs interests of the United States. Moreover, to put a finer point on it, he thought that the Bill directly conflicts with a well-established federal policy, which is clearly defined in the caselaw in favor of enforcing sovereign debt contracts as written,²⁴ as well as the clearly stated policy of the US of maintaining New York's status as a commercial center, including as a center of the sovereign debt market.²⁵

The Bill also injects the NY Department of Finance directly into the sphere of international public debt finance by putting it into an oversight role over "Supervisory Authorities" such as the IMF. Moreover, he claimed that his colleagues at Cleary Gottlieb are also of the view that the Bill intrudes into the field of matters Congress intended to preempt when it enacted the 1976 Foreign Sovereign Immunities Act. And, finally, the Bill obviously would impair sovereign debt contracts, and, therefore, creates issues under the Contracts Clause of the US Constitution.

Schwarcz responded to the various market, sovereign debt architecture and legal implications of the proposed Bill by claiming they were all a result of "fear of change", rather than a logical response to the Bill. This was not a drastic change to contract rights, and the Bill would go no further than what ICMA attempted to do with its CAC's formulation, simply trying to solve a market failure (specifically, the holdout problem). He disagreed with Clark's assertion that the Bill's procedural deficiencies are unfair to investors since the Bill was based on parallel bankruptcy laws²⁶ designed to solve collective action problems in corporate bankruptcy²⁷ and restructuring contexts.

Moreover, the Bill provides minority protection by going further than the greater than 50% referenced by Clark; even 1/3 of those holding outstanding debt could veto a restructuring plan²⁸. The Bill would, in fact, provide more certainty for creditors (other than holdouts) and issuers since empirical research shows that solving problems would reduce the costs of credit and investors would appreciate the certainty the Bill introduces.

²⁴ *Elliott v. Peru* (2d Cir 1999); *Pravin Banker* (2d Cir 1997).

²⁵ *Allied Bank* (2d Cir 1985).

²⁶ 11 U.S. Code § 1126

(c) A class of claims has accepted a plan if such plan has been accepted by creditors, other than any entity designated under subsection (e) of this section, that hold at least two-thirds in amount and more than one-half in number of the allowed claims of such class held by creditors, other than any entity designated under subsection (e) of this section, that have accepted or rejected such plan.

²⁷ Although, one may argue that countries are not companies, and attributing a corporate bankruptcy mindset to sovereigns is highly inappropriate.

²⁸ The Clifford Chance Client Briefing, however, offers a counter to that argument: "the conjunctive requirement in the voting by class under which a majority by number as well as two thirds by value of claims is the threshold is potentially open to abuse. A creditor seeking to undermine the process could sell one dollar, or even one cent claims, to multiple like-minded parties who then all vote against the plan".

As to concerns about the audit, it is still unclear how the audit would work. The fear of New York engaging in the type of oversight that the IMF was going to engage in when the bankruptcy-like Sovereign Debt Restructuring Mechanism (SDRM)²⁹ was discussed decades ago for sovereigns is unwarranted because the supervisory authority will be a neutral body (and not a NY governing body, like the NY State of Finance), and would only make ministerial³⁰ decisions, without much discretion or exercise of judgment.

On the legal arguments, after research and discussion with Treasury and Cleary Gottlieb, Schwarcz thinks that the Bill should survive federal pre-emption because it focuses upon the police powers of the state to protect investors and to prevent the systemic collapse of the financial system. Moreover, the concepts in the Bill are consistent with what the US government is attempting to do and would help develop consensus around commercially sound and legally effective ideas. If New York law is not modified in this way, UK law may be as there is movement underway there to do so³¹, with the possibility that debtors and creditors will then choose UK law instead, thereby marginalizing the importance of New York law in international finance.

The retroactive application of the Bill has two strong and compelling reasons why retroactivity should be effective³²: (1) the contracts clause of the NY Constitution doesn't

²⁹ As stated in the 2016 paper, "It is also informative to assess the political feasibility of a model-law approach from the perspective of the politics of the IMF's failed SDRM. [T]hat approach failed because it was opposed both by Wall Street and by certain emerging market countries that feared it would raise their cost of borrowing... a model-law approach should reduce those costs".

³⁰ How ministerial can the duties actually be if a determination is made that the sovereign acted in good faith (not defined in the Bill) in bringing about the Article 7 claim, self-certifying as to its unsustainable debt?

³¹ At least one prominent law firm in the UK is unaware (after discussions with HM Treasury) of any such movement to adopt a similar Bill. And, clearly, the UK would profit from NY's adoption of the Bill as the uncertainty of outcome of the Bill's enactment may lead all financial institutions and issuers to choose English law as a "safe" jurisdiction for their sovereign debt contracts going forward.

³² As stated in his 2016 Paper, "Legal retroactivity is respected under international law so long as it is neither discriminatory nor arbitrary. In particular, the issue is whether U.S. constitutional law would restrict the retroactivity of New York law based on the Model Law. The "Contracts Clause" in Art. I, § 10 of the U.S. Constitution prohibits states (as opposed to the federal government) from enacting any legislation that impairs existing contractual obligations. Nonetheless, New York State should be able to frame its enactment of the Model Law in such a way as to not violate the Contracts Clause. The Contracts Clause does not extinguish a state's ability to exercise its police powers to promote or protect the public commonwealth, including protecting economic activity within its borders. The U.S. Supreme Court generally defers to state economic regulation, especially during times of "emergency." A state statute that substantially alters preexisting contractual obligations does not automatically violate the federal Contracts Clause.

The Supreme Court has articulated five factors that a court should consider when determining if a state statute violates the Contracts Clause. Such a statute would survive a Contracts Clause challenge if it (1) addresses a grave temporary emergency, (2) protects a "basic societal interest, not a favored group," (3) provides relief – in the form of supermajority aggregate voting for debt relief and temporary funding – that is appropriately tailored to the emergency it is enacted to address, (4) imposes reasonable conditions,

prevent retroactivity in terms of contract impairment if it's justified by police powers and (2) the impairment to contracts is not substantial³³ because the effect of the legislation to change payment terms is minimal since payment terms will be modified only if the supermajority of every single affected class of creditors agrees that those payment terms should be modified, which signals that any such change is by consensus. Thus, only payment terms that are realistic under the circumstances would prevail, and no one would get more than what's agreed to in the restructuring plan.

V. Impact of the Proposed Law on the Timetable for Sovereign Restructurings

Hranitzky noted that there are several destructive features of the Bill that would hardwire delays into restructurings. First, there are no timetables or deadlines in the proposed Bill, and no apparent limit on the number of plans a sovereign may propose. Second, the Bill prohibits creditors from proposing a plan if whatever plan proposed by the issuer fails to obtain creditor support. Third, the Bill doesn't contemplate creation of one or more creditor committees. And fourth, the choice of glacially-paced ICSID arbitration as the forum selection mechanism could add years to sovereign restructurings.³⁴ Why aren't the local courts the proper forum? Usually they are the forum chosen by the parties for all disputes "arising under or relating to" the debt being restructured. And, the local courts have procedural mechanisms for the expedited resolution of disputes.

Clark responded by claiming that this was a "troubling and surreal discussion", as there is nothing more important to the stability of the financial system around the globe than a well-understood process for sovereign debt restructuring. ICMA, the International Institute of Finance (IIF), the official sector and others, along with stakeholders, have created a process, which, in difficult circumstances, attempts to resolve, in a fair and transparent way, for the issuer and stakeholders the restructuring effort without upsetting the international financial system. The process is working and has been proven in many different contexts. There may be different dynamics in each case, but the most common theme in all successful restructurings is engagement with creditors in order to create

and (5) is limited to the duration of the emergency. [The Bill] therefore should meet the U.S. Supreme Court's criteria to survive a Contracts Clause challenge.

More recent jurisprudence suggests even more leeway, enabling a state law to retroactively impair contracts if the impairment is reasonably necessary to further an important public purpose and also reasonable and appropriate to effectuate that purpose. This leeway may be even greater if the contractual impairment is not substantial, being limited to changes that are voluntarily agreed to by a supermajority of *pari passu* creditors based on the debtor-state's deteriorating economic circumstances.. Moreover, the party asserting a Contracts Clause violation appears to have the burden of proving the violation. New York State therefore should be able to frame its enactment of the Model Law in such a way as to not violate the Contracts Clause. Such enactment would represent an exercise of New York's police powers to reduce a sovereign debt default that could lead to a systemic economic collapse, thereby protecting economic activity within its borders.

³³ *General Motors Corp. v. Romein* (US Supreme Court 1992).

³⁴ As noted above, the final version of the Bill modified the dispute mechanism from ICSID arbitration to a court of competent jurisdiction appointing a referee or a special master to make recommendations to the court regarding the resolution of any disputes.

credibility of result, which is the by-product of broad voluntary acceptance of the market. Using this ad hoc approach has still been efficient and rather speedy. The current financial architecture is of paramount importance in making the restructuring process work. Adding a whole new layer of supervisory authority is ambiguous and potentially detrimental. How will good and bad faith by debtors be measured? How will a comprehensive audit affect the timing of a restructuring, which may be delayed for months or years? Timing very much matters in a sovereign debt crisis as economies begin to stagnate, political pressures grow and asset values are affected, and injecting this legislative framework into a system that is working may be regrettable.

Schwarcz again remarked that he surmised that fear of the unknown was at the core of all these concerns, and that the panelists each had a vested interest in the Bill not passing. While the process seemed to be working, it may not continue to do so, and it may not work in other future contexts. Viewing this in the right perspective, the Bill was not introducing a NY governing body to make decisions based on discretion; any decision-making would be extremely limited to avoid any exercise of judgment. The concern that investors are not familiar with the process is specious as they are very familiar with the US Federal Bankruptcy Code for corporate bankruptcies, and nothing suggested in the Bill is new, radical or troublesome in that regard. The concern about delays since the Bill offers no timetable is likewise not an issue because issuers can opt in to the Bill if they so choose; if they believe the existing process is adequate, they need not opt into the Bill. The Bill would govern and be utilized only for those issuers that need a safety net to propose a plan based on tried-and-true tested bankruptcy debt-restructuring procedures. If the period is about to terminate, then courts typically will order a liquidation. Since the amounts in controversy are large enough, creditors have an incentive to create their own de facto creditor committees not necessarily traditionally paid for by issuers. Any delays may affect the issuers adversely, so issuers are incentivized to propose a plan that would be accepted by consensus.

Hranitzky countered that his bankruptcy experience is diametrically opposed to Schwarcz's rendering of liquidations, and that some issuers can't get their plan approved, so why not permit creditors to propose a plan? Why does there need to be exclusivity with only debtors proposing a plan? Schwarcz was not opposed to eliminate the exclusivity provision if that would get the Bill passed since the primary goal is to solve the CAC problem.

VI. Should We Be Concerned About Issuers Abusing the System?

Hranitzky noted that the proposed framework departs from existing practice by allowing the issuer to prepare its own DSA rather than looking to the IMF to perform a DSA. There is no requirement that an issuer agree to abide by any fiscal responsibility guidelines—whether under the umbrella of an IMF-supported program, or otherwise—as a condition to invoking the proposed statutory restructuring process. Tangentially he remarked that the fact that Argentina restructured without first having negotiated a new IMF financing arrangement for itself and agreed to the corresponding fiscal guidelines is currently

imposing a serious drag on its economy above and beyond the drag the COVID pandemic has imposed.

Moreover, debt owned or controlled by the state is not excluded from the voting process on a proposed plan. And by giving the issuer exclusive power to define the creditor classes, while not requiring all *pari passu* claims to vote in the same class, the Bill creates opportunities for the issuer to gerrymander the voting process.

Heller pointed out that the ICMA CAC's don't just provide for a supermajority over a minority; there were lengthy negotiations that resulted in the ICMA covenants being accepted, which included constraints on who can vote and under what circumstances (important information for creditors before a vote is taken). These protections are not included in the Bill (if they were, the Bill would look more like the ICMA CAC's), which renders potential abuse by issuers even more salient. Most issuers would want to avoid delays and, therefore, would not opt into the Bill since the current system was working. However, there are abusive debtors who are dilatory for political and other reasons would favor delays and "kicking the can down the road"; thus, there's a danger that the Bill can be used for delay tactics.

Clark, who was involved in the discussion of how the use of "redesignation" by both Argentina and Ecuador arguably undermined confidence in the restructuring process under the ICMA model CAC's, and was also involved in drafting the newest state-of-the-art indenture language aimed at curbing issuers' ability to invoke redesignation (thus possibly further undermining confidence), remarked that the Bill gave too much discretion to issuers to create voting pools to achieve their objectives, with no constraints placed on the creation of those pools and their attendant range of differing instruments that would not be otherwise permitted to be aggregated under ICMA's aggregated CAC's. Claims could be subject to manipulation to effectively disenfranchise certain creditors. An artificial pool of creditors would emerge that would reach certain voting thresholds over other creditors. The redesignation and Pacman tools used at their disposal by the issuers in Argentina and Ecuador were used to achieve outcomes not contemplated by the drafters of the CAC clauses. While solutions in both cases were negotiated, these are examples of what issuers can do with ambiguous language, which, in turn, contributes to uncertainty in the whole process, which we all should seek to avoid.

Schwarcz explained that claims under the Bill must be *pari passu* in priority (similar to US Bankruptcy Law, which has stood the test of time with hundreds of cases balancing interests and reaching consensus between borrowers and lenders), not necessarily payment on equal and ratable basis (which is what the contract provision may provide)³⁵.

³⁵ As he stated in the 2016 Paper, "The Model Law [would] overcome the veto power of *pari passu* clauses, which have stymied the effectiveness of existing sovereign debt restructurings efforts. In response to the Argentina holdout litigation, ICMA...proposed a new form of standard *pari passu* clause for sovereign debt instruments. This new form clarifies that although claims against the debtor-state rank *pari passu* in principle, they need not be paid on an equal and ratable basis with other such debt claims – even if such other debt claims arose under the same contract:

The Model Law would not be subject to *pari passu* problem since it legally changes the terms of the restructured debt into new terms. The main thing that the Bill does is attempts to solve the debtor-in-possession (DIP) lending problem. The problem is that countries facing financial difficulties may need financing for essential services, but won't be able to obtain the financing through the IMF (who may not have the cash, impose conditions or otherwise), so the Model Law would provide notice and a supermajority voting mechanism for this emergency funding of essential services, which is senior to other debt.

The larger the claim, the more difficult for holdouts to buy a veto; that's the reason the Bill provides issuers with the discretion to create large classes against holdouts. The protection for the creditor not placed in the large class is to veto the issuer's plan, unless a supermajority agrees to such plan. Creditors like China who may be placed in their own class are so placed so as not to manipulate the large class of voters. Protection arises in that every class has its own veto³⁶, which motivates fair bargaining by and with the issuer.

Hranitzky remarked that the fact that disparate creditors can be lumped into the same large class isn't as disconcerting as the fact that they don't have to be, and the issuer has complete discretion to appoint a class, which can include deciding to limit the class to one creditor and thus provide preferential treatment to it (e.g., a single creditor like China). And, he questioned the objective to allowing issuers to prepare their own DSA instead of relying on the official sector under the existing financial architecture.

Schwarcz replied that, if creditors believe another class is getting preferential treatment, then they can vote against the plan. Unless the issuer submits a fair plan, it will not get all the classes to agree to it. Likewise, if creditors don't believe in the issuer-prepared

INTERNATIONAL CAPITAL MARKET ASSOCIATION STANDARD *PARI PASSU* PROVISION FOR THE TERMS AND CONDITIONS OF SOVEREIGN NOTES GOVERNED BY NEW YORK LAW

The Bonds constitute and will constitute direct, general, unconditional and unsubordinated External Indebtedness of the Issuer for which the full faith and credit of the Issuer is pledged. The Bonds rank and will rank without any preference among themselves and equally with all other unsubordinated External Indebtedness of the Issuer. It is understood that this provision shall not be construed so as to require the Issuer to make payments under the Bonds ratably with payments being made under any other External Indebtedness.

There are problems with ICMA's approach. Most significantly, its new form of *pari passu* clause will only apply to future debt contracts, and then only to such future debt contracts that explicitly incorporate that new form. The Model Law, however, would implicitly solve the problem of *pari passu* clauses. Once sovereign debt claims are modified in accordance with the Model Law's supermajority aggregate voting, their principal amounts would, as so modified, legally change. Because the restructuring is intended to restore the debtor state to debt sustainability, it thereafter should be able to pay all of those changed debt claims".

The enhanced *pari passu* and aggregated CAC's have now been in use for seven years, with higher than average participation rates than in the previous pre-2014 period (e.g., 85% and above) – see the Table 1 in the IMF paper.

³⁶ Although query whether we want China to exert such a veto, thus toppling an otherwise consensual supermajority restructuring.

DSA or think the opt-in by the issuer was specious and not necessary, then they can vote against the plan (although he could contemplate a process where the IMF does the DSA, but it's more of a political issue at that point). Issuers have incentives to work with their creditors in a give-and-take process and provide a DSA that will get the plan they propose to be adopted by a consensus of creditors. IMF conditionality has not uniformly been positive for countries (e.g., Greece), and the Model Law relies on sophisticated parties to provide checks on the DSAs created by sovereigns.

VII. Does the Proposed Model Law Scheme Make it Easier for Issuers to Extend Better Treatment to Chinese Creditors Than to Similarly Situated New York Law Creditors?

[Note to Readers: Due to lack of time, the issues mentioned in this Part VII were, at best, only minimally addressed in the panel discussion, but, for the sake of completeness, they are added to this Compendium.]

Hranitzky stated that Anna Gelper's fascinating article in March 2021, "[How China Lends: A Rare Look into 100 Debt Contracts with Foreign Governments](#)", reviews debt contracts between Chinese state lenders and 24 developing country borrowers. Its findings go a long way toward explaining why the growing presence of Chinese state loans have become such an obstacle to orderly restructurings, where those loans represent a significant part of the sovereign's financing.

First, the contracts contain confidentiality clauses that prohibit the debtor from disclosing the existence of the terms of the debt, thus creditors would not be aware of the Chinese stock of debt when they voted on a restructuring plan.

Second, they generally contain covenants to keep the debt out of any collective restructuring the borrower may pursue.

And third, they are governed by Chinese law and specify China arbitration as the dispute resolution mechanism.

If we assume that China will not enact its own version of the Model Law, then the proposed NY law might actually incentivize issuers to concentrate their demands for relief on creditors holding New York law or other Model Law jurisdiction debt. The fact that the issuer prepares its own DSA is also cause for concern in this regard.

He posited that the Model Law, while it may be well-intentioned, is in direct conflict with the Common Framework by making it easier for borrowers to play creditor constituencies against each other, and by not including China as an issuer in comprehensive restructurings, while doing nothing to require transparency, or a coordinated approach, to restructuring that treats all similarly-situated creditors equally.

VIII. Timing of the Bill

Lowenthal, responding to why the proposed Bill had not yet been introduced³⁷, what might be going on behind the scenes, and what might be expected in terms of process and timetable once the Bill was introduced, made some speculative political comments and expressed the Populist vantage point so the audience could better understand what opponents of the Bill were up against.

The IMF was not credible to the Democratic Party or in New York in connection with the Greek restructuring where German taxpayers took the loss instead of banks. The IMF imposed a regime on Greece, which has cost the US in terms of national security, empowered Putin, harmed the country, made no accommodation for malnutrition, and enabled a lost generation with an outflow of brain capital and all of the attendant catastrophic events from which Greece is only now recovering.

Moreover, all the above sentiments are coupled with a strong belief that the system is overly weighted in favor of wealthy entities with plenty of resources who can absorb the losses in lieu of the individual. A nation should never have to choose between an education, nutrition or housing program and paying off an irresponsible debt that shouldn't have been incurred in the first place. The system was not working and banks should not have lent all that money to defenseless countries.

In Lowenthal's estimation, it was no wonder that the current Bill was proposed. Proponents of the Model Law wanted a giant reset in the balance of issuers and creditors in favor of issuers who are less rich and can't speak for themselves. The entire system has slipped out of balance, with issuers acting in good faith but with guns to their heads not just by the creditors, but also by the IMF/World Bank to restructure their debt – or else. The viability and importance of the global financial system, as well as the consensus among right and left parties, is gone. There's a desire to reframe how capital markets should work, including the relationship of government to liquidity providers and the market generally. The robustness of the capital markets and profitability of the banking system in the face of COVID and great misery around the world is the clarion call for reform. The Bill is trying to catalyze global debate, not just to fix a problem.

Lowenthal thought the Bill would get the requisite "oxygen to launch" by Memorial Day, having been delayed due to the complexities of the Mayoral race and other pending matters. This highly controversial piece of legislation will be debated for quite a while, not just in NY, but in DC, UK, EU and other jurisdictions. The debt markets have heretofore been of benefit and used by most issuers (outside of a few outliers) for financial growth and economic agenda; this will be jeopardized by the Bill.

Schwarcz predicted that the Bill would be introduced shortly, similar to what was proposed in November 2020, with some possible small modifications of ICSID being replaced by local courts and a Special Master (as needed) and other non-material changes as the Bill goes through the legislative process.

³⁷ As noted above, the Bill was introduced on May 10, 2021.

Hranitzky concluded that the Bill imports corporate bankruptcy principles into sovereign restructurings, while discarding some well-established restructuring principles – an IMF DSA, state-of-the-art CAC's, allowing competing plans by creditors, encouraging transparency and comprehensive restructurings that includes all creditors (not just NY- and UK-governed ones) and including Chinese lenders in the mix. Why not continue to use sovereign debt restructuring architecture and principles?

Schwarcz replied that he was familiar with, and analyzed, and attempted to take into account all the current financial architecture principles, in drafting the Model Law, balanced all the practicalities and competing interests based on what he thought made sense, reviewed the Chapter 11 Bankruptcy Code and didn't think the Model Law upends the Common Framework or the Paris Club Principles. The Common Framework would work consistently with the Model Law because the Common Framework only requires that "G20 and Paris Club creditors with claims on the debtor country...will coordinate their engagement with the debtor country and finalize jointly the key parameters of the debt treatment." The Model Law provides that those creditors have their own voting classes anyway. The Model Law is much more effective than the Common Framework because the Model Law, unlike the Common Framework, provides a mechanism to bind private creditors, and also because the Model Law, unlike the Common Framework, includes the option of debt write-off or cancellation if each affected class of creditors agrees to that by supermajority voting. In order to comply with the Model Law, debtors would have to comply with the requirement that all debts be disclosed. The Bill did not contemplate the egregious nature of China in terms of confidentiality and disclosure of claims, some of which may even be deemed odious debt. He concluded that he believed the Model Law was not perfect, but it was good and we "shouldn't let the best be the enemy of the good".

Annex A

RIVERA

Add Art 7 §§300 - 309, Bank L

Provides for restructuring unsustainable sovereign and subnational debt.

STATE OF NEW YORK

6627

2021-2022 Regular Sessions

IN SENATE

May 10, 2021

Introduced by Sen. RIVERA -- read twice and ordered printed, and when printed to be committed to the Committee on Banks

AN ACT to amend the banking law, in relation to restructuring unsustainable sovereign and subnational debt

The People of the State of New York, represented in Senate and Assembly, do enact as follows:

1 Section 1. The banking law is amended by adding a new article 7 to
2 read as follows:

3 ARTICLE 7

4 SOVEREIGN AND SUBNATIONAL DEBT

5 Section 300. Legislative intent.

6 301. Definitions.

7 302. Petition for relief; recognition.

8 303. Notification of creditors.

9 304. Auditing process.

10 305. Submission, contents and voting on plan.

11 306. Financing the restructuring.

12 307. Priority of repayment.

13 308. Adjudication of disputes.

14 309. Application; opt in.

15 § 300. Legislative intent. The purpose of this article is to provide
16 effective mechanisms for restructuring unsustainable sovereign and
17 subnational debt so as to reduce:

18 1. the social costs of sovereign and subnational debt crises;

19 2. systemic risk to the financial system;

20 3. creditor uncertainty; and

21 4. the need for sovereign and subnational debt bailouts, which are
22 costly and create moral hazard.

23 § 301. Definitions. For purposes of this article:

24 1. "creditor" means a person or entity that has a claim against a
25 state;

EXPLANATION--Matter in italics (underscored) is new; matter in brackets
[-] is old law to be omitted.

LBD09859-02-1

S. 6627

2

1 2. "claim" means a payment claim against a state for monies borrowed
2 or for the state's guarantee of, or other contingent obligation on,
3 monies borrowed; the term "monies borrowed" shall include the following,
4 whether or not it represents the borrowing of money: monies owing under
5 bonds; debentures; notes, or similar instruments; monies owing for the
6 deferred purchase price of property or services, other than trade
7 accounts payable arising in the ordinary course of business; monies
8 owing on capitalized lease obligations; monies owing on or with respect
9 to letters of credit, bankers' acceptances, or other extensions of cred-
10 it; and monies owing on money market instruments or instruments used to
11 finance trade;

12 3. "comprehensive audit" means a supervisory action taken to examine
13 and evaluate the public debt contracting, refinancing, or negotiation
14 process, in order to determine the lawfulness, transparency, quality,
15 efficacy, efficiency, and sustainability thereof;

16 4. "plan" means a debt restructuring plan contemplated by section
17 three hundred five of this article;

18 5. "state" means a sovereign nation; or unincorporated territory; or
19 any subnational unit thereof, excluding any municipality whose adjust-
20 ment or debts is governed by 11 U.S.C. 9; and

21 6. "supervisory authority" means an independent body referred by the
22 New York state senate finance committee.

23 § 302. Petition for relief; recognition. 1. A state may invoke appli-
24 cation of this article by filing a voluntary petition for relief with
25 the supervisory authority.

26 2. Such petition shall certify that the state:

27 (a) seeks relief under this article, and has not previously sought
28 relief under this article, or under any other law that is substantially
29 in the form of this article, during the past ten years;

30 (b) needs relief under this article to restructure claims that, absent
31 such relief, would constitute unsustainable debt of the state;

32 (c) agrees to restructure those claims in accordance with this arti-
33 cle;

34 (d) agrees to all other terms, conditions and provisions of this arti-
35 cle; and

36 (e) has duly enacted any national or subnational law needed to effec-
37 tuate these agreements. If requested by the supervisory authority, such
38 petition shall also attach documents and legal opinions evidencing
39 compliance with this paragraph.

40 3. Immediately after such a petition for relief has been filed, and so
41 long as such filing has not been dismissed by the supervisory authority
42 for lack of good faith, the terms, conditions, and provisions of this
43 article shall:

44 (a) apply to the debtor-creditor relationship between the state and
45 its creditors to the extent such relationship is governed by the law of
46 this jurisdiction;

47 (b) apply to the debtor-creditor relationship between the state and

48 its creditors to the extent such relationship is governed by the law of
49 another jurisdiction that has enacted law substantially in the form of
50 this article; and

51 (c) be recognized in, and by, all other jurisdictions that have
52 enacted law substantially in the form of this article.

53 § 303. Notification of creditors. 1. Within thirty days after filing
54 its petition for relief, the state shall notify all of its known credi-
55 tors of its intention to negotiate a plan under this article.

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1 2. The supervisory authority shall prepare and maintain a current list
2 of creditors of the state and verify claims for the purposes of super-
3 vising voting under this article.

4 § 304. Auditing process. 1. A comprehensive audit shall be conducted.

5 2. The supervisory authority shall choose an independent body to
6 conduct such comprehensive audit.

7 3. The costs associated with a comprehensive audit shall be borne by
8 the state.

9 4. The audit process shall abide by the general principles related to
10 the International Standards of Supreme Audit Institutions 100 issued by
11 the International Organization of Supreme Audit Institutions.

12 § 305. Submission, contents and voting on plan. 1. The state may
13 submit a plan to its creditors at any time, and may submit alternative
14 plans from time to time.

15 2. No other person or entity may submit a plan on behalf of the state.

16 3. A plan shall:

17 (a) designate classes of claims in accordance with subdivision six of
18 this section;

19 (b) specify the proposed treatment of each class of claims;

20 (c) provide the same treatment for each claim of a particular class,
21 unless the holder of a claim agrees to a less favorable treatment;

22 (d) disclose any claims not included in the plan's classes of claims;

23 (e) provide adequate means for the plan's implementation including,

24 with respect to any claims, curing or waiving any defaults or changing
25 the maturity dates, principal amount, interest rate, or other terms or
26 canceling or modifying any liens or encumbrances; and

27 (f) certify that, if the plan becomes effective and binding on the
28 state and its creditors under subdivision four of this section, the
29 state's debt will become sustainable.

30 4. A plan shall become effective and binding on the state and its
31 creditors when it has been submitted by the state and agreed to by each
32 class of such creditors' claims designated in the plan under subdivision
33 three of this section. Thereupon, the state shall be discharged from all
34 claims included in those classes of claims, except as provided in the
35 plan.

36 5. A class of claims has agreed to a plan if creditors holding at
37 least two-thirds in amount and more than one-half in number of the
38 claims of such class voting on such plan agree to the plan.

39 6. Each class of claims shall consist of claims against the state that
40 are equal in priority, provided that:

41 (a) equal claims need not all be included in the same class;

42 (b) claims of governmental or multi-governmental entities each shall
43 be classed separately; and

44 (c) claims that are governed by this article or the law of another
45 jurisdiction that is substantially in the form of this article shall not
46 be classed with other claims.

47 § 306. Financing the restructuring. 1. Subject to subdivision three of
48 this section the state shall have the right to borrow money on such
49 terms and conditions as it deems appropriate.

50 2. The state shall notify all of its known creditors of its intention
51 to borrow under subdivision one of this section, the terms and condi-
52 tions of the borrowing, and the proposed use of the loan proceeds. Such
53 notice shall also direct those creditors to respond to the supervisory
54 authority within thirty days as to whether they approve or disapprove of
55 such loan.

1 3. Any such loan shall be approved by creditors holding at least two-
2 thirds in amount of the claims of creditors responding to the superviso-
3 ry authority within that thirty-day period.

4 4. In order for the priority of repayment, and corresponding subordi-
5 nation, under section three hundred seven of this article to be effec-
6 tive, any such loan shall additionally be approved by creditors holding
7 at least two-thirds in principal amount of the covered claims of the
8 creditors responding to the supervisory authority within that thirty-day
9 period. Claims shall be deemed to be covered if they are governed by
10 this article or by the law of another jurisdiction that is substantially
11 in the form of this article.

12 § 307. Priority of repayment. 1. The state shall repay loans approved
13 under this article prior to paying any other claims.

14 2. The claims of creditors of the state are subordinated to the extent
15 needed to effectuate the priority payment under this section. Such
16 claims are not subordinated for any other purpose.

17 3. The priority of payment, and corresponding subordination, under
18 this section is expressly subject to the approval by creditors under
19 subdivision four of section three hundred six of this article.

20 § 308. Adjudication of disputes. A court of competent jurisdiction may
21 appoint a referee or a special master to make recommendations to the
22 court regarding the resolution of any disputes arising under this arti-
23 cle.

24 § 309. Application; opt in. 1. This article applies where, by contract
25 or otherwise,

26 (a) the law of New York state governs the debtor-creditor relationship
27 between a state and its creditors; and

28 (b) the application of this article is invoked in accordance with
29 section three hundred two of this article.

30 2. Where this article applies, it shall operate retroactively and,
31 without limiting the foregoing, shall override any contractual

32 provisions that are inconsistent with the provisions of this article.

33 3. Any creditors of the state whose claims are not otherwise governed
34 by this article may contractually opt in to this article's terms, condi-
35 tions, and provisions.

36 4. The terms, conditions, and provisions of this article shall apply
37 to the debtor-creditor relationship between the state and creditors
38 opting in under subdivision one of this section as if such relationship
39 were governed by the laws of New York state under subdivision three of
40 section three hundred two of this article.

41 § 2. This act shall take effect immediately.

**NEW YORK STATE SENATE
INTRODUCER'S MEMORANDUM IN SUPPORT
submitted in accordance with Senate Rule VI. Sec 1**

BILL NUMBER: S6627

SPONSOR: RIVERA

TITLE OF BILL:

An act to amend the banking law, in relation to restructuring unsustainable sovereign and subnational debt

PURPOSE:

To effectively restructure unsustainable Sovereign and Subnational debt to reduce the need for bailouts, negative social costs, systemic risk to the economy and creditor uncertainty.

SUMMARY OF PROVISIONS:

Under the provisions of Section 1 of this legislation the banking law is amended to add a new Article 7 which includes sections 300-309. Section 300 provides the

Legislative intent for this article. Section 301 provides definitions of "creditor", "claim", "monies borrowed," "comprehensive audit," "plan", "state", and "supervisory authority" for the purpose of this article. Section 302 provides for the petition of relief and recognition which authorizes the state to file a voluntary petition for relief with the department. This relief is certified albeit that the state has not previously sought relief under this article within the past 10 years, that not receiving relief would place an unsustainable burden of debt on the state, the state agrees to restructure claims in accordance to this article, the state agrees to all terms, conditions and provisions of the article and that the state has enacted any national or Subnational law needed to catalyze the agreements. After a petition has been filed, the terms, conditions and provisions of the article shall apply to the debtor-creditor relationship between the state and its creditors of this jurisdiction, another jurisdiction and all other jurisdictions that have enacted the law sufficiently to this article. Section 303 provides for the notification of intention to creditors and approves that the state shall notify all of its known creditors within 30 days of filing its petition for relief, with the department verifying the states list of current creditors. Section 304 provides for the Auditing process to be conducted and authorizes the Supervisory Authority to choose an independent body to conduct the comprehensive audit, with costs associated with the audit being borne by the state. Section 305 provides for the submission, contents and voting on a plan. A plan shall designate classes of claims, specify the proposed treatment of each class of claims, provide the same treatment for all claims, disclose any claims not included, provide means for the plans implementation and certify that if the plan becomes effective on the state and its creditors, that the states debt will become sustainable. This plan will become binding on the state and its creditors when it has been submitted and agreed upon by each class of the creditors claims. The state will then be discharged from all claims included in the classes of claims. The claims can only be agreed to if the creditors holding at least 2/3 in amount and more than % in number of the claims. Each class of claims shall also be of equal priority to the state. Section 306 provides for the financing the restructuring. The state shall have the right to borrow money if the terms and conditions deem it appropriate. The state must notify all of its known creditors and the creditors must respond to the department within 30 days of notification. Any such loan must be approved by the creditor holding at least 2/3 in principal amount if the covered claims of the creditor are responded to the department in the 30 day period. Section 307 provides for the priority of repayment. The state shall repay loans lent under this article prior to any other claims and the priority of payment shall be approved by the states known creditors. Section 308 provides for the adjudication of disputes and states that all disputes arising under this article must be resolved by a court of competent jurisdiction who may appoint a referee or special master to make recommendations for the resolution of disputes. Section 309 provides for the application and opt in which applies that the law governs the debtor-creditor relationship between a state and its creditors. This article shall operate retroactively, overriding any contractual provisions that are not consistent with the article and any creditors of the state whose claims are not governed by the article may opt in to the articles terms, conditions and provisions. Section 2 of the bill provides for an effective date.

JUSTIFICATION:

Nation states and subnational territories across the world have found themselves mired in debt that they are unable to pay. Unlike individuals and corporations, countries and subnational territories in the United States cannot use bankruptcy law to restructure unsustainable debt. Instead, they are forced to negotiate each of their debt contracts individually, which often fails as it requires unanimity by various debt holders. The absence of a predictable, orderly, and rapid process for restructuring sovereign debt has created a "Wild Wild West" system, hurting debtor nations, their citizens and their creditors, while also posing serious systemic threats to the international financial system. Approximately half of sovereign debt contracts are governed by New York law. Because New York has no financial and legal architecture governing sovereign debt contracts, its power is being superseded by a few bad faith actors who are exploiting a void in the State's legal system to engage in destabilizing and speculative behavior. This jeopardizes the functioning of sovereign lending markets and the authority of New York State. Although attempts have been made to try to bypass the unanimity requirement in sovereign debt contracts by including so-called collective action clauses, many contracts still lack them. Furthermore, most collective action clauses only bind a party to the particular contract that includes it. Herein emerges one of the central challenges in sovereign debt restructuring known as "the holdout problem"-- a type of collective action problem where certain creditors, such as vulture funds that may have bought debt in the secondary market for a steep discount, sue to receive full payment by refusing to agree to a debt restructuring plan that proposes to change critical terms, even though the other debt holders consider the plan reasonable. These tactics delay the finalization of a restructuring plan, leading to inequities between creditors while posing severe consequences for debtor nations. Unsustainable debt burdens that are unresolved for a prolonged period of time can lead to sovereign nations losing access to the credit market, hampering the ability to provide for their population's most basic needs. Most recently, vulture funds are engaging in these predatory practices in Puerto Rico, where they have attempted to co-opt debt restructuring proceedings to make huge profits while the people of Puerto Rico continue to be hit with austerity measures. The human cost of protracted debt restructuring processes has also led to everything from famines in the Congo, to a sustained economic depression in Argentina, where vulture funds were allowed to extract ransom money by buying debt claims to block the ability of majority creditors to reach a settlement. Judicial decisions like these, issued by a federal court interpreting New York law, threaten New York's dominance as the law that governs sovereign debt contracts. Because of its role in the sovereign debt market, New York is uniquely positioned to help solve the sovereign debt crisis and preserve its dominance through the model law. The model law would create a systematic legal resolution framework for helping debtor states restructure unsustainable debt. The proposed legislation would address the holdout problem by legally mandating supermajority voting that can bind dissenting creditors. Contracts that now require unanimity for revisions could be amended to allow changes that are approved by at least a supermajority of similarly situated creditors (even if those creditors' claims arise under different debt contracts); such a law would overcome the major hurdle to sovereign debt restructuring. That, in turn, would give struggling nations and subnational territories the real prospect of equitably restructuring their debt to sustainable levels, thereby lowering sovereign borrowing costs and increasing creditor confidence by reducing uncertainty. Absent an actual federal treaty, New York has the right and responsibility to fill this clear legal void. Even though the model law could

retroactively impair contract rights, any impairment would be a reasonable exercise of the state's police powers to protect its economy reducing the likelihood that a country-debt default could trigger a systemic collapse, as occurred in 2008 when mortgage-debt defaults triggered a global economic meltdown. And because any impairment must be voluntarily agreed to by a "supermajority" of creditors, such a law would preserve reasonable contractual expectations based on what creditors then realistically expect to receive as payment. Additional key aspects of the legislation include, but are not limited to: addressing the critical need for financially troubled debtor states to obtain liquidity during their restructuring process by giving new-money lenders priority over existing creditors; mandating a comprehensive audit that is undertaken prior to the formulation of a debt restructuring plan to ensure transparency and maintain validity of debt claims; enabling the New York State Department of Financial Services to select a neutral supervisory authority to fact-check information and oversee the creditor voting process. This is a financially powerful opportunity for New York. Never before has a U.S. state had the power to influence the international community to such an extent. Circumstances have given New York State the astonishing ability to make history by establishing an orderly sovereign debt resolution procedure under the rule of law. New York would benefit, and the world would benefit. This extraordinary opportunity is too important for the state to ignore.

PRIOR LEGISLATIVE HISTORY:

New bill

FISCAL IMPLICATIONS:

EFFECTIVE DATE:

Immediately.

Annex B

ICMA thoughts on the key high level, policy issues -

The Bill will have adverse consequences for both sovereign borrowers and investors in NY law-governed bonds:

- Reduces options and lacks refinements that are features with the existing market based framework - less opportunity for the most optimal, mutually agreed outcomes.
- The existing practice - relying on aggregated CAC's - is designed to avoid holdout creditor litigation. The Bill forces the whole process into a legal proceeding. Making debtors and creditors legal opponents from the onset will result in rounds of interlocutory legal challenges and rulings. This will substantially delay restructurings beyond the existing typical timeframes causing far greater losses to investors and possibly creating systemic financial risks (i.e., as we know, the longer a restructuring takes, the greater the haircuts and losses for investors).
- The Bill creates two areas of uncertainty that are highly problematic:
 - the proposed "comprehensive audit" of a sovereign borrower begs questions as to who will carry this out, what is their expertise and how will this possibly conflict with or undermine the exiting role of IFI's such as the Paris Club and the IMF's DSA that restructurings importantly rely upon. The time to carry out the audit will add even further delay compared with existing typical timeframes for concluding restructurings; and
 - the proposed "supervisory authority" is determined by the chair of the NY state senate finance committee and raises concerns as to whether this body would have relevant market experience with sovereign debt and risk management and will lead to anomalous outcomes.
- The Bill improperly and unconstitutionally involves the State of NY rewriting the material terms of international financial contracts validly entered into in good faith by the parties. Moreover, and more unacceptably, it applies retroactively to outstanding sovereign bonds with the attendant risk of creating dislocation and disruption in international financial markets.
- The Bill is overreaching by the State of New York into areas of federal jurisdiction including international relations and the financial affairs of other sovereign states.