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COVER NOTE

Subject:	EU common position on the UN draft resolution A/69/L.84 on 'basic principles on Sovereign debt restructuring processes'

Delegations will find attached the draft EU common position on the UN draft resolution A/69/L.84 on 'basic principles on Sovereign debt restructuring processes'.

1. BACKGROUND

1.1. Discussions on a possible debt restructuring framework in the United Nations General Assembly

Discussions on the possible establishment of an institutional and legal framework for sovereign debt restructuring have been reignited, after lying dormant for many years. This renewal is partly driven by New York court rulings in relation to the 2001 Argentine default.

Until discussions were reignited, discussions have mainly taken place in the IMF in order to focus on a technical analysis and build on the IMF's expertise when addressing this particularly sensitive and complex topic. EU MS have generally welcomed the IMF's work in this area and in reviewing the current framework, they most recently endorsed the institution's recommendations regarding a clarification of *pari passu* (equal treatment) clauses in sovereign bond contracts issued under foreign law.

A contractual market based approach has been the prevailing institutional approach and has been again endorsed in the context of current IMF discussions. Improving the design of sovereign bond contracts (to address the holdout problem) through the inclusion of collective action clauses (CACs) and the clarification of the previously mentioned equal treatment clauses reflects a market-compatible approach that has already been carefully and gradually introduced during the last decade. This is also the prevailing approach in the Euro Area (EA), where model EA CACs with strengthened aggregation clauses have been introduced in all EA sovereign bonds issued after 1 January 2013 and with a maturity of more than one year. In addition, recent recommendations for strengthening this contractual approach have been developed in cooperation with market participants. This approach based on the inclusion of CACs, which are already in use for new sovereign issuance under US, UK, and EU law (key jurisdictions), would therefore pose fewer risks to financial stability.

However, the United Nations General Assembly (UNGA), which has also had this issue on its radar for many years with a focus on the development policy context, has called, in Autumn 2014, for a re-examination of the approach to sovereign debt restructurings and has made a push to establish a multilateral legal framework for sovereign debt restructuring. On 9 September 2014, the UNGA passed a resolution (UN Resolution 68/304) deciding to "elaborate through a process of intergovernmental negotiations, as a matter of priority … a multilateral legal framework for sovereign debt restructuring processes with a view, inter alia, to increasing the efficiency, stability and predictability of the international financial system and achieving sustained, inclusive and equitable economic growth and sustainable development…" The ensuing draft modalities for intergovernmental negotiations called for the establishment of an ad hoc committee that would elaborate the said "multilateral legal framework", with a view to adopting it at the UNGA's 69th session (originally expected for June-July 2015).

The push came from the Group of 77 countries, where Argentina in particular has driven momentum and taken the helm in UN discussions and the above-mentioned resolution because of its interest in a specific outcome in light of its own ongoing litigation.

Following discussions in the EFC – which concluded on 04.09.2014 that Member States should not support the draft Resolution being discussed by the UNGA - the COREPER adopted on 5.11.2014 a common position whereby it was decided that any participation by the EU and Member States for discussions in reference to UN Resolution 68/304 would be guided by the following considerations:

o The work of the ad-hoc Committee should be limited to the elaboration of a non-binding 'set of principles' which builds upon a market-based voluntary contractual approach to sovereign debt restructuring and aims at furthering its implementation and use. Neither the EU nor Member States would participate in discussions aiming at the establishment of a binding multilateral legal framework for sovereign debt restructuring processes.

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The work of the ad-hoc Committee should reflect the recent and ongoing work on sovereign debt restructuring undertaken in the IMF, subject to the previous considerations, and should take place in close coordination with and with technical support from the Fund. Discussions should also make reference to the work in other fora on these issues, such as the Paris Club, which has a history of discussing sovereign debt restructuring issues. The EU and its Member State should make their best possible efforts to influence the work of the ad hoc committee along these lines.

o Should, at any time, the work of the ad-hoc committee not reflect the above conditions, the EU and its Member States agreed that they would no longer participate in discussions in reference to UN Resolution 68/304.

After a number of unsuccessful attempts to re-orient the discussion within the UN, the EU and its Member States decided to discontinue their participation, in line with the common position agreed in COREPER. All Member States followed the common position and disengaged from discussions.

Meanwhile, the content of the UN discussions has progressively evolved, with the G77 making attempts to soften the language so as to achieve wider support from UN members. The new resolution submitted to the UN General Assembly no longer contains explicit references to a statutory debt restructuring process and intends instead to set a number of basic principles (see draft annexed). That said, some of the content remains of a problematic nature (see section 1.2 below).

The evolution of discussions over the last months now calls for a further EU discussion on the position to be taken in New York by the EU and its Member States. While the US, Canada and Japan have communicated their clear intention to vote against the resolution, the spontaneous views of Member States as expressed by their representatives in New York tend to diverge. A split vote would undermine the efforts undertaken so far to establish and maintain a common position on this very sensitive file, which is of major importance for the EU itself, ever more so in the current context.

The vote is expected to take place on 10 September.

1.2. Problems attached to the new draft Resolution

While the draft resolution is overall less problematic than the one discussed last year, a number of important issues should, however, be stressed:

(1) The UNGA is not the appropriate forum for discussing the complex issues attached to Sovereign debt restructuring. The IMF has a history of discussing issues related to the sovereign debt restructuring which results from its role as one of the key institutions for multinational crisis resolution. Its lending policies play a crucial part in facilitating a necessary adjustment process to address a country's external financing problems (i.e. an unsustainable balance of payments deficit) and to catalyse other forms of public and private sector financing. Its economic analysis – and in particular its debt sustainability analysis – is usually the main focal point for the discussions between the sovereign debtor and its creditors. The IMF is, therefore, the main forum for discussing technical capital market issues related to restructuring sovereign debt. It is also a forum where the influence of the EU and of its Member States is significant, in contrast with the EU's structural difficulty to orient the work in the UNGA. Discussions on enhancing the contractual framework for addressing the issues attached to Sovereign debt restructuring are ongoing within the IMF framework - with the active participation of the EU and of its Member States - and should not be undermined by competing processes.

(2) The content of the draft resolution includes a number of problematic statements for the EU. Three issues should in particular be highlighted:

(a) Paragraph 4 requests 'all institutions and actors involved in sovereign debt restructuring', including 'at regional level', to ' refrain from exercising any undue influence over the process and other stakeholders or engaging in actions that would give rise to conflicts of interest'. Such a statement fits poorly with both the EU institutional setting and its practical situation, where possible discussions related to the stock of debt of a Member State take place primarily at regional level, against a background in which the Member States themselves are often the main creditors (directly or via the financial assistance mechanisms that they have established).

(b) Paragraph 5 states that 'creditors have the right to receive the same proportionate treatment in accordance with their credit and its characteristics' and that 'no creditors or creditor groups should be excluded ex ante from the sovereign debt restructuring process'. Such a statement denies the customary preferred creditor status recognized to the International Financial Institutions (IMF, ESM…) when lending to a Sovereign in distress, with possible major negative implications on their ability to fulfil their primary mission.

(c) Paragraph 9 states that 'sovereign debt restructuring agreements that are approved by a qualified majority of the creditors of a State are not to be affected, jeopardized or otherwise impeded by other States'. This statement is very problematic for issuances under foreign jurisdiction (the overwhelmingly dominant case for developing and emerging countries). Issuing under a foreign jurisdiction does, by definition, involve accepting the competence of the courts of another State. This is a point of major importance for the EU, as a very large part of the world's sovereign issuances under foreign jurisdiction are made under the jurisdiction of one of its Member States (UK).

2. CONCLUSION

It is important that Member States enter into and follow through on a common position in respect of the IMF and UN contexts and that this position is the basis for internal and external coordination.

A draft common position is presented below.

Draft

EU common position

On UN draft resolution A/69/L.84 on 'basic principles on Sovereign debt restructuring processes'

The following EU common position is intended as a basis for agreement among EU Member States on how to further proceed on this matter.

- The Union and its Member States take note of the draft UN resolution on 'basic principles on Sovereign debt restructuring processes'. Given that this discussion will deal with sensitive issues, it is important to ensure consistency of the positions taken in the IMF Board and the UN context and to coordinate the positions among Member States in the best possible way.

- While we note the on-going discussions in the UN context, we maintain that the IMF is the appropriate institution to host global discussions on this subject and that the work on sovereign debt restructuring should remain in the IMF. We support the ongoing IMF work, which is intended to contribute to the objective of facilitating timely and orderly sovereign debt restructuring, where such a process is deemed necessary, based on a robust contractual approach.

- The draft resolution contains a number of statements that do not accurately reflect existing law or international practices. It appears notably to question the preferred creditor status of the international financial institutions (such as the IMF or the ESM) and the need to respect the decisions of the competent Courts for the restructuring of Sovereign bonds issued under foreign jurisdiction.

- Although stressing the necessity not to create unnecessary tensions with third country partners (e. g. in the G77), the EU Member States are not in a position to support draft resolution L.84 as crafted and will as a consequence abstain in the vote. Any future participation in work resulting from draft resolution L.84 shall be premised upon the work respecting existing law and international practices.

Annex – Draft resolution A/69/L.84

* On behalf of the States Members of the United Nations that are members of the Group of 77 and China.

Basic Principles on Sovereign Debt Restructuring Processes

The General Assembly,

Recalling its resolutions 68/304 of 9 September 2014 and 69/247 of 29 December 2014 concerning sovereign debt restructuring processes,

Welcoming the work carried out by the Ad Hoc Committee established under resolution 69/247, throughout its working sessions in New York from 3 to 5 February, from 28 to 30 April, and on 27 and 28 July 2015,

Stressing the importance of a clear set of principles for the management and resolution of financial crises that take into account the obligation of sovereign debtors and their creditors to act in good faith and with a cooperative spirit to reach a consensual rearrangement of the debt of sovereign States,

Considering the desirability of the wide dissemination and implementation of the principles, in accordance with national policies and circumstances,

1. Declares that sovereign debt restructuring processes should be guided by the following Basic Principles, as included in the report of the Ad Hoc Committee:

1. A Sovereign State has the right, in the exercise of its discretion, to design its macroeconomic policy, including restructuring its sovereign debt, which should not be frustrated or impeded by any abusive measures. Restructuring should be done as the last resort and preserving at the outset creditors' rights.

2. Good faith by both the sovereign debtor and all its creditors would entail their engagement in constructive sovereign debt restructuring workout negotiations and other stages of the process with the aim of a prompt and durable re-establishment of debt sustainability and debt servicing, as well as achieving the support of a critical mass of creditors through a constructive dialogue regarding the restructuring terms.

3. Transparency should be promoted in order to enhance the accountability of the actors concerned, which can be achieved through the timely sharing of both data and processes related to sovereign debt workouts.

4. Impartiality requires that all institutions and actors involved in sovereign debt restructuring workouts, including at the regional level, in accordance with their respective mandates, enjoy independence and refrain from exercising any undue influence over the process and other stakeholders or engaging in actions that would give rise to conflicts of interest or corruption or both.

5. Equitable treatment imposes on States the duty to refrain from arbitrarily discriminating among creditors, unless a different treatment is justified under the law, is reasonable, and is correlated to the characteristics of the credit, guaranteeing inter-creditor equality, discussed among all creditors. Creditors have the right to receive the same proportionate treatment in accordance with their credit and its characteristics. No creditors or creditor groups should be excluded ex ante from the sovereign debt restructuring process.

6. Sovereign immunity from jurisdiction and execution regarding sovereign debt restructurings is a right of States before foreign domestic courts and exceptions should be restrictively interpreted.

7. Legitimacy entails that the establishment of institutions and the operations related to sovereign debt restructuring workouts respect requirements of inclusiveness and the rule of law, at all levels. The terms and conditions of the original contracts should remain valid until such time as they are modified by a restructuring agreement.

8. Sustainability implies that sovereign debt restructuring workouts are completed in a timely and efficient manner and lead to a stable debt situation in the debtor State, preserving at the outset creditors' rights while promoting sustained and inclusive economic growth and sustainable development, minimizing economic and social costs, warranting the stability of the international financial system and respecting human rights.

9. Majority restructuring implies that sovereign debt restructuring agreements that are approved by a qualified majority of the creditors of a State are not to be affected, jeopardized or otherwise impeded by other States or a non-representative minority of creditors, who must respect the decisions adopted by the majority of the creditors. States should be encouraged to include collective action clauses in their sovereign debt to be issued;

10. Invites all Member and observer States, competent international organizations, entities and other relevant stakeholders to support and promote the Basic Principles set out above, and requests the Secretary-General to make all efforts so that the Principles become generally known;

11. Decides to continue to consider improved approaches to restructuring sovereign debt, taking into account the Basic Principles set out above and work carried out by the international financial institutions, in accordance with their respective mandates, and to this effect decides further to define the modalities for such consideration