FROM THE LOST TO THE SECOND GENERATION COLLECTIVE ACTION CLAUSES:
IS THE INCLUSION OF NO-ACTION CLAUSE THE NEXT STEP FORWARD?

By Anthony Mrad
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FROM THE LOST TO THE SECOND GENERATION COLLECTIVE ACTION CLAUSES:
IS THE INCLUSION OF NO-ACTION CLAUSE THE NEXT STEP FORWARD?
I INTRODUCTION

A sovereign bond will typically consist of hundreds of creditors.¹ Those resemble a crowd of ‘theatre audience: each one has decided to see a particular play on a particular night, but none has any idea who they will be seeing it with.’² In the same way that each member of the audience has bought his own entry ticket, a closer look at a sovereign bond issue will reveal multiple bilateral agreements.³ This being said, the notion of investors as a group would therefore, and to a certain extent, remain a mere appearance absent statutory or contractual provisions binding bondholders together. As far as statutory provisions are concerned, and unlike corporate debt issues, no sovereign statutory insolvency regime will apply to a sovereign’s default.⁴ This reality established contractual provisions as the pillar tool in binding creditors as a group to facilitate an orderly sovereign debt restructuring.⁵

A sovereign debt restructuring implies modification of the bond terms. Prior to the 1990s, and absent collective action clauses (‘CAC(s)'), a variation of the terms of the bonds would require the unanimous consent of the holders of each of the said bonds. Obtaining a unanimous consent however is far from easy due to many factors including the considerable numbers of bondholders, the unknown identity of the end investors, the sub-custodianships of the accountholder and the individual interests of minority bondholders.⁶ As a result, individual bondholders were able to holdout, jeopardize a collective renegotiation of the debt⁷ and extract individual benefits to the detriment of the distressed issuer and majority of bondholders. Issuers mostly used bond exchange techniques in which they included ‘sticks’ (e.g. change in domestic laws, exit consents, less advantageous treatment of holdouts, etc.)⁸ and ‘carrots’ (financial incentives, contractual protections, option menus, etc.)⁹ features to bind holdouts. However, since the early 1990s the Group of Ten, G7 and

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³ Ibid.
⁶ Pm 424, 425.
⁷ Lee Buchheit and Mitu Gulati, see above n2, 1320.

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the US Treasury stepped-in to promote the use of CACs in bond contracts. Moreover, the Mexican sovereign debt issue in 2003 and the success of holdouts (referred to as the vultures) in a series of litigations against distressed sovereigns have triggered a ubiquitous use of CACs in sovereign debt contracts and raised awareness as to the necessity of improving the said CACs to deal with holdout problems.

A CAC is a standardized provision in sovereign-bond contracts providing procedural rules that permit a supermajority of the bondholders to restructure the bonds and bind any dissenting minority.

Thus, first and foremost CACs help the process of restructuring outstanding bonds through (i) facilitating communication between the issuer and the creditors, and (ii) providing a better inter-creditor coordination and a better voting mechanism, and (iii) saving the majority bondholders from the ‘tyranny of the minority.’

CACs can be divided into majority modification CACs and majority enforcement CACs. The former typically operates pre or post default to set the quorum and percentage of votes required to modify the payment terms of the contract. It also identifies the type of bonds that can participate in the voting (outstanding or disenfranchised bonds) the modality of voting (series-by-series or aggregated vote).

As for the majority enforcement CACs, who have attracted less literature than modification clauses, they are included in almost all CACs models to prohibit an individual bondholder

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10 Ibid 44.
12 See, eg, NML Capital, LTD and EM v Banco Central de la Republica Argentina Unreported, United States Court of Appeals, Second Circuit, 5 July 2011; see also Elliott v peru, Elliott Assocas. No. 2000/QR/92 [Court of Appeals of Brussels, 8th Chamber, September 26, 2000]
13 Udaibir Das, above n 9, 44.
14 Deborah Zandstra, Andrew Yianni and Simon James, above n 5.
15 Christian Hofmann, see above n 11, 388.
18 Buchheit and Gulati, see above n2, 1345.
21 See especially IPMA, Standard Collective Action Clauses (CACS) For the Terms and Conditions of Sovereign Notes (October 2004) International Primary Market Association
from accelerating the debt once a default has occurred. The acceleration can typically be voted by the holders of 25% of the value of the bond issue and of the higher percentage of 50% to reverse such acceleration. Such clauses reduce the risk of disruptive bondholders’ enforcement action. However, most international sovereign bonds do not expressly include a no-action clause limiting the rights of a bondholder to individually institute proceedings against the sovereign issuer, or to say it differently, a clause ‘channeling’ lawsuits through a trustee, fiscal agent or any other bondholders representative. Absent such clause, individual bondholders can still sue individually after the acceleration is declared.

This study will shed light on the importance of including such clause as a standard CACs provision – an inclusion that will enhance collectivity by treating bondholders as class and further disrupting the bondholders’ ‘race to the courthouse door’. It will start with an overview of the development of CACs in light of English and New York-law governed bonds with more emphasis on the latter due to the radical changes that shaped its history. It will argue that the inclusion of CACs in New York-law bonds in the early years was not the result of drafting inadvertence as some authors opined. Second, this study will state the triggering events that led to the widespread of CACs in the wake of the Mexican debt issuance of 2003 and ICMA’s first generation standard CACs. The first generation CACs adopted series-by-series voting procedures which proved problematic during the Greek debt restructuring. The third part of this study will analyze this issue together with two innovations introduced by the Eurozone CACs - CACs that were mainly triggered by the Greek restructuring events - the cross-series modification procedures and the Sole Holder Action clause. Thereafter, this study will describe ICMA 2014 second generation Standard CACs. Under this latter part, special emphasize will be put on the advantages of the aggregate single-limb voting procedures together with an analysis as to whether such procedures would lead to an abuse by the issuer or the majority creditors of the minority creditors. In the last part, this study will argue that the next step in the path of strengthening CACs should be made on the level of further restricting disruptive holdout litigation through no-action clauses – a clause limiting individual bondholders’ right to sue.

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22 Liu, above n 20, 3.
23 Ibid 10-12.

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II THE LOST CACs

Research has proven that small intermediaries on the financial market take as much credit as the big players in innovating boilerplate clauses. These clauses vary ‘rarely, slowly and quietly’. Innovations pertaining to CACs, especially those included in bonds issued under New York law, like other boilerplate clauses, were not immediately adopted, nor were they properly noticed. These CACs and their importance were lost from the nineteenth century until 2003.

The sovereign bond market is dominated by New York and English law issuances. Innovations pertaining to the English law issues were building up since the nineteenth century with no radical modifications. As for the innovations related to New York law issues, they were more radical and require a more scrutinized analysis.

A English Law CACs

By the second half of the nineteenth century, the London market started to include CACs in corporate bond issues and trust deeds. The man behind the inclusion of these CACs was Francis Beaufort Palmer, an English barrister who announced the birth year of CACs to be 1879.

The dominating CAC model governed by the English law was the one stipulated under the Swedish debt issue of 1977. The Swedish model dominated more than 90% of English debt issues’ market share from 1977 to 2004. The said model provided for a low voting threshold for amending payment terms (18.75%) that coupled with a mandatory meeting requirement and for a 50% voting threshold for amending non-payment terms. This model did not contain disenfranchisement provisions.

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26 Ibid 1647.
27 Choi, Gulati and Posner, above n 1, 7-8.
28 Gelperrn and Gulati, above n 25, 1629.
29 Choi, Gulati and Posner, above n 1, 7-9.
30 Ibid 30.
31 Geoffrey Fuller, The Law and Practice of the International Capital Markets (Lexis Nexis), 629 [15.41].
32 Choi, Gulati and Posner, above n 1, 30.
33 Buchheit and Gulati, see above n2, 1325.
34 Choi, Gulati and Posner, above n 30.
36 Ibid.
37 Ibid.
In 2004, Hungary issued its sovereign bonds governed by English law. Since then, Hungarian CACs model became the most commonly used in the English-law governed bonds. The latter provided for 75% voting threshold to amend payment and non-payment terms. It also removed the mandatory bondholders meeting that was required under the Swedish model and introduced disenfranchisement provisions.

**B New York Law CACs**

1 **The Pre 1990s CACs**

Innovation under New York law issues was more radical than the English law issues. Indeed, it consisted in a shift from ‘unanimity action clauses’ to CACs.

Prior to 1990, save some exceptions, a sovereign debtor willing to restructure its debt had to agree with each individual bondholders pursuant to the unanimity action clause that was stipulated in these issues.

The earliest form of CACs introduced under New York-law bonds was the Belgian Congo model of 1958 pursuant to which collectivity meant almost nothing but ‘unanimity’. The next notable model was the 1967 CACs based on the Irish debt issue pursuant to which unanimity was still a requirement with respect to any change in the payment terms and a majority of 50% was sufficient to amend non-payment terms. The final CAC model in the pre-1990s period, is the 1983 Indonesian model. The latter is the closest to the modern CACs and provides for a majority of 75% to amend payment terms.

It is noteworthy that the Irish model was used in 80% of this period’s issuances.

2 **The Shocks Period**

The 1991-2002 period, was described as the ‘multi-shock period’. Indeed the 1990s and the early 2000s have suffered three major financial crises that pushed market participants towards the adoption of new CACs models. Many developing countries, such as Egypt,
Bosnia, Qatar, Kazakhstan, Bulgaria and Lebanon, have responded to these crises by including CACs in their NY law governed bonds.

It should be noted that the pre-1990s CACs, namely the Irish CACs, were still dominating the market during this period. 

What is notable during this period is the readoption by the 1997 Kazakh debt issue of the Indonesian CACs model. The Indonesian model, as mentioned above, is the closest to modern CACs but was abandoned by Indonesia itself in the earliest stage of the issue. The readoption by Kazakhstan of the said model was substantial to the development of CACs.

3 Why ‘Lost CACs’?

The pre-2003 Mexican CACs models used in sovereign debt issued under New York law had a small and marginal effect on the market. Indeed, Anna Gelpern and Mitu Gulati, two of the most prominent academic figures in the world of sovereign debts, had made two important arguments with respect to the pre-2003 New York law CACs:

The first argument is that the issuers of the pre-Mexican sovereign debts were so small that ‘the borrowers themselves seemed unaware, or at least indifferent, to the shift’ from the unanimity to the collectivity requirement in the market. Statistics have proven the first argument to be correct as the universal shift towards the use of CACs in New York Law contracts only flourished post 2003. Prior to that date many have argued that ‘US bonds typically do not have CAC features’.

The second argument was that the pre-Mexican collectivity clauses were not innovations but rather the result of drafting inadvertence. To our view however, it would be difficult to sustain the idea that professional market participants have inadvertently included CACs in their contracts.

48 Gelpern and Gulati, above n 25, 1642; see also Choi, Gulati and Posner, above n 1, 21.
49 Choi, Gulati and Posner, above n 1, 20-22.
50 Ibid.
51 Gelpern and Gulati, above n 25, 1647.
52 Ibid.
53 Ibid.
54 Ibid.
56 Gelpern and Gulati, above n 25, 1647.

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The authors refer to another study to opine that law firms representing sovereigns and investors were copying English-law CACs into New-York law contracts. However, the prospectus of the Indonesian bonds of 1983, for instance, was drafted by lawyers at Sullivan & Cromwell. Sullivan & Cromwell is one of major players in the sovereign bonds market and has many New York law sample agreements. The firm is familiar with the New York-law contract. Thus, it would be a mistake to think that its lawyers inadvertently copied English law provisions into these Indonesian bonds.

A more concrete example relates to a small country’s issue. In July 1995 Lebanon issued its first bond under the English-law model. The quorum and minimum vote threshold required for passing extraordinary resolutions for amending payment terms under these bonds was very low. The Second bond issue of October 1997 on the other hand was based on the New York-law model and the required the approval of the holders of a supermajority of 75% of aggregate principal amount of the bonds to change payment terms. The higher minimum vote requirement was carefully planned by Lebanon’s lawyers who expressly commented that the change had taken into consideration the possibility of a future restructuring of the Lebanese debt and the need for having a higher majority to approve such restructuring.

All this being said, the development of CACs in NY-law bonds from its earliest stages up until 2003 was not the result of inadvertence and poor drafting skills. It was rather a matter of design and skilled planning.

III THE WIDESPREAD OF CACs:
THE MEXICAN ISSUANCE & ICMA’S FIRST GENERATION STANDARD CACS

A The Triggering events: Vultures’ Success and Fear From SDRM

In February 2003 the Mexican sovereign debt issuance happened and with it CACs became ubiquitous in almost every sovereign debt issue thereafter. The wide-spread of CACs was attributed to two main triggering events.

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58 Gelpen and Gulati, above n 25, 1648.
59 Gugatti and Richards, above n 57, 821.
61 Ibid 78-79.
62 Ibid.
63 Ibid 79.
64 See generally Gelpen and Gulati, above n 25.
1 Vultures’ Success

The first event was the success which a holdout vulture fund (Elliott Associates LP) had achieved against Peru in the Court of Appeals of Brussels in Elliot v Peru.\footnote{Elliott Assocs. No. 2000/QR/92 [Court of Appeals of Brussels, 8th Chamber, September 26, 2000].} The case underlined, in circumstances where CACs were lacking and pari passu clause wrongly interpreted, an unprecedented use by a holdout creditor of litigation mechanism to obtain a ‘disproportionate payment out of a sovereign’.\footnote{Michael Bradley, James D. Cox and Mitu Gulati, ‘The Market Reaction to Legal Shocks and Their Antidotes: Lessons from the Sovereign Debt Market’ (2010) 39(1) Journal of Legal Studies 289, 293 (The fund made a USD 44 Million in profits as a result of the injunction).}

2 Fear from SDRM

The second and more important triggering event was the fear from the Sovereign Debt Restructuring Mechanism (‘SDRM’) proposal made by the IMF. In 2001, the IMF suggested a quasi-statutory regime to deal with collectivity problems in Debt restructuring.\footnote{Gelpern and Gulati, above n 25, 1643} The IMF supported CACs but considered them insufficient.\footnote{Robert Gray, ‘Collective Action Clauses’ (November 11, 2003) International Primary Market Association 1, 5 <http://www.icmagroup.org/assets/documents/111103%20RBG%20UNCTAD%20Speech.PDF>}. As a remedy, it proposed to create a similar regime to the national insolvency procedures by virtue of which sovereigns and their creditors abide to the decisions of an independent institution such as the IMF itself.\footnote{See, eg, Mark Sobel, ‘Strengthening Collective Action Clauses: Catalyzing Change—The Back Story’ (2016) 11(1) Capital Markets Law Journal 3, 5.} The argument was that, as is the case in corporate issuances, creditors of the sovereigns debts should be bound into a restructuring through a bankruptcy regime and that the lack of same should be remedied through SDRM.\footnote{See generally Gelpern and Gulati, above n 25, 1643.}

However, the major financial players did not positively welcome SDRM. It was rejected by the USA treasury\footnote{See generally Gelpern and Gulati, above n 25.} and by England. The fear was that the mechanism would be subject to political influences, interfere with the legal authority of the national courts and posit the IMF as a supernational authority.\footnote{see generally Mark Sobel, see above n 70, 5.} Market participants also viewed in SDRM a tool to encourage sovereign defaults.\footnote{Gelpern and Gulati, above n 25, 1643.}
The fear from SDRM fuelled the need to establish an alternative method to globally solve the creditor coordination dilemma. The majority of the market participants have seen the shift towards the global adoption of CACs in 2003 as a riposte to the SDRM threat.

B A Milestone Issuance

The NY-law bond issue of Mexico in 2003 have answered the ongoing debate between SDRM and CACs in favour of the latter.

CACs have appeared in almost every issuance since 2003. Many factors have played an important role in the widespread of CACs in 2003. Indeed, the leading status of Mexico as a major player on the financial market coupled with the intervention of the Group of Ten (‘G-10 Countries’) countries with their set of CACs by late 2002 have helped the universal adoption of CACs in NY-law bonds. One other important factor was the endeavours of the U.S. Treasury to promote the use of CACs.

Mexico’s CACs adopted the recommendations of the G-10 Countries by using 75% majority threshold to make amendments to payment terms under each individual series of bonds. However, the Mexican issuance did not follow other recommendations made by the G-10 Countries as they omitted to include trustees provisions to disrupt individual actions of bondholders. The new CACs also introduced disenfranchisement provisions as standard clauses.

The Mexican issue was a pioneering issue and established CACs as a standard practice in almost 75% of sovereign bonds issued as from February 2003.

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74 see generally, Gelpen and Gulati, above n 25; Mark Sobel, see above n 70; see also Christian Hofmann, see above n 11.
75 Gelpen and Gulati, above n 25, 1649.
76 Weidemaier and Gulati, see above n 60, 58.
77 Ibid 60.
78 Gelpen and Gulati, above n 25, 1669-1671.
79 Gelpen and Gulati, above n 25, 1681.
80 Mark Sobel, see above n 70, 5.
81 Gelpen and Gulati, above n 25, 1681.
83 Choi, Gulati and Posner, above n 1, 24.
C ICMA First Generation Standard CACs

Following the Mexican issue, the ICMA (then IPMA) had published standard CACs that were endorsed by the major trade associations and that were ‘intended to provide a market standard’ (the ‘IPMA CACs’). The IPMA CACs applied to English law governed bonds using fiscal agency agreements. In a nutshell, they mainly required a 75% of the aggregate principal amount of the outstanding notes (‘APAOB’) quorum and majority to resolve on Reserved Matters.

In sum, the Mexican and IPMA standards have revolutionized the use of CACs throughout sovereign debt issuances from 2002 to 2012. However, these CACs suffered a major caveat: They applied single-series voting mechanism.

This is not the end of the evolution story.

IV POST MEXICAN CACs: THE NEED FOR AGGREGATED ‘SUPER-CACs’

A The Greek Domestic Aggregated CACs

Most of the post-Mexican issuances mimicked the series-by-series voting CACs of Mexico and IPMA. However, the said voting mechanism could limit the effectiveness of CACs. It sufficed for holdouts to acquire a blocking minority of 25.1% of a single series to block the restructuring endeavours. The proponents of this argument pushed towards the advantageous effect permitting the ‘aggregation’ of claims across all the sovereign bonds. CACs with aggregation voting provisions were described as ‘super-CAC[s]’. Aggregation would make the ability to block the restructuring of a given series a far more difficult task for holdouts.
Back in 2003, few sovereign issues, such as those of Turkey\textsuperscript{93} and Uruguay, had provisions that allowed for aggregation\textsuperscript{94} as the latter was not a market standard.\textsuperscript{95}

Things were about to change in February 2012 with the CACs model used in the Greek debt workout. The domestic Greek law governed 90% of the total Greek bonds in contrast to 10% governed by foreign laws (mainly English law).\textsuperscript{96} The international sovereign bonds provided for single series voting CACs with a 75% qualified majority. ‘One adviser to investors who held out in the Greek restructuring in March 2012 explained that [English law] CACs made the process more predictable for his clients’\textsuperscript{97} – the process of holding out.

As for the other bonds issued under the local Greek law, they lacked CACs and other basic protective provisions and were consequently hard to restructure.\textsuperscript{98} To have such bonds restructured, Greece employed a mixture of sticks and carrots techniques (\textit{e.g.} exit consents,\textsuperscript{99} financial incentives, collateralized securities, etc).\textsuperscript{100} The main stick though was a change in the domestic Greek law to retroactively fit CACs in the domestic bonds.\textsuperscript{101} This technique was applauded and considered to be the ‘single most important restructuring provision in the new bonds’.\textsuperscript{102}

Importantly, the retrofitted CACs introduced by Greece contained an aggregated two-limb voting procedure targeting both the outstanding bonds series on one hand and the individual series on the other.\textsuperscript{103} The Aggregation feature in domestic bonds’ CACs has shown its efficiency when contrasted to other Greek bonds issued under foreign law. Indeed, the restructuring would not have advanced as smoothly as it did absent these provisions.\textsuperscript{104}

\begin{thebibliography}{10}
\footnotesize
\bibitem{93} Choi, Gulati and Posner, above n 1, 24.
\bibitem{94} Anna Gelpern, above n 84, 143.
\bibitem{95} see, eg, Choi, Gulati and Posner, above n 1; See also, IMF Staff Report 2014, above n 89.
\bibitem{96} greek debt, the end game scenario, p2
\bibitem{97} Anna Gelpern, above n 84, 144; see also Anna Gelpern, ‘Sovereign Damage Control’ (May 2013) WP 13-12 \textit{Peterson Institute for International Economics} 1, 12 <https://piie.com/publications/pb/pb13-12.pdf>.
\bibitem{98} such cross-default, \textit{pari passu} and/or negative pledge: see Mitu Gulati and Jerome Zettelmeyer, ‘Making a Voluntary Greek Debt Exchange’ (2012) 7(2) \textit{Capital Markets Law Journal} 169, 177.
\bibitem{100} Ibid; see also Zettelmeyer, Trebesch, and Gulati, above n 8, 25.
\bibitem{101} Jeromin Zettelmeyer, Christoph Trebesch, and Mitu Gulati, above n 8, 24.
\bibitem{102} Simmons, above n 99, 325.
\bibitem{103} Ibid 324.
\bibitem{104} IMF Staff Report 2014, above n 89, 19.
\end{thebibliography}
B The Eurozone CACs

1 General Overview

The Greek crisis and the potential financial problems of Ireland, Spain, and Portugal\(^{105}\) have raised awareness within the European Union (‘EU’) to the need to include CACs in future European sovereigns’ debts.\(^{106}\) This objective was reached when the Treaty Establishing the European Stability Mechanism,\(^{107}\) provided for the mandatory inclusion of CACs in all sovereign debts issuances made by EU member states as from January 1\(^{st}\), 2013. These CACs (‘Eurozone CACs’) follow the standard euro-zone Common Terms of Reference (‘CTR’) and apply to domestic and foreign law bonds issues with a maturity date greater than one year.\(^{108}\) Eurozone CACs were published by a sub-committee of the Economic and Financial Committee of the EU (‘Sub-committee’) in March 2012.\(^{109}\) For ease of reference, the below table dissects the quorum, minimum approval threshold and voting options under the CTR.


\(^{106}\) Gulati and Zettelmeyer, see above n 98, 178.


\(^{108}\) ibid art 12(3).

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<td>Quorum</td>
<td>66(^{2/3})%(^{110})</td>
<td>50% or 25% when adjourned</td>
<td>66(^{2/3})%(^{112})</td>
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<td>Minimum Approval Threshold</td>
<td>75% of APAOB(^{113})</td>
<td>50% of APAOB(^{114})</td>
<td>Not available</td>
<td>66(^{2/3})% of APAOB(^{116})</td>
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<td>75% of APAOB of all affected series in aggregate AND 66(^{2/3})% of APAOB of each affected series(^{115})</td>
<td>Not available</td>
<td>66(^{2/3})% of APAOB(^{116})</td>
<td>50% of APAOB of each affected series(^{118})</td>
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\(^{110}\) Euro Model CAC, above n 21, art 4.5(a).
\(^{111}\) Ibid art 4.5(b) and 4.6(b).
\(^{112}\) Ibid art 4.6(a).
\(^{113}\) Ibid art 2.1(a).
\(^{114}\) Ibid art 2.5(a).
\(^{115}\) Ibid art 2.2(a)(i) and (b)(i).
\(^{116}\) Ibid art 2.1(b).
\(^{117}\) Ibid art 2.5 (b).
\(^{118}\) Ibid art 2.2(a)(ii) and (b)(ii).

FROM THE LOST TO THE SECOND GENERATION COLLECTIVE ACTION CLAUSES: IS THE INCLUSION OF NO-ACTION CLAUSE THE NEXT STEP FORWARD?
2 Notable Innovations

Two important innovations of Eurozone CACs should be scrutinized. The first is on the level of the modification provisions whereas the second is on the level of the enforcement provisions.

(a) Cross-Series Modification

The first innovation is the cross-modification feature that can be exercised by the issuer. The rationale behind the technic is that a series-by-series vote would make it beneficial for bondholder of each series to vote against a restructuring in the hope that other series would approve the restructuring. This would improve the financial situation of the holding out series.\textsuperscript{119} Moreover, series-by-series modification allows holdouts to buy ‘cheap’ blocking stacks and disrupt workouts. Aggregation or cross-series modification introduced within the CTR is a remedy to single series holdout problems.\textsuperscript{120} If a cross-series modification is invoked, a minimum approval threshold is required both on the level of the APAOB of all affected series in aggregate and of each affected series.\textsuperscript{121} Furthermore, the same modification terms or modification options (when offered) should be offered for the bondholders to vote on in order to ensure an equal treatment of bonds.\textsuperscript{122} If the holders of one series do not agree to the modification terms, the said series would then be excluded from the restructuring and the issuer would proceed as if the modification proposal was initially made to the other series, excluding the holdout series.\textsuperscript{123}

Although the form of aggregation offered by CTR constituted a leap into a better creditors coordination mechanism and is undeniably a better remedy against holdouts than single-series CACs, it was still raising some concerns. On the one hand, it might leave a creditor who is willing to accept the restructuring proposal outside such restructuring if the series of its bonds is voted out;\textsuperscript{124} on the other hand, the existence of the bond-by-bond requirement still permit the acquisition of a blocking stack within a single series to cast it out of the restructuring.\textsuperscript{125} This undermines aggregate two-limb voting procedures as the ultimate tool against holdouts.

\textsuperscript{119} Christian Hofmann, see above n 11, 401.
\textsuperscript{120} Supplemental Explanatory Note, above n 109, 3.
\textsuperscript{121} Euro Model CAC, above n 21, art 2.2.
\textsuperscript{122} Supplemental Explanatory Note, above n 109, 4.
\textsuperscript{123} Linklaters, above n 17, 3.
\textsuperscript{124} Contra Mark Sobel, see above n 70, 8.
\textsuperscript{125} see generally Jesse Kaplan, see above n 88, 26-32.
(b) Sole Holder Action

The second important innovation in CTR is related to enforcement rights and is included in the CTR's Supplemental Provisions. The latter provides for a limitation on 'Sole Holder Action'. Article 3 of the Supplemental Provisions provides that no bondholder will be entitled to individually institute proceedings against the issuer unless the trustee or fiscal agent fail to do so. This provision only applies where the bonds stipulate for a trustee or a fiscal agent.

Such provisions were not included in the IPMA CACs which only provide for collective acceleration and reversed acceleration rights without giving the fiscal agent or the Noteholders’ Committee an express right/obligation to sue on behalf of individual bondholders. Moreover, trustees were not mentioned in the IPMA CACs. The inclusion of such provision in the Eurozone CACs is an important step towards strengthening CACs as will be argued hereunder.

It is noteworthy though that the no-action clause was marginally mentioned in the Eurozone CACs. Indeed, it was mentioned in the Supplemental Provisions of the Eurozone CACs (rather than in the CTR). Furthermore, the Sub-Committee discussed the said clause in a paragraph titled ‘Other Provisions’ in its Explanatory Note. The form under which said clause was mentioned undermines its importance. This might be justified by the fact that the clause is to be included ‘only if the Bonds provide for a fiscal agent or trustee’. Because such appointment is not mandatory, the said clause is therefore not always applicable. Nevertheless, mentioning no-action clauses within the Eurozone CACs was a step forward in the evolution of CACs.

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127 Ibid.
128 Ibid.
129 Ibid
130 2004 IPMA Standard CACs, above n 21.
131 See Part VI-B-5-(b).
132 Supplemental Explanatory Note, above n 109, 7.
V THE LATEST STANDARDIZED INNOVATION:
ICMA 2014: SECOND GENERATION CACs

A Triggering Events

In December 2013 ICMA, the primary objective of which is to create an orderly and efficient international capital markets, consulted its members with respect to a proposition for the inclusion of a new standard model of aggregated CAC in all international sovereign bonds that are not otherwise subject to Eurozone CACs. The intervention of ICMA was triggered by a need to publish new CACs and a standard pari passu clause in the wake of the NML Capital Ltd v The Republic of Argentina case in which the courts of New York expansively interpreted the pari passu clause. The court ruled that the clause was comprised of two parts. The first prohibited Argentina from subordinating a class of bonds to another class. The second part, however, obliged Argentina to pay the plaintiffs (holdouts) ‘rateably’ with other creditors.

The expansive interpretation by the US courts of the pari passu clause and the success of holdouts had perturbed the understanding of an old stipulation in financial transactions and was one of the triggering events leading to the intervention of ICMA to readdress the drafting of the clauses in sovereign debt contracts.

As for the second reason that triggered the intervention of ICMA to set a new model CACs, it was the inefficiency of the series-by-series CACs model. This was particularly evidenced by the inability of Greece to exchange more than half of its English-law governed bonds because of the said model.

B General Overview

In August 2014, ICMA published its Standard Aggregated CACs (‘Standard Aggregated

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136 Unreported, United States Court of Appeals, Second Circuit, 5 July 2011.
137 EM Ltd et al v The republic of Argentina (7 April 2007) (No 3-civ-2057-TPG); See also NML Capital, LTD and EM v Banco Central de la Republica Argentina, Unreported, United States Court of Appeals, Second Circuit, 5 July 2011.
138 NML Capital, LTD and EM v Banco Central de la Republica Argentina Unreported, United States Court of Appeals, Second Circuit, 5 July 2011.
139 Mark Sobel, see above n 70, 5.
140 Ibid 6.
141 IMF Staff Report 2014, above n 89, Annex 1.
142 2014 Standard Aggregated CACs, above n 21.
CACs’) and a *pari passu* clause model designed to prevent the expansive interpretation of the US courts by expressly providing that the clause does not create any obligation on the issuer to make equal or rateable payments.\textsuperscript{143}

On the level of their scope, the Standard Aggregated CACs only apply to foreign law (English or New York law only) sovereign bonds and do not extend to domestic issuances\textsuperscript{144} as the Eurozone CACs do.

On the level of innovation, ICMA had the financial world welcome the introduction of the aggregate single limb voting procedures.\textsuperscript{145} Before engaging in a further study of the new aggregation mechanism, it should be noted that ICMA gave sovereigns an option to choose between three voting procedures for restructuring purposes, namely the series-by-series, the aggregate two-limb and the aggregate single-limb voting procedures.\textsuperscript{146} For ease of reference, the below table will show the quorum, minimum approval threshold and voting options under the Standard Aggregated CACs:

<table>
<thead>
<tr>
<th>Single series modification (meeting &amp; Written Resolution)</th>
<th>Multiple Series Aggregation – Single Limb Voting (Meeting &amp; Written Resolution)</th>
<th>Multiple Series Aggregation – Two Limb Voting (Meeting &amp; Written Resolution)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reserved matter</td>
<td>Non-reserved matter</td>
<td>Reserved matter</td>
</tr>
<tr>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Quorum</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Minimum Approval Threshold</td>
<td>75% of APAOB\textsuperscript{147}</td>
<td>75% of the APAO Debt Securities of all affected series of Debt Securities Capable of Aggregation (taken in aggregate)\textsuperscript{149}</td>
</tr>
<tr>
<td>50% of APAOB\textsuperscript{148}</td>
<td>50% of APAOB\textsuperscript{148}</td>
<td>Not available</td>
</tr>
<tr>
<td>66⅔% of APAO Debt Securities of all affected series (taken in aggregate) AND 50⅔% APAO Debt Securities of in each affected series (taken individually)\textsuperscript{150}</td>
<td>Not available</td>
<td>Not available</td>
</tr>
<tr>
<td>Not available</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

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\textsuperscript{143} Ibid.
\textsuperscript{145} 2014 Standard Aggregated CACs, above 21, Meetings of Noteholders; Written Resolutions [c].
\textsuperscript{146} ICMA Sovereign Bond Consultation Supplement, above n 144.
\textsuperscript{147} 2014 Standard Aggregated CACs, above 21, Meetings of Noteholders; Written Resolutions (b).
\textsuperscript{148} Ibid.
\textsuperscript{149} Ibid [c].
\textsuperscript{150} Ibid [d].
Some comments should be made with respect to the above table. First, shareholding meetings do not require quorate as the majority is calculated by reference to the APA of the outstanding bonds, not by reference to the bondholders who vote. The quorum was eliminated as it was thought to weaken the efficiency of CACs by allowing holdouts to prevent the restructuring of a given series through the quorum requirement.

Moreover, unlike the Eurozone CACs, Aggregated Standard CACs do not require different minimum approval thresholds based on whether the decision is taken in a meeting or by written resolution. ICMA justifies this innovation as one that would make the CACs more advantageous since, given that the approval threshold required in a meeting is usually higher than the one for a written resolution, holdouts would no longer be able to buy a more affordable blocking stake to use it in the course of a bondholders meeting.

C Aggregate Single-Limb Voting Procedures: Benefits and Risks

1 Advantages: Efficient Tool against Holdouts

Aggregated single-limb voting mechanism represents the most radical innovation introduced by ICMA and consists of allowing bondholders across all series of bonds, in a single vote across multiple series, to approve a proposal made for the modification of multiple series of bonds. The voting threshold is 75% of all APAOB across all affected series. This technique would highly diminish the power of holdouts to block restructurings as the price of the required blocking stack is extremely high when compared to the one that is sufficient under the two other voting mechanisms. Consequently, the core advantage of the new procedure is that it ‘shifts the incentives against potential holdouts.’ Moreover, the new voting mechanism allows the issuer to pool different series together to dilute

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152 see ICMA Sovereign Bond Consultation Supplement, above n 144, 7[9].
153 Deborah Zandastra, see above n 152, 3
154 ICMA Sovereign Bond Consultation Supplement, above n 144, 1 [4].
155 2014 Standard Aggregated CACs, above 21, Meetings of Noteholders; Written Resolutions [c].
157 Ibid.
holdouts’ blocking strategies.\textsuperscript{158} Hence, a potential holdout would not be able to predict what series will be pooled together, which highly reduces the risk of holdouts.\textsuperscript{159} By reducing the uncertainty of outcome existent under an aggregated two-limb voting procedure, the new procedure facilitates and expedites the reach of a settlement.\textsuperscript{160}

However the single-limb aggregation voting, as a powerful tool against holdouts, should be exercised carefully so it does not turn into a weapon used abusively by an issuer and/or majority of creditors against an oppressed minority.

\section*{2 Risks: A Tool for Majority Abuse?}

Unlike what was wrongfully suggested by the court in \textit{NML v Argentina}\textsuperscript{161}, CACs are not designed to and should not totally eliminate holdouts.\textsuperscript{162} The role of CACs and their relationship with \textit{pari passu} clauses was wrongly interpreted by the New York court as the role of CACs is not to remove the risk of litigation but to rather avoid unnecessary use of litigation by a disruptive minority.\textsuperscript{163} CACs are a tool to help restructuring by reducing, not eradicating, the capacity of a minority to block a restructuring.\textsuperscript{164} As such, the rights granted by the CACs to the majority of shareholders should be exercised in an orderly and non-abusive manner; otherwise, CACs might exacerbate litigation rather than reducing them.

Some authors have argued that the simple inclusion of single-limb aggregation voting procedures within the terms of CACs ‘may run afoul of equitable principles’ and ‘allows a borrower to collude with a large majority creditor to repress minority’.\textsuperscript{165} In response to these concerns, ICMA had all proposals made under aggregated single-limb voting procedures be given in compliance with the Uniformly Applicable requirements.\textsuperscript{166} The Uniformly Applicable provisions were expanded and better explained under ICMA’s new Standard CACs model published in May 2015.\textsuperscript{167} Their main purpose is to ensure that any proposal made by the issuer is offered in the same manner and under the same terms to all creditors holding affected bonds so that the amended bonds have identical provisions.\textsuperscript{168}

\begin{flushleft}
\begin{footnotesize}
\textsuperscript{158} Alejandro Díaz de León, ‘Mexico’s Adoption of New Standards in International Sovereign Debt Contracts: CACs, Pari Passu and a Trust Indenture’ \textit{(2016) 11(1) Capital Markets Law Journal} 12, 18-19.
\textsuperscript{159} Makoff and Kahn, above n 156, 44-5.
\textsuperscript{160} ICMA Sovereign Bond Consultation Supplement, above n 144, 1 [2]
\textsuperscript{161} NML Capital, LTD and EM v Banco Central de la Republica Argentina, Unreported, United States Court of Appeals, Second Circuit, 5 July 2011.
\textsuperscript{162} Anna Gelpern, above n 97, 13.
\textsuperscript{163} Jill Fisch and Caroline Gentile, above n 4, 1095.
\textsuperscript{164} Jesse Kaplan, see above n 88.
\textsuperscript{165} Ibid 31.
\textsuperscript{166} 2014 Standard Aggregated CACs, above 21, Meetings of Noteholders; Written Resolutions [c]-[v].
\textsuperscript{167} Ibid [c]-[vi]
\textsuperscript{168} ICMA Sovereign Bond Consultation Supplement, above n 144, 3.
\end{footnotesize}
\end{flushleft}

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Thus, an offer made under different terms cannot be voted under the single-limb voting procedures but can still be made under the two-limb procedures.

Additional safeguards against abuse conducts are provided by the provisions of the Standard Aggregation CACs such (i) the high approval threshold (75%), and (ii) the inclusion of fairly protective disenfranchisement provisions excluding from the right of vote all bonds owned or controlled by the issuer, and (iii) the inclusion of an ‘Information’ covenant to ensure that the restructuring plan is made available to the voting bondholders before they vote on its approval.170

In addition to the provisions of the Standard Aggregate CACs, the contract law principles of good faith and bona fide which require a party to consider the interests of its counterparty171 also apply to the newly introduced voting procedures. The modern English case law had ruled that the right to vote should be exercised bona fide, in good faith and for the purpose of which it was conferred - this being the facilitation of debt restructuring in the present context.172 A mere disadvantage suffered by the minority is not sufficient to hold the majority liable for abuse.173 The vote is not abusive as long as it is not directly made to maliciously oppress the minority.174 The same position was held by the US courts where good faith was established as a minimum general voting requirement.175

The position of the English and US courts are related to corporate bonds issues but can be applied to sovereign issues by analogy. This said position has also been endorsed by the IMF who solemnly declared that the single-limb voting procedures would be enforceable in England law provided there is no bad faith or abuse of power.176 Abuse of power occurs when decisions are taken for the sole purpose of benefitting the majority rather than the group of affected creditors. However, the sole fact that minority creditors received less benefits than the majority does not constitute an abuse of power.177 The IMF also confirms that these voting procedures would be enforceable under New York law provided that (i) the voting is ‘exercised in the best interests of bondholders as a class’, and (ii) is ‘free of collusion or corruption’.178

169 2014 Standard Aggregated CACs, above 21, Meetings of Noteholders; Written Resolutions [i].
170 See 2014 Standard Aggregated CACs, above 21, Meetings of Noteholders; Written Resolutions [f].
172 See Redwood Mater Fund v TD Europe Bank Europe Ltd [2002] EWHC (Ch) 2703.
173 Ibid.
174 Ibid, [105].
176 IMF Staff Report 2014, above n 89, 29.
177 Ibid.
178 IMF Staff Report 2014, above n 89, 30.
ICMA itself, the IMF, the IIF, the IMFC and the G20 encouraged the use of the Standard Aggregated CACs. As at April 2016 over 90% of the sovereign debts issued under New York law (e.g. Mexico, Chile, Turkey and Indonesia) and over 75% of sovereign debts issued under English law (e.g. Armenia, Croatia, Kazakhstan and Tunisia) have adopted the new model of single-limb aggregation voting procedures.

It is noteworthy that in May 2015, ICMA published an updated version of the Standard Aggregate CACs that did not interfere with the core of the 2014’s model. The May 2015 update was published to clarify and expand the ‘Uniformly Applicable’ requirements to better safeguard against majority abuse. The update also meets formalistic and stylistic drafting differences between New York law and English law contracts by adding a new set of New York-law CACs. The said set of CACs is only included to accommodate the drafting style of NY-law contract but does not change any substantive terms or conditions applicable under the October 2014 model.

VI WHERE TO GO FROM HERE?

A General Propositions

Many recommendations and questions are still being argued to further strengthen Standard Aggregated CACs. Those include but are not limited to whether or not aggregation should be possible for different series of bonds when the latter are governed by different laws and whether or not Standard Aggregated CACs should be included in domestic law governed bonds especially that in domestic contexts, issuing governments can always intervene, provided such intervention is not anti-constitutional, to retroactively or proactively include those CACs in the debt contract as was the case with Greece.

179 Zandstra, Yianni and James, above n 5, 2; see also IMF Staff Report 2015, above n 135.
180 Zandstra, Yianni and James, above n 5, 2.
181 IMF Staff Report 2015, above n 135, 5[7].
182 Ibid.
183 Deborah Zandstra, Andrew Yianni and Simon James, above n 5, 2;
185 Ibid 17-29.
186 IMF Staff Report 2015, above n 135, 7[13].
187 Deborah Zandstra, see above n 152, 3.
188 Ibid.
189 see Makoff and Kahn, above n 156, 46.
However, all these questions and propositions seem to focus on modification clauses with almost no attention to the necessity of strengthening enforcement clauses within CACs. Whilst the IPMA 2004 CACs, the Eurozone CACs and the Standard Aggregated CACs all provide for collective acceleration and reverse acceleration clauses, only Eurozone CACs recommend to limit the right of an individual bondholder to sue the issuer.

B No-Action Clause: the Step Forward?

It is agreed amidst scholars and market participants that submitting the power to accelerate and to reverse acceleration to a collective vote of bondholders is crucial for deterring disruptive litigation. This author concurs with these views but argues that reaching the objective of limiting disruptive litigation remains fragile absent a limitation on individual bondholders’ right to sue.

1 The Rationale

Absent limitation on the right of individual holders to sue, the latter might institute proceedings to undermine the ongoing negotiations between the issuer and the majority after default and before a restructuring agreement is reached. No-action clauses would also prevent pre-acceleration individual actions that could otherwise be caused by the non-payment by the sovereign of a coupon to a single bondholder. Moreover, once Acceleration is declared by a qualified majority of holders, the claims resulting from such acceleration can still be individually enforced by each bondholder absent no-action clauses. Multitude of actions means additional costs, less creditors’ coordination, several enforcement attempts and distress to the sovereign and its national socio-economical welfare. Thus, limitation of the bondholders’ individual enforcement rights should be seen as complementary to the collectivisation of acceleration rights provided under most standardized CACs models.

The guiding principle behind the limitation of individual rights to sue is that bondholders should be seen as a class and classes act collectively. No-action clauses help to achieve

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190 Bradley and Gulati, above n 105, 51-52.
191 See 2004 IPMA Standard CACs; see also Model Collective Action Clause: Supplemental Provisions, above n 126; and 2014 Standard Aggregated CACs, above n 21.
192 see e.g. Christian Hofmann, see above n 11, 399-400; see also Bradley and Gulati, above n 105; see also Report On Contractual Clauses, above n 82, Cl 3-5; See also ICMA, ‘Sovereign Bonds Consultation Paper’, above n 134.
193 IMF Staff Report 2015, 13[28].
194 Bradley and Gulati, above n 105, 51[8.5].
195 Christian Hofmann, see above n 11, 399
collectivity by centralising enforcement actions\(^{197}\) and ‘preventing the race to the courthouse door’.\(^{198}\)

### 2 Legal Standing of No-Action Clauses

No-action clauses are enforceable under New York and English laws. Since 1931, US judges had always dismissed attacks on clauses limiting the right of individual holders to sue for being in breach of public.\(^{199}\) English courts have followed the same lead.\(^{200}\)

Not only are these clauses enforceable but were also expansively interpreted by the US and English courts. It is true that some few judgments have narrowly interpreted the scope of no-action clauses, but the general practice followed by the courts remains however to give such clause its expansive purposive nature,\(^{201}\) namely the limitation of disruptive litigation.

The expansive interpretation of the no-action clause means that the courts do not only refer to the exact terms of the clause to narrowly interpret them but rather give such clauses a broader scope to cover lawsuits that are not expressly covered by the clause.\(^{202}\) In this perspective, no-action clauses have been expanded to prevent bondholders from instituting proceedings either before or after the occurrence of an event of default.\(^{203}\) They were also expanded to cover extra-contractual actions, such as tort actions,\(^{204}\) as long as the claims alleged affect the bondholders as a class as opposed to the rights of the bondholder as an individual.\(^{205}\)

The attitude of the courts towards such clauses underlines the importance of their inclusion in sovereign bond issuances as a powerful tool against disruptive litigation with claims going beyond the contract itself in some cases.

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\(^{197}\) Simmons, above n 99, 323.

\(^{198}\) Benjamin Liu, above n 198, 3.

\(^{199}\) *Home Mortgage Co v Ramsey*, 49 F 2d 738 (4th Cir NC, 1931).

\(^{200}\) See, eg, *Colt Telecom Group plc* [2006] EWHC 2815.

\(^{201}\) Benjamin liu, above n 198, 3.

\(^{202}\) See the Canadian Case, *Casurina Limited Partnership v Rio Algom Ltd* 2004 CanLII 30309 (Ontario CA); see also, *Feldbaum v McCrory Corp*, 18 Del J Corp L 630 (Ct Ch Del, 1992); See also *Colt Telecom Group plc* [2006] EWHC 2815; See also, *Elektrim SA v Vivendi Holdings 1 Corp* [2008] EWCA Civ 1178 (LJ Lawrence Collins).

\(^{203}\) *Colt Telecom Group plc* [2006] EWHC 2815.

\(^{204}\) Philip Rawlings, ‘Reinforcing Collectivity: The Liability of Trustees and the Power of Investors in Finance Transactions’ (2009) 23(1) *Trust Law International* 14

\(^{205}\) *Elektrim SA v Vivendi Holdings 1 Corp* [2008] EWCA Civ 1178, LJ Lawrence Collins.
International sovereign bonds are usually issued under a fiscal agency agreement (‘FAA’) or a trust structure – the latter being referred to as trust indenture under New York law or trust deed under English law.\textsuperscript{206} Practice has proven that FAA are more frequent than trust structures in sovereign bond issuances for many reasons,\textsuperscript{207} one of which is that the former is less costly,\textsuperscript{208} The provisions stipulating for FAA or trust structures are commonly referred to as Representation Clauses.\textsuperscript{209} It is through the operation of these clauses that the right of individual bondholders to sue can be channelled through the fiscal agent or the trustee. This right can also be channelled, as the Declaration of Acceleration provisions is,\textsuperscript{210} through any other ‘bondholders representative’.\textsuperscript{211}

However, FAA and trust structures are legally different. A Fiscal agent is appointed by the issuer and acts as an agent for the latter. He does not act on behalf of bondholders nor does he owe any duty to them.\textsuperscript{212} A trustee on the other hand acts on behalf of the bondholders and represents their interests. As such, trust structures usually grant the trustee the right to enforce the bondholders’ rights against the issuer and simultaneously deprive them from individual enforcement actions.\textsuperscript{213}

Moreover, within trust structures the duties of a trustee are not the same depending on whether they fall within a trust deed or a trust indenture.\textsuperscript{214}

Under the \textit{US Trust Indenture Act of 1939},\textsuperscript{215} which mandates the appointment of a trustee in public corporate bonds issuances, a trustee has fiduciary duties towards the bondholders upon the occurrence of an event of default, and should use the same degree of care in representing the interests of the latter as it would have done in the conduct of its own business.\textsuperscript{216} However, such fiduciary duty does not usually exist in the form of trust indenture used in sovereign bond issues governed by New York Law.\textsuperscript{217}

\textsuperscript{206} IMF Staff Report 2015, above n 135, 10 [22].
\textsuperscript{207} Simmons, above n 99, 323.
\textsuperscript{208} IMF Staff Report 2015, above n 135.
\textsuperscript{209} Bradley and Gulati, above n 105.
\textsuperscript{210} 2014 Standard Aggregated CACs, above 21, Event of Default.
\textsuperscript{211} Ibid.
\textsuperscript{212} Liu, above n 20, 1-2.
\textsuperscript{213} Ibid 2.
\textsuperscript{214} Buchheit and Gulati, see above n2, 1331-1332.
\textsuperscript{215} Trust Indenture Act of 1939, 15 USC (1939).
\textsuperscript{217} Ibid 9.
As for the English law, the general view is that the responsibilities of a trustee are determined and should be interpreted in light of the parties’ autonomy principle as expressed in the trust deed. This view has been confirmed by LJ Collins in *Elektrim SA v Vivendi Holdings* who said that it would be ‘surprising’ to accept that the trustee has fiduciary duties. However, under the English law a trustee should nonetheless perform its duties honestly and in good faith for the benefit of the bondholders and the trust deed can always be drafted in a way to reflect a fiduciary duty.

Moreover, the legal concept of trust might not exist or be recognized in many jurisdictions. Mostly, those are the civil law jurisdictions that have developed alternative mechanisms or bodies to represent bondholders as a class (e.g. The Japanese commissioned company for bondholders under the Japanese Commercial Code). The responsibilities of such bodies can also be different from those of a trustee under US or English law.

4 Why Is All That Important?

The differences that can arise between the responsibilities of a fiscal agent, trustee or any other bondholders representative underline the importance of the terminology and drafting precision that should be employed when drafting the no-action clauses and the structure under which they should operate to make clauses more efficient. For instance, FAA should be amended to ban the right of individual bondholders to sue and trust deeds or trust indentures can be drafted in a manner to give the trustee more fiduciary powers to reduce the risk of its actions not reflecting the best interests of the bondholders. This was the case for instance when the trustee failed to exercise its discretionary power to institute proceedings when Ecuador defaulted on its international bonds in late 2008, because the trustee was not sure whether it obtained the 25% necessary votes to enforce and did not employ its discretionary fiduciary duty to litigate. This has led the famous practitioner Lee Buccheit and professor Mitu Gulati to propose ‘a higher post-default standard of trustee responsibility’ provision under New York sovereign bond issues.

All this being said, market participants should be aware of the importance of the nature and scope of the legal responsibilities of the body (whether a trustee, fiscal agent or other

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218 1 Corp [2008] EWCA Civ 1178, LJ Lawrence Collins.
219 Simmons, above n 99, 323.
220 Liu, above n 20, 3.
221 Fisch and Gentile, above n 4, 1104.
222 See generally Mitu and Buchheit, above n 216.
223 Ibid.
224 Ibid 9 &12.

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bondholder representative) through which proceedings will be instituted under a no-action clause and make sure that the clauses governing the operations of such body are well drafted in a way to reflect the bondholders interests and to avoid abuse. Such is the way towards strengthening collectivity on the level of enforcement provisions stipulated in CACs.

5 Market Practice: Shift Towards the Adoption of No-action Clauses

(a) The Early Position

The G-10 countries in their recommendation of 26 September 2002 had tackled the problem of disruptive legal action from which New York-law bonds suffered. The purpose of the recommendation in relation to that matter was to give the sovereign a possibility to find solutions after a default and in anticipation to a restructuring. The Working group expressly proposed to have the power to enforce bondholders’ rights concentrated within a bondholder representative coupled with an explicit provision prohibiting individual enforcement actions.

From 2002 to 2013 most of the restructured sovereign debts were issued under New York Law rather than English law. The former mostly used FAA with no limitation on the right of individual bondholders to sue. Indeed, from 2002 to 2013, only 16.58% of the New York Law bonds had trust provisions. Thus, there was no need to follow the G-10 countries’ recommendation on this level. Hence, IPMA 2004 CACs did not provide for no-action clauses.

(b) An Express Stipulation in the Eurozone CACs

As for the Eurozone CACs, and as mentioned hereinabove, they provide for a limitation on ‘Sole Holder Action’ in the Supplemental Provisions. However, one caveat remained: The limitation is not mandatory and is scarcely explained by the Sub-Committee, which undermines its importance, as we will argue below.

227 Report on Contractual Clauses, above n 82, 6.
228 Ibid.
229 See Bradley and Gulati, above n 105, 49.
230 Lee Buchheit and Mitu Gulati, see above n2, 1331-1332.
231 Bradley and Gulati, above n 105.
232 See Part IV-B-2-(b).
The Eurozone CAC applies to both domestic and international government bonds issuances and the appointment of trustees and fiscal agents and/or the modality of such appointment are not always common in or similarly regulated by different domestic laws. The differences in the domestic law provisions between the EU member states resulted in a scarce mentioning of the limitation on individual bondholders’ rights to sue in Eurozone CACs.

As for the application of the limitation on Sole Holder Action clause in the context of international government bonds issuance, the Sub-Committee explained that ‘the Committee does not expect that the introduction of the model CAC will affect... [the] existing practice of appointing fiscal agents and trustees’. It is on this level that the Eurozone CAC could have put more emphasis on the no-action clause. Although the Sub-Committee expressly recognizes that the limitation on individual legal proceedings is found in many international sovereign debt issuances, it nonetheless only recommends their inclusion ‘to the extent they are consistent with an issuer’s existent practice and applicable law’.

However, Eurozone CAC could have provided a more powerful language in favour of the inclusion of such clauses; a language discouraging the uncoordinated domestic practices of each country. In a world of sovereign debts restructurings, where a statutory bankruptcy regime is still far from being adopted, the need for a standardized and consistent practice with respect to the contractual restructuring framework is of crucial importance for an orderly and efficient restructuring regime for both the sovereigns and their creditors.

Eurozone CACs is a mandatorily applicable ‘contractual framework’ and could have achieved this purpose with respect to no-action clauses through the use of a clearer formalistic and linguistic approach. Indeed, from a formalistic point of view, the goal of pushing towards the use of no-action clauses to protect both the sovereign and the majority of its creditor against disruptive legal action would have dictated the inclusion of the ‘Sole Holder Action’ clause in the CTR rather than the Supplemental Provisions, confining its scope to international sovereign debt issuances alone.

As from a linguistic/drafting point of view, the recommendation to use these clauses could have been drafted using a language that recommends their inclusion to the extent they are consistent with an issuer’s public policy rules and mandatory laws rather than a language requiring them to be consistent with an issuer’s ‘existent practice and applicable law’.

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234 Supplemental Explanatory Note, above n 109, 8; see also Christian Hofmann, see above n 11, 404.
235 Christian Hofmann, see above n 11, 404.
236 Supplemental Explanatory Note, above n 109, 8.
237 Ibid.
238 Ibid 8.

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Such a language would reflect a clearer intent to shift towards the use of no-action clauses whether on the level of domestic or international debt issuances within the Eurozone.

**(c) Standards Aggregated CACs and post 2014 trends**

Surprisingly, the Standard Aggregated CACs only focused on modification CACs and did not strengthened enforcement CACs by following the Eurozone CACs lead through the inclusion of a limitation on individual enforcement actions. However, the market practice underlined the importance of no-action clauses through the switch from the FAA to trust structures in sovereign bond issues in the past couple of years.

Between October 2014 and July 2015, 45% of international sovereign bonds were issued using trust structures and around 83% of said issues were governed by New York law. The IMF explained this considerable market shift towards the use of trust structures in New York law governed bonds by the fact that pursuant to such structures (i) only the trustee can initiate litigation upon the instruction of 25% of the bondholders, and (ii) even when one bondholder holds the necessary 25% majority to instruct the trustee, the trustee’s obligation to share or distribute on a *pro rata* basis the proceeds of the litigation will diminish said bondholder’s desire to make such instruction.

According to market participants, the lesser use of trust structures in English law bonds on the other hand is not based on principled legal grounds but rather caused by ‘lack of awareness’ and cost-sensitive reasons, nothing more.

The recent Mexican debt issue governed by New York law illustrates this shift. In November 2014, as was the case back in 2003, Mexico played a pioneering role in the market by adopting the Standard Aggregated CACs (only one month after its publication) and by switching from FAA to a trust indenture structure. The switch was based on the need to ‘reduce the scope for opportunistic holdouts’ and ‘improve the overall safety feature’.

The increase in the use of trust indenture and the market shift towards adopting them resembles to a large extent the market shift towards the use of CACs – a slow but steady one. In September 2015, the IMF opined that the shift towards a trust structure is now one of the ‘NEXT STEPS’ in the progress of CACs in international bond contracts.
This author believes, that the road towards strengthening CACs passes through the inclusion of a clause limiting individual bondholders’ rights to institute proceedings against the issuer. The clause itself should be stipulated in the next standard model CACs. The practical implication of such inclusion is a further limitation of disruptive holdouts litigation and an increase of market safety. The body through which litigation should be channelled can be a trustee, a fiscal agent or any other representative of the bondholders as long as the latter has the legal capacity to litigate. Indeed, future CACs standard models can follow the lead of the Euro CACs and leave the choice of the litigating body to the issuer. However, for all the reasons expressed under paragraph VI-B-3 above, and congruently with the opinions of the IMF, the advantages provided by a trust structure makes the latter the best body through which litigation should be channelled.

Finally, in order for ICMA to duly attain its objective of creating a more orderly and efficient market and a lower cost of funding on the long-term, this study recommends the inclusion of no-action clauses within ICMA’s standard CACs to cope with the market shift towards the use of these clauses in the context of international debt issues and to increase investment safety.

VI CONCLUSION

In the absence of CACs, each sovereign bond would be a totally independent debt instrument. Its modification would require the consent of its holder and when its issuer defaults, the holder is entitled to pursue individual remedies, including lawsuits, to enforce its rights. Consequently, a financially distressed sovereign would have to negotiate with and get the consent of each individual bondholder to restructure its debt. However:

‘self-interested individuals will not act to achieve their common or group interests. In other words, even if all of the individuals in a large group are rational and self-interested, and would gain if, as a group, they acted to achieve their common interest or objective, they will still not voluntarily act to achieve that common or group interest.’

Hence, seeking the consent of each individual holder would probably result in the tyranny of a minority of holders who, by their dissent to the sovereign proposals and in the absence of a sovereign bankruptcy regime, will get paid in full while their peers bear the burden of the sovereign distress. This rigid legal structure of the bonds had to be changed to establish

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246 See generally IMF Staff Report 2015, above n 135.
247 See de León, above n 158, 24.
248 Lee Buchheit and Mitu Gulati, see above n2, 1323.
better inter-creditors coordination tools, to fight minority abuse and facilitate sovereign debt restructuring. This was, is and will remain the purpose of CACs.

The aim of this study is twofold.

The first is to illustrate and analyse the evolution pattern of CACs from the nineteenth century to date; The study made observations that draw CACs as important pillars in and throughout the sovereign debt restructuring history and demonstrated how their development contributed and contributes still to a more efficient sovereign debt workouts environment and more predictable international capital markets.

The second is to propose the next step in the path of the CACs evolution. Of course many things can be done and important suggestions can be presented to strengthen and enhance the operation of CACs: should aggregation be possible with and across bonds having different governing laws? Should the issuer have the sole right to choose between different voting procedures under the Standard Aggregated CACs? Should the latter apply and be introduced into domestic laws? How should CACs improve the process of debtor-creditor engagement to achieve a quicker sovereign debt restructuring? How to accelerate the adoption of the Standard Aggregated CACs and how to convert outstanding debt to the new CACs?

It is not possible to cover these propositions in one study and we do not pretend to do so. However, this study had focused on no-action clauses limiting the right of individual bondholder to institute proceedings as the next step in the evolutionary path of CACs and argued the importance of such inclusion. This study also recommended channelling litigation through a trustee in contrast to a fiscal agent. This study also showed that this type of clauses is now being increasingly adopted by sovereign issuers and promoted by institutions such as the IMF.

It has been said that international sovereign debt contracts ‘should be updated periodically in light of the lessons and new standards that could improve the ‘safety features’ embedded in the contracts for the benefit of both creditors and debtors’ This author concurs with this view and recommends no-action clauses provisions as the next safety feature to be embedded in future standardized CACs models.

251 Ibid.
252 Makoff and Kahn, above n 156, 6.
253 Deborah Zandstra, Andrew Yianni and Simon James, above n 5.
254 See generally Makoff and Kahn, above n 156.
255 See de León, above n 158, 24.
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