

# ODIOUS DEBT, OLD AND NEW: THE LEGAL INTELLECTUAL HISTORY OF AN IDEA\*

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## I

### INTRODUCTION

In a sense, all debts are odious; that is, to use dictionary definitions, “hateful; disgusting; offensive.”<sup>1</sup> Yet insofar as international economic law today is concerned, only a certain few debts can be considered “odious debts” in order to contest and perhaps eventually to repudiate them. In this article, the concepts of odious debt and related international legal phenomena will be examined, in both historical and contemporary context, with a view of determining the role that denomination of certain debts as odious may play in the overall process of sovereign debt rescheduling.

The article begins with a brief description of the concept of odious debt. It then proceeds to assess other fundamental doctrines of international law which relate to the ultimate determination of some debts as odious. Once this basis has been established, the article undertakes a brief historical survey of both the de facto and de jure invocation of odious debt as a rationale for renunciation of sovereign debt obligations, culminating with a quick tour of recent reconceptualizations of odious debt doctrines in connection with both Jubilee 2000 and the Iraqi debt incurred by Saddam Hussein’s regime. It concludes with a consideration of new proposals to create international institutions to deal with future odious debt claims.

## II

### ANALYSIS OF THE INTERNATIONAL LAW ISSUES: STATE SUCCESSION AND ODIOUS DEBT

At international law, a successor government is liable for the financial obligations incurred by a prior regime. Changes in the government of a state do not usually alter previously existing rights and obligations.<sup>2</sup> Thus, as a general

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\* This article has been revised to rectify a failure to properly attribute portions of section III. It is otherwise identical to that first published in *70 Law & Contemporary Problems* (August 2007).

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1. WEBSTER’S NEW UNIVERSAL UNABRIDGED DICTIONARY 1240 (2d ed. 1972).
2. *Jackson v. People’s Republic of China*, 550 F. Supp. 869, 872 (N.D. Ala. 1981).

matter, successor governments must honor the debts incurred by predecessor regimes. Many new revolutionary regimes, on the other hand, have asserted both the longevity and wide acceptance of the principle that successor governments could renounce “odious debts” contracted by predecessor regimes. Having risen to power as a revolutionary regime, such polities characterize all financial obligations of previous reactionary governments as such “odious debts” and refuse to pay.

The history and the development of the doctrines in this area—state succession—must be carefully analyzed in order to establish some benchmarks for assessing the international acceptance of this position. In considering the merits of the different claims, it also must be kept in mind that widely varying historical experience, both with international law and with foreign relations and trade, have had significant impact on the current stances not only of the United States, but also of large groupings of nations such as developed countries, on the one hand, and the developing, or third-world, countries on the other. Only a careful analysis of the present international legal doctrine that also takes into account the breadth of global culture underlying it will permit a proper understanding of the future direction of international law.

One fairly typical case, involving a claim of repudiation of sovereign debt as odious was the 1981 case, *Jackson v. People's Republic of China*.<sup>3</sup> In determining that the government of the People's Republic of China (PRC) was liable to holders of the bonds, the district court in the *Jackson* default judgment briefly summarized its analysis of the international law of state succession. Citing only a single case<sup>4</sup> decided over fifty years ago, the court announced, “It is an established principle of international law that ‘changes in the government or the internal policy of a state do not as a rule affect its position in international law.’”<sup>5</sup> Following that principle, the court simply deduced that the PRC government, as the successor to the Imperial Chinese government, was therefore the successor to the prior government's obligations and thus liable for the payments due on plaintiffs' bonds. The court summarily disposed of the issue in a single paragraph.<sup>6</sup>

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3. *Id.*

4. *Lehigh Valley R.R. Co. v. State of Russia*, 21 F.2d 396, 401 (2d Cir. 1927) (Manton, J., opinion) (quoting 1 JOHN BASSETT MOORE, DIGEST OF INTERNATIONAL LAW 249 (1906)). The quoted passage from Moore states,

Changes in the government or the internal policy of a state do not as a rule affect its position in international law. A monarchy may be transformed into a republic, or a republic into a monarchy; absolute principles may be substituted for constitutional, or the reverse; but, though the government changes, the nation remains, with rights and obligations unimpaired.

*Lehigh Valley R.R. Co.*, 21 F.2d at 401 (Manton, J., opinion).

5. *Jackson*, 550 F. Supp. at 872 (quoting MOORE, *supra* note 4, at 249).

6. *Jackson*, *supra* note 2, at 872.

### A. Theories of State Succession

In fact, there does not appear to be any universal rule of international law with regard to state succession. Although there is considerable support for the position that a successor government should be liable for the obligations incurred by its predecessors,<sup>7</sup> there is a competing minority argument that succession of one government severs it so completely from its predecessors that it has no responsibility for the acts and obligations of preceding governments.<sup>8</sup> However, several nations whose governments came to power as a result of revolutionary activity have developed a legal theory between these two extreme views of international law. This intermediary view holds that revolutionary regimes may succeed to certain obligations of their predecessors but do not have any responsibility for so-called “odious debts,” a term used to describe debts incurred in opposition to a revolution or for other oppressive purposes.<sup>9</sup>

The U.S. interpretation of international law places it clearly among the group of nations—most of them creditor countries—that upholds state succession to a predecessor’s debts, no matter what the change of government. The interpretation of revolutionary regimes, such as the PRC,<sup>10</sup> though

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7. See, e.g., ERNEST H. FEILCHENFELD, PUBLIC DEBTS AND STATE SUCCESSION 623–42 (1931); D. P. O’CONNELL, 1 STATE SUCCESSION IN MUNICIPAL AND INTERNATIONAL LAW 4–14, 369–415 (2d ed. 1967); HERBERT A. WILKINSON, THE AMERICAN DOCTRINE OF STATE SUCCESSION 71–96 (1934). See also 2 MARIORIE M. WHITEMAN, DIGEST OF INTERNATIONAL LAW 810–11 (1963) (obligation of the successor state is to respect the acquired rights of the predecessor state).

8. See, e.g., FEILCHENFELD, *supra* note 7, at 535–45; O’CONNELL, *supra* note 7, at 14–17; WILKINSON, *supra* note 7, at 71–96. See also Tinoco Case (Gr. Brit. v. Costa Rica), 1 R. Int’l Arb. Awards 369, 376–84 (1923), reprinted in 18 AM. J. INT’L L. 147 (1924) (holding that the Law of Nullities passed by the restored Costa Rican government rendered oil-grant concession granted by the predecessor government invalid; but, with respect to debt owed by the predecessor government to a British bank, the successor government ordered to assign interest in mortgage upon Tinoco estate to bank and bank to then deliver money owed to successor). See M. H. Hoeflich, *Through a Glass Darkly: Reflections Upon the History of the International Law of Public Debt in Connection with State Succession*, 1982 U. ILL. L. REV. 39, 60–65 (1982).

9. See FEILCHENFELD, *supra* note 7 at 337–42, 450–52, 701–05, 862; O’CONNELL, *supra* note 7, at 356, n. 5; WILKINSON, *supra* note 7, at 83–86. The commentators generally divide “odious debts” into two types: hostile debts and war debts. Hostile debts are those debts imposed upon a community against its will, without consent and adverse to the community’s best interests. The leading example of a hostile debt is the Cuban debt, which caused controversy between the United States and Spain in 1898. The American government vigorously took the position that the debts resulted from the actions of the Spanish government for its own colonial ambitions and that Cuba had no say in these actions. The then-prevailing American political philosophy did not acknowledge that incurring such a debt might actually be beneficial; these debts were considered repugnant. War debts are those debts used to finance aggressive campaigns against other states or against the successor state. A war debt of this type was incurred following the annexation of the Boer Republics by Great Britain in 1900. The British government refused to repay notes issued as security for loans, the proceeds of which were used to wage war. As to both kinds of debts, the theory is that such debts were raised for purposes other than the needs and interests of the state; since there was no benefit from the indebtedness incurred, the successor has no obligation to repay such debts.

10. See *Aide Memoire* [of U.S. Dep’t of State in Jackson], *Aide Memoire* of Chinese Foreign Ministry on Case of Huguang Railway Bearer Bonds, Feb. 2, 1983, in Xinhua News Agency Release, Feb. 9, 1983, U.S. Foreign Broadcast Information Service (FBIS), Daily Report: China, FBIS-CHI-83-028, Feb. 9, 1983, at B-1, reprinted in 22 INT’L LEGAL MATS. 81 (1983) [hereinafter *Aide Memoire*]. The PRC has taken note of United States’ invocation of “odious debt” rationales for refusing to honor predecessor-regime obligations in several instances. See, e.g., Richard Tien-Shi Hsu, *The Invalidity of*

borrowing some of the “odious debt” rhetoric of other countries, seems to adopt the most extreme nonsuccession theory in regard to external debts. Underlying these competing statements are certain equitable considerations that may furnish a common ground for explaining and reconciling their differences.

The principles evinced by nations maintaining that successor governments inherit the obligations of their predecessors are most often discussed under the rubric of “acquired rights.”<sup>11</sup> If one accepts the “acquired rights” analysis, international law imposes the relationship between the lender of money to sovereign borrowers (or, in this situation, the buyers of government-issued bonds) to the successors of such sovereign governments, to prevent the unjust result of extinguishing the lender’s (or buyer’s) interest in repayment because of the sovereign borrower’s disappearance.<sup>12</sup> Respect for “acquired rights” at international law has been described as “no more than a principle that change of sovereignty should not touch the interests of individuals more than is necessary.”<sup>13</sup> A further argument under the “acquired rights” analysis is that a successor government recognizing such rights retains the power to permit it to continue, alter, or cancel those rights, with appropriate provisions for compensation if it alters or cancels previously existing rights.<sup>14</sup> This analysis

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*the Default Judgment in Jackson v. People’s Republic of China*, 23 VA. J. INT’L L. 569, 575–76 (1983) (discussing Cuban and Texas debt).

11. O’CONNELL, *supra* note 7, at 237–68. Discussing the working of the theory to protect a lender’s interest in repayment where the predecessor government to which he lent has been succeeded, O’Connell writes,

What is always ‘inherited’ is the state of facts which the now extinguished legal relationship has brought about; and the equitable interest which the lender has in this factual situation is as much an ‘acquired right,’ ‘property right’ or ‘vested right’ as the interest of a titleholder in tangible property. The obligation of the successor state is to respect this interest. It is not an obligation derived from the predecessor, but one imposed *ab exterior*e by international law. It rises when the successor, through its own action in extending its sovereignty, becomes competent to destroy the titleholder’s interest. The general principle in which this obligation is embodied, and which underlies the whole problem of state succession, is the principle that acquired rights must be respected.

*Id.* at 238–39.

12. *Id.* See also WHITEMAN, *supra* note 7, at 810–11 (the obligation to honor acquired rights arises when a successor is enabled through its own action to eliminate the title holder’s interest).

13. O’CONNELL, *supra* note 7, at 266.

14. *Id.* O’Connell writes,

This does not mean that these interests may not be interfered with at all. The doctrine merely indemnifies titleholders from complete and arbitrary destruction of their interests, and secures for them an impartiality on the part of the successor State in the exercise of its discretion. There can be no general immunity from expropriating legislation. Such expropriation, however, is only justified when accompanied by a recognition of the equities involved. If the doctrine of acquired rights does not protect the titleholders from expropriation, it at least guarantees them restitution. The successor State, once it extends its sovereignty over the absorbed area, has a choice as to the course it will adopt. On the one hand it may permit acquired rights to continue in existence; on the other hand, it may legislate to alter or entirely cancel them. If it adopts the latter course it must then comply with the minimum standards set by international law, and either pay compensation or grant new titles of some equivalent value. A successor State thus stands in the same position with respect to acquired rights as any

does not extend the principles so far as to limit the successor sovereign's discretion to nationalize or to expropriate property.

The original position of countries such as the PRC regarding foreign debts upon its succession to power appears to have been one of total renunciation.<sup>15</sup> The PRC proclamation issued in 1949 left little doubt that the PRC would never feel itself bound by obligations assumed by previous Chinese governments.<sup>16</sup> The revolutionary nature of the PRC government, both in its announced policies and in its methods of acquiring power, makes this position unsurprising. Moreover, in renouncing the debts of its predecessors, the PRC was merely following the example of several other revolutionary regimes that came to power in the twentieth century.<sup>17</sup> Renunciation was also a practical and understandable course for a new government emerging from years of war and civil strife with considerable debts and little or no foreign exchange.

## B. Odious Debts

In justifying its position once the *Jackson* suit began, however, the PRC came to rely on the additional argument that the Huguang bonds were "odious debts" that the PRC was not obligated to repay.<sup>18</sup> In several leading articles in the Chinese press, various commentators<sup>19</sup> took considerable pains to explain

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other State, and the fact that the rights have come into existence under its predecessor is immaterial.

*Id.*

15. Cf. COMMON PROGRAM OF THE CHINESE PEOPLE'S POLITICAL CONSULTATIVE CONFERENCE art. 3, translated in ALBERT P. BLAUSTEIN, FUNDAMENTAL LEGAL DOCUMENTS OF COMMUNIST CHINA 36 (1962) [hereinafter *Common Program*] ("The People's Republic of China must abolish all the prerogatives of imperialist countries in China. It must confiscate bureaucratic capital and put it into the possession of the people's state."). See also JEROME A. COHEN & HUNGDAH CHIU, 1 PEOPLE'S CHINA AND INTERNATIONAL LAW 681-82 (1974).

16. *Common Program*, supra note 15. See also JEROME COHEN & HUNGDAH CHIU, PEOPLE'S CHINA AND INTERNATIONAL LAW 681-82 (1974).

17. Successor regimes that have renounced the debts of their predecessors include those in the Soviet Union, Yugoslavia, and East Germany. For a discussion of renunciation of predecessor debts see O'CONNELL, supra note 7, at 19-21.

18. See *Aide Memoire*, supra note 10, at B-2, para. 2. The Chinese analysis of "odious debts" is drawn from various sources discussed in the commentaries listed infra note 17. See also WHITEMAN, supra note 7, at 860-61.

19. See Fu Zhu, *The U.S. Court's Trial of and Judgment on "The Case of Huguang Railway Bearer Bonds" Are a Gross Violation of International Law*, RENMIN RIBAO, Feb. 25, 1983, at 7, translated in FBIS DAILY REPORT: CHINA, FBIS-CHI-83-040, Feb. 28, 1983, B-2, at B-6 [hereinafter *U.S. Court's Trial*].

From the angle of international law, the PRC, as an entity of international law, is the continuation of the old China before liberation. However, the birth of New China came after the Chinese people overthrew the rule of imperialism, feudalism and bureaucratic capitalism through protracted, hard armed struggle and won the great victory of the new democratic revolution. China has undergone radical changes in its social system to make it a new-type socialist state. The old government that oppressed and exploited the Chinese people in the past has been replaced by the new government, which represents the interests of all the people of all China. Therefore, the new Chinese government naturally disavows all unequal treaties imposed on China in the past by the imperialists and all international obligations incompatible with the new regime. This is not unprecedented in the history of international relations. For example, after the October Revolution in Russia, the Soviet Government of Workers and

how the principle of “odious debts” provided a generally acceptable rationale at international law for renouncing these types of obligations. The Huguang bonds were also analogized to the “unequal treaties”<sup>20</sup> imposed on the Qing dynasty government by a number of foreign powers, against which both the Chinese Republic and the PRC have bitterly complained.<sup>21</sup> Consistent with its steadfast argument in international fora that it has a right under international law to abrogate unilaterally “unequal treaties” concluded by predecessor Chinese governments, the PRC has more recently argued that the odious nature of the debt incurred by the Qing government to finance the Huguang railway permitted renunciation.<sup>22</sup> Although neither position has received the general international acceptance which the PRC claims, the PRC’s continued insistence on its position has probably given both positions greater currency than they might otherwise command.

The PRC also argued strongly that considerations of fairness and equity should foreclose any attempts to recover amounts lent under the scheme to finance the construction of the Huguang railway.<sup>23</sup> Arguing that rapacious foreign powers eager to carve out spheres of influence in Qing China foisted the railway project and the loans to underwrite the contracts upon a weak, corrupt

Peasants issued a decree on January 1918 abrogating all national debts. Provision No. 1 says: “All national debts borne by the previous landlord and bourgeois governments as listed in the special notice have been abolished as from 10 December 1917.” Provision No. 3 of the decree stipulates: “All external debts should be unreservedly abolished, without any exception.” (“Selected Documents of Reference for International Law,” Chinese edition, 1956, p. 80). When disavowing all external debts of the Tsarist government in 1921, (Chichilin) [qi qielin 7871 0434 2651], members of the Russian People’s Commission for Foreign Affairs, proclaimed: “People of no country should be responsible for repaying the debts imposed on them like shackles in past centuries.”

Not inheriting “bad debts” has been a well-established principle in international law. The so-called “bad debts” include debts incurred by one country borrowing from another country out of the need to suppress its own people at home or people in its colonies.

*Id.* See also Shih Chun-yu, *Idiotic U.S. Court Judgment*, TA KUNG PAO, Feb. 10, 1983, at 2, translated in FBIS DAILY REPORT: CHINA, FBIS-CHI-83-033, Feb. 16, 1983, W-9, at W-10 (citing U.S. court judgment as absurd); Lan Mingliang, *Sovereign Immunity Is an Important Principle of International Law—Commenting on the Statement Released by the U.S. State Department on the So-Called Huguang Railway Bearer Bonds*, GUANGMING RIBAO, Feb. 26, 1983, at 3, translated in FBIS DAILY REPORT: CHINA, FBIS-CHI-83-050, Mar. 14, 1983, B-3, at B-6 [hereinafter *Sovereign Immunity*]; Liu Dagon, *The Odious Nature of the Huguang Railway Loan*, RENMIN RIBAO, Sept. 13, 1983, at 7 (excerpts of an article to be published in 1983 GUOJIWENTI YANJIU, No. 4), translated in FBIS DAILY REPORT: CHINA, FBIS-CHI-83-179, Sept. 14, 1983, B-1 [hereinafter *Odious Nature*].

20. The distinction between equal and unequal originally is made by HUGO GROTIUS, 3 DE JURE BELLA AC PACIS (ON THE LAW OF WAR AND PEACE) 394 (Francis W. Kelsey trans., 1964). The similarities between “odious debts” and “unequal treaties” are explored in *U.S. Court’s Trial*, *supra* note 19, at B-6, and in Jin Shixuan & Xu Wenshu, *The 1911 Huguang Railroad Loan and Its Rejection by the Chinese People Fighting for Railroad Protection*, RENMIN RIBAO, Mar. 12, 1983, at 7 (originally published in RENMIN TIEDAO (PEOPLE’S RAILROAD), Mar. 9, 1983), translated in FBIS DAILY REPORT: CHINA, FBIS-CHI-83-052, Mar. 16, 1983, B-1 [hereinafter *Railroad Loan*]. See also *Odious Nature*, *supra* note 19, at B-4.

21. See Hungdah Chiu, *Comparison of Nationalist and Communist Chinese Views of Unequal Treaties*, in CHINA’S PRACTICE OF INTERNATIONAL LAW 239 (Jerome A. Cohen ed., 1972).

22. *U.S. Court’s Trial*, *supra* note 19, at B-7; *Sovereign Immunity*, *supra* note 19, at B-5, B-6.

23. *U.S. Court’s Trial*, *supra* note 19, at B-7; *Railroad Loan*, *supra* note 20.

government,<sup>24</sup> the PRC government appealed to history for vindication of its stance in *Jackson*.

Generally, most commentators would agree that extraordinary pressures were brought to bear on the Imperial Chinese Government by the foreign powers in the late Qing period.<sup>25</sup> Even with respect to foreign lending, a number of studies have documented the struggle of each nation's bankers to keep portions of the Chinese borrowing from that country's banks, as well as the dominance of various nations over certain railroads or sections of railway lines in China.<sup>26</sup> Nevertheless, the high degree of foreign involvement in the railway construction and lending during the late Qing period does not, in itself, prove the PRC's contention that the Huguang bonds were not just debts.<sup>27</sup>

An additional factor in the PRC's insistence that it would not honor the Huguang bonds is the history of popular opposition to foreign loans for railway construction in general, and the outcry that greeted these bonds in particular.<sup>28</sup> In the early 1900s, a fairly widespread Chinese popular movement emerged that

24. *Railroad Loan*, *supra* note 20, at B-1.

The loan was a foreign debt contracted by the Qing government on the eve of its collapse, or on 20 May 1911, with a banking syndicate of the four countries of Britain, France, Germany and the United States in the name of building the Huguang railroad, but actually was a last-ditch struggle to maintain its reactionary rule. It was also a product of an act of collusion between international imperialism and the Qing government and an intensified effort to oppress and exploit Chinese people.

*Id.* See also *Odious Nature*, *supra* note 17, at B-3, B-4.

25. O. EDMUND CLUBB, *TWENTIETH CENTURY CHINA* 39 (1978); JOHN G. REID, *THE MANCHU ABDICATION AND THE POWERS, 1908–1912* 34 (1935).

26. See, e.g., CHI-KEUNG LEUNG, *CHINA: RAILWAY PATTERNS AND NATIONAL GOALS* 26–35 (1980) (discussing the role of international politics in China's railway development and the foreign "scramble for concessions"); Joseph Cheng, *Chinese Law in Transition: The Late Ch'ing Law Reform, 1901–1911* 20–22 (1976) (unpublished Ph.D. dissertation, Brown University) (discussing Chinese attempts at self-strengthening to oppose foreign railway-building concessions). *But cf.* RALPH W. HUENEMANN, *THE DRAGON AND THE IRON HORSE* (1984) (providing an economic history of railroad construction in China from 1876 through 1937, which concludes that there are no grounds for Leninist charges of exploitation by foreign railroad companies).

27. Without further evidence, which would have to be evinced by the PRC government, it is impossible to determine whether the terms of the Huguang bonds (interest rate, discount or premium, use of proceeds) were fair. In any number of developing countries, both earlier in this century and at present, developed countries have lent their capital for use in construction projects undertaken by less-developed countries. These loans are generally acknowledged to be legal debts of the borrowing countries that must be repaid according to their terms, even when borrowers subsequently suffer financial or political difficulties. *But see Odious Nature*, *supra* note 19, at B-4–B-6 (arguing that the terms of the loan were unfair and unilaterally disadvantaged China).

28. *U.S. Court's Trial*, *supra* note 19, at B-7 ("[T]he government of New China cannot repay such debts as the bonds issued by the Qing government for the building of the Huguang railways, because recognizing and repaying this kind of debt would mean denying the ongoing revolutionary struggles waged by the Chinese people in the past 100 years or more since the Opium Wars."); *Railroad Loan*, *supra* note 20, at B-3, B-4; *Odious Nature*, *supra* note 19, at B-6.

The Huguang Railway Loan agreement severely violated China's sovereignty and the people's fundamental interests. The Chinese people started their struggle to cancel the contract and to turn down the loan as soon as planning of the loan scheme began. This mighty anti-imperialist and antifederalist revolutionary struggle was turned into an armed uprising soon after the contract was signed and became an incident that touched off the downfall of the reactionary Qing government.

*Odious Nature*, *supra* note 17, at B-6.

opposed foreign construction and control of China's railways. The movement generated discontent among the Chinese populace, a discontent that eventually burst forth in numerous uprisings against the Qing government. Ultimately, the opposition culminated in sustained attempts to topple the Qing government, climaxing in an event in the city of Wuhan in Hubei province (northern terminus of the Huguang railway), which was generally considered to have begun the 1911 revolution ending imperial dynastic rule in China.<sup>29</sup> These historic instances of opposition to the imperial government remain important milestones of the revolution in the PRC political history of today. Thus, it would be difficult, if not impossible, for the PRC government to rationalize honoring the Huguang bonds in the light of their significance in Chinese revolutionary history.<sup>30</sup> Accordingly, the PRC attempted to invoke the nationalistic opposition of the period when the Huguang bonds were issued to buttress the PRC's renunciation of them.

### C. Balancing Considerations

The appeal to concepts of fairness, however, does not necessarily support the PRC's claims. Modern notions of state succession, centered on a balancing of competing interests,<sup>31</sup> first examine where benefits have been received and where burdens have been imposed in assigning responsibility for claims such as those over the Huguang bonds. Even conceding the PRC's claims about the foreign machinations surrounding the funding of the Huguang Railway construction, the railway was nonetheless built using foreign funds raised by the bonds. Moreover, for a considerable period of time thereafter (indeed, right up to the present day), China indisputably derived benefits from the Huguang Railway.<sup>32</sup> The extent of these benefits must be evaluated before the PRC could

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29. EDWARD RHOADS, CHINA'S REPUBLICAN REVOLUTION: THE CASE OF KWANGTUNG, 1895–1913 207–10 (1975); SICHUAN PROVINCIAL ARCHIVES (SICHUAN SHENG DANG'AN GUAN), SICHUAN BAOLU YUNDONG DANG'AN XUANBIAN (1981) [Selected Documents of the Railway Protection Movement in Sichuan], XINHAI NIAN SICHUAN BAOLU YUNDONG SHILIAO HUIBIAN (1981) [Collection of Historical Materials on the Railway Protection Movement in Sichuan in 1911]. See also CLUBB, *supra* note 25, at 39; JOHN FAIRBANK ET AL., EAST ASIA: THE MODERN TRANSFORMATION 629–31 (1965).

30. *Odious Nature*, *supra* note 19, at B-7.

The acknowledgement of the Huguang Railway bonds is by no means an issue simply concerning old debts but is a fundamental problem concerning our effort to safeguard the fruit of the revolution for which the Chinese people have unremittingly fought at the cost of blood for more than 100 years. The just stand of the Chinese Government toward the Huguang Railway bonds case conforms to the will of the 1 billion Chinese people. Adhering to this stand, the Chinese Government has safeguarded the dignity of the PRC and has won the strong support of the Chinese people of all nationalities and the sympathy of Third World countries.

*Id.*

31. See, e.g., James L. Foorman & Michael E. Jehle, *Effects of State and Government Succession on Commercial Bank Loans to Foreign Sovereign Borrowers*, 1982 U. ILL. L. REV. 12–14 (1982) (brief review of modern theories of state succession). See also FEILCHENFELD, *supra* note 6, at 387–89, 546–70; O'CONNELL, *supra* note 7, at 436; WILKINSON, *supra* note 7, at 95–96.

32. See LEUNG, *supra* note 26, at 72–81; Zen Sun, *The Pattern of Railway Development in China*, 14 FAR E. Q. 161, 179–99 (1955). But see *Odious Nature*, *supra* note 19, at B-2:

deny any obligation for repayment of the Huguang bonds. In addition, the PRC's denial of liability for the Huguang bonds ignores the fact that the regime which succeeded to the Imperial Chinese Government following the Revolution of 1911 felt obliged to continue repayment of the bonds, despite their role in the revolution. It may be argued convincingly that the Republican government recognized the usefulness of the railway and its benefits to national development, notwithstanding the controversy its financing engendered.<sup>33</sup>

The burden-benefit analysis of modern notions of state succession also seems to undercut the suggestions of several observers that the government of the Republic of China, still in power on the island of Taiwan and recognized by the United States as the government of all China after 1948 until normalization of relations with the PRC, should arguably have assumed the obligation to repay the Huguang bonds. First, the Taiwan government had no use of the benefit because it no longer controlled the Huguang Railway.<sup>34</sup> All the assets of the railway remained in place on the mainland after the Republic of China government fled to Taiwan. Second, this lack of benefit outweighs the fact that the Taiwan government remained the U.S.-recognized government of China and is still the same government, using the title "Republic of China," that promised several times to remedy its defaults on the obligations at the earliest opportunity.<sup>35</sup> Whatever the government's historical responsibility was to Taiwan for honoring the Huguang bonds, its flight to Taiwan certainly diminished the obligation it had earlier assumed.

In summary, international law adopts neither the U.S. nor the PRC views concerning the ability of states to renounce the obligations of their predecessors under international law, but rather has sought in recent times to minimize the disruption of vested rights having a legitimate expectation of being honored. The PRC's formulation of a rule at international law that "odious debts" may be repudiated has not found favor outside what remains of the socialist world today and in a few other past instances. Yet even were the rule advanced by the PRC to be adopted, it is rather unlikely that the Huguang bonds are the sort of debt which should be characterized as "odious," especially when the role of the railway that they were used to finance is considered objectively in its historical

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Take, for example, the Huguang Railway bonds held in the hands of the American bearers: [a]ccording to the contract, this railway should be "finished in approximately 3 years," and the American loans should be used in building the railway from Yichang in Hubei to Kuizhou (now called Fengjie) [in Sichuan province]. However, nearly 40 years passed before liberation and there was still no railway between the two cities.

*Id.*

33. Despite Sun Yatsen's announced opposition to the railway loans from foreign powers at the time they were made, before the 1911 revolution, the necessity of using foreign capital for expansion of China's railways after the establishment of the Republic of China became obvious. See LEUNG, *supra* note 26, at 51-53.

34. The government of the Republic of China fled to Taiwan in 1949; on September 29, 1949, the PRC government took responsibility for railroads on the mainland by virtue of Article 36 of the COMMON PROGRAM OF THE CHINESE PEOPLE'S POLITICAL CONSULTATIVE CONFERENCE, translated in BLAUSTEIN, *supra* note 16, at 47-48.

35. Jackson, *supra* note 2, at 872 (also citing Plaintiffs' Exhibit 6 in Jackson).

context. On the other hand, the political imperative for such characterization is quite obvious.

### III

#### THE ODIIOUS DEBT DOCTRINE WITH RESPECT TO LENDING OF THE 1970S AND INTERNATIONAL PUBLIC POLICY<sup>36</sup>

Some experts such as Bryan Thomas trace the bulk of the debt crisis currently facing much of the developing world “to a period of intense, indiscriminate lending by private commercial banks and International Financial Institutions (IFIs) which began in the in early 1970s.”<sup>37</sup> Though Thomas notes

disagreement over the root causes of the 1970s lending frenzy . . . , commentators across the political spectrum agree that there *was* a lending frenzy, primarily on the part of private banks, which took place roughly between 1971 and 1982 (when crisis finally struck). . . . In recent years, officials with the World Bank and the International Monetary Fund (IMF) have been [surprisingly] candid about the failings of their respective institutions throughout this period.<sup>38</sup>

The gist of Thomas’s thesis is that “there is a long history of sovereign-debt crises, which to a limited extent resemble the most recent [one and which] speak[] to the need for innovation.”<sup>39</sup>

Thomas notes what he regards as a depressing but “recurring pattern”:

sovereigns borrow more than they can afford to repay, . . . consequently borrow[ing] more to service the initial debt, and before long the situation spirals into a full-blown debt crisis. Lenders and borrowers learn their lesson, for a time, but collective memory ultimately erodes, and the cycle is repeated. . . . When the stakes are high, both creditor and debtor have an interest in finding manageable solutions, or at least workable stop-gap measures. Debtors struggle to service debts, at least minimally, so that they are not shut off from further lending; creditors offer further loans so that debtors are not driven into complete bankruptcy.<sup>40</sup>

#### A. What Led to the Debt Crisis of the 1970s

As far back as the debts incurred to finance the disastrous Spanish Armada in the 1580s, there have been cycles of excessive lending which lead to debt crises, refinancing through downward spirals, and firm resolve never to sin again. During the nineteenth century, the Bank of England intervened to

36. As originally published, section III of this article borrowed several passages, without signaling proper attribution, from Bryan Thomas, *The Doctrine of Odious Debts and Lending of the Seventies: Assessing the Options* 86-106 (CISCL Working Paper: Advancing the Odious Debt Doctrine, Feb. 2002). This revision remedies these errors. James V. Feinerman

37. Bryan Thomas, *The Doctrine of Odious Debts and Lending of the Seventies: Assessing the Options* 86 (CISCL Working Paper: Advancing the Odious Debt Doctrine, Feb. 2002), available at <http://www.cisd.org/pdf/debtentire.pdf>.

38. See, e.g., P. MOSELEY, J. HARRIGAN & J. TOYE, *CONDITIONALITY AS BARGAINING PROCESS IN INTERNATIONAL BORROWING: NEGOTIATING AND STRUCTURING INTERNATIONAL DEBT TRANSACTIONS* 117-26 (Daniel D. Bradlow ed., 3d ed. 1994).

39. Thomas, *supra* note 37, at 86.

40. *Id.*

prevent famous merchant bankers from descending into bankruptcy. At the beginning of the twentieth century, the Great Depression brought another debt crisis to Latin America, which took decades to conclude.<sup>41</sup> “What distinguishes earlier lending from the lending of the 1970s, among other things,” with particular implications for the doctrine of odious debts

is . . . that loans of previous eras came in the form of bonds, supplier credits, and direct investment. In the 1970s, by contrast, loans were arranged primarily between private commercial banks and the national governments of developing countries. In assessing the viability of applying the odious debt doctrine to loans of the 1970s, this distinction is crucial. Bondholders of earlier eras were *too far removed* from the end uses of their lending for the courts to establish . . . subjective awareness of odious use (recall, subjective awareness of odious use, on the part of creditors, is a primary criterion in applying the odious debt doctrine). In the words of one commentator, “[B]anks [in the 1970s] had branches or representative offices in the debtor countries and they were thus in a position to assess first-hand the local political and economic scene. A similar presumption cannot be made about bondholders.”<sup>42</sup>

In the early 1970s, many developing countries were experiencing rapid economic growth:

Brazil’s economy, for example, grew, on average, by 11 percent annually between 1968 and 1971; in 1970, Mexico had thirty years of solid economic growth behind it (6 percent per annum, on average). There was therefore a widespread expectation that the successes of the Asian “tigers” would be replicated in these and other Latin American countries. [Obviously,] [t]hese high hopes never came to fruition. Indeed, it was obvious (to some) by the mid-1970s that the debt load of developing countries was unsustainable. As it became obvious in the late 1970s that debts loads were unsustainable, lending to developing countries promptly dried up.<sup>43</sup>

The rise of syndicated lending in the late 1960s allowed banks [—major U.S. banks: Citicorp, Chase Manhattan, Bank of America, J.P. Morgan, and Manufacturers Hanover—] to negotiate much larger loans; . . . the [lead] bank in a lending syndicate collected an array of fees from other participants, creating an incentive for what has since been called “loan pushing.”

In the parlance of a UN study, the major “leader banks” (listed above) aggressively marketed loans to developing countries, particularly Latin American states, throughout the 1970s, prompting “challenger” banks of Europe, Canada, and Japan to enter the market. Smaller banks, dubbed “followers,” eventually got in on the action . . .<sup>44</sup>

41. ROSS P. BUCKLEY, *EMERGING MARKETS DEBT: AN ANALYSIS OF THE SECONDARY MARKET* 8 (1999).

42. Thomas, *supra* note 37, at 87 (quoting Lee Buchheit, *The New Latin American Debt Regime—Cross-Border Lending: What’s Different This Time?*, 16 NW. J. INT’L L. & BUS. 44, 48 (1995)).

43. Thomas, *supra* note 37, at 88 (citing BUCKLEY, *supra* note 40, at 16, 9). For the growth of Brazilian and Mexican economies in this period, see generally William Easterly et al., *Good Policy or Good Luck? Country Growth Performance and Temporary Shocks* (NBER Working Paper No. W4474, Sept. 1993), available at SSRN: <http://ssrn.com/abstract=260539>.

44. Thomas, *supra* note 37, at 89 (citing ECONOMIC COMMISSION FOR LATIN AMERICA AND THE CARIBBEAN, *TRANSNATIONAL BANK BEHAVIOUR AND THE INTERNATIONAL DEBT CRISIS*, ESTUDIOS E INFORMES DE LA CEPAL SERIES, No. 76 (LC/G.1553/Rev.1-P, Santiago, Chile, 1989) (quoted in BUCKLEY, *supra* note 41, at 9); WILLIAM A. DARITY & BOBBIE L. HORN, *THE LOAN PUSHERS: THE ROLE OF COMMERCIAL BANKS IN THE INTERNATIONAL DEBT CRISIS* 65 (1988).

The debts of the 1970s were incurred as an indirect result of the oil crises of that decade. Higher oil prices put cash in the hands of wealthy Organization of the Petroleum Exporting Countries (OPEC) nations, who in turn deposited these funds in commercial bank accounts. Commercial banks from global money centers were “eager” to make loans with this money, but due to the recession induced by the oil crises, found few interested borrowers in the developed world.<sup>45</sup> They “turned to the developing world in search of borrowers, [who] seemed a reasonable credit risk” due to the steady rise in prices of raw materials—their main exports.<sup>46</sup> The commodity price boom of the early 1970s is seen by some as an even bigger reason for the explosive growth in bank lending than the surge in oil prices.<sup>47</sup> Moreover, many developing countries were experiencing rapid economic growth during the 1970s, especially Brazil and Mexico, Latin America’s two largest countries. Many expected the region to copy the experience of the Asian “tigers,” hopes which were not subsequently realized.

Recession in the developed world, the soaring value of the U.S. dollar relative to Latin American currencies, and plunging prices of many commodities exported by developing countries in the 1980 brought this period to a calamitous close.<sup>48</sup> Although bankers of that era may have been careless or profligate in their loan-making, such carelessness and profligacy on the part of creditors is not grounds for debt cancellation under the doctrine of odious debts. That doctrine requires that creditors have been subjectively aware of the odious purpose of the loan.<sup>49</sup>

As Thomas notes, economists Darity and Horn reach the conclusion that, even if bad loans were good business for major banks in the 1970s, this would not necessarily make these loans “odious.”

They write . . . [.] “Ironically . . . loan pushing is most consistent, within the context of the rational expectations hypothesis, with [the view that] bankers knowingly made bad foreign loans.” Darity and Horn claim, among other things[,] that banks received substantial up-front fees for arranging loans to developing countries; that major banks relied, with good reason, upon IFIs (such as the IMF) as de facto guarantors of their loans to developing countries; [and] that due to economies of scale, small banks were put at greater risk than large banks by their involvement in lending to developing countries, so that at the end of the day, debt crises may actually have further strengthened the market dominance of the major banks.<sup>50</sup>

Walter Wriston, then Chairman of Citicorp, asserted, “Countries don’t go out of business. . . . The infrastructure doesn’t go away, the productivity of the people doesn’t go away, the natural resources don’t go away. And so their

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45. Thomas, *supra* note 37, at 87–88 (citing Alberto. G. Santos, Note, *Beyond Baker and Brady: Deeper Debt Reduction for Latin American Sovereign Debtors*, 66 N.Y.U. L. REV. 66, 72 (1991)).

46. *Id.*

47. *See id.*

48. DARITY & HORN, *supra* note 44, 15–39 (1988).

49. ALEXANDER N. SACK, *LES EFFETS DES TRANSFORMATIONS DES ÉTATS SUR LEURS DETTES PUBLIQUES ET AUTRES OBLIGATIONS FINANCIERES* 157 (1927).

50. Thomas, *supra* note 37, at 90 (quoting DARITY & HORN, *supra* note 44, at 138).

assets always exceed their liabilities, which is the technical reason for bankruptcy. And that's very different from a company."<sup>51</sup> With such a world view, it was no wonder that loan officers were eager to make these large loans and that senior bank officials profited from the interest rates, upfront fees, and other charges received from Latin American borrowers.

There is no simple explanation of the lending frenzy that took place in the 1970s. The behavior of major lenders throughout this period admits of several explanations. A mixture of short-sightedness and greed, combined with layers of principal-agent problems combined to produce [this] latest developing country debt crisis. Note that these explanations are, for the most part, compatible with the supposition that both local bankers and senior bank officers knew what they were getting involved in [as the 1970s loan crisis fomented]. Local officers went ahead with risky loans because they were rewarded for bringing in contracts and seldom punished for defaults. Senior bank officers went ahead with risky loans because high interest loans, accompanied by substantial front-payments, are impressive on the current balance sheet, which in turn drives up the value of a bank's shares (in the short run, at least).<sup>52</sup>

To be fair, from the perspective of Western banks, many developing countries were good loan prospects in the 1970s. Most produced raw materials, foodstuffs, or manufactured goods that were in demand, and at record high prices. Their growth rates looked even better than those for industrial countries: from 1960 to 1980, Latin America's economic growth rate was nearly twice the U.S. rate. Developing countries thought it made sense for them to borrow as long as interest rates were low and inflation was high—the loans fueled their economies at little cost. With high inflation through most of that decade, by the time the dollars had to be repaid, their real value had decreased. Meanwhile, the borrowers could invest the money in economic development. And, most importantly (at least until the loans became due), it worked. Between 1973 and 1980, the economies of oil-importing developing countries grew an average of 4.6%, compared with 2.5% for the industrial world.<sup>53</sup>

Yet, "[b]y 1982, when the debt crisis came to a head, total exposure of U.S. banks to developing countries accounted for 287.7% of the banks' total capital."<sup>54</sup> Debt repudiation or a collapse by even a single country could have jeopardized the survival of not only many money-center banks, but even the financial system as a whole. Fortunately, borrowers did not unilaterally repudiate their debts. The main reason may be that they did not want to burn any bridges with international lenders. They may also have feared that if they invoked the doctrine of odious debts, it would scare away future lenders. As the *Economist* noted in contemplating South Africa's potential use of the doctrine, "[South Africa's] credit rating would be wrecked as it came to be lumped with other deadbeats. Foreign investors would be deterred, and South Africa would

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51. INTERNATIONAL MONETARY FUND, MONEY MATTERS: AN IMF EXHIBIT—THE IMPORTANCE OF GLOBAL COOPERATION: DEBT AND TRANSITION 1981–1989, [http://www.imf.org/external/np/exr/center/mm/eng/mm\\_dt\\_01.htm](http://www.imf.org/external/np/exr/center/mm/eng/mm_dt_01.htm) (last visited June 3, 2009).

52. Thomas, *supra* note 37, at 91.

53. Jay Palmer, *The Debt-Bomb Threat*, TIME, Jan. 10, 1983, at 1.

54. Thomas, *supra* note 37, at 92 (citing BUCKLEY, *supra* note 41, at 25); see also Jeffrey Sachs, *Making the Brady Plan Work*, FOREIGN AFF., Summer 1989, at 89.

have to pay more for future borrowings.”<sup>55</sup> “Furthermore, syndicated lending, by its legal nature, tends to discourage lenders from suing on their debt. Syndicated loans invariably contain contractual provisions [that] require . . . any recovery made by any single creditor be shared with all other creditors.”<sup>56</sup>

The perils for countries choosing the course of unilateral debt repudiation is illustrated by the difficulties encountered by the Peruvian economy, following President Alan Garcia’s decision, in 1984, to repudiate a substantial portion of that country’s debt. The jury, however, remains out as to whether Peru’s subsequent economic problems resulted from this act (and foreign investors’ reactions) or from other causes. As Lothian writes,

Peru did not experience a sudden shut-down of foreign loans and equity capital in response to the infamous ten percent debt moratorium. Furthermore, Peru’s trade and short-term credit were not measurably affected by international hostility toward the country. Indeed, export credits increased annually each year from 1983–1988. Shortfalls in the flow of import credit could be financed, at least temporarily, from increased reserves brought about by reduced remittances on external debt.<sup>57</sup>

Peru experienced serious economic difficulties in the years following, but disaster struck the Peruvian economy due to a combination of price controls and a radical program of government spending. In the end, Garcia had to return—hat in hand—to the IMF, “where he agreed to repay old debts and submit Peru to an austerity program.”<sup>58</sup> These problems were homegrown, however, and not the result of Peru’s repudiation of its foreign debt or of retribution by foreign investors. More significantly, Peru’s unilateral repudiation was not a cancellation of debt pursuant to the doctrine of odious debts. Peru did not claim its debts were odious, but rather unaffordable.

Obviously, the hope of those who considered invoking the doctrine of odious debts in the 1970s and 1980s was that it would encourage lenders to consider various factors before making sovereign loans, with the threat that future “odious lending” might result in such debts being dishonored. Thus, attempts to articulate a modern doctrine was intended to have the positive long-term effect of discouraging lenders from participating in odious debts. But lenders are not cavalier in making loans to sovereign debtors. Major loan agreements must first be approved by lawyers on all sides, beginning with a due-diligence investigation on the part of the lenders’ counsel. These agreements also “require a . . . written ‘opinion of counsel’—both from the lender and the borrower’s counsel, and, in the case of foreign borrowers, an

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55. *Unforgivable: South Africa’s Apartheid Debts*, ECONOMIST, Apr. 24, 1999, quoted in Thomas, *supra* note 37, at 92–93.

56. Thomas, *supra* note 37, at 92 (citing R. MacMillan, *The New Latin American Debt Regime: Towards a Sovereign Debt Work-out System*, 16 J. INTL. L. BUS. 57, at 72); see also Keith Clark & Martin Hughes, *Approaches to the Restructuring of Sovereign Debt*, in MICHAEL GRUSON & RALPH REISNER, *SOVEREIGN LENDING: MANAGING LEGAL RISK* 131, 136–37 (1984).

57. Tamara Lothian, *The Criticism of the Third-World Debt and the Revision of Legal Doctrine*, 13 WIS. INT’L L.J. 421, 435 (1995), quoted in Thomas, *supra* note 37, at 93.

58. Thomas, *supra* note 37, at 93.

independent foreign counsel, of the bank's choosing, before the loan is advanced."<sup>59</sup>

## B. Difficulties in Applying the Doctrine of Odious Debts to Debts Incurred in the 1970s

As commercial banks exposed themselves to great risk by over-lending to developing countries, their overexposure "created, in the early 1980s, a threat to the stability of the entire system of international finance. . . . [A]ttempts to foreclose on this debt [c]ould [have] . . . spell[ed] disaster[] by triggering widespread defaults. [So] [c]ommercial banks were coaxed, in part by the IMF and in part by the U.S. government, in the case of US banks, into participating in efforts to 'restructure' these debts. . . ." <sup>60</sup> When debtor countries, such as Peru, voluntarily participate in IMF renegotiation of their debts, they appear to acknowledge that these debts were legitimate; as a consequence, they may subsequently be estopped from arguing that the debts were odious. The Latin American debts of the 1970s (like most later debt) were restructured by the scheme which became known as the Brady Plan, "rely[ing] on a blend of . . . partial debt forgiveness, exten[ded] . . . payment schedules, the conversion of private loans into long-maturity bonds, [and debt-for-equity swaps]."<sup>61</sup>

A large portion of the 1970s debts of Latin American countries would probably be considered non-odious. For example, borrowed capital spent on schools, hospitals, and other beneficial projects (or at least not squirreled away in Swiss bank accounts for private use) would not be considered odious. Restructuring plans lump together all loans, legitimate and illegitimate. Furthermore, many of these debts are then converted into bonds, ultimately consolidating legitimate and odious debts. Thus, it may be almost impossible to separate odious from non-odious debts. So, despite the view of Noam Chomsky and some others,<sup>62</sup> that all developing-country debt is odious, the combination

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59. Thomas, *supra* note 37, at 94 (citing Michael Gruson, *Legal Aspects of International Lending: Basic Concepts of a Loan Agreement*, in INTERNATIONAL BORROWING: NEGOTIATING AND STRUCTURING INTERNATIONAL DEBT TRANSACTIONS 299–300 (Daniel D. Bradlow ed., 2d ed. 1986)).

60. Thomas, *supra* note 37, at 95. "The U.S. government's interest in restructuring LDC debt was motivated in part by a concern that crippling LDC debts was bad for domestic exporters. . . . Lothian writes[.] . . . "Toward the end of the 1980s, the positions of governments and commercial banks collided. In the minds of international bureaucrats and policy-makers, two considerations were paramount: first, the prospect of deepening recession and policy instability in debtor countries; second, the related effects on international economic activity." *Id.* at 95, n.46, quoting Lothian, *supra* note 57, at 433.

61. *Id.* at 96, (citing Theodore Allegaert, *Recalcitrant Creditors Against Debtor Nations, or How to Play Darts*, 6 MINN. J. GLOBAL TRADE 429, 436 (1997)).

62. David Barsamian, *Talking 'Anarchy' With Noam Chomsky*, THE NATION, Apr. 24, 2000, at 29 available at <http://www.thenation.com/doc/20000424/chomsky> ("Debt is not valid if it's essentially imposed by force. The Third World debt is odious debt. That's even been recognized by the US representative at the IMF, Karen Lissaker, an international economist, who pointed out a couple of years ago that if we were to apply the principles of odious debt, most of the Third World debt would simply disappear.") (quoting Noam Chomsky).

of non-odious and possibly odious debt virtually guarantees that they all will be repaid, albeit with negotiated reductions.

The IMF played an important role in overseeing debt-restructuring plans in the mid-1980s through the mechanism of “structural adjustment plans.” From the early 1980s on, the IMF took a lead role in supervising restructuring plans, offering loans to developing countries so they could meet short-term balance-of-payment needs, and imposing drastic structural adjustment programs on developing countries to assure creditors. The IMF oversaw these plans, insuring that debtor nations got their fiscal houses in order and were positioned to repay their debts.<sup>63</sup>

Although Thomas’s analysis begins “by arguing that 1970s commercial bank lending to developing countries was in a sense *uniquely* amenable to cancellation under the doctrine of odious debts[] [because] those lenders, in most cases, had more information at their disposal about the end uses of their loans than did bondholders of previous eras,”<sup>64</sup> he ends by acknowledging that odious debt doctrine contributed little to the solution of the debt repayment crisis in Latin America of the 1970s. Perhaps the biggest difficulty in applying the doctrine of odious debt during that era was establishing creditors’ subjective awareness of “odiousness.” In Thomas’s view, “[the] restructuring plans had the effect of rolling odious debts together with non-odious debts, and subsequent trading on secondary markets immensely complicated the task of sorting them out again.”<sup>65</sup>

To the extent that IFIs played a part in creating the 1970s debt crisis, developing countries—“in their efforts to have debts cancelled under the doctrine of odious debts”—may have been “required to demonstrate that IFIs [undertook] loan agreements despite subjective awareness, on the part of their agents, that the loans were likely to be used for corrupt or tyrannical purposes. . . . [There is] considerable evidence to suggest that agents of these IFIs have indeed turned a blind eye to corruption, and as a result may have contracted odious debts.”<sup>66</sup>

World Bank lending was in many important ways unlike the *laissez faire* policies of commercial banks in the 1970s. With World Bank loans, projects were monitored through to completion. But this does not result in the conclusion that some International Bank for Reconstruction and Development (IBRD) and International Debt Association (IDA) loans of the 1970s were in part odious. In recent years, the World Bank has been surprisingly candid about its failings throughout this period, effectively confessing to willful blindness in

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63. INTERNATIONAL BORROWING: NEGOTIATING AND STRUCTURING INTERNATIONAL DEBT TRANSACTIONS 147–230 (Daniel D. Bradlow ed., 3d ed. 1994).

64. Thomas, *supra* note 37, at 99.

65. *Id.* at 100.

66. *Id.*, citing Ana Isabel Eiras, *The Senate’s Blank Check to International Financial Institutions*, HERITAGE FOUND. REPS. No. 1928, Apr. 17, 2006, at 3–4.

the face of corruption on the part of developing country borrowers.<sup>67</sup> “To ‘deal with the cancer of corruption,’ the World Bank created an Anti-Corruption Task Force charged with the task of revising World Bank protocol to combat corruption.”<sup>68</sup>

. . . World Bank loans . . . might offer some of the best test cases for innovative uses of the doctrine of odious debt. First, the extensive involvement of World Bank loan officers throughout projects will make subjective awareness . . . relatively easy to establish. Second[], recent statements by World Bank officials amount, essentially, to confessions of the prior involvement of these organizations in odious lending. Third, World Bank debts have not been sold on secondary markets, nor have they been restructured in the way that private commercial debt has been. . . . And finally, World Bank loan contracts, as explained above, are subject to arbitration tribunals. [This forum] may be more willing to entertain a principle of international law such as the doctrine of odious debts.”<sup>69</sup>

IMF loans, on the other hand, will not likely qualify for cancellation under the doctrine of odious debt.

[T]he IMF always imposes conditions upon its loans, and corrupt governments of the 1970s preferred to contract unconditional loans from private creditors. . . . Furthermore, the IMF has a purely macroeconomic mandate: its role is not to fund projects, or even to gather information on the political economic activities of its members. . . .<sup>70</sup> [M]uch of the developing-country debt held by the IMF is from the period of restructuring that came *after* the 1970s debt crisis; . . . it seems untenable to suppose that loans intended . . . to avert default and aid in balance-of-payment problems are *odious*.<sup>71</sup>

#### IV

### ODIOUS RULERS, ODIOUS DEBTS— ODIOUS DEBTS IN THE 1990S AND BEYOND

In an article in the *Atlantic Monthly*,<sup>72</sup> Joseph Stiglitz noted,

At the end of World War I, John Maynard Keynes, later to become the founder of modern macroeconomics, returned from the Versailles Treaty negotiations

67. Former World Bank staff member James Wesberry wrote, “From the end of World War II to almost the end of this century, IFIs maintained a ‘three-monkey policy’ toward corruption—they did not see it, they did not hear of it, and they never, never spoke of it—except perhaps in hushed words like ‘rent-seeking.’” James Wesberry, *International Financial Institutions Face the Corruption Eruption: If the IFIs Put Their Muscle and Money Where Their Mouth Is, the Corruption Eruption May Be Capped*, 18 NW. J. INTL. L. & BUS. 498, 499 (1998), *quoted in* Thomas, *supra* note 37, at 102.

68. Thomas, *supra* note 37, at 102 (citing J. Wesberry, *supra* note 67, at 499 (quoting President of the World Bank James Wolfensohn)); *see also* John Brademas & Fritz Heimann, *Tackling International Corruption: No Longer Taboo*, FOREIGN AFF., Sept.–Oct. 1998, at 17.

69. Thomas, *supra* note 37, at 104; *see also* SEAMUS O’CLEIREACAIN, THIRD WORLD DEBT AND INTERNATIONAL PUBLIC POLICY 109 (1990).

70. “The IMF’s Managing Director, Michael Camdessus, explained in 1998 that ‘[the IMF] has a macroeconomic mission, and our mandate is restricted to those specific instances of corruption that may have a significant—some would say demonstrable—macroeconomic impact.’” Thomas, *supra* note 37, at 104, n.79, (quoting Wesberry, *supra* note 67, at 517).

71. *Id.* at 104.

72. Joseph Stiglitz, *Odious Rules, Odious Debts*, ATLANTIC MONTHLY, Nov. 2003, at 39.

disappointed by the outcome and wrote a forceful little book, *The Economic Consequences of the Peace*. Its message was simple: the burden of reparations imposed on Germany would lead to economic crisis and social and political turmoil—and the result would not be good for Europe. Keynes turned out to be right. Today, after a decade of isolation and a devastating war, Iraq faces the daunting task of reconstructing its economy while moving from a form of ersatz socialism to market capitalism.

Stiglitz went on to note that the problem for Iraq today is debt—totaling anywhere from \$60 billion to the hundreds of billions—including reparations imposed on the country after the 1991 Gulf War, earlier debts from ammunition purchases, and obligations assumed under contracts signed during Saddam Hussein's regime. Once the oil starts to flow again, much of the revenue generated would go directly into the hands of international creditors, to the detriment of reconstruction efforts. Stiglitz argues that the country needs a respite from what others have called its “odious debts”—debts incurred by a regime without political legitimacy, from creditors who should have known better, with the monies often spent to oppress the very people who are then asked to repay the debts. As he notes with a jabbing sense of irony, “Most of Iraq's current debt was incurred by a ruthless and corrupt government long recognized as such—although complicating the matter is the fact that the Iraqi regime appears to have received some support from the United States under Ronald Reagan.”<sup>73</sup>

Yet Stiglitz noted that international agreement on the matter of debt relief would be no easier to come by than on the need to invade Iraq. And as he went on to observe, Iraq is not the only country needing debt forgiveness. In the queue are the Congolese, who would otherwise be forced to repay loans made to Mobutu that went to his Swiss bank accounts; Ethiopia, whose people would have to repay the loans made to the Mengistu “Red Terror” regime; Chileans still paying off debts incurred during the Pinochet years; South Africans with debts incurred under apartheid; and Argentines who can ill afford repayment of the money that financed the “dirty war” in their country from 1976 to 1983.<sup>74</sup>

The problem, as Stiglitz readily noted, is basically one of legal infrastructure:

Regrettably, we have no rule of law at the international level for the restructuring of government debts. In the past, Western governments had an easy way of dealing with countries that didn't meet their financial obligations: they invaded them. Today we live in what we hope is a more civilized world: we no longer openly condone armed attacks by one country on another for a failure to pay up. At the level of personal debt we've made progress, by instituting bankruptcy laws to replace debtors' prisons, portrayed so graphically in the work of Charles Dickens. And yet to date we have no parallel set of laws governing the restructuring and relief of international debt. Two years ago the International Monetary Fund at last recognized that this is a major problem and proposed a set of guiding principles. Achieving international consensus on these principles would have been difficult (the IMF was insisting, problematically, that it serve as the bankruptcy judge, or play some other central role in the bankruptcy process, despite the fact that it is one of the international community's major

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73. *Id.*

74. *Id.* at 42.

creditors), but the United States pronounced the initiative unnecessary, effectively blocking it altogether.<sup>75</sup>

Stiglitz also remarked upon the “heads we win, tails you lose” nature of United States moves for debt forgiveness and repayment. When other countries are the creditors, we counsel debt forgiveness; when our own money is at stake, we fall back on arguments for the sanctity of contract, regardless of the political circumstances. When Indonesia’s Suharto was overthrown in 1998, the Clinton Administration was adamant that Indonesia honor the contracts the U.S. government had encouraged the country to enter into.<sup>76</sup> When India threatened to abrogate energy contracts with the infamous Enron corporation (which forced it to pay outrageous prices for electricity), top officials in the Bush Administration insisted that those contracts be honored.

Looking back on the experience of the 1970s and 1980s, Stiglitz drew some significant conclusions with implications for the current Iraqi debt:

We must now recognize that debt forgiveness and debt restructuring make as much sense for governments—benefiting debtors and creditors alike—as they do for companies and individuals. Absolutely nobody gained from the over-hang of debt in Latin America in the 1980s, a decade during which growth in the region stalled and poverty increased enormously. Creditors certainly didn’t get their money back, and it was only with the implementation of the long-delayed Brady plan of debt restructuring, set in motion by U.S. Treasury Secretary Nicholas F. Brady in 1989, that growth resumed.<sup>77</sup>

Others have echoed Stiglitz’s concerns. In an article in the *Financial Times*, Harold James noted that the current situation in Iraq eerily recalls the circumstances following the Allied victory after the first World War. Most importantly, the idealism of Woodrow Wilson and the new peaceful world order he sought to install failed because

[t]he second threat to Wilsonianism arose out of the financial legacy of the first world war. A debate about the distribution of war debts and reparations paralysed the international financial system and eventually contributed significantly to the financial meltdown of the Great Depression. Reparations looked like an impossible burden, in which a moral and political claim threatened the ability of the debtors—especially Germany—to service normal public and commercial debt.<sup>78</sup>

James argued that it would be a mistake to apply what he terms “financial Wilsonianism”; introducing high-risk premiums and making international lending significantly more precarious would not insure the end of odious debt. Rather, he suggests that—as was the case with the reparations and war debts in the 1920s, which also had a basis in morality—Wilsonianism applied to the debt of dictators would produce new uncertainties and a new threat to the entire international financial system.<sup>79</sup> So what was to be done?

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75. *Id.*

76. *Id.*

77. *Id.* at 45.

78. Harold James, *The Danger of Being Too Forgiving*, FIN. TIMES, May 1, 2003, at 19.

79. *Id.*

Ultimately, as least for the Iraqi debt incurred by Saddam Hussein, the nineteen member nations of the Paris Club<sup>80</sup> agreed to forgive eighty percent of Iraq's debt. The plan reduced Iraq's total debt owed to the member nations to \$7.8 billion, from the original \$38.9 billion, over a period of four years.<sup>81</sup> The three-phase plan approved by the creditors called for an immediate cancellation of thirty percent of Iraq's current debt, which was to be followed by another thirty percent in 2005 upon approval of an economic program for the nation by the International Monetary Fund, and an additional twenty percent in 2008 after an evaluation of the effectiveness of the program.<sup>82</sup> Adel Abdul Mahdi, Iraq's Finance Minister, said that the deal was "historic."<sup>83</sup> He also expressed optimism that other creditor nations, including neighbors in the Middle East as well as several Eastern European nations, would follow the West's lead in forgiving Iraqi debt.<sup>84</sup> For purposes of this arrangement, however, Iraq's non-odious and possibly odious debts were lumped together; no accommodation was made in the forgiven portion to separate the types of debt.

## V

### JUBILEE 2000 PROPOSAL

The Jubilee 2000<sup>85</sup> Charter proposed that due to the overwhelming need for remission of the backlog of unpayable debts owed by highly indebted poor countries, there should be a complete forgiveness of the debts owed by those countries. Debt remission would have related to commercial, government, and IMF–World Bank debts, and debt reduction would have comprehensively included all three forms of debt. In the view of the proponents of Jubilee 2000,

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80. The Paris Club is an informal group of financial officials from nineteen of the world's richest countries, which provides financial services such as debt restructuring, debt relief, and debt cancellation to indebted countries and their creditors. Debtors are often recommended by the IMF after alternative solutions have failed. It meets every six weeks at the French Ministry of the Economy, Finance, and Industry in Paris. It is chaired by a senior official of the French Treasury. The club grew out of crisis talks held in Paris in 1956 between the nation of Argentina and its various creditors. Its principles and procedures were codified at the end of the 1970s.

81. Paul Carrell & Glenn Somerville, *Paris Club Drops 80 Pct of Iraq Debt it Owed*, REUTERS, Nov. 21, 2004.

82. See Press Release, Paris Club, Iraq: The Paris Club And The Republic Of Iraq Agree On Debt Relief (Nov. 21, 2004), available at <http://www.clubdeparis.org/sections/services/communiqués/irak6017/switchLanguage/en> (last visited Sept. 5, 2007).

83. John Leicester, *Group Agrees to Reduce Iraqi Debt*, WASH. POST, Nov. 22, 2004, at A14.

84. See the Paris Club's website for full details of the Iraqi debt deal and its current status at <http://www.clubdeparis.org/sections/traitements/irak-20041121/viewLanguage/en> (last visited Oct. 25, 2007).

85. Jubilee 2000 was an international coalition movement in over forty countries calling for cancellation of unpayable third world debt by the year 2000. This movement coincided with the Great Jubilee, the celebration of the year 2000 in Christian churches.

In the Jubilee Year, as quoted in the Old Testament, those enslaved because of debts are freed, lands lost because of debt are returned, and a community separated by economic inequality is restored. "Consecrate the fiftieth year and proclaim liberty throughout the land to all its inhabitants. It shall be a jubilee for you; each one of you is to return to his family property and each to his own clan." *Leviticus* 25:10 (New International Version).

creditors as well as debtors must accept responsibility for these high levels of indebtedness.

The Jubilee 2000 Charter contained the following provisions:

1. There is an overwhelming need for remission of the backlog of unpayable debts owed by highly indebted poor countries. Debt remission should relate to commercial, government, and IMF–World Bank debts and debt reduction should comprehensively include all three forms of debt.
2. Creditors as well as debtors must accept responsibility for these high levels of indebtedness.
3. The remission should be a one-off, unrepeatable act, tied to the celebration of the new millennium. It would set no precedents for future loans.
4. The precise details of remission should be worked out in consultation with both creditors and debtors for each debtor country.
5. These details should be agreed by arbitrators nominated in equal numbers by both creditor and debtor, under the aegis of the United Nations.
6. Their deliberations should be transparent and well-publicized, taking into account for each debtor country, that country's probity, economic management, social policies and human rights record.
7. Funds available after the remission of debt should be channeled into policies which benefit the poor, in line with UNICEF's recommendations for investment in social development.
8. Low income countries—with an annual income per person of less than U.S. \$700—should receive full remission of unpayable debt.
9. Higher income countries—with an annual income per person between U.S. \$700 and U.S. \$2000—should receive partial remission.<sup>86</sup>

The remission proposed was to be a one-off, unrepeatable act, tied to the celebration of the new millennium. It would have set no precedents for future loans. Beyond the general principle of debt forgiveness, the precise details of remission were to be worked on a country-by-country basis for debtor nations in consultation with both creditors and debtors. The details would have to have been agreed jointly by arbitrators nominated by both creditors and debtors, with United Nations supervision. The process was also supposed to be transparent and public, requiring debtor countries to address anticorruption, sound economic management, and other social policies, including the debtor nations' overall human rights practices.

In keeping with the general spirit of the Jubilee 2000 proposal, funds available after the remission of debt were to be channeled into policies which would have benefited the poor, in line with UNICEF recommendations for

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86. Jubilee 2000, Jubilee 2000 Charter, <http://gbgm-umc.org/umw/jubilee.html> (last visited Sept, 16, 2007).

investment in social development. The remission was also expected to be related to the longer-term economic prospects of the nations whose debt would be forgiven. Low-income countries—those with an annual income per person of less than US \$700—were to receive full remission of unpayable debt. Higher-income countries—those with an annual income per person between US \$700 and US \$2000—were to receive only partial remission. “The Jubilee 2000 Charter [was] offered as a model for a workable and acceptable solution to the problem of poor country debt, emanating from a global, grass roots movement. It [was hoped to] create a new, disciplined beginning for financial relations between North and South, as well as a fresh start for millions of the world’s poor.”<sup>87</sup>

In the United States, the Jubilee USA Network began as Jubilee 2000/USA in 1997, when a diverse gathering of people and organizations came together in response to the international call for Jubilee debt cancellation. Eventually, over sixty organizations—including labor, churches, religious communities and institutions, AIDS activists, trade campaigners, and over 9,000 individuals—became active members of the Jubilee USA Network. The advocates of this movement sought to create a strong, diverse network dedicated to working for a world free of debt for billions of people. In the view of its founders, international debt had become a new form of slavery. In their view this “debt slavery” also meant that hundreds of millions of the world’s poorest people had to work harder and harder in a futile effort to keep up with the interest payments on debts owed to rich countries including the U.S. and international financial institutions such as the IMF and the World Bank.

Partly in response to these efforts, the Clinton Administration took note of the indebtedness of the poorest nations and sought to relieve some of their burdens. Among President Clinton’s final acts as president was securing Congressional approval for a \$435 million component within the foreign-aid bill of October 2000, to fulfill a pledge the United States originally made in 1996 at the Group of Seven (G-7) summit. At that time, the world’s seven richest governments agreed to finance a debt-relief plan for forty-one of the poorest third-world nations.<sup>88</sup>

This plan—formally called the Debt-Relief Initiative for Heavily Indebted Poor Countries (HIPC) and commonly referred to as the HIPC initiative—was announced by the G-7 countries in a predictable bout of self-congratulation and publicity. Yet, the plan’s serious shortcomings and the strings attached rendered it subject to almost immediate criticism by the most significant advocates of third-world debt relief.<sup>89</sup> Many of them argued that most third-world debt was incurred by corrupt, unaccountable regimes; moreover, although the bulk of the loans were officially targeted toward large, wasteful infrastructure projects, the

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87. *Id.*

88. Rick Rowden, *A World of Debt*, AM. PROSPECT, July 2, 2001, at 29.

89. *Id.*

money more often was siphoned into private Swiss bank accounts of the top one or two hundred people surrounding the regime leaders. The lion's share of the third world's present debt represents not the principal, but rather the accrued interest on the original loans or the refinancing of them.

By the turn of the millennium, third-world debt had come to be administered by the IMF and the World Bank, seen as controlled by the G-7 governments. Under policies begun during the Reagan Administration and supported by Britain's Margaret Thatcher, new economic thinking then-prevailing turned these institutions into the "micromanagers" of dozens of third-world economies. Chief among their economic prescriptions was the reduction of the role of the state and an increasing role for private international investment in these countries' economic development.

Since this shift in the early 1980s, the IMF and the World Bank have based new loan-making on nations' compliance with "structural-adjustment programs"—economic reform policies with a pronounced free-market bias. Only then will the IMF and World Bank authorize the release of additional bilateral and multilateral loans. Since nearly all private foreign investment goes to a small handful of emerging market economies—in recent years China has become the largest recipient of foreign direct investment in the world, surpassing even the United States—most poor nations depend entirely on bilateral or multilateral loans and foreign aid simply to service the interest payments on decades of previous debt. Yet these same poor nations must assure the IFIs that they are implementing the economic reforms at a satisfactory pace in order to have each "tranche," or portion of the loan, released for their use.<sup>90</sup>

As an international insolvency framework, the Jubilee framework sought to involve ordinary citizens in the resolution of international debt crises. The hope of its proponents was that this debt relief would be the first vital step towards democratizing international capital markets and the global economy as a whole. In their view, the deregulation of capital markets, from the late 1970s onwards, led them to become detached from democratic institutions in both creditor and debtor nation states. The insolvency framework they sought to introduce would have regulated and disciplined the flows of international capital through lending and borrowing. It was intended to do so not just in bankrupt states but also in other nations where lax lending and excessive borrowing could lead to bankruptcy. The very existence of the framework was expected to help regulate capital movements and prevent future crises.<sup>91</sup>

The Jubilee 2000 call for debt cancellation was welcomed and supported by many in the developed West. For example, the public intellectual Noam Chomsky praised it, with some qualifications. He noted that the debt accrued does not go away; *someone* pays, and risks tend to be socialized, just as costs

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90. *Id.*

91. *Debt Relief for the Poorest Countries*, 21 CANADIAN J. DEV. STUD., No. 2 (John Serieux & Yiagadeesen Samy eds., 2001).

commonly are in the free-enterprise capitalist system.<sup>92</sup> He was attracted to the complementary approach that responsibility falls upon those who borrow and lend. As Chomsky noted, in justifying the debt-relief initiatives,

[t]he money was not borrowed by campesinos, assembly plant workers, or slum-dwellers. The mass of the population gained little from the borrowing, indeed often suffered grievously from its effects. But they are to bear the burdens of repayment, along with taxpayers in the West—not the banks who made bad loans or the economic and military elites who enriched themselves while transferring wealth abroad and taking over the resources of their own countries.<sup>93</sup>

With a similar rationale and purpose, campaigns were launched at the turn of the millennium by southern African economies still burdened by apartheid debt, a decade after the racist political system was abolished in South Africa. These campaigns claimed that the debts were “odious.” This term was invoked in the hope that the doctrine of odious debt would impose a sort of international financial morality on the part of the IFIs and make them more responsible for the purposes to which their loans might be put.<sup>94</sup> These campaigns go further and demand reparations for victims of apartheid, and they target banks in the West that continued to lend money to apartheid regimes even up to the close of their existence. Front line states also claim to qualify for debt relief because they had to borrow to protect, defend, and repair themselves from the aggression of the regime.

## VI

### NEW PROPOSALS FOR ODIIOUS DEBT TREATMENT—CANDIDATES AND APPROACHES

Two economists, Michael Kremer and Seema Jayachandran, have tried to revive the concept of odious debt as a means for dealing with past, current, and future debt crises, particularly those of some of the most corrupt, scandal-ridden regimes from the past two decades. Potential recent examples of candidates for the label of “odious debts” identified by Kremer and Jayachandran<sup>95</sup> include debts incurred in the following countries by the regimes such as

1. Nicaragua (Anastasio Somoza reportedly looted \$100–\$500 million.)
2. Philippines (Ferdinand Marcos amassed a \$10 billion fortune.)
3. Haiti (Duvalier regime was reported to have absconded with \$900 million.)

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92. Noam Chomsky, Jubilee 2000, <http://www.chomsky.info/articles/19980515.htm> (last visited Oct. 25, 2007).

93. *Id.*

94. ANN WHITEHEAD, U.K. GENDER AND DEV. NETWORK, FAILING WOMEN, SUSTAINING POVERTY: GENDER IN POVERTY REDUCTION STRATEGY PAPERS (2003), available at [http://info.worldbank.org/etools/docs/library/99169/CD\\_CC/precourse/CCFY04CDRom/Week1/2Tuesday/S3%20PRSPs/GenderinPRSPs.pdf](http://info.worldbank.org/etools/docs/library/99169/CD_CC/precourse/CCFY04CDRom/Week1/2Tuesday/S3%20PRSPs/GenderinPRSPs.pdf).

95. Michael Kremer & Seema Jayachandran, *Odious Debt*, FIN. & DEV., June 2002, at 36.

4. South Africa (apartheid government spent heavily on police and military to repress majority population.)
5. Congo (former Zaire) (Mobutu Sese Seko had personal accounts for \$14 billion.)
6. Nigeria (Abacha reportedly held \$2 billion in Swiss bank accounts in 1999.)
7. Croatia (Tudjman looted unknown amounts, suppressed media, and attacked violently his political opponents.)

As Kremer and Jayachandran note, at present countries repay even odious debts for several reasons.<sup>96</sup> First of all, if they failed to repay, their assets abroad might be attached to make payments. Second, in the international community, a high priority is placed on reputational interests in not being perceived as defaulting on debt, or as financial scofflaws. Third, as countries such as Peru, Argentina, and Mexico have learned, there are real financial consequences of not being able to borrow in international markets if there were to be a default, whatever the reason. Finally, most developing countries have well-grounded fears of difficulty in attracting foreign investment if any public debts were repudiated.

These real difficulties have led some analysts—including Kremer and Jayachandran—to conclude that the international community should try to establish an international institution which could impartially assess and definitively determine that certain debts or the regimes that contracted them were “odious.” This would have to be done in advance, putting lenders on prior notice that successor governments would be justified in repudiating any new loans that would be advanced to such odious regimes.

In an important contribution to the literature on this problem,<sup>97</sup> they propose the creation of an institution that would truthfully announce whether regimes are odious and that could create an equilibrium in which successor governments would suffer no reputational loss from failure to repay odious debt. As a result, they hypothesize that creditors would curtail odious lending. Under their scheme, equilibrium with odious lending would be eliminated by amending creditor country laws to prevent seizure of assets for failure to repay odious debt and to eliminate current rules restricting foreign aid and other assistance to countries not repaying odious debt. They argue that shutting down the borrowing capacity of illegitimate regimes can be viewed as a form of economic sanction with two significant advantages over most sanctions: it helps rather than hurts the population, and it does not create incentives for evasion by third parties. Recognizing that an institution empowered to assess regimes might falsely term legitimate debt odious if it favored debtors *ex post*, and that creditors who anticipated this would not make loans to legitimate governments,

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96. *Id.* at 37.

97. See Michael Kremer & Seema Jayachandran, *Odious Debt* (Nat'l Bureau of Econ. Research, Working Paper No. 8953, 2002).

their proposal seeks to establish the odiousness of a loan *ex ante*. They posit that an institution empowered only to declare *future* lending to a particular government odious would have greater incentives to judge truthfully. They argue that this approach could also be used to reduce moral hazard associated with World Bank and IMF loans.<sup>98</sup>

The legal issues are not insignificant. Among other things, the laws in creditor countries would have to be changed in some way to make odious debt contracts legally unenforceable, unless it were understood that courts might already apply general principles such as unconscionability or *contra bonos mores* to odious debt agreements. International financial institutions, such as the World Bank and IMF, would have to make it abundantly clear that they would decline the opportunity to bail out creditors disadvantaged by odious debt that was either repudiated or not repaid for other reasons. And the independent institution that would determine whether regimes are legitimate and whether their debts are obligations for successor regimes to pay must be structured in a manner that inspires global confidence.

In a more recent article on odious debt, Kremer and Jayachandran argue for what they term “loan sanctions” to prevent the repayment of odious debts.<sup>99</sup> Loan sanctions, in contrast to an international institution which would decide the legitimacy of debts, could be self-enforcing and could protect the population from being saddled with “odious debt” run up by looting or repressive dictators. Governments could impose loan sanctions by instituting legal changes that prevent seizure of countries’ assets for nonrepayment of debt incurred after sanctions were imposed. This would reduce creditors’ incentives to lend to sanctioned regimes. Restricting sanctions to cover only loans made after the sanction were imposed would help avoid time-consistency problems.

## VII

### CONCLUSION

The obvious attractiveness of the concept of odious debt, and the possibility of its justifying repudiation of debts so denominated, belies the difficulty in establishing it as a settled matter in public international law. Almost a century after it was articulated by Professor Sack, and more than a century after it was first invoked following the Spanish-American War, it is often discussed (at least in academic circles) but infrequently asserted by debtor countries.

The response of Latin American nations and the IFIs to the 1970s debt crisis illustrates the difficulties in employing the doctrine of odious debt. Whereas none of this addresses the question of whether the doctrine has become a principle of international law, after more than a quarter of a century has passed, it would be hard to argue that the doctrine of odious debt is now entrenched in customary international law. Rather, it remains an elegant legal construct

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98. *Id.*

99. Seema Jayachandran & Michael Kremer, *Odious Debt*, 96 AM. ECON. REV. 82 (2006).

seeking great utility and more applicability to actual situations that it has enjoyed in the past.

In considering the more recent Iraqi debt, Professor Stiglitz has also suggested that the United Nations could devise a set of principles based on the idea of “odious debt”—a rule of law—that would guide the court as it assessed the validity of contracts made with, and debts incurred by, outlaw regimes. Loans to build schools might be permitted, and the debt obligation, accordingly, would not be treated as odious; loans to buy arms might not be permitted. In some cases the court might decide that a loan for an ostensibly good purpose ran a high risk of being used for nefarious objectives—in which case the loan would be disallowed. Governments and banks that lend money to oppressive regimes would be put on notice that they risk not getting repaid, and the contracts and debts of countries with outlaw regimes would be re-examined once those regimes were no longer in power.<sup>100</sup> Stiglitz went on to argue,

If the United States expects the international community to work cooperatively on the reconstruction of Iraq’s economy, and to cut Iraq the slack it needs on its debts, then America must commit itself to something in return: the establishment of a framework for addressing debt relief, debt restructuring, and odious debts—a framework that includes an international court that can develop and enforce a set of widely agreed-upon principles. Only with those principles in place will decisions seem fair. And without them the prospects for winning the peace in Iraq will further diminish.<sup>101</sup>

The proposals of Kremer and Jayachandran take the next step in outlining what such a framework might become in institutional form. Although their recommendations have yet to be taken up seriously by the international community, they have generated a great deal of academic and public policy attention. No doubt part of their appeal is the terminology of odious debt, which evokes an immediate, visceral reaction and aptly describes the onerous financial obligations now burdening nations that have at long last shed the shackles of hateful, repressive regimes. Whether the proposed new international institutions will be created using the notions of odious debt remains to be seen. As the resolution of the Iraqi debt burden demonstrates, other mechanisms such as the Paris Club process can handle unpaid and unpayable sovereign debts on an ad hoc basis. Nevertheless, after more than a century, the concept of odious debt retains considerable strength and may yet be implemented in an international institutional form.

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100. Stiglitz, *supra* note 72, at 45.

101. *Id.*