

# **Alternatives to the traditional odious debts doctrine**

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With the current boom in academic literature on the topic of odious debts, it is impossible to discuss and evaluate all approaches to odious debts in one short paper. I will therefore not even attempt to do that, but instead, very briefly, summarise my own critique of the traditional odious debts doctrine and then present some reflections on potential alternatives.

## **1. Critique of the ‘traditional’ odious debts doctrine**

The ‘traditional’ doctrine of odious debts, as formulated by Alexander Sack in 1927 and then further developed, more recently, for example in the CISDL working paper, but also by other activists and academics, states that a sovereign debt is odious and can be repudiated if (1) it was contracted without the consent of the people of the country that is said to owe the debt; (2) it was not contracted for the benefit of the people of that country; and (3) the creditors were aware of the odious nature of the debt.

The odious debts doctrine as it is usually understood and promoted is not only not a principle that is firmly established in international law, but it has moreover many insufficiencies as a means to address the debt problem. This is mainly because of the vagueness of its criteria, but also because of the ideological connotations of the doctrine which cause problems of sovereignty and political bias (for example by vesting the power to decide whether a loan was beneficial to the people of the debtor state in an international tribunal) and raise concerns as to the implementation of the doctrine. Moreover, although it is based on the idea that odious debts do not need to be repaid, the doctrine mainly seems to be regarded as providing a defence against claims for debt repayment, which means that it would not help the debtor states to reclaim payments that were already made. Overall, from a legal perspective, the doctrine of odious debts in its traditional form has so many weaknesses that it does not provide a useful tool with which debt repayment can be successfully challenged.

## **2. Alternative approaches**

### **2.1. International law approach**

In his report to the ILC on a draft of the Vienna Convention on Succession of States in respect of State Property, Archives and Debts (1983), Special Rapporteur Bedjaoui suggested that in addition to the traditional definition, the term odious debts should comprise ‘all debts contracted by the predecessor State with an aim and for a purpose not in conformity with international law and, in particular, the principles of international law embodied in the Charter of the United Nations’.

The differences to the traditional doctrine are that the international law approach:

- concentrates on conformity with international law, and it is then primarily the international community that is harmed by the odious nature of the debt, not the people of the debtor state

- if, as Sack foresees for the traditional odious debts doctrine, it is not the people of the debtor state, but instead an international institution that will define the beneficial or unbeneficial nature of the debt, the decision to be made by an international body would here be whether the loan was in violation of international law principles, an evaluation seems to fall much more comfortably within the competence of international bodies than whether a loan benefited the people of a state.
- Its prerequisites could be determined in analogy to Article 53 of the Vienna Convention on the Law of Treaties (1969): ‘A treaty is void if, at the time of its conclusion, it conflicts with a peremptory norm of general international law. For the purposes of the present Convention, a peremptory norm of general international law [*ius cogens*] is a norm accepted and recognized by the international community of States as a whole as a norm from which no derogation is permitted and which can be modified only by a subsequent norm of general international law having the same character.’

How can it be determined that a loan agreement violates *ius cogens*?

- One of the problems here is that the loan agreements themselves will in most cases be neutral with regard to *ius cogens* violations, unless it can exceptionally be determined that the loan contract included the agreement on a purpose which amounts to a violation of *ius cogens*, such as a loan that was contracted for the purchase of torture equipment.
- In many cases, it will only be possible to demonstrate that governments use the loans obtained in order to commit violations of *ius cogens* norms, for example where they use the incoming money in order to purchase arms with which they commit crimes against humanity within their own country, or acts of aggression towards the people of other countries. When focusing on the use of the borrowed money it becomes more difficult to establish a direct link between the loan and the *ius cogens* violation, or at least a sufficiently close link that would justify to regard the loan contract itself as void. However, it could be argued that it is sufficient that the loan contributed to the *ius cogens* violation. A loan can make a contribution to a *ius cogens* violation whether or not the money lent to the regime is directly used to finance this violation; for example because it facilitates the violation by adding to the financial resources of the regime or makes it possible by having a stabilizing effect on the political position of the regime. A loan that directly financed torture equipment or operations has a significant effect on the commission of torture, but the same might also be true, though this would be more difficult to establish, for a loan that enables a regime to remain in power and carry on with torture practices.
- If it were accepted that loans to regimes that commit *ius cogens* violations will in all likelihood at least indirectly facilitate these violations, a presumption could be applied in favour of the odiousness and consequent invalidity of such loans, unless it can exceptionally be shown that the loan did not even have such an indirect effect. This would require a determination of the regimes to which such a presumption could be applied, that is which regimes qualify as committing *ius cogens* violations. While this would include judgments on the policies of regimes, to invite the international community and potential lenders to beware of dealing with regimes that violate *ius cogens* is different from

asking them to make a democracy assessment as sometimes suggested in the context of the traditional odious debts doctrine. After all, despite all its uncertainties, the concept of *ius cogens* is recognized as part of international law, and it has at least a core content on which wide agreement exists. However, it is submitted that a seriousness threshold should be applied with regard to the *ius cogens* violations of the relevant regime. The ILC's Articles on State Responsibility distinguish between serious and other breaches of state obligations arising under peremptory norms of international law (Articles 40 and 41) and attach particular consequences to the former. A serious breach is defined as one that 'involves a gross or systematic failure by the responsible State to fulfil the obligation' (Article 40(2)). While a systematic violation is one that is 'carried out in an organized and deliberate way ... the "gross" refers to the intensity of the violation or its effects.' Similar considerations should be applied in the context of loans.

#### Consequences:

- This would mean that banks could see loans declared to be odious simply on the basis that they were made to regimes that commit *ius cogens* violations, thus for doing business with such a regime.

#### Problems with this approach:

- Whether *ius cogens* is recognized by customary international law beyond the particular case of treaties between States is not clear, but a good case can be made that this is the case.
- *ius cogens* is a very narrow concept and only very few principles are regarded as forming part of it, such as the outlawing of wars of aggression and crimes against humanity, the prohibition of torture, and the right to self-determination
- The *ius cogens* approach developed here will in all likelihood be unacceptable to all those who regard trade with regimes that commit *ius cogens* violations, including those that were as blatant and as widely and strongly condemned as those of the apartheid regime, as acceptable or even desirable. It would also probably be objected that such an approach might have a negative impact on developing countries and their access to the international financial market. However, it should not be forgotten that what is under discussion here is no more than the suggestion that contracts might be invalid and unenforceable if they make a contribution to *ius cogens* violations, that is acts that are regarded as so reprehensible by the whole international community that they cannot be tolerated. An application of the odious debts doctrine to cases in which principles that are commonly accepted to be part of *ius cogens* are violated by a state would not hinder trade or investment, but instead only make sure that trade and investment do not have the effect of enabling or facilitating such violations.

#### Advantages of this approach:

- A doctrine based on *ius cogens* violations provides clearer criteria than the traditional doctrine of odious debts
- it overcomes one of the fundamental weaknesses of the doctrine in its traditional form in that it would extend to restructured debt, because where a contract violates *ius cogens*, it is not only void, but it can moreover not be

ratified. Thus, not only the original loan transactions taken up by dictators who violate *ius cogens* norms would be invalid, but the restructuring and refinancing agreements referring to debt that falls into this category could not be regarded as valid ratifications of these loans. Furthermore, many argue that no limitation period applies to claims based on a violation of *ius cogens*, which would be significant with regard to potential claims for restitution of payments made on such loans.

- While the underlying assumption that the mere fact of doing business with a regime that violates *ius cogens* norms could lead to the invalidity of a loan transaction will in all likelihood mean that the doctrine will not be greeted with enthusiasm by large parts of the international community, it is exactly this focus that makes it attractive, as the doctrine challenges the assumption that it is only a moral, but not a legal obligation not to contribute to such violations. Furthermore, to the extent that the content of *ius cogens* might gradually expand, such a doctrine might see its scope of application increase.
- Ideally, this approach would involve an international tribunal, but it could also be invoked before national courts that hear claims for debt repayment, to the extent that the relevant legal system within which the court operates requires the national courts to take principles of international law into account. As the courts would then be prevented from handing down decisions that violate international law principles, the creditors' contractual claims could be countered by relying on the invalidity of the loans because of their violation of *ius cogens* norms. Moreover, an argument could be made that the reasons that militate in favour of the recognition of such a doctrine as part of international law also favour integrating the doctrine into the national *ordre public* of countries.

## 2.2. Focusing on the potential invalidity of the loan

The traditional odious debts doctrine does not question the general validity of loan transactions that were concluded with dictatorial regimes. However, it is not at all evident that contracts entered into by dictators on behalf of the country will always create legally binding obligations for the country. Indeed, Sack distinguished between regular and irregular despotic regimes, although it does not become clear according to which criteria the distinction is to be made. Where a loan was not contracted by a regular government and according to the correct procedure, he seems to have assumed that the creditors were limited to recovery according to the principles of unjust enrichment. The odious debts doctrine, on the other hand, would only apply to those cases in which a debt was properly contracted by a regular government, but nevertheless odious. This distinction between contracts that validly bind the country, and those that do not, is important in law, but largely overlooked by discussions of the doctrine of odious debts. If a contract is invalid, for example because the dictator did not have the power validly to indebt the country, or where the contract was void because of other irregularities, *pacta sunt servanda* cannot apply, and a reliance on the odious debts doctrine would be unnecessary.

One reason for which a loan contract with a dictatorial regime might be invalid is that of lack of agency, ie that the acting government was not, under its own constitutional or other law, duly authorised to represent the country in this way, which

might lead to the invalidity of the contract. The potential of this approach would vary according to the law of each country. However, my research into the particular situation of Argentina showed that constitutional law could have played an important part in dramatically reducing the problem of the debt burden. Indeed, if constitutional principles had been complied with, large parts of Argentina's debt could not have been incurred, and the debt crisis would accordingly have been avoided and that, based on constitutional arguments, the validity of the debt can be challenged.

### **2.3. Private law approaches**

An alternative to the approach suggested here would be not to focus on the domestic law of the debtor country, but instead on the law that governs the loan contract, and to develop legal arguments against the validity or enforceability of the contract on the basis of the provisions of that law. This could, for example, be achieved by extending private law principles to states by way of analogy. While the possibilities of such an approach are worth exploring, it is submitted that an approach that refers the questions of actual and ostensible authority and ratification to the law of the debtor state is, in principle, preferable, as it allows to take into account the specific situation of a state as sovereign and the constitutional limitations imposed on state organs, instead of artificially treating the state as if it was in the same position as a private actor.

### **3. Concluding remarks**

As a form of conclusion, it is submitted that in the context of any discussion of the doctrine of odious debts and potential legal ways of implementing such a doctrine, it is essential to be clear about the goals one wants to achieve. As the recent academic discussion shows very clearly, the proposals vary considerably depending on the authors' views on whether the primary goal should be to change future lending policies; to search for convincing legal ways to repudiate parts of the existing Third World debt; or to develop a theory that achieves both. More importantly, the approaches will differ fundamentally depending on where one stands with regard to the question of whether it is desirable that certain regimes should not receive any loans, or whether one rather thinks that all depends on the use that is made of a specific loan.