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Courts and Sovereigns in the Pari Passu Goldmines

Anna Gelpern  
*Georgetown University Law Center, ag1348@law.georgetown.edu*

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Courts and Sovereigns in the *Pari Passu* Goldmines

Anna Gelpern

**Introduction**

This article revisits a once-notorious case brought by a Swedish holder of defaulted German bonds, decided by the highest federal court in Switzerland in 1936. Like another notorious case, prompted by Argentina’s default and decided in New York between 2011 and 2014, it considered a sovereign debtor’s promise to rank its creditors *pari passu* (“on equal footing”). Swiss and U.S. courts both read this contract term to require the sovereign to make proportional payments to its creditors. Nonetheless, Germany’s creditors lost, while Argentina faced a worldwide financial boycott ordered by U.S. courts in the name of equal treatment.

Courts and advocates in the United States, the United Kingdom, and Belgium, among others, have operated on the assumption that no court had considered the meaning of *pari passu* in sovereign

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1 Professor, Georgetown Law, and Non-Resident Senior Fellow, Peterson Institute for International Economics. I am grateful to Benjamin Chabot, Christine Desan, Daniel Ernst, Juan Flores, Mitu Gulati, James Kerr, Adam Levitin, Frank Partnoy, Marylin Raisch, Brad Snyder, Jerome Sgard, Larry Solum and Mark Weidemaier for helpful insights, and to Nicholas Brock, Katherine Incantalupo, Vijay Khosa, Sohee Rho and Alex Severens for research assistance. I am especially indebted to Sung Hui Kim for sharing extracts from the Foreign Bondholders Protective Council archives, and to Jacques Oberson and the staff at the United Nations and League of Nations Archives in Geneva for document access and invaluable guidance. A revised and edited version of this essay will appear in the Capital Markets Law Journal.


debt before 2000. The Swiss interpretation, tangled up in the financial and economic wreckage of World War I and the collapse of the gold standard, has gone unremarked in the huge scholarly literature on the *pari passu* clause—even though it resurfaced in 1980 as part of a high-profile dispute involving the same clause in the same bonds, which had been restructured after World War II. This article reviews the opinions from the 1930s and 1980, and explores their implications for today’s contracts.

To the extent they paid attention to the *pari passu* clause in sovereign debt, U.S. and U.K. writers and practitioners at the turn of the 21st century read it as a promise of equal ranking, which emphatically did not require the debtor to make pro rata payments to its creditors. A Belgian court decision in 2000 advancing the payment interpretation was called “rogue”; similar U.S. court rulings since 2011 have been derided as so historically and functionally unmoored as to threaten New York’s position as a global financial center.

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5 See e.g., Declaration of Lord Nicholas Phillips, K.G., P.C., in Red Pines LLC et al. v. Republic of Argentina, Case No. 14-cv-09427 (TPG) § 23 ("Remarkably, until the decision of the Belgian court of Appeal in the case of Elliot Associates L.P. v Banco de la Nacion 2000 WL 1449862, it does not appear that any court anywhere in the world had ruled on the meaning of the *Pari Passu* Clause in the context of sovereign debt.")


8 See e.g., *Gulati & Scott*, supra note 6 (interview reports and literature review); Buchheit & Pam, *supra* note 6, Gulati & Klee, *supra* note 6.

9 See e.g., Gelpert, *supra* note 6 at n. 59 (citing an industry association position paper that called the Belgian decision “rogue”); Brief for the United States of America as Amicus Curiae in Support of the Republic of Argentina’s Petition for Panel Rehearing and Rehearing En Banc at 1, No. 12-105-cv(L) (2d Cir. Dec. 28, 2012) at 5 (arguing that “the decision could harm U.S. interests in promoting issuers’ use of New York law and preserving New York as a global financial jurisdiction”).
Yet decades earlier, three Swiss courts—the trial court in the Basel canton, the canton appellate court and the supreme federal court—all read a *pari passu* clause in German bonds as a promise of ratable payment. The intermediate appeals court even described a plausible enforcement strategy through lawsuits by bondholders against one another. At no point did any of the Swiss judges or expert commentators on *AB Obligationsinteressenter v. Bank for International Settlements* (hereinafter, *AB Obligationsinteressenter*) suggest that the meaning of *pari passu* was ambiguous, or that a meaning other than ratable payment was conceivable. The same German bonds were the subject of an international arbitration between 1971 and 1980, where creditors again claimed discrimination in breach of the *pari passu* clause. The arbitral ruling cited to the Swiss case in its discussion of *pari passu*, but seems to support a mix of ranking and ratable payment interpretation.

A lost judicial reading of an improbably famous, recently litigated clause is an exciting discovery. Yet without more, it would be of little interest outside the circle of *pari passu* enthusiasts. Especially now that Argentina’s new government tries to settle the last of the lawsuits from its 2001 debt default, why should anyone bother with ancient history—or “contract paleontology”?

Exhuming *AB Obligationsinteressenter* and its aftermath prompts four uncomfortable questions about the uses of history in financial contract interpretation and sovereign debt enforcement:

- First, should a 1936 Swiss reading of a 1930 contract carry any weight with U.S. courts in 2016? While not formally binding, the old decision might be persuasive if it revealed a general market understanding of the clause, which could or should be attributed to contracting parties decades later. The 1980 arbitral ruling is less distant—but more ambivalent about the meaning of *pari passu*.
- Second, does the experience with interpreting German bond contracts argue against trying to construe *pari passu* in contemporary sovereign debt? The old decisions discussed the meaning of the clause, but would not enforce it. Recent injunctions cast doubt on whether any reading of the *pari passu* clause should be a vehicle for sovereign debt enforcement. Where interpretation leads to feckless or damaging remedies, abstention might be wise.
- Third, has the *pari passu* obsession distracted commentators from more pressing and tractable problems in sovereign debt? Germany’s interwar default and its aftermath confirm the centrality of trustees, payment and clearing systems for sovereign debt. Market institutions have also figured in recent lawsuits, but have drawn far less academic commentary than the meaning of *pari passu*. Scholarly inattention is costly: courts seem to have chronic trouble dealing with market infrastructure in sovereign debt.

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• Fourth, are sovereign debt contracts really up to the contracting parties? Attempts to enforce sovereign bonds in the 1930s and 2000s both triggered concerted international policy responses to blunt the impact of judicial rulings. Whether a given policy response makes sense is for another day; the take-away here is only that sovereign debt contracts, perhaps more than others, live in its shadow.

This project came about by accident, when I stumbled on translations of *AB Obligationsinteressenter* in the archives of the League of Nations Committee for the Study of International Loan Contracts (hereinafter, the “League Committee”) in Geneva, while researching policy-driven contract reform.\(^{11}\) I do not aim to provide a definitive treatment of the case here; instead, I use its reception by the League committee to illuminate recurring challenges facing courts and international policy makers in sovereign debt crises. The treatment of the 1980 decision in the Young Loan/London Agreement arbitration is similarly confined to its implications for the *pari passu* case study, where it serves as a link between the German and Argentine default episodes, and helps extract lessons for interpretation.

After summarizing the contemporary *pari passu* debate in Part I and introducing the German interwar debt controversy in Part II, I devote the bulk of the article to a detailed account of the Swiss decisions. Part III reviews the Swedish lawsuit, the Swiss court opinions and expert reactions, drawn from the League Committee archives, practitioner and academic commentary. Part IV is devoted to the 1980 arbitral decision, while Part V discusses implications for the courts and contract drafters today.

My conclusions are necessarily preliminary, pending further investigation in BIS and national archives, and in-depth consideration of the Swiss legal context, among others. Nonetheless, continuing turmoil in sovereign debt markets at the start of 2016, coupled with the market and policy fallout from attempts to enforce Argentina’s debt, all argue for sharing the preliminary evidence sooner rather than later.

## I. *Pari Passu* Who?

For the jilted creditor of a sovereign, the *pari passu* clause has turned into the most promising collection weapon to come along since 19th century gunboats. Its apparently simple pledge of inter-creditor equality has made the world’s most powerful politicians and bankers squirm. Early in the 21st century, claims of *pari passu* violation made Peru and Congo pay a king’s ransom to a few

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creditors for the privilege of paying a pittance to the rest; in 2014, it made Argentina default on $28 billion in restructured bonds. Yet it is far from clear that the pari passu undertaking, which has accompanied sovereign bonds since at least the mid-19th century, was ever meant to be a collection tool at all, let alone the creditors’ best hope.

The quest for the true meaning of pari passu in sovereign debt contracts has driven countless deep thinkers to distraction. To this day, there are more definitive accounts of what it does not mean than what it does. For example, according to the Encyclopedia of Banking Law,

[T]he pari passu clause has nothing to do with the time of payment of unsecured indebtedness, since this depends upon contractual maturities. … It is suggested that a pari passu clause in state credit is primarily intended to prevent the legislative ear-marking of revenues of the government, or the legislative allocation of inadequate foreign currency reserves to a single creditor and is generally directed against legal measures which have the effect of preferring one set of creditors over the others or discriminating between creditors at a time when the state is unable to pay its debts as they fall due.

With very few notable exceptions, most academic and professional treatments of the clause published since the 1990s shared the Encyclopedia view: “rank pari passu” could not possibly mean “pay pari passu.”

Scholars typically put the rise of pari passu as a sovereign debt enforcement tool to a 2000 Brussels commercial court ruling, which blocked Peru from paying its restructured debt unless it paid its defaulted debt in full. Holdout creditors, who had paid approximately $11 million for the debt, got $56 million from Peru in a quick settlement, while other creditors had agreed to deep haircuts. A similar Belgian court ruling against Nicaragua was later overturned on appeal since the injunction had improperly targeted the Euroclear system. A handful of other lawsuits around the world left the meaning and the legal effect of pari passu unresolved until 2013, when U.S. federal courts held that Argentina’s pari passu clause forbade selective default—the debtor must either

\[\text{\footnotesize 12 Benjamin Chabot & Mitu Gulati, Santa Anna and his Black Eagle: The Origins of Pari Passu?, 9 CAP. MKTS L.J. 216 (2014).}\]
\[\text{\footnotesize 13 Supra note 6.}\]
\[\text{\footnotesize 14 ENCYCLOPEDIA OF BANKING LAW (2002).}\]
\[\text{\footnotesize 15 See e.g., Bratton, supra note 6.}\]
\[\text{\footnotesize 16 See e.g., Gulati & Klee, supra note 6; Buchheit & Pam, supra note 6.}\]
\[\text{\footnotesize 17 Elliott Assocs., L.P., General Docket No. 2000/QR/92 (Court of Appeals of Brussels, 8th Chamber, Sept. 26, 2000).}\]
\[\text{\footnotesize 18 Republic of Nicaragua v. LNC Investments LLC and Euroclear Bank SA, (Commercial Court of Brussels 2003).}\]
pay all its creditors in proportion to their current contract claim, or default on them all—and promptly triggered comprehensive default when the government refused to settle.\textsuperscript{19}

The U.S. rulings met with outrage in some quarters and jubilation in others. Critics accused the courts of twisting the meaning of the clause. The governments of Brazil, France, Mexico, and the United States filed briefs supporting the “ranking” view advanced by Argentina before the U.S. Federal Courts.\textsuperscript{20} They too said that\textit{ pari passu} was designed to protect against legal subordination (which hardly ever happened), not selective payment (which happened all the time). Other commentators observed that even if ratable payment had been the goal, the court’s valuation was inequitable: putting restructured and un-restructured claims on the same footing gave some creditors a fraction of the original principal amount and others a big multiple.\textsuperscript{21} At the other extreme, fans of the rulings said that the clause was meant precisely as a nuclear commitment device for immune sovereign debtors, which could otherwise default and discriminate with impunity. To give the creditors the benefit of their bargain, the court had to enforce equal treatment in the broadest sense.\textsuperscript{22}

Both sides were struggling with the same awkward problem: if the clause meant what they said,\textit{ pari passu} was a contract version of the human appendix. It had no discernible function in the 21\textsuperscript{st} century, but threatened mass damage when inflamed.

History can help allay some of the awkwardness. It is comforting to know that once upon a time, a distant author contracted for\textit{ pari passu} with the knowledge and specific intent lacking in today’s

\textsuperscript{19}Supra note 3. Argentina’s \textit{pari passu} clause is reproduced in Appendix I.


\textsuperscript{21}Mark L.J. Wright, \textit{Interpreting the Pari Passu Clause in Sovereign Bond Contracts: It Is all Hebrew (and Aramaic) to Me}, \textit{Capital Markets Law Journal} (2014) 9 (3): 259-265. Some of the contracts had been reduced to less than a third of the original value; others were a multiple of it thanks to accrued past-due interest.

\textsuperscript{22}See, e.g., Bratton, supra note 6 and Declaration of Lord Nicholas Phillips, supra note 5, for discussion of parties’ intent. The \textit{pari passu} clause was easy to apply to firms, which could be liquidated in bankruptcy, with proceeds distributed to creditors in order of priority. Creditors who ranked equally would naturally also be paid ratably. \textit{Pari passu} was harder to operationalize for sovereign debtors, which could not be liquidated. The rank of a claim might be conferred by contract or statute before the debtor became insolvent, but determining the implications for distribution is harder: there is no moment of insolvency and no bankruptcy estate; creditors are paid from revenues as claims come due. Sovereign immunity complicates matters further because it makes formal subordination seem inessential: the debtor might pay some of its creditors and stiff others for a long time before the stiffed obtain meaningful remedies.
users of his words. The idea of an accessible historical meaning also fits with institutional explanations of contract boilerplate, where parties might reject bespoke language in favor of widely used terms whose meaning is anchored in commercial usage, construed by the courts, or both, but where vestigial phrases can also malinger long past their prime.

History has its limits: while studying ancient clauses might help transactional lawyers make more educated drafting choices today, it is much less likely to help judges ascertain modern-day drafters’ intent. On the other hand, historical evidence can successfully challenge a claim that a given term can only one meaning. For instance, if contract drafters in the 1930s used pari passu as a promise of ratable payment, it would be hard to argue in 2016 that such a meaning were logically inconceivable.

Earlier excursions into pari passu’s origins have uncovered contract and statutory texts that, in the political and economic context of the day, could variously support either payment or ranking interpretations of the clause. This article adds adjudication to the mix. Judges and arbitrators can put forward an authoritative meaning binding on the contracting parties, illuminate contemporary usage, or elaborate the legal effect of the clause under different circumstances. Decisions prompted by Germany’s interwar default on the Young Loan bonds did a bit of all three.

II. Doomed Bonds

The Bank for International Settlements (BIS) was no ordinary bond trustee. Established in 1930 with subscriptions from leading European central banks and the active involvement of leading U.S. financiers, it was both a bank and a policy institution. It tried to coordinate international monetary and financial affairs amid a deepening depression, the demise of the gold standard, proliferating capital controls, and viral banking crises. A key part of the BIS’s initial mandate was to

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23 The “distant author” is a fixture in contracts. Unable to access the specific intent of actual parties or to discern the meaning of a term from the text, a reader might look to history, custom, or trade association pronouncements. See e.g., Stephen J. Choi & Mitu Gulati, Contract as Statute, 104 Mich. L. Rev. 1149 (2006). For a broader discussion of the distant author phenomenon in contract drafting and interpretation, see e.g., Lori D. Johnson, Say the Magic Word: A Rhetorical Analysis of Contract Drafting Choices 65 Syracuse L. Rev. 451, 465 (2015) (considering the implications of Michel Foucault’s discussion of contracts as authorless documents).


25 Chabot & Gulati, supra note 12, Sung Hui Kim, Pari Passu: The Nazi Gambit, 9 Cap. Mkts. L.J. 242 (2014). (payment); Buchheit & Pam, supra note 6 (ranking)

administer a convoluted scheme whereby Germany borrowed foreign currency from international bondholders to pay World War I reparations to the Allied powers in Europe, which in turn owed money to the United States.

Germany had borrowed approximately $200 million in 1924 from foreign bondholders in U.S. dollars, British pounds, Italian lire, Swedish kronor, and Swiss francs. The Dawes Plan Loan (as the bond issue was called) had been part of a deal to resume reparations payments and help stimulate the German economy. The Dawes bonds had priority claim on Germany’s foreign exchange, and were secured by revenues, notably from tobacco and alcohol taxes. The U.S. dollar tranche alone was indexed to gold, to protect it from currency depreciation. The Agent-General for Reparations, U.S. banker Parker Gilbert, was charged with overseeing currency transfers to minimize exchange rate disruptions; this gave him considerable power over German economic management.  

Even as an interim settlement, the Dawes Plan soon proved to be both politically and economically untenable. It was replaced in 1930 by the Young Plan, named after U.S. industrialist and diplomat Owen D. Young. The new plan rescheduled reparations payments and provided for the withdrawal of French troops from German territory. It also included a new international bond issue. The Young Plan Loan raised approximately $300 million, with bonds denominated in French francs, U.S. dollars, British pounds, Swedish kronor, Dutch florins, Swiss francs, German reichsmarks, Italian lire, and Belgian belgas. Two thirds of the proceeds went to pay reparations; the rest to the German government for investment in railways and the postal service. In contrast to the Dawes Loan bonds, the Young Loan bonds had no priority on foreign exchange transfers; however, all its tranches were indexed to gold at their value on the date of issue. Germany was now responsible for procuring the foreign exchange for external payments. The Young Loan bonds were partially secured with railway tax revenues, and a second lien on the revenues already securing the Dawes Loan bonds. The office of the Agent-General was eliminated, ceding economic policy authority


28 The listing is in the order of tranche sizes. One third of the loan represented “postponable annuities,” whose repayment could be deferred under certain adverse conditions. For a contemporary discussion, see George P. Auld, The Dawes and Young Loans: Then and Now, FOREIGN AFFAIRS (1934).

29 See e.g., Eichengreen, supra note 26 at 245; Barry Eichengreen, Hall of Mirrors: The Great Depression, the Great Recession, and the Uses—and Misuses—Of History (2015) at 434n21 (describing the bonds issued under the Young Plan as subordinate to reparations obligations owing to their lack of transfer priority).

30 “As regards the two-thirds of the service monies which were provided out of the non-postponable annuities the German Government constituted as collateral guarantee for the annuities a special tax payable by the German Railway Company and undertook, subject to the charge securing the German External Loan 1924 [the Dawes Loan], to reserve free from any charge securing any loan or credit in priority to, or pari passu with, the said annuities, the
back to the German government. The BIS became Trustee for the Young Loan bonds and Fiscal Agent for the Dawes Loan bonds.\footnote{Prominent U.S. and European financiers, including Gates McGarrah, former Chairman of the Federal Reserve Bank of New York and the first Chairman of the BIS, served as trustees for the Dawes loan. The three men were charged among other duties with overseeing the distribution of German revenues from collateral accounts. \textit{See} note 68 \textit{infra}.}

The BIS was envisioned as a neutral international organization that would distribute payments from Germany in different currencies to the bondholders in different countries with an eye to minimizing market disruptions and promoting policy coordination. Turning war reparations into a commercial financing administered by a technocratic institution was meant to diffuse political controversy around the plan, and to insulate politicians on all sides from the associated taint.\footnote{Beth A. Simmons, \textit{Why Innovate? Founding the Bank for International Settlements}, 45 \textit{WORLD POLITICS} 361 (1993); Thomas W Lamont, \textit{The Final Reparations Settlement}, 8 \textit{FOREIGN AFFAIRS} 336 (1930).}

Commercialization translated some of the national rivalries and mutual suspicions of the day into the language of contract. The Young Loan bond terms use the phrase \textit{pari passu} in five different provisions, excerpted in Appendix II. The recitals and Paragraph XII reflect Germany’s promise not to give any future creditors equal or better rights in the revenue pledge securing the Young Loan bond. Paragraph II says that the bonds in the nine different currency tranches would be payable to bearer, and would “rank \textit{pari passu} irrespective of date or place of issue or otherwise.” Paragraphs IX and XIV clarify that Germany may issue more bonds “ranking \textit{pari passu} as to payment with the Bonds of the present Loan.” Paragraph IX in particular refers to the application of Germany’s periodic payments to the BIS among existing and future loans of equal rank. In all, \textit{pari passu} in the Young Loan referred to three kinds of equality: (1) equality among bondholders of different issues with respect to revenues pledged as collateral, (2) equality among bondholders of different issues with respect to periodic payment distribution, and (3) equality among bondholders of the same issue. The last category did not refer to collateral or payments, but expressed concern about discrimination based on currency and, implicitly, creditor nationality.

On the face of the document, it is hard to tell whether the reference to different debts ranking \textit{pari passu} with the Young Loan bonds could include debt outside the reparations financing arrangement cleared through the BIS. At least two borrowings could fit this description, the first of which was certainly contemplated by the parties to the Young Loan. In October 1929, Swedish industrialist and financial schemer Ivar Kreuger agreed to lend the German government approximately $125 million in parallel with the Young Loan, in exchange for a match monopoly. A year later, Boston financial firm Lee, Higginson and Company arranged another $125 million proceeds of the customs, the tobacco taxes, the beer tax and the tax on spirits.” Bank for International Settlements, Fourth Annual Report, April 1, 1933-March 31, 1934, Basel, May 14, 1934 (Hereinafter, “BIS Fourth Annual Report”), at 40.
in shorter-term credits for the government.\textsuperscript{33} Swedish and U.S. creditor representatives later demanded that these be paid \textit{pari passu} with the Young Loan.\textsuperscript{34}

The Young Plan fell apart almost as soon as it began. The failure of Austria’s Creditanstalt bank in May of 1931 started a wave of panics and crashes across Europe. When German officials raised the possibility of a moratorium on reparations, German banks suffered dramatic outflows. Shortly after, U.S. President Herbert Hoover offered to suspend Allies’ debt payments to the United States if they agreed to pause German reparations; the “Hoover Moratorium” went into effect later that year. Another round of intergovernmental negotiations in Lausanne ended Germany’s reparations obligations in 1932, but specifically preserved the rights of private bondholders under the Dawes and Young Loans.

Meanwhile, the gold standard was crumbling. Britain and Sweden went off the gold standard in the fall of 1931; their currencies soon fell by 40 percent. The United States followed suit in April of 1933; in June, the Congress passed a Joint Resolution declaring gold indexation clauses unenforceable.\textsuperscript{35} Germany imposed exchange controls to stem the loss of reserves, but continued to peg the reichsmark to gold. It stuck to the peg even as the falling currencies of its trading partners made its exports uncompetitive, and made it impossible to generate enough foreign exchange to service its debts.

\textsuperscript{33} On Kreuger’s quest for match monopolies and his financing for Germany, see Frank Partnoy, \textit{The Match King: Ivan Kreuger, The Financial Genius Behind a Century of Wall Street Scandals} (1999). In addition to the $125 million “Match Loan,” Kreuger also took up about half of the $20 million Swedish Young Loan tranche himself, with another quarter for his firm, Kreuger & Toll. William H. Stoneman, \textit{The Life and Death of Ivar Kreuger} 204 (1932; reprinted by Forgotten Books, London, 2013); Toniolo, \textit{supra} note 26 at 507 (n. 59, reporting Kreuger’s stake at $15 million). Scholars have pointed to Kreuger’s financial dealings as the principal factor behind the weakness of the Swedish banking system and Sweden’s financial crisis in 1931. Peter Kugler, Tobias Straumann, and Florian Weber, \textit{How the German Crisis of 1931 Spread Across Europe: Evidence from the Swedish Twin Crisis} (mimeo, July 2013) 20-22, 37 at http://www.ehes.org/STRAUMANN%20et%20al.pdf (also forthcoming in Economic History Review 2016).

On the two-year Lee, Higginson Loan, see Edward W. Bennett, \textit{Germany and the Diplomacy of the Financial Crisis}, 1931 (1962) at 17-21 and 101 (n. 32). Kreuger had ties with Lee, Higginson and also participated in the Lee, Higginson Loan to Germany. \textit{Id}.

\textsuperscript{34} For example, the Swedish representative at a meeting called to address foreign exchange transfer disruptions and held in Basel in April of 1934, insisted, “As fully laid down in a special memorandum of June 4, 1933, the Kreuger loan is in all respects equal to the Young loan, with which it ranks pari passu. It ought, therefore, to receive the same treatment as this latter loan not to speak of the Lee Higginson credit.” Statement of Mr. P. Brundell of Skandinaviska Aktiebolaget, April 9, 1934, attached to Report of Pierre Jay, Laird Bell and W.W. Cumberland on the German Long and Medium Term Debt Conference of April-May 1934 (June 25, 1934), pp. 14-15, 87. Foreign Bondholders Protective Council (FBPC) Archives, Call No. M1287, Box 63. See also Toniolo, \textit{supra} note 26 at 153 and 531 (n. 199).

Law, economics, and politics all played a part in Germany’s choice. The Young Plan agreement required it to keep the reichsmark convertible into gold at fixed value.36 Treaties aside, devaluing would have increased the cost of servicing foreign-currency debt, including the large short-term debts owed by German financial institutions to foreign private creditors.37 The experience of hyperinflation in the 1920s further made going off the gold standard politically unpalatable. Both Hitler and Reichsbank president Hjalmar Schacht had publicly committed to maintain the reichsmark’s value.38

Germany continued to pay the BIS the gold value of all the Young Loan coupons through 1932, including those due to the British and Swedish bondholders. Several events at the start of 1933 might have contributed to a change in course. Hitler became Chancellor in January, and secured extraordinary powers in March. The Nazi party had long targeted the Dawes and Young Plan payments as symbols of Germany’s postwar humiliation.39 On the other hand, U.S. legislation and English court decisions (later reversed) barring gold value payments40 gave Germany a new legal argument. The BIS Annual Report for 1934 described the unraveling:

On May 10, 1933, however, the United States dollar having also left the gold standard, the Finance Minister of the German Reich informed the Trustee that in view of the decisions of certain English courts to the effect that the interest and principal of bonds expressed in sterling and containing a gold clause are nevertheless payable in current legal tender sterling, in the nominal amount of the coupon or bond, and having regard, also, to the fact that the Government of the United States of America had taken the position that obligations expressed in dollars and containing a gold clause were payable at their nominal value in current legal tender without regard to such clause, it was the intention to effect future payments in respect of the American, British and Swedish issues of the German Government International 5 ½ % Loan 1930 in current legal tender dollars, sterling and

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36 Debt Certificate of the German Reich, Sec. II.5, Annex III to the Agreement Regarding the Complete and Final Settlement of the Question of Reparations from Germany (The Hague, January 20, 1930, in force generally May 17, 1930)


38 TOOZE, supra note 37 at 113-114.

39 AHAMED, supra note 27.

40 The Court of King’s Bench and the Court of Appeal held in Feist v. Societe Intercommunale Belge d’Electricite (1 Ch. 684 (1933)) that a promise to pay in gold coin did not imply a promise to pay gold value in currency when payment in gold was against public policy. The House of Lords reversed the following year (A.C. 161 (1933)). The case is discussed in Arthur Nussbaum, COMPARATIVE AND INTERNATIONAL ASPECTS OF AMERICAN Gold Clause Abrogation, 44 YALE L.J. 53, 56-57 (1934) and in Contracts. Gold Clause, 34 COLUM. L. REV. 552, 560-62 (1934).
crowns, respectively, in amounts sufficient to pay coupons and to meet the sinking fund obligations at the respective nominal amounts, only.\textsuperscript{41}

The trustee was in a bind. The BIS could either do as Germany said and discriminate among bondholders from different countries, or pool the money and distribute it among all the tranches in proportion to their claims on a gold value basis. As the BIS saw it, neither option complied with the bond terms. Germany’s bond contract committed it to rank all the different currency tranches “pari passu in all respects irrespective of date or place of issue or otherwise.”\textsuperscript{42} Simply transmitting the money as instructed would give the U.S., U.K. and Swedish bondholders 40 percent less than the others, measured by gold value. On the other hand, the gold clause in the general bond required Germany to pay principal and interest at the gold value of the currency of denomination at the time of issue, “but not less than the nominal amount of the principal and interest specified in each Bond.”\textsuperscript{43} Pooling and redistributing the funds proportionately would result in payment below nominal and gold value for the French, whose franc was still tied to gold, but above nominal and below gold value for the Swedes, now off gold. The BIS chose to pass on the discriminatory payments under protest:

> After taking legal advice the Trustee decided that it was necessary, under the circumstances, while reserving the rights to the unpaid amount computed on a gold value basis, at least to pay the coupons of all issues of the Loan at their respective nominal amounts… Certain paying agents have expressed dissatisfaction … taking the position that the aggregate service should have been pooled, and divided pro rata on a gold value basis. They have indicated that a competent judicial ruling might be sought.\textsuperscript{44}

And so it was.

\section*{III. An Awkward Case}

Among the three aggrieved tranches, the Swedish one appears to have been the only one to sue.\textsuperscript{45} The United States vigorously and fruitlessly protested the plight of its bondholders through

\begin{enumerate}
\item BIS Fourth Annual Report, April 1, 1933-March 31, 1934 (May 14, 1934), \textit{supra} note 30 at 40.
\item German Government International 5 ½ Per Cent. Loan 1930, §II (reproduced in Appendix II).
\item \textit{Id.}, §VI(a). Payment currency did not alter the valuation, which was based on the currency of denomination.
\item BIS Fourth Annual Report, \textit{supra} note 30 at 41.
\item The plaintiff appears to be an investment vehicle established by members of the Wallenberg family (Marcus and his sons Jacob and Marcus Jr.) on March 3, 1931. Its purpose, according to the corporate records, was “[t]o purchase manage and sell deposits and foreign bonds and other comparable value documents and other related operations.” (An electronic search for “Aktiebolaget Obligationsinteressenter” at Riksarkivet.se (Swedish national archives) yielded one entry in the Records for Incorporated Companies 1901-1935 under the name AB Obligations-Interessenter.)
\end{enumerate}
diplomatic and banking channels;\textsuperscript{46} on the other hand, both the United Kingdom and Sweden eventually concluded bilateral clearing agreements with Germany, taking advantage of their trade surpluses with the recalcitrant debtor to recoup the bond payments.\textsuperscript{47}

\textbf{A. The Trial}

AB Obligationsinteressenter sued the BIS in the Basel-Stadt canton civil court, where the BIS was located.\textsuperscript{48} As a first order of business, the court struggled with the choice of law, which had not been specified in the General Bond conditions. The BIS apparently argued that “Anglo-Saxon” law should apply, because U.S. and U.K. tranches accounted for half of the total Young Loan, because of the preeminence of U.S. and British bankers in arranging the loan, but also because the case required the court to determine its duties as trustee, a concept that had no ready equivalent in continental European law or practice.\textsuperscript{49} After concluding that none of these factors required recourse to English law and observing that neither side argued for Swedish law, the court

\begin{quote}
The Wallenbergs were prominent Swedish bankers and industrialists, who were also active in international business and diplomatic circles. They took over a substantial portion of the assets of the disgraced “Match King” Ivar Kreuger after his suicide in 1932. It is possible that the Wallenbergs ended up owning most of Sweden’s Young Loan bonds as a result of Kreuger’s death.

It is curious that a Wallenberg firm would be the only one to sue. Marcus Wallenberg, Sr. sat on the three-man arbitration committee with jurisdiction over disputes concerning the maintenance of short-term private credits to German banks. \textit{TONIOLO}, supra note 26 at 127. After Germany started withholding foreign exchange for its debt payments, Jacob Wallenberg was part of the Swedish delegation negotiating transfers, and later annual bilateral clearing arrangements with Germany. John Foster Dulles’s 1933 reports to FBPC contain several references to Wallenberg’s interventions, the most vocal of which concerned the imperative of preserving equal status for the Kreuger Match Loan. At $125 million, it probably represented the largest single Swedish exposure. Memorandum of Proceedings of the German Long-Term Debt Conferences, Held at the Reichsbank, December 5, 1933, p. 8, and December 6, 1933, p. 12. FBPC Archives, Call No. M1287, Box 63. \textit{See also} Sven-Olof Olsson, \textit{Nordic Trade Cooperation in the 1930s}, in \textit{MANAGING CRISES AND DE-GLOBALIZATION: NORDIC FOREIGN TRADE AND EXCHANGE, 1919-1939} (2010), (Sven-Olof Olsson, ed.) at 25.

The lawsuit might have been a way for creditors from a relatively small and over-exposed country to gain leverage in a multilateral negotiation. On the other hand, bringing a lawsuit might have antagonized German officials and complicated Sweden’s negotiating efforts.

\textsuperscript{46} Kim, supra note 25.

\textsuperscript{47} Auld, supra note 28; Clement, supra at 27.

\textsuperscript{48} The plaintiffs might have thought that suing Germany was pointless in light of the absolute sovereign immunity doctrine of the day; it also might have been politically wiser to sue the trustee rather than pick a fight with Hitler.

\textsuperscript{49} \textsc{Luc Thevenoz}, \textit{Trusts in Switzerland: Ratification of the Hague Convention on Trusts and Codification of Fiduciary Transfers 179} (2001) (dating the earliest decision to 1874); \textsc{Felix Weiser}, \textit{Trusts on the Continent of Europe: A Study in Comparative Law} (1936).
proceeded to apply Swiss law as the law of the place of performance.\textsuperscript{50} As predicted by the BIS, this led to some awkward reasoning on the question of trust.

The plaintiff argued that the BIS violated its obligations as trustee when it paid them in nominal money contrary to the gold and pari passu clauses in the general bond. The case turned on the scope of the BIS’s duties—whether, as trustee, it “had not only the duty to pass on the payments to the bondholders but had the additional obligation of ensuring in all circumstances payment to the bondholders on the basis of equality, irrespective of the attitude adopted by the debtor.”

The canton trial court concluded that the plaintiffs failed to prove such “additional obligation” in two steps. First, it pointed out that the German position on differential payment did not arise out of financial difficulties, nor because the debtor “wished to favor” some bondholders over others, but rather because it challenged the validity of the gold clause in the three tranches in question. Overriding German instructions would have required an independent decision by the BIS as to the validity of the gold clause. Second, the court decided that the BIS’s duties were “not those of an arbitrator but of a paying agent,” a mostly-passive payment conduit. In light of the complexity of the loan, “having its origin in political events,” the court assumed that BIS “did not intend to contract any such far-reaching obligation as is implied by the contention of the plaintiff.”\textsuperscript{51} The court thus re-attached political roots to Germany’s “commercialized” debt, and used the BIS’s political origins to turn it from “representative of the bondholders” into “paying agent” of the debtor. With that, the court easily absolved the BIS of all liability under both the gold and pari passu clauses.

Along the way the trial court made important observations about the meaning and consequences of a pari passu undertaking. First, the judges found it uncontroversial that, “if the German Reich had made a partial payment, for the sole reason that it had difficulties in raising the necessary amounts, it might have been incumbent upon the defendant to employ the said payment only in such a way as to take into account the gold clause and the pari passu clause, that is to say, only for the uniform partial payment of all bondholders according to the gold value of their claims.”\textsuperscript{52}

In other words, under different circumstances, the clause could be enforced as a promise of ratable payment, and could bind third parties, such as trustees.\textsuperscript{53} Yet the court also held that the trustee in this case—a passive conduit—could not deprive the sovereign debtor “of the practical possibility

\textsuperscript{50} AB Obligationsinteressenter Trial Court Judgment, supra note 2.

\textsuperscript{51} Id. at 4-5.

\textsuperscript{52} Id. at 3.

\textsuperscript{53} The court seemed to envision a situation where Germany would send a lump sum, short of the total owed, to the BIS with no instructions as to its distribution. Separately, it observed that the case might have come out differently “if the bondholders also had a claim to equal treatment inter se – a contention which has not been made.” Id. at 4. The canton appellate court addressed inter-creditor liability in dicta.
… of departing … vis-à-vis a section of the bondholders, from the agreements concluded.”\textsuperscript{54} Put differently, it was Germany’s prerogative to discriminate in breach of its bond contract. As a practical matter, the BIS (and, implicitly, the court) could do nothing about it.

\textbf{B. First Appeal}

The Court of Appeal for Basel-Stadt began by affirming the trial court’s application of Swiss law.\textsuperscript{55} The appeals court then focused on the BIS’s duties, analogizing to “the bailee holding a pledge … the representative of creditors … and the testamentary executor.”\textsuperscript{56} While it did not use the term “paying agent,” the court ruled that the BIS’s primary task was to move payments, and only “as far as possible” to see to the performance of the bond terms. The court also saw “no reason” to suppose that the BIS would, “particularly without special remuneration—... undertake a further duty to make a decision as to the validity of the Reich’s attitude … not manifestly unjustified…” (emphasis in the original).\textsuperscript{57}

Moreover, by describing the Young Loan bonds as “independent claims against the Reich,” issued in the form of “self-contained” bearer securities, the appeals court seemed to foreclose pooling and redistribution by the trustee across tranches. This description created a limited opening for payment discrimination: “the debtor who owes more than one debt may determine how his payments are to be appropriated … if consistent with the basic contract.”

Thus if Germany had valid reasons to pay the French but not the Swedes,\textsuperscript{58} it could. But even if Germany were wrong, the BIS could not intervene at payment, since avoiding potential pari passu breach against the Swedes would have certainly breached the gold clause against the French (paying less than the nominal value of their coupon).\textsuperscript{59} The court thus validated the BIS’s decision to follow instructions, rather than make an independent choice between the two violations.

Of the three opinions in \textit{AB Obligationsinteressenter}, the Court of Appeals offered the most elaborate reading of the pari passu clause in the Young Loan bonds, and possible remedies for its breach:

\begin{quote}
The stipulation in the bonds that all issues ‘rank pari passu in all respects’ means primarily that in the event of partial payments by the Reich, caused by diminished solvency, each
\end{quote}

\begin{itemize}
\item \textsuperscript{54} It noted tartly that “a uniform ‘Anglo-Saxon’ law, such as the defendant endeavors to invoke, does not exist.” \textit{Id.}
\item \textsuperscript{55} \textit{AB Obligationsinteressenter} Appeals Court Judgment, \textit{supra} note 2, at 6.
\item \textsuperscript{56} \textit{Id.} at 7.
\item \textsuperscript{57} \textit{Id.} at 8.
\item \textsuperscript{58} For example, if it were excused by supervening legislation abrogating gold indexation.
\item \textsuperscript{59} \textit{AB Obligationsinteressenter} Appeals Court Judgment, \textit{supra} note 2, at 7-8.
\end{itemize}
bond is entitled to an equal share and no issues can claim to be in a privileged class …
Such a right would be conceivable as a reciprocal claim between the bondholders, or as a
claim of the bondholders against the Reich…  

“Rank pari passu” according to this court meant that, if Germany had been short on funds, it would
have had to pay all the Young Loan creditors ratably. Moreover, bondholders could sue one
another to recover disproportionate payment, although the lower court reported that no reciprocal
claims had been brought. Had the Swedish creditors successfully sued Germany (presumably
shielded by immunity) or the French and Dutch bondholders, then the BIS could ignore Germany’s
distribution instructions. However, the BIS could intervene on its own only if Germany sought to
discriminate on “manifestly untenable grounds” (emphasis in the original), for example, cutting
off creditors from countries “hostile to Germany.”  

Like the trial court, the canton court of appeal held that the Young Loan trustee fulfilled its duties by making feckless protests while doing as it was told by Germany.

C. Second Appeal

On its second and final appeal, AB Obligationsinteressenter argued before the highest federal court
in Switzerland that the lower courts had (i) misconstrued the concept of trust under the Young
Loan agreements, (ii) wrongly held that the bonds represented independent claims against
Germany, (iii) misapplied the “manifestly unfounded” standard, discussed above, to Germany’s
gold clause repudiation, (iv) wrongly concluded that the BIS could and did interpret the bond
contracts in good faith, and (v) wrongly assumed that the BIS was not compensated for considering
the validity of Germany’s gold clause claims. The BIS, well-served by Swiss law so far, meanwhile had “rightly abandoned” its claim to “Anglo-Saxon” governing law.

The federal court’s holding was anticlimactic. Like the two canton courts, it held that the bondholders stood in direct contractual relationship to the German Reich, and that the BIS was a
“mere intermediary between creditor and debtor,” obliged to carry out Germany’s instructions
unless they were “manifestly untenable”—and upheld the appellate court judgment.

60 Id.
61 Id. at 8.
62 ABObligationsinteressenter Federal Court Judgment, supra note 2. At least in the League of Nations translation,
the terms “manifestly unjustified,” “manifestly untenable,” and “manifestly unfounded” are used interchangeably.
63 Id. at 11.
64 Id.
65 Id. at 13.
Although the court refused to apply the *pari passu* clause in the Young Loan bonds, it did spin out counterfactual scenarios where the clause would come into play. For example, had Germany owed a single global debt to the BIS, with creditors holding claims against the BIS, “the so-called *pari passu* clause, on which the plaintiff relies, could only represent an obligation of the defendant [BIS],” and discrimination “would be out of the question.”66 In contrast, on the facts of this case “the *pari passu* clause, like the gold clause, represent[ed] a contractual obligation of the Reich....,” and did not bind the BIS directly. The BIS was thus bound to follow Germany’s payment instructions even if they were “indisputably” in breach of the *pari passu* clause:

> [T]he reasons given by the German Reich for its course of action—which, it must be conceded, indisputably infringed both the gold clause and the *pari passu* clause—show that this measure was intended as a reprisal devised from the point of view of international law against those States which for their part had gone off the gold standard and which, disregarding obligations provided with gold clauses, had prejudiced the interests of nationals of the German Reich. It was not for the defendant to decide whether such a right of reprisal appertained to the German Reich or whether the non-observance of the provisions of the contract was impermissible even from the point of view of international law. In the absence of a clear and unmistakable provision to that effect in the loan contract, it cannot be assumed that there was any intention to grant the defendant so extensive authority, far exceeding the functions of a paying agent and a representative of the bondholders. It had to suffice for the defendant that the standpoint of the Reich was not manifestly untenable.67

In other words, Germany had breached the *pari passu* clause to get back at the countries that went off the gold standard and harmed its trade. Because this course of action could be characterized as reprisals and excused under international law, the trustee could do nothing about it.

**D. The Fallout**

The Swiss courts were surely caught up in the complex political economy forces of the day. Hitler was gaining power on the platform of repudiating what had been left of the post-war settlement. The BIS embodied an effort to salvage the financial core of that settlement. By the time of the Swedish lawsuit, reparations were dead, international clearing arrangements were fragmenting, and the Dawes loan trustees had blocked German revenues to fierce protests from the Nazi

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66 *Id.* at 12.

67 *Id.* at 13.
authorities. Attempts to depoliticize reparations with private finance and technocratic expertise might have looked fanciful in retrospect.

An in-depth analysis of how all these forces affected the Swiss courts is far beyond the scope of this article. The range of possible motives is relevant, however, for evaluating the courts’ reasoning and the implications of the case today. The judges might have been wary of fueling political conflict, simultaneously worried about antagonizing Germany, the Allied governments, and the prominent financiers who did business with Swiss banks. They might have felt bound to protect the BIS, a new international institution reluctantly entrusted to their jurisdiction: Switzerland was a rising financial power that had beat out London in a diplomatic compromise that emphasized neutrality and expertise. This case was a high-profile test of Swiss courts’ legal and financial sophistication in construing complex Anglo-American-style contracts, as well as their ability to navigate political landmines.

According to the cognoscenti, the judges failed miserably. The English barrister who wrote a 1937 memorandum for the League Committee, identifying “leading difficulties” in sovereign debt practice, put the courts’ analysis in *AB Obligationsinteressenter* at the very top of his list, several pages ahead of “inability to enforce securities” (states reneging on revenue pledges). He observed, “It was hardly necessary to point out that the … decision is completely at variance with the whole conception of trusteeship as understood in England.” A German expert on trusts, who was also an English barrister, advanced similar criticisms, arguing that the opinions were symptomatic of a broader failure by continental European lawyers to understand the common-law concept of trust. The League Committee experts generally agreed that the Swiss courts embarrassed themselves by

68 The trustees’ actions to freeze German revenues made headlines around the world in the summer of 1934. See e.g., Dawes Loan. Germany’s Breach with Trustees, THE SYDNEY MORNING HERALD (Australia), July 18, 1934, p. 18, Dawes Trustees Protect Holders: German Revenues Withheld for Benefit of Foreign Bond Holders, THE SPARTANBURG HERALD (South Carolina), July 18, 1934, p. 10; German Money Tied Up: Trustees of Dawes Loans in Move to Protect Payments; Trickery is Charged by Defiant Nazis, THE NEW LONDON DAY (Connecticut), July 17, 1934, p. 1.


70 The BIS’s location was heavily negotiated at its founding. Some of the negotiators felt strongly that the bank should reside in London, a global financial center; however, Switzerland was chosen as a rising financial market and a more neutral host. Basel made sense in part for its proximity to the borders of three countries, and good rail links. TONIOLO, *supra* note 26 at 44; David J. Bederman, *The Bank for International Settlements and the Debt Crisis*, 6 BERKELEY J. INT’L LAW 92, 98 (1988); Kugler et al., *supra* note 33 at 23.


72 FELIX WEISER, *supra* note 49 (Weiser also sent reports and corresponded extensively with the secretariat for the League Committee).
conflating trustees with paying agents and concluding that the BIS had to follow German directions in breach of the pari passu clause. Instead, they said, the proper course was for the BIS as trustee to seek advice from the courts upon receiving an incomplete payment.

In light of this expert debate, the League Committee recommended in its final report that the institution of bond trustee be specified more clearly in sovereigns’ contracts, along with governing law. The report also suggested renaming the office of bond trustee, to avoid lulling creditors into a false sense of security where the “trustee” had limited capacity (and perhaps limited incentives) to protect them before national courts.73

A leading 20th century treatise on sovereign debt, published in 1951, devoted most of the chapter on trustees to criticizing AB Obligationsinteressenter—fifteen years on, still the only definitive judicial treatment of sovereign bond trustees on the European continent.74 The author, Yale law professor Edwin Borchard, noted in passing that Germany’s payment scheme “was violative of the pari passu as well as of the gold value clauses of the loan contract,”75 but otherwise focused on criticizing the Swiss judges’ confusion of trustees and paying agents (citing League Committee experts at length).

Despite the criticism, no one seriously suggested that the BIS should have redistributed the money it got from Germany pro rata among the Young Loan tranches, or that another court would have ordered it to do so. Borchard, in a footnote at the end of the chapter on trustees, cited the foremost French jurist on the League Committee for the proposition that,

The practical result of the [Swiss] decision must be approved since the question whether payment was due on a gold basis “really concerns the debtor and the bondholders” and should not be left to a decision by the trustee.76

The quarrel then was all about the reasoning. In the eyes of the critics, the proper course of action for the BIS was to seek a court ruling before making the payments, instead of waiting to be sued after; however, by the time the trial court got the case, it was too late. In all likelihood, had the BIS done what the critics suggested, a court following their recommendations would have endorsed

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74 EDWIN BORCHARD, STATE INSOLVENCY AND FOREIGN BONDHOLDERS 52 (1951). With just a whiff of faux sadness, Borchard observed that “[t]hree successive Swiss courts labored with the proper solution of the question, only to give evidence of the profound confusion created by the attempt to transplant the institution of the loan trust in the unfavorable soil of Continental law.” Id.

75 Id.

76 Id. at 62 n.58 (citing Jules Basdevant, who served on the League committee and was, at the time of Borchard’s publication, President of the International Court of Justice).
what the BIS did anyway. On the other hand, Anglo-American style bond trustees might have taken root sooner in Europe.

The BIS and the Swiss judges must have known about the law and practice of seeking judicial guidance for trustees in common law jurisdictions, but decided not to follow it. The trial court in Basel explained its refusal to apply English law partly by highlighting “the impossibility of having recourse, in cases of doubt, to a so-called court of equity, which might give the defendant [BIS] guidance.” The BIS’s Annual Report says that it had sought legal advice after receiving insufficient funds from Germany to pay the bondholders. Moreover, the difficulty of translating the common-law concept of trust in civil law systems had been debated by elite commentators at the time. In Switzerland, there had been a handful of published decisions grappling with the problem long before the German default. As the gold standard and international clearing arrangements fell apart in the early 1930s, bondholders filed lawsuits against trustees in several countries, although AB Obligationsinteressenter appears to be the only reported case involving sovereign bonds. Against this background, it is hard to believe that the Swiss courts were simply ignorant. Rather, they might have elected to sacrifice analytical purity to reach the only politically viable outcome—shielding the BIS from bondholders and politicians—while trying to reassure the new bank that it did not need English law or the English courts to fulfil its mandate.

IV. Epilogue—Interpretation Marches On

German debts were renegotiated after World War II, with the new terms set by the London Agreement of 1953 that also effected unprecedented debt relief. Germany’s residual obligations

77 AB Obligationsinteressenter Trial Court Judgment, supra note 2 at 2.

78 BIS FOURTH ANNUAL REPORT, supra note 30 at 41. Given the prominence of English and U.S. financiers at the founding of the BIS, and the BIS’s insistence on applying “Anglo-American law” at the first trial, it seems likely that English lawyers were part of the decision-making process. See also BIS FIFTH ANNUAL REPORT, APRIL 1, 1934-MARCH 31, 1935 (May 13, 1935) at 59-60 (describing the payment disruptions, the bilateral clearing arrangements, the initial lawsuit by “[a] bondholder” and the ruling in its favor by the trial court).

79 See e.g., WEISER, supra note 49; THEVENOZ, supra note 49.

80 A 1937 League Committee memorandum noted that “[a]ctions have been brought by bondholders against one or more of the Trustees in France, the United States, Switzerland, Belgium and Holland, claiming in each case that the Trustee should have made payments on a gold basis out of the funds at their disposal.” Fachiri Memorandum, supra note 71. According to Borchard, writing in 1951, AB Obligationsinteressenter was the only reported case against a trustee for sovereign bonds. BORCHARD, supra note 74 at 60-61. An Austrian national holding a gold-indexed U.S. dollar bond issued by the Austrian government in 1930 challenged a nominal dollar payment directly, suing the government in an Austrian court in 1933. BIS FOURTH ANNUAL REPORT, supra note 30 at 44. The case went up to the highest court in Austria, where the government won in 1936. Commentators later debated whether the creditor could next sue the trustee, to force ratable distribution among different tranches. Borchard, supra note 74 at 61.

81 Among the restructured debts, the Young Loan was extended until 1980, and the Kreuger Match Loan until 1994. The Lee, Higginson Loan, originally made for two years, would be replaced with a new two-year German
to the Young Loan bondholders were no longer indexed to gold, but rather provided for a fixed relationship among the currencies of denomination. In the event that any of the currencies declined by more than five percent relative to another, the bondholders of the affected tranche would be compensated by reference to the value of the stronger currencies. The agreement also contained a broad prohibition on discrimination among bondholders.

In 1971, Belgium, France, Switzerland, the United Kingdom and the United States instituted proceedings against Germany before the seven-person arbitral tribunal established under the London Agreement. They argued that the two revaluations of the Deutschemark in the 1960s meant that their currencies had lost value relative to the mark, giving their bondholders a right to compensation under the agreement.


The Young Loan/London Agreement Arbitration, supra note 7. The exchange rate protection mechanism, found in Annex I of the London Agreement, required Germany to index its payments to the value of “the least depreciated currency,” measured by reference to the exchange rates in 1952:

Should the rates of exchange applying to any of the currencies mentioned in the text of this Bond on 1st August, 1952, thereafter change to the extent of 5 per cent or more, the instalments due after that date, while still being made in French Francs, shall be calculated on the basis of the least depreciated currency (in relation to the rate of exchange current on 1st August, 1952) reconverted into French Francs at the rate of exchange current when the payment in question becomes due.

The provision is reproduced in full below:

PROHIBITION OF DISCRIMINATORY TREATMENT
The Federal Republic of Germany will not permit, nor will the creditor countries seek from the Federal Republic of Germany, either in the fulfilment of terms of settlement in accordance with the present Agreement and the Annexes thereto or otherwise, any discrimination or preferential treatment among the different categories of debts or as regards the currencies in which debts are to be paid or in any other respect. Differences in the treatment of different categories of debts resulting from settlement in accordance with the provisions of the present Agreement and the Annexes thereto shall not be considered discrimination or preferential treatment.

The London Agreement, Art. 8, supra note 81.

The arbitration is the subject of several articles, and is mentioned in at least one book that also discusses the pari passu litigation against Peru. MICHAEL WAIBEL, SOVEREIGN DEFAULTS BEFORE INTERNATIONAL COURTS AND TRIBUNALS (2011). It also attracted some of the leading legal lights of the day, including Professor Francois Gianviti, who later served as General Counsel of the International Monetary Fund during the pari passu enforcement
exchange rate protection mechanism in the London Agreement against the background of Germany’s general obligation not to discriminate among its creditors,\textsuperscript{85} and the same pari passu clause in the Young Loan bonds that had been previously interpreted in \textit{AB Obligationsinteressenter}.

The complaining countries insisted that equality among creditors in different currency tranches was central to the object and purpose of the London Agreement, preserved from the original Young Loan.\textsuperscript{86} They argued that in economic terms, a rise in the Deutschemark was equivalent to a fall in all other currencies relative to the Deutschemark, which should trigger the exchange rate protection mechanism. Without it, payments on Deutschemark-denominated bonds would be worth more than the rest, which would be tantamount to impermissible discrimination.

The panel split 4:3, in Germany’s favor. The majority held that exchange rate protection in the agreement addressed devaluation but not revaluation, just like the 1930 gold clause, and that payments consistent with this mechanism could not be prohibited discrimination. Along the way, the tribunal considered the Young Loan pari passu clause:

\textit{[T]he prohibition of discrimination in Article 8 of the LDA [London Debt Agreement] in the special context now before the Tribunal has no bearing beyond that of the pari passu clause incorporated in Article II of the General Bond. This pari passu clause does not cover the eventuality of "inequality in outcome", i.e. that of unequally high redemption payments.}

The customary function of a pari passu clause in loan contracts is, in the interest of the bondholders, to prevent the borrower from entering into new, additional obligations which then rank before the bonded debt itself. The intention is to prevent, for example, a creditor being put in a worse position in the servicing of loans than another with regard to the amount paid, if the borrower is unable to meet all claims fully and uniformly at the same time. [Internal citation omitted.]

The decisive purpose of a pari passu clause, therefore, is to guarantee a specific, an equal ranking for loans furnished with such a clause. Article II of the General Bond accordingly states—in the English text, which, according to Article III of the Bond, shall prevail—that the different issues in the various currencies "shall rank pari passu in all respects irrespective of date or place of issue or otherwise". The article seeks to guarantee that, e.g., diminished solvency or even temporary insolvency on the part of the borrower will affect each bondholder to the same degree. In particular, the specific intention was to prevent the

\textsuperscript{85} The general anti-discrimination provision specifically carved out differential treatment permitted under the London Agreement itself. London Agreement, Art. 8, \textit{supra} note 83.

\textsuperscript{86} Bathurst, \textit{supra} note 84 at 542.
German Reich, in the event of difficulties with interest payments or redemption, from making payment un-equally as between the various tranches, with the consequence that, for example, bonds expressed in Italian lire or in Belgian francs could be paid in full while those in dollars or sterling were not serviced at all. Cf. the judgment of the Swiss Bundesgericht of 25 May 1936 … [Swiss federal court judgment in AB Obligationsinteressenter, citation omitted]87

Although it purports to state the “customary function” and “decisive purpose” of pari passu, the arbitral decision is anything but straightforward. The opinion starts by warning that the clause does not guarantee absolute equality of outcome, but rather protects creditors from involuntary subordination to new debt.88 But it goes on to reaffirm the broad objective of ratable payment in financial distress: “the specific intention was to prevent the German Reich, in the event of difficulties with interest payments or redemption, from making payment un-equally” (emphasis added). In all, the majority of arbitrators seemed to suggest that pari passu generally meant ranking, but with the goal of ratable payment in financial distress, when the debtor’s obligation to pay is uncontested. Recall that in AB Obligationsinteressenter, it was Germany’s possible right of reprisal that required the BIS to abstain; in the London Agreement arbitration, it was the exchange rate protection mechanism that rendered pari passu inoperable. This seems to be at odds with Argentina’s position in the NML case, where it argued that it did not breach the pari passu clause because its legal obligation to the holdouts remained unchallenged throughout its lengthy period of nonpayment, justified primarily by economic distress.

V. Implications beyond NML v. Argentina

As this article goes to print, a new government in Argentina is on the verge of settling the case that turned pari passu into a super-potent sovereign debt enforcement weapon. The judge who had issued the injunctions has indicated that he would lift them to facilitate settlement, which would deprive the remaining holdout creditors of their biggest bargaining chip.89 Nonetheless, for all but the immediate protagonists in that case, the ending changes little. The ratable payment interpretation of pari passu remains the law in New York, as does the possibility of an injunction

87 Young Loan/London Agreement Arbitration, supra note 7 at 101. The opinion essentially tracked Germany’s position, which “rejected the idea that the Young Loan’s pari passu clause was a means of creating fixed equality in payments on the bonds, since the clause was limited to giving each tranche equal rank or priority only in the event that Germany could not meet its full debt service for any reason.” Bathurst, supra note 84 (citing Germany’s Rejoinder in the Young Loan/London Agreement Arbitration at paras. 144-151 (internal citations omitted)).

88 Presumably this would happen before default. Cf. Declaration of Lord Peter Millett, K.G., P.C., in Red Pines LLC et al. v. Republic of Argentina, Case No. 14-cv-09427 (TPG) (February 12, 2016) (emphasizing the same ex ante early warning function of the clause). Buchheit and Pam, among others, correctly point out that such involuntary subordination is impermissible in most jurisdictions today. Supra note 6.

to enforce it. And although the courts are yet to rule on the meaning of the clause beyond the Second Circuit in the United States, the collateral effects of New York proceedings include new uncertainty about the meaning of *pari passu* in London, perhaps elsewhere. As it stands, the *pari passu* saga can easily spring back to life in other sovereign debt crises; Ukraine and Venezuela appear to be the most likely candidates at this writing.

In such a revival, *AB Obligationsinteressenter* and its progeny could be invoked to bolster the ratable payment interpretation, or at least testify to its plausibility. But should it be? On balance, probably not, for four reasons.

**First**, inasmuch as interpretation still tries to give contract terms a meaning that the parties had reason to know, *AB Obligationsinteressenter* seems beyond the pale. Attributing a 1936 Swiss interpretation of a 1930 German bond to contemporary sovereigns and their creditors would require some commonality of practice, context, or both. The legal, political, economic and institutional context of sovereign borrowing has changed drastically since the 1930s. Restrictive sovereign immunity has replaced absolute immunity, so that sovereigns can be sued directly in foreign courts. The gold standard is gone. Revenue pledges are rare, as is the practice of giving creditors control over revenue administration and putting countries in receivership. Governments do not openly deputize the likes of J.P. Morgan to coordinate national syndicates in long-term multi-currency bond offerings for friendly sovereigns. There is the International Monetary Fund for stabilization loans, multilateral development banks for reconstruction and development finance, and an elaborate infrastructure for bilateral foreign aid.

To be sure, some old practices persist, while many more have shaped modern finance, leaving marks like the *pari passu* clause behind. Governments still lean on big banks to manage international financial crises. Crises still bring discrimination between domestic and external

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90 For example, Argentina and certain creditors holding its English-law bonds have submitted warring declarations on the meaning of the clause in an attempt to convince U.S. judges of the likely interpretation of *pari passu* by an English court. See Declaration of Lord Phillips, *supra* note 5 and Declaration of Lord Millett, *supra* note 88.


92 It is worth pointing out that the dedicated revenue pledge in the Young Loan bonds turned out to be useless. When Germany suspended foreign exchange transfers for the Young Loan bonds in June of 1934, the BIS found it “impracticable to have recourse, for the fulfilment of the German Government’s obligations, to the collateral security in the form of the railway tax which is constituted in reichsmarks and relates to only two-thirds of the service of the Loan.” BIS Fifth Annual Report, April 1, 1934-March 31, 1935 (March 13, 1935) at 59.

93 See e.g., *Paul Blustein, The Chastening: Inside the Crisis That Rocked the Global Financial System and Humbled the IMF* (2001, 2003), at 175-205 (recounting Group of Seven initiative to coordinate their banks to maintain exposure to Korean banks).
creditors, though not so much among external creditors of different nationalities. Nonetheless, it would be a stretch to presume that creditors in 1990, 2000, or 2010 worried, or should have worried, about the same things as creditors in 1930. For all the questions of fairness and comparability prompted by contemporary holdouts’ demands for equal treatment between restructured and unrestructured bonds, at a more basic level, such demands only make sense in a world where the two kinds of bonds can trade side by side, without regard to their origins—not the Young Loan world.

The function of the pari passu clause in sovereign debt contracts probably changed several times over the course of the 20th century, even as it retained much of the wording and a broad equitable thrust. For example, it is unlikely that the pari passu clause in Article II of the Young Bond, litigated in AB Obligationsinteressenter was meant primarily as an anti-earmarking device (a purpose highlighted in the International Encyclopedia of Banking). Two other pari passu clauses in the same bonds specifically addressed revenue pledges, while Article II was phrased in much broader terms. Perhaps because the revenue pledges turned out to be useless when Germany defaulted on the Young Loan, neither the courts nor the arbitrators mention earmarking or collateral when they discuss pari passu. In contrast, the challenge of collective action among Germany’s creditors, and fears of discrimination based on currency, nationality and bilateral trade balances were at the forefront of everyone’s thinking at the time. With no high-profile court battles to anchor its meaning and function at every turn, pari passu could have meant “no earmarking” at one time, “pay everyone gold value” in 1936, and “pay everyone ratably, but only if you have no valid legal defense” in 1980.

Diplomatic accounts and League Committee files suggest that by 1930, the phrase “pari passu” had already become vernacular for somewhat elastic notions of inter-creditor equity. This general meaning stayed with the term in the Young Loan through the arbitration decades later, but was applied differently in a changed context. Absent evidence that modern-day drafters looked to a


95 See Wright, supra note 21 (discussing the principle of differentiation in applying the pari passu clause).

96 See GULATI AND SCOTT, supra note 6 at 111-138 (reporting different explanations for the origins of the pari passu clause in sovereign bonds advanced by transactional lawyers).

97 The pari passu promise in Paragraph II of the Young Loan is what the Bank of England Financial Market Law Committee (FMLC) has called “the internal limb” of the clause, whereby bonds in the same issue have equal ranking among themselves. Bank of England, Financial Market Law Committee Report, Issue 79: Pari Passu Clauses (2005) at 4.21. The FMLC suggests that the internal limb might (though need not necessarily) imply obligations beyond equal ranking, such as ratable payment. On the other hand, Swedish diplomats and financiers used pari passu rhetoric to secure payment on the Krueger Loan, in parallel with the Young Loan. The internal-external distinction becomes more muddled as one considers the web of transactions between Germany and its various creditors at the time. See notes 33-34 supra and accompanying text.
particular historical meaning and function—be it 1843, 1871, or 1936—courts should seek evidence of the parties’ intent closer to home.

Second, the Young Loan story adds to the oddly dismal record of the *pari passu* clause in sovereign debt. It seems to have done very few creditors much good, from its first known appearance in Mexico in 1843 through its starring role in Argentina since 2011, with the settlements in Peru and Congo as possible exceptions. Time and again, sovereigns promise “equal footing,” only to discriminate in distress. It does not appear that creditors use the *pari passu* covenant as an early warning of distress, since sovereigns do not resort to formal subordination on the eve of default. Nor have creditors been successful at stopping selective nonpayment. Sovereigns might well discriminate even more without the clause, but different courts’ visible struggles with the meaning and application of equality in sovereign debt should give judges and contract drafters pause.

Argentina illustrates. If the goal of its *pari passu* clause was ratable payment, it failed miserably long before the latest controversy. 98 The *pari passu* injunction was then supposed to promote settlement. Instead, it dragged U.S. courts into a five-year standoff with a government that made fighting U.S. courts a political cause at home and abroad, drew a stream of invective and prompted a $28 billion default, affecting scores of market bystanders and ordinary Argentines. 99 The court and the departed government of President Cristina Fernandez de Kirchner in Argentina found themselves boxed in by their respective reputational commitments. It seems improbable that the old government would have changed course had the injunction stayed in place longer, just as it is implausible that a ruling against the BIS in *AB Obligationsinteressenter* would have made Germany pay its creditors ratably. Unless the *pari passu* clause is to be viewed as a ratchet to produce regime change (a big question best left for another day), it is not useful enough, and too dangerous to keep in sovereign debt contracts.

Since the first successful use of *pari passu* as an enforcement device by Elliott Associates against Peru in 2000, the academic debate has quietly conflated the meaning and the function of the clause. 100 The clause could not mean ratable payment because it simply could not work as ratable payment where a sovereign debtor was involved, went the argument. *AB Obligationsinteressenter* suggests that the ratable payment meaning is perfectly plausible; combined with *NML v. Argentina*, it also suggests that specific enforcement can be both fruitless and damaging. For all its clunky

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98 See e.g., Gelpern & Setser, supra note 94.

99 Announcing his intention to lift the *pari passu* injunctions, the U.S. Federal District Judge observed, “Vacating the injunctions would serve the public interest by ceasing the collateral effects they have on third parties. The most notable third parties affected by the injunctions are the exchange bondholders. But there are others, too: the financial intermediaries that the Republic engages to help it pay the exchange bondholders; the FAA bondholders who favor settlement but who are not parties to every single case; and the Argentine people generally.” See Indicative Ruling, supra note 10. See also Weidemaier & Gelpern, supra note 4 (arguing that injunctions in sovereign debt litigation operate through third parties and backfire on the court).

reasoning, the decision in *AB Obligationsinteressenter* only harmed the law of trusts in Europe. *NML v. Argentina* harmed vastly more banks, bondholders, and ordinary citizens than it helped—and backfired on the court by demonstrating its futility. This is an argument against overinvesting in construction. As one English court observed,

> [T]he nature of the relief sought generally… is directed towards the coercion of third parties rather than securing immediate compliance by the defendant. Because I regard this last point as determinative, I regard it as unnecessary to attempt any analysis of the pari passu clause.101

Meanwhile, *pari passu* will continue to challenge contract drafters. On several occasions, financial industry working groups and academic experts have argued for removing the clause from sovereign bonds, but have run into staunch resistance on the part of the creditors, whose response is usually “keep it just in case.” The latest industry consensus model of the *pari passu* clause narrows its meaning to ranking, and expressly excludes ratable payment102—which ensures that it would never be used (governments do not subordinate when they can simply not pay). Yet market insistence on retaining the clause in sovereign bonds should not be dismissed as mindless risk-aversion or a symptom of agency problems. It channels perennial, acute, and ever-changing concerns about inter-creditor equity in sovereign debt, which were justified in the 1930s and remain justified today. However, drafters are yet to find a workable term to address equity in general. Like the Young Loan, modern bond contracts contain multiple proxies for it.

**Third,** the time devoted to drafting and interpreting the phrase *pari passu* is better spent on reconsidering the institution of trustee and the payment mechanics of sovereign bonds. Market structures, such as stock exchanges, payment and clearing systems, have long filled the gaps left by purely judicial enforcement and reputational sanctions in sovereign debt.103 By controlling market access and fund transfers, they can exert meaningful pressure on immune sovereigns—and are tempting to commandeer in the name of judicial enforcement. If payment and clearing utilities are to be deployed to make sovereigns pay their debts, at a minimum, it should not be done *ad hoc* for the benefit of individual creditors, but as part of a coherent framework to guide the courts and


102 Leland Goss, *NML v. Argentina: The Borrower, the Banker and the Lawyer—Contract Reform at a Snail’s Pace,* 9 CAP. MKTS. L.J. 287, 289–290 (2014) (describing proposals to eliminate the *pari passu* clause and the new industry standard). ICMA Model Clause (English Law), August 29, 2014: “The Notes are the direct, unconditional and unsecured obligations of the Issuer and will rank *pari passu*, without preference among themselves, with all other unsecured External Indebtedness of the Issuer, from time to time outstanding, *provided, however,* that the Issuer shall have no obligation to effect equal or ratable payment(s) at any time with respect to any such other External Indebtedness and, in particular, shall have no obligation to pay other External Indebtedness at the same time or as a condition of paying sums due on the Notes and vice versa.”

shield essential market infrastructure. Until then, payment and clearing systems should be immune from injunctions whose sole purpose is individual debt collection, as in *NML v. Argentina*.*¹⁰⁴*

Bond trustees stand between the sovereign debtor and the bondholders, and make an attractive enforcement target—as illustrated in *AB Obligationsinteressenter*. However, as that case shows, they are ill-equipped and poorly incentivized to represent bondholders. They are at once too rigid—for example, lacking authority to engage in debt restructuring even when it would bolster bondholders’ recovery—and too lax, too reluctant to sue defaulting debtors. This problem is not unique to sovereign bonds,*¹⁰⁵* but it is made worse in sovereign bonds owing to a combination of debtor immunity and the absence of bankruptcy. The League Committee and later scholars, notably Borchard, commented on this problem in the middle of the 20th century.

Bond trustees’ unwillingness to pursue aggressive enforcement strategies has been the subject of recent lawsuits involving Ecuador and Argentina. Sovereign bond contracts typically require at least 25% of all bondholders to instruct the trustee to sue; they must also indemnify the trustee to its satisfaction against litigation costs. From the debtor’s perspective, this makes trustees a near-impermeable barrier to litigation—and useful as such. From the bondholder’s perspective, this may make trustees useless. For their part, the courts in the 21st century appear to be as confused as the courts in 1936 about the trustee’s functions.*¹⁰⁶* Specifying a more coherent and meaningful role for trustees in coordinating sovereign debt restructuring in advance (presumably, in exchange for substantial new compensation) seems in order.

*Fourth,* the fact that both *AB Obligationsinteressenter* and *NML v. Argentina* were followed by policy interventions to reform sovereign debt contracts is significant. The League of Nations considered contract and institutional reform in direct response to the Swiss case, advocating for a new role and a new name for bond trustees, proposing model language on choice of law, and dispute resolution terms in sovereign bonds.*¹⁰⁷* While *NML v. Argentina* was still being appealed through the U.S. court system, a group of officials from wealthy and middle income countries,

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¹⁰⁶ At a hearing before the U.S. Court of Appeals for the Second Circuit, a lengthy exchange over the compensation mechanism for the bond trustee (standard in the market at the time) came close to declaring the trustee to be an agent of the Argentina, either in parallel with or instead of representing the bondholders. Transcript of Oral Argument, at 105-107, NML Capital Ltd. v. Republic of Argentina, No. 12-105-CV(L) (Feb. 27, 2013).

¹⁰⁷ *Supra* note 73.
together with the IMF and a leading market association, proposed new \textit{pari passu} and creditor collective action clauses designed to insulate sovereigns from \textit{NML}-style enforcement in the future. The modern-day reform effort has been remarkably successful, especially compared to the limited impact of its interwar precursor.\footnote{Weidemaier, et al. \textit{supra} note 11 (reporting on the interwar contract reforms); Chanda DeLong and Nikita Aggarwal, \textit{Strengthening the Contractual Framework for Sovereign Debt Restructuring—the IMF’s Perspective}, 11 Cap. Markets L.J. 25 (2016) (reporting on recent changes in sovereign bond contracts in line with IMF and market association recommendations).}

The broader lesson is not confined to reform substance or the fortunes of any particular initiative. It is rather to point out that, at least by 2016, a shock involving sovereign debt contracts almost inevitably invited concerted policy intervention in the contracting process—as did the European crisis in 2010, Argentina’s default in 2001, the Mexican “Tequila” crisis in 1995, and the Third World Debt Crisis in the 1980s. This phenomenon puts both contract drafters and the courts in an implicit dialogue with international policy officials. Sovereign debt contracts come to operate in the shadow of intervention. As a result, they might be properly seen as a product of three-way negotiation among debtors, creditors, and the leading economic powers and international financial institutions of the day.\footnote{Jeremy Bulow & Kenneth Rogoff, \textit{Multilateral Negotiations for Rescheduling Developing Country Debt: A Bargaining Theoretic Framework}, 35 \textit{Int’l Monetary Fund Staff Papers} 644 (1988).} Faced with this reality, courts can either try to accommodate policymakers, for example, seeking their input and deferring to it—or position themselves as a check on or counterweight to the policy position. While in-depth consideration of policy intervention in sovereign debt contracts must be left for another project, it is worth noting that in \textit{AB Obligationsinteressenter}, the courts went out of their way to protect the BIS and steer clear of open conflict with governments, while in the later stages of \textit{NML v. Argentina}, they consistently rejected U.S. and other governments’ arguments.

\section*{Conclusions}

Contract paleontology is addictive fun. It is easy to get carried away in the archives, especially when one is looking for two magic words in Latin. When they pop up on the yellowed pages and purple mimeos, the paleontologist’s heart skips a beat—maybe this time, the true meaning of \textit{pari passu} will be revealed. The story of the Swiss litigation over the German Young Loan in the 1930s and its arbitral post script in the 1970s starts a new quest. But to what end?

The implications of the Swiss \textit{pari passu} litigation for contract paleontology, and for contract interpretation more broadly, could be more interesting than its application to \textit{NML v. Argentina}. As a viable field of study, paleontology needs a theory for giving voice to historical meanings of
private contracts. The questions might be similar to those raised in the debates about distant authorship and boilerplate, but made more complex by the extreme temporal gap between the life of the contract fossil and its present use. What weight, if any, should we give to the original drafters’ intent? And how do we know, in the global, decentralized sphere of financial contracting, that any given drafter was the true progenitor of today’s clause?110 Should we search for the intent of all the original contracting parties, or just those that cared enough to archive their most persuasive thoughts? Should highly deliberate “off-label” adoption of an old clause change its meaning? How to assess the relevant context? Is it necessary to trace the entire evolution of the clause, or merely take two snapshots, then and now? What role for the Stone Age courts, Bronze Age politicians, Neanderthal law scholars?

Finally, should sovereign contract fossils be treated differently? Then and now, sovereign debt contracts are extraordinarily hard to enforce, politically fraught, and prone to extreme spillovers. They live in the shadow of policy intervention, never quite as autonomous as the dealings of private parties. Perhaps the Swiss courts chose political accommodation over analytical clarity in the 1930s. U.S. Federal courts professed to do the opposite in 2010s, when they took an ambiguous clause to its logical limit, and issued injunctions to enforce it. Might paleontology help fashion a more principled tradeoff? Or will it simply feed new origin myths that let today’s drafters and courts off the hook in solving today’s problems?111

At least for now, extreme caution is in order while dealing with fossils. In some cases—as with the pari passu clause—it might make sense to refrain from construing an obscure contract term altogether, where all plausible interpretations yield empty or destructive outcomes, including for the courts themselves. In sovereign debt, where the limits of court intervention are so palpable, reform should instead focus on institutions that continuously shape governments’ participation in the capital markets as a practical matter, such as trustees and payment systems. Meanwhile, paleontologists and reformers alike must keep in mind the public and contingent character of sovereign debt contracts. Even without statutory bankruptcy, sovereign debt crises never unfold organically.

Policy intervention in crisis and official attempts to shape private contracts have been a feature of the sovereign debt markets going back at least to the 1930s. Once upon a time, pari passu might have meant ratable payment. Today, it means anything but ratable payment—until it morphs into something else entirely, as yet unknown.


111 Mark C. Weidemaier et al., supra note 6.
Appendix I

Argentina’s *Pari Passu* Clause

(c) The Securities will constitute (except as provided in Section 11 below) direct, unconditional, unsecured and unsubordinated obligations of the Republic and shall at all times rank pari passu and without any preference among themselves. The payment obligations of the Republic under the Securities shall at all times rank at least equally with all its other present and future unsecured and unsubordinated External Indebtedness (as defined in this Agreement).

Fiscal Agency Agreement dated as of October 19, 1994, between the Republic of Argentina and Banker’s Trust Company
Appendix II

Pari Passu and Related Terms in the General Bond Instrument for German Government International (Young) 5 ½% Loan 1930
June 10, 1930, at 112 L.N.T.S. 237.

Whereas:

(a) Under and by virtue of an Agreement (hereinafter called “The Hague Agreement”)

... the German Government has undertaken to pay to the Bank for International Settlements for the benefit of the other parties to The Hague Agreement (in addition to the postpayable annuities mentioned therein) unconditional and non-postpayable annuities (hereinafter called “the unconditional annuities”) of Six Hundred and Twelve Million Reichsmarks per annum during the period therein specified and in respect of both the said postpayable annuities and the unconditional annuities has constituted as collateral guarantee a special tax payable to the German Government by the German Railway Company and has undertaken subject to the charge securing the German External Loan 1934 to reserve free from any charge securing any loan or credit in priority to or pari passu with the said postpayable and unconditional annuities the proceeds of the Customs, the Tobacco Taxes, the Beer Tax and the Tax on Spirits (Administration of the Monopoly) and such additional Revenues as may be required by the Bank for International Settlements pursuant to the conditions contained in The Hague Agreement.

II

The Reichsmark Bonds, the Dollar Bonds, the Belgé Bonds, the Franc Bonds, the Sterling Bonds, the Florin Bonds, the Lira Bonds, the Krone Bonds and the Swiss Franc Bonds shall be payable to Bearers, and shall rank pari passu in all respects irrespective of date or place of issue or otherwise.

IX.

For the purpose of providing the amounts required for paying or providing for interest and redemption and all other monies payable by the German Government under these presents and the Bonds of the Loan (hereinafter called the service monies) there shall in accordance with the provisions of The Hague Agreements be paid to the Bank by the German Government in each year ending the first day of June:

(a) As part of the unconditional annuities which are the direct and unconditional obligation of the German Government, sure in Reichsmarks, Dollars, Belges, Francs, Sterling, Florins, Lire, Kronor and Swiss Francs respectively equal to two-thirds of the amounts required for the service monies in respect of the Reichsmark Bonds, Dollar Bonds, Belgé Bonds, Franc Bonds, Sterling Bonds, Florin Bonds, Lira Bonds, Kronor Bonds and Swiss Franc Bonds respectively and the said payments forming part of the unconditional annuities shall operate to discharge the German Government to the extent of their equivalent in Reichsmarks calculated at the average of the middle rates prevailing on the Berlin Bourse during the fifteen days preceding the date hereinafter fixed for payment of each monthly installment from its obligation to pay the unconditional annuities to the Bank for International Settlements pursuant to The Hague Agreement — the not yet mobilized portions of the unconditional annuities ranking pari passu with the payments provided for in this paragraph.

XII.

Pursuant to The Hague Agreement and in particular subject to the charge securing the German External Loan 1934 the German Government shall not while any part of the unconditional or the said postpayable annuities remains outstanding create without the consent of the Bank for International Settlements acting in accordance with The Hague Agreement any mortgage or charge upon the Customs, the Tobacco Taxes, the Beer Tax or the Tax on Spirits (Administration of the Monopoly) to secure any other loan or credit of the German Government in priority to or pari passu with the said annuities.

XIV.

Nothing in these presents shall prevent further loans or bonds issued to mobilise the unconditional annuities ranking pari passu as to payment with the Bonds of the present Loan.