Financial Markets Law Committee ("FMLC")

Sovereign Debt Scoping Forum

Date: Monday 10 December
Time: 12.00pm to 1.30pm

In Attendance:

Francis Fitzherbert-Brockholes (Chair)  White & Case LLP
Ian Clark  White & Case LLP
Robert Gray
Leland Goss  ICMA
Jim Ho  Cleary Gottlieb Steen & Hamilton LLP
Rosa Lastra  Queen Mary University of London
Rodrigo Olivares-Caminal  Queen Mary University of London
Philip Wood QC
Deborah Zandstra  Clifford Chance LLP

Venessa Parekh  FMLC
Thomas Willett  FMLC

Guest Speakers:

Lee Buchheit  Cleary Gottlieb Steen & Hamilton LLP
Mitu Gulati  Duke University

Regrets:

Carter Brod  Morgan, Lewis & Bockius UK LLP
Duncan Kellaway  Freshfields Bruckhaus Deringer LLP
Yannis Manuelides  Allen & Overy LLP
Harriet Territt  Jones Day
Minutes:

1. Introductions

1.1. Alex Rutter opened the meeting.

2. Administration: Scoping Exercise – Lifecycle of a Project and confirmation of the 2019 Forward Schedule (Venessa Parekh)¹

2.1. Venessa Parekh described to the members how new issues of legal uncertainty on which the FMLC can undertake work are raised. She elaborated on the Committee’s process of adopting new projects, how working groups operate, the publication drafting process and the profile of past FMLC publications.

2.2. Attendees did not raise any issues in relation to the draft Forward Schedule of meetings for 2019. These meetings dates were therefore confirmed.

3. U.S. Executive Branch Power and Sovereign Debt Restructuring (Lee Buchheit and Mitu Gulati)

3.1. Mitu Gulati lead a discussion of the paper, written by him and Lee Buchheit, entitled Sovereign Debt Restructuring and U.S. Executive Power.² Using Venezuela’s recent debt crisis as the primary case study, the paper analyses the way in which the country can resolve its debt problems without the use of conventional sovereign debt restructuring techniques. As an alternative, the paper explores the possibility of using the legal power vested in the Executive Branch of the U.S. Government to facilitate a foreign sovereign debt restructuring. Professor Gulati explained that Venezuela’s large and diverse pool of creditors means that the traditional approach to debt restructuring is not suitable. The state owned oil company, PDVSA, owes an estimated $65 billion to a diverse range of claimants: $6 billion is owed to Paris Club bilateral creditors, £22 billion to non-Paris Club bilateral creditors and a variety of uncertain claims are owed, such as foreign entities like airlines which hold blocked local currency deposits.

3.2. A Forum member asked about the inter-creditor tension between bond holders who have collection action clauses (“CACs”) and those who do not. Mr Gulati explained that, owing to the diverse nature of the creditors and the fact that Venezuelan proceedings will not have the benefit of a bankruptcy code, it will be a challenge to convince all creditors to grant debt

¹ Please see Appendix I below.

relief. This is exacerbated by the knowledge that if any significant number of creditors decline, the reconstruction of the economy might fail.

3.3. Mr Buchheit then explained that the nature of Venezuela’s economy adds to the frustration of conventional sovereign bond restructuring mechanisms. Oil makes up 95% of the country’s foreign currency earnings, with most of the oils sales for cash being made into the U.S. Approximately 25 percent of Venezuelan oil shipments go to China, Russia and India to pay down previous loans. The amount of oil that is sold for cash has been steadily decreasing and most of that is sold into the United States. The entire economy would be strangled should some of the unpaid creditors find a legal strategy in the U.S. that resulted in the seizure of the oil or cash proceeds from the sale of the oil. Mr Buchheit stated that the key question needing to be answered is what could be done to produce an orderly outcome for Venezuela, taking into account not only the country’s finance, but also the deep humanitarian and refugee crisis.

3.4. Next, Mr Buchheit summarised the case studies that provided the precedents for their research into Venezuela’s sovereign debt crisis. The first was the restructuring of the Saddam-era debt of the Republic of Iraq (2003-2011). In this instance, the U.N. Security Council encouraged the restructuring of a diverse Saddam-era debt stock by immunising Iraq’s principal external assets against seizure by private creditors holding Saddam-era claims. The second case study examined was the diplomatic crisis between the U.S. and Iran (1979-1981) during which President Reagan issued an Executive Order suspending all U.S. lawsuits and attachments against Iranian defendants and diverting them instead to a new claims tribunal established in The Hague. This decision had been controversial and lawsuits had been filed against the administration but it does demonstrate that the U.S. President has the authority to suspend normal creditor access to U.S. courts where this is necessary to further a national security and foreign policy objectives of the U.S.

3.5. Taking into account Venezuela’s diverse and antagonistic creditor universe, the fact that its economy is thoroughly dependent on oil and the deepening humanitarian crisis, using the Executive Branch’s legal authority to facility an orderly and consensual resolution of Venezuela’s debt problem to encourage negotiated, not litigated, outcomes might be the best course of action. This, however, cannot be achieved without either a change in regime or a change in policy by the current regime.

3.6. When given the opportunity to ask questions, one member asked what amount of Venezuelan debt can be sustained and serviced. The speakers suggested that this depends on what a regime change produces. To date, an International Monetary Fund ("IMF") team
has been unable to go into Venezuela and will only be able to do so once the regime changes. Discussions concerning a change in regime continued. Mr Buchheit explained that hopes for an opposition party to take charge of Venezuela had faded. Any attempt at an opposition has been fractured and attempts have been ineffective.

4. **Any other business**

4.1. A participant suggested that the following topics could be discussed at the next meeting: (i) the agreement from the European Union finance ministers on reforms to strengthen the euro area’s preparedness to tackle any future financial crisis; and (ii) the development of state-contingent debt instruments for sovereigns.
Lifecycle of a Project
How an issue of legal uncertainty is raised

• New issues of legal uncertainty on which the FMLC can undertake work are raised in Scoping Forum meetings, bilateral radar meetings with Joanna Perkins (FMLC CEO) and during monthly Patron relationship calls with members of the Secretariat.

• Once an issue is raised, the Secretariat usually asks for a briefing note to be prepared by the person(s) making the recommendation. This is then put before the Committee for their consideration. (The FMLC Secretariat will normally offer formatting and other assistance in preparing the brief.)
The brief

FINANCIAL MARKETS LAW COMMITTEE (FMLC)

Briefing Note: Issues of Legal Uncertainty on Brexit and Judicial Interpretation

1. Introduction

1.1. Following the referendum in June 2016, in which the U.K. voted to withdraw from the European Union, the FMLC established a High Level Advisory Group (HLAG) of experts to give direction to the Committee’s work relating to Brexit. At a meeting of the HLAG in December 2017, members of HLAG recommended that the FMLC establish a Working Group to identify potential legal uncertainties arising from the interpretations by U.K. courts of autonomous EU legal concepts which appear in received EU legislation as it is incorporated into U.K. law.

1.2. An overview of HM Government’s proposal to incorporate E.U. law into the U.K. and the various legal complexities relating to the interpretation of autonomous EU terms are set out below.

2. The European Union (Withdrawal) Bill—and domestic preparations for Brexit so far

2.1. In the run up to the referendum, those who campaigned for withdrawal from the E.U. argued for an end to the principle of the supremacy of E.U. law and judgments of the European Court of Justice (ECJ). The European Union (Withdrawal) Bill (the “Withdrawal Bill”), introduced into the House of Commons on 13 July, aims to fulfil this purpose by: (i) repealing the European Communities Act 1972 on the day the U.K. leaves the E.U.; and (ii) incorporating E.U. law as it stands into domestic law. The Withdrawal Bill also provides guidance for a new relationship between domestic law and U.K. law.

2.2. Clause 5 of the Withdrawal Bill states that the principle of the supremacy of E.U. law will not apply to any enactment or law passed or made on or after Exit Day (i.e., the date defined in the Withdrawal Bill as the day for the U.K. leaves the E.U., except so far as relevant to the interpretation, application or validity of any enactment or law passed or made before exit day). Clause 6, quoted below, provides guidance on the relationship between courts in the U.K. and the ECJ.

Interpretation of retained EU law

(1) A court or tribunal—

(a) is not bound by any principles laid down, or any decisions made, on or after exit day by the European Court, and

(b) cannot refer any matter to the European Court on or after exit day.

(2) A court or tribunal need not have regard to anything done on or after exit day by the European Court, another EU entity or the EU but may do so if it considers a approach to do so (emphasis added).

3. Relevant issues of Legal Uncertainty

3.1. As a consequence, where the meaning of an autonomous EU term or concept is defined before Exit Day, the U.K. will follow that interpretation. Where the meaning of terms, which may appear in the incorporated aspect of E.U. law, is not fixed by Exit Day—or their interpretation is discussed and adjudicated upon by the ECJ post-Brexit—there remains ambiguity as to how U.K. courts should proceed. Following the publication of the Withdrawal Bill, the former President of the Supreme Court, Lord Neuberger, remarked in the media that judges would require guidance from HM Government on how U.K. courts should interpret European concepts and judgments post-Brexit.

3.2. Referring to this, members of the HLAG also highlighted the importance of interpretational equivalence between the U.K. and E.U. in preventing legal uncertainty in the context of negotiations for a future trade agreement, or in the event the U.K. applies for “equivalence” under the E.U.’s Third Country regime, where regulatory coordination might be deemed important.

3.3. The questions before HM Government and U.K. judges (and for this Working Group to study and attempt to address) begin with a consideration of whether, and in what circumstances, U.K. courts might follow the ECJ’s judgments as so far as they settle, after Brexit, the meaning of terms in E.U. legislation previously received into U.K. law.

3.4. In the event that the U.K. courts choose not to abide by the ECJ’s interpretation, questions of legal complexity arise in relation to other aids to interpretation on which judgments in the U.K. might rely. One such aide might be found, it has been suggested, in the Model conventions and laws proposed and signed under the auspices of the United Nations. The Model Conventions are not, however, signed by a majority of E.U. member states, which raises further questions as to their authority and comprehensiveness.

3.5. A final area of legal uncertainty which requires consideration is the basis for judicial interpretation in the event it is agreed that international conventions and existing aids do not provide sufficient guidance. In such a scenario, Lord Neuberger’s call on Parliament for direction becomes more relevant. The Working Group might wish to reflect upon the overarching principles which might facilitate Parliament’s determination of its guidance to judges on the interpretation of E.U. law and ECJ judgments post-Brexit.

4. Working Group—Brief

4.1. The Working Group is invited to examine in general the legal issues surrounding the judicial interpretation of autonomous legal terms post-Brexit and to document the results of their inquiry into a paper. As a guide, the paper should address the subject according to the following outline: (i) summary and introduction; (ii) legislative background; (iii) legal issue analysis; (iv) wider impact or potential impact of the issues; (v) proposed solutions and mitigations; and (vi) conclusion.

4.2. More detail about drafting a paper for the FMLC can be found in the FMLC Contributors’ Guidelines.

* The FMLC has previously considered, for instance, the effects of the UNCITRAL Model Law on Cross-Border Insolvency (1995) in the acceptance of cross-border insolvency proceedings post-Brexit. The Working Group’s research would need to focus on each.
The issue is presented to the Committee

The Committee considers the issue

The issue is adopted

Only a limited number of uncertainties are identified, or it is a reiteration of comments the FMLC has made previously

The Committee delegates to the Secretariat responsibility for undertaking research and drafting of the publication

The issue does not fall within the remit of the FMLC e.g. too political in nature, not an issue of legal uncertainty etc. and is benched

The issues of uncertainty are complex and numerous

The Committee resolves to establish a working group to conduct an in-depth analysis which will lead to a publication
Working Group membership, conduct of business

• Members of the relevant Scoping Fora as well as academics, experts and other FMLC stakeholders are invited to join working groups.

• Working groups are convened under Terms of Reference, including conduct of business guidelines. These include the following:
  1. participation is limited to one member per organisation;
  2. alternates are not permitted to attend meetings; and
  3. working group meetings are to be attended in person, where possible. Dial-in details are only provided to members who are permanently based abroad.
Working Group meetings

- Working groups typically meet between two and five times to identify relevant issues of legal uncertainty, make decisions as to any work product (i.e., a paper or a letter), and review draft contributions. Working group members volunteer to draft sections of the paper.

- The Secretariat will support the Chair and the working group during meetings and manage Group-related communications. The Secretariat will help draft and circulate meeting agenda and related documents and take minutes.

- On completion of a publication, the Working Group is likely to shut down.
Review process and publication

- For publications drafted by the Secretariat, draft copies will be circulated to the individual(s) who raised the issue for comment and then to the Committee for their review before being finalised. In these cases, the Scoping Forum, as the Committee’s pool of experts on the general area of financial services law, will be asked if they have any feedback.

- For working groups, members who committed to writing sections of a paper will send their drafts to the Secretariat, who will align it to FMLC house-style as defined in the contributors’ guidelines and collate the sections into one document. Working group members will have the opportunity to comment on the draft publication before it is sent to the Committee.

- Once approved by the Committee, the publications will be uploaded to the FMLC website and circulated to relevant stakeholders and authorities.
Examples of recent projects suggested by Scoping Fora

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Achievements and impact

Professor Hugh Beale (University of Warwick) and Simon Firth (Linklaters LLP) gave evidence to the House of Lords E.U. Financial Affairs Sub-Committee on the topic of post-Brexit contractual continuity as an extension of work conducted by the FMLC Working Group on Brexit—Robustness of Financial Contracts.

In response to the FMLC paper exploring uncertainties as to the financial instruments that fall within the scope of MAR, the FMLC received a letter from the FCA stating that the paper was circulated to the FCA policy team who worked with ESMA to develop the MAR guidance materials. Subsequent ESMA Q&A’s on MAR were updated to include questions on market soundings.

In response to the FMLC paper on issues of uncertainty arising from the European Commission’s proposed directive and regulation on data protection, the FMLC was asked by the Commission to conduct further work. Subsequently, draft texts of the regulation were closely aligned with changes proposed by the FMLC.