Drafted by Michael Waibel, University of Cambridge with extensive inputs and comments from stakeholders and experts participating in the study group.

This guidance on creditor committees for engagement between debtors and creditors complement two private sector initiatives on creditor engagement by the International Capital Market Association (ICMA) and by the Institute of International Finance (IIF) [illegible]

First, in 2004, ICMA published a template for a Noteholders' Committee under English law.[2] ICMA [illegible] append the [illegible] ach). [illegible]

stakeholders and experts could assist sovereign issuers and their creditors in their engagement process, and provide a roadmap of issues to consider on whether and how to establish CCs.

This guidance includes the following

II.

A. default is made in the payment of any principal or interest in respect of the debt securities (or any of them) of any series of debt securities (or any of them) and the default continues for a period in excess of any applicable grace period

B. a public announcement by the [authorised representative] of the Issuer, to the effect that the Issuer is seeking or intends to seek a rescheduling or restructuring of the debt securities (or any of them) of any series of debt securities (or any of them) (whether by amendment, exchange offer or otherwise); or

C. with the agreement of the Issuer, whilst the debt securities (or any of t h o (oesf t

securities, as soon as practicable after such written notice and such certificate are delivered to the Issuer.

(c) Steering Group

If Holders of affected debt securities have established more than one Creditor Committee in accordance with the provisions of (b) *(Appointment)* i. and/or ii. and/or equivalent provisions set out in the terms and conditions of any affected debt securities, the Issuer does not have to engage with such committees[9] or have any obligations whatsoever towards any of them. Such committees may appoint a single Steering Group (to be comprised of representatives from such committees (the Steering Group), whereupon the Issuer shall engage with such Steering Group. The Steering Group shall comprise at least one member from each appointing Creditor Committee.

Commentary:

The Pros and Cons of a Steering Group:

Pros: The issuer needs to only engage and potentially bear the costs of one committee (the steering group). One possibility is that once the steering group is established, only costs incurred by the same are compensable.

If two or more CCs operate without the benefit of a steering group, some CCs may demand preferential treatment and so block the entire process (a problem that occurred in Iraq's 2005 debt restructuring). Also, costs may increase because of the inefficiencies associated with more than one CC operating without guidance and management by a steering group.

Cons: The issuer may want to strike different deals with different CCs. This flexibility may be undermined by a steering group representing the interests of all CCs. Even in the absence of preferential treatment of one CC over another, one CC may have different

stake, but also considering that individual CC members should not be able to block acceptance by the CC.

ii. may, in its discretion engage legal, financial or other advisers to assist it in representing the

restructuring), the involvement of CDS protection potentially changes this state of affairs. CC (steering group) members with CDS protection may not be as interested in a successful restructuring, and be better off financially if the issuer defaults. This will be the case where the CDS have a higher value than what the CC (steering group) member could gain by a reasonable restructuring deal. This may result in obstructing the negotiations, rather than working together with the issuer on a mutually acceptable solution.

Ethical Walls or Lock-ups are possible solutions. However, they would only address part of the problem. Having an information barrier between the CC (steering group) member (the person) and the trading department of his/her financial institution may help to avoid insider trading with CDS (forbidden under the laws of most major jurisdictions). Yet, the CC member will still be fully aware that his/her institution holds CDS which may influence his/her actions in the way described above. Lock-ups are time periods in which an entity is 'not allowed to redeem or sell shares' or in this case sovereign debt. Again, this only addresses the trading problem, leaving a wider conflicts of interest problem untouched.

As a result, holding CDS for the event of the issuer's partial or total default on the sovereign debt at issue should be included in the CC guidance as a conflict of interest with all the consequences that such a conflict triggers. This line of thought is also reflected in US bankruptcy proceedings, where the committee is formed of creditors of unsecured claims. A more lenient approach for creditors would be to oblige CC members to disclose the CDS protection they hold. But mere disclosure does not suffice

Creditors may be concerned that this approach unduly restricts the current flexibility in forming a CC. Yet, this procedure combined with a supervising body may be necessary to give the conflicts of interest provision teeth.

Such a mechanism might be unnecessary if the CC guidance were linked to a modified 'lending into arrears' policy of the IMF to the effect that the IMF would not make available funds if the issuer does not comply with the guidance on CCs. However, the IMF is unwilling to assume this task. In addition, the IMF – as a creditor – would be conflicted and not best placed to assess whether negotiations between its members and private creditors were in good faith. Moreover, the Fund only assesses the debtor state's behavior. It is difficult to see how the IMF could ever be able to assess the behavior of creditors, with the result that the assessment would be asymmetrical. Moreover, the IMF has no right to sit in the negotiations either, even if only to monitor the debtors. Accordingly, the IMF would be vulnerable to receiving incomplete and skewed information. Finally, the IMF is not in an equidistant position to arbitrate in conflicts. Nor does its policy of neutrality permit any involvement in debtor-creditor disputes.

A better solution is for the IMF to defer to the judgement of an independent supervising body when deciding whether the h Td (any 0 Tw 3.23 0 Td ( )Tj 0.23 0 [(4 0 Tj 0N-2 (i)v(t)-6

Should there be a cap on the time an issuer has to engage in good faith with the CC (the steering group)? The alternative seems to be that the issuer is only bound to negotiate as long as there is a reasonable chance of eventual agreement. Deciding whether there is such a reasonable chance (a possible responsibility for a supervising body) may be difficult. However, a time limit would not solve this problem, as the issuer would still have to be allowed to discontinue engagement with the CC if there is no reasonable chance of reaching an agreement, this even before the necessary time has passed. Refusing this right would be unreasonable given that continued engagement would bear no fruits. On the other hand, negotiations that have lasted for say 8 months should continue if there is still a reasonable chance to agree. Thus, as difficult as it may be to decide whether negotiations have broken down beyond repair, a limit on the negotiation period does not seem desirable.

Another major concern is that CC (steering group)thsicern sthad3d22 Tw 0.26 0 Td (is)2 -0 0

committee (the group), provided that the reimbursement sum is less than the aggregate sum paid to all creditors represented by the Creditor Committee (the Steering Group).[12]

Commentary:

If the objective is rapid engagement between the debtor and creditors, reimbursement by the Issuer of a certain minimum of expenses, if not all, is probably advisable. However, even if expenses are not reimbursed, or only subject to certain limits, the incentive to become a committee (group) member may still be sufficiently high for creditors considering that they take part in the decision-making.

The 2015 ICMA clause provides that the issuer will pay all duly documented reasonable fees and expenses.

A second possibility is that issuer and CC (the steering group) to agree on costs in advance. Once the agreed limit is exceeded, members of the CC pay additional costs. Conversely, in the absence of agreement, no costs are reimbursed. A downside of this approach is that it may be a source of delay in committee formation.

A third, and possibly the most viable approach, is for the issuer to only pay CC costs in case of a successful restructuring. If there is no successful restructuring, the CC costs are shared among all restructured creditors according to their share of the aggregate principal. This approach has potentially three advantages. First, it incentivizes the issuer to engage with a CC in the first place. Costs and expenses only need to be reimbursed in the event of a successful rescheduling or restructuring and if they are – all things considered – reasonable. This takes account of issuers' concern that they would need to pay the costs of unsuccessful CCs without limit. Second, it incentivizes the CC to work towards an agreement with the issuer. It will also encourage the CC to work more quickly and more efficiently. Third, however, if no agreement can be reached the represented creditors cover the CC costs and not its members means the financial risk is evenly distributed among all creditors.

The Belize restructuring used a fourth approach. Belize deducted the expenses of the CC from the first coupon payment made to holders of the restructured bonds and then reimbursed these expenses to the committee members, ensuring that all restructured bondholders shared the costs of the committee equitably.

(k) Settlement of Disputes

Either the Issuer or the Creditor Committee (the Steering Group) may refer disputes concerning the application of these provisions to either

i. the competent courts of the jurisdiction to which the majority of the affected debt securities in the aggregate principal amount outstanding are subject.

ii. a specially appointed Supervising Body. The decision of the Supervising Body shall be final and binding on the disputing parties.

[12] Thus, reimbursement is

Each party may request the appointment of such a Supervising Body. Any request shall be made available to the other party in writing. The request shall briefly outline the disputed issue, the declaration sought and appoint one individual as a member of the Supervising Body.

The responding party shall within 10 days after receipt of the request make available to the requesting party a reply. Therein it shall briefly respond to the outline and appoint an additional individual as a member of the Supervising Body.

Following the appointment of the second member of the Supervising Body, the two party-appointed members shall within 10 days after this date together appoint a third member.

If the responding party does not appoint the second member of the Supervising Body within 10 days after receipt of the request, the requesting party may appoint the second and third member of the Supervising Body within 10 days after this date.

The members of the Supervising Body shall be independent and impartial. Any member of the Supervising Body may be challenged by either party if circumstances exist that give rise to justifiable doubts as to the member’s impartiality or independennlindependentmembe1

Annex A: Issuer/Holder Consultations

The Issuer and the holders from time to time of the Bonds acknowledge and agree that debtor/creditor consultations should precede any request by the Issuer [illegible]