7 Sovereign debts under the SADC Model Bilateral Investment Treaty (SADC Model BIT)

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> In effect, sovereign debt litigation has begun to resemble a chess match: a move by a vulture is blocked or countered, and a new move or theory comes into vogue as another avenue to try to increase the chances of recovery. Unfortunately, for the state defendant, this is not a game; the vulture's portfolio may be diversified, and it may believe that it only needs an occasional big win to recoup its costs of carry-and-litigation expense. For the state however, what is at issue is not a litigation gamble, but the economic and social welfare of its citizens.
>
> *J Blackman & R Mukhi 2010*

7.1 Introduction

This chapter addresses how bilateral investment treaties (BITs) can potentially be used to protect sovereign credits in case of default. The main argument of the chapter is that including sovereign debt within the BIT framework is problematic and defeats the very foundation of sovereign debt restructuring (SDR). States should exclude sovereign debts from the scope of their BITs. This will enable them to fully utilise the important role sovereign debts play in state financing. States should opt to either continue with the existing SDR mechanisms or introduce a new continental framework for SDR.

According to the United Nations Conference on Trade and Development (UNCTAD) database, there currently are more than 2 298 BITs in force around the world.[1] With the progress in global investment law, states have adopted new model BITs to replace the old model BITs. UNCTAD has also advised on the need of modernising the old-generation treaties as part of the international investment treaties reform.[2] The old

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1 https://investmentpolicy.unctad.org/international-investment-agreements (accessed 1 May 2021).

2 United Nations Conference on Trade and Development (UNCTAD) 2017 World investment report (2017), https://unctad.org/en/PublicationsLibrary/wir2017_en.pdf (accessed 1 May 2021).

regime of investment treaties has been criticised for favouring investors to the detriment of host state policy space and regulatory power. A typical old regime BIT contains a broad definition of investment and investor, a most-favoured-national clause (MFN) without exceptions, fair equitable treatment (FET), full protection and security (FPS) and lack of safeguard provisions for states. On the other hand, the new generation of BITs have tried to limit the definition of investor and investment and provide some clarity on the meaning of FET and FPS clauses.

The Southern African Development Community (SADC) Model BIT is a non-binding model template that contains different alternatives and recommendations for states to adopt when negotiating BITs. The model has been adopted as a means to address the shortcomings emanating from the old regime of investment treaties. It provides alternative provisions to replace and clarify controversial old regime BIT provisions such as the definition provisions, the MFN clause; fair and equitable protection (FEP); FPS; and the investor-state dispute settlement (ISDS) clause.[3] The model has narrowed the definition of investor and investment with an express exclusion of sovereign debt;[4] it has excluded the MFN;[5] replaced the FEP standard treatment clause with a fair administrative treatment clause;[6] it has tried to clarify the scope and meaning of full protection and security; and it has excluded the ISDS mechanism in favour of the domestic and regional dispute settlement framework.[7]

This chapter addresses the provisions of the SADC Model BIT in relation to sovereign debts. The chapter does not intend to provide an analysis of how different BITs have addressed the question of sovereign debts, but only aims to provide insights to states, particularly SADC member states, on the legal implication of SADC Model BIT provisions in relation to sovereign debts. The chapter is divided into three parts. The first part introduces and discusses sovereign debt and BITs as concepts; the second part addresses the interplay of BITs on sovereign debt and how the interplay has been addressed by the SADC Model BIT; the third and last part highlights the general conclusion of the chapter.

3 SADC Model BIT is a non-binding template developed by the SADC Secretariat as assistance for countries when negotiating BIT.

4 South African Development Community Model Bilateral Investment Treaty Template with Commentary (SADC Model BIT) July 2012, art 2.

5 SADC Model BIT (n 4) art 4.

6 SADC Model BIT art 5.

7 SADC Model BIT art 29.

7.2 Introduction to sovereign debt and bilateral investment treaties

7.2.1 Sovereign debt

There has never been an agreed international legal definition on what sovereign debt is. The Vienna Convention on Succession of States in Respect of State Property, Archives and Debt (not yet in force) defines state sovereign debt as 'any financial obligation of a predecessor state arising in conformity with international law towards another state, an international organisation or any other subject of international law'.[8] Despite the fact that the Convention has not entered into force, it remains the only international treaty to try and define sovereign debt. However, the definition under the Convention excludes private lenders as creditors and municipal law as legal framework governing sovereign debt. This chapter adopts the definition of sovereign debt as the debt a state (central government) owes to its creditors.[9]

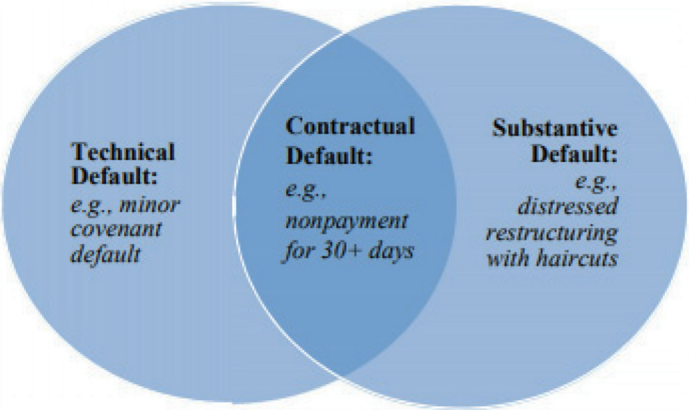
States can, and periodically do, default on their sovereign debt. A sovereign debt default occurs when a state fails to meet its payment obligation to its creditor. Legally speaking, the definition of sovereign debt default should be extracted from the sovereign debt agreement/instrument itself, because the instrument usually provides for factors and incidences of default (events of default). These incidences provide for which obligations, including covenants or warranties in the agreements when breached are considered to lead to default. However, at this point it is imperative to highlight the varying incidences of default. Sometimes default happens when there is a missed interest/principal payment and sometimes only a delay in disbursing payment by the borrower can be considered default. It is mostly the breach of payment obligations and substantive covenants rather than warranties that occasions defaults.

Considering the lack of agreed definition of what default is, some authors have tried to provide different forms of defaults. Ams et al have categorised defaults into three categories based on default as per the underlying contract and default as per credit rating agency such as Moody's, Fitch Group and S&P Global Ratings (S&P). The first category is technical default. This occurs when an event of default in the underlying

8 UN General Assembly Vienna Convention on Succession of States in Respect of State Property, Archives and Debts (8 April 1983) art 33.

9 M Tomz & M Wright 'Empirical research on sovereign debt and default' (2013) 5 *Annual Review of Economics* 247.

debt contract happens, but the credit rating agency does not regard the default as default. The second category is contractual default, which occurs when the event of default arises from the underlying contract. The occurrence will also constitute default under third parties (credit rating agencies) definitions of default. The last category is substantive default; this occurs when an event happens which, according to the credit rating agency, is an event of default, but the default does not constitute an event of default under the underlying debt contracts.[10] Credit rating agency definition of default is worth considering because of the influence of this agency in the financial market when it comes to the rating of government bonds.[11] Of the three categories the second category (contractual default) is the focus of this chapter.



Categories of default by Ams et al (2019)[12]

The causes of default are diverse and not always straightforward. For example, lax fiscal discipline and excessive budget deficits have been attributed as the causes of the Euro area's sovereign debt crisis.[13] However,

10 J Ams et al 'Sovereign default' in SA Abbas, A Pienkowski & K Rogoff (eds) *Sovereign debt: A guide for economists and practitioners* (2019) 3.

11 US Securities and Exchange Commission Report on the Role and Function of Credit Rating Agencies in the Operation of the Securities Markets (2003). Also see the conclusions of the financial crisis inquiry commission.

12 Ams et al (n 10) 4. Also see IMF Conference of 13-14 September 2018 'Sovereign debt: A guide for economists and practitioners', https://www.imf.org/en/News/Seminars/Conferences/2018/05/24/sovereign-debt-a-guide-for-economists-and-practitioners (accessed 20 January 2021).

13 PR Lane 'The European sovereign debt crisis' (2012) 26 *Journal of Economic*

the 2001 Argentine default was not one of excessive budget deficits but more one to do with policy failures, particularly the convertibility plan (*Ley de Convertibilidad del Austral*).[14] In the ten years preceding the default, Argentina's average deficit was 1,2 per cent of gross domestic product (GDP), whereas the debt levels in 2001 stood at 55 per cent of GDP.[15] The recent defaults in the SADC region (Mozambique[16] and Zambia) have been attributed to government fiscal mismanagement. As for Zambia, evidence shows that Zambia was struggling with mounting debt[17] even before the financing gap caused by the COVID-19 pandemic.[18] It has been pointed out that the country's default has more to do with incompetent fiscal management than anything else.[19] Zambia's finance minister Ng'andu noted that the government borrowing was over-ambitious and the debt was unsustainable.[20] This over-borrowing noted by Ng'andu reverberate with the 1980s African countries; sovereign default. Indebtedness was a characteristic feature of post-colonial reconstruction during the 1960s and indebtedness was widely accepted as an unavoidable prerequisite for development. It was the heavy indebtedness that turned countries into insolvency in the early 1980s.[21]

In order to be able to borrow, states avoid defaulting to maintain a good reputation as good borrower.[22] However, sometimes states face

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14 G Nataraj & P Sahoo 'Argentina's crisis: Causes and consequences' (2003) 38 *Economic and Political Weekly* 1641-1644.

15 Y Li & U Panizza 'The economic rationale for the principles on promoting responsible sovereign lending and borrowing' in CD Espósito, Y Li & JP Bohoslavsky (eds) *The UNCTAD principles on responsible sovereign lending and borrowing* (2013).

16 The Mozambique debt crisis was also partially caused by unlawful transactions as per domestic laws and corruption. See A Nuvunga & A Orre 'The 'secret loans affair' and political corruption in Mozambique' in I Amundsen (ed) *Political corruption in Africa. Extraction and power preservation* (2019).

17 C Mfula & K Strohecker K 'UPDATE 6 Zambia will miss Eurobond payment, setting stage for default (13 November 2020), https://www.reuters.com/article/zambia-debt/update-5-zambia-will-miss-eurobond-payment-setting-stage-for-default-idINL1N2HZ0R1 (accessed 20 January 2021).

18 M Hill & TC Mitimingi 'Zambia seeks restructuring after 'over-ambition' on debt' (18 May 2020), https://www.bloomberg.com/news/articles/2020-05-18/zambia-sees-to-restructure-debt-after-over-ambition-on-loans (accessed 20 January 2021).

19 E Olander 'Zambia's Eurobond default – What we have learned' (17 November 2020), https://www.theafricareport.com/50664/zambias-eurobond-default-what-we-have-learned/ (accessed 20 January 2021).

20 Hill & Mitimingi (n 18).

21 W Biermann & J Wagao 'The quest for adjustment: Tanzania and the IMF, 1980-1986' (1986) 29 *African Studies Review* 89.

22 M Tomz *Reputation and international cooperation: Sovereign debt across three centuries*

difficult choices and defaulting becomes necessary. One of these choices is whether to refinance/pay bondholders or to buy medicine and food for the population as pinpointed by Vera Songwe, the executive secretary of the Economic Commission for Africa (ECA).[23] Songwe's concern of choosing whether to provide citizens with essential services or servicing debts is not recent. In 1985, following a heavy burden of debt that trapped most African countries, the then Organisation of Africa Unity (OAU) Chairperson, Mwl Nyerere, said that 'Africa's debt burden is now intolerable. We cannot pay. It is not a rhetorical question when I ask, should we really let our people starve so that we can pay our debts?'[24] In a situation such as this, states sometimes choose to default on their debts.

SADC countries default 1956 – 2020

Country Name	**1956-1965**	**1966-1975**	**1976-1985**	**1986-1994**	**1995-2020**	**Total**
Angola	…	…	…	1	…	1
Malawi	…	…	2	1	…	3
DRC	…	…	8	3	…	11
Mozambique	…	…	1	4	1	6
South Africa	…	…	1	4	…	5
Tanzania	…	…		4	…	4
Zambia	…		2	4	1	7
Total per timeline	**…**	**…**	**14**	**21**	**2**	**37**

Source: from 1956-1994 David F Babbel (1995) and from 1995-2020 by the author

After a state defaults on its debt, creditors find it difficult to enforce their sovereign debt entitlements in courts of law due to sovereign immunity.[25] Even when the bond instruments contain sovereign immunity waivers, courts have been reluctant to enforce these clauses.[26] State immunity in

(2011).

23 A Soto 'The ticking debt bomb in Africa threatens a global explosion' (10 June 2020), https://www.bloomberg.com/news/articles/2020-06-10/africa-will-be-the-next-debt-explosion-after-coronavirus (accessed 20 January 2021); also see J Tim ''Why not default?' The political economy of sovereign debt' (2021) 56 *Community Development Journal* 180-183.

24 RH Green 'Unmanageable: Toward sub-Saharan African debt bargaining' in S Griffith-Jones *Managing world debt* (1988) 245.

25 E Jonathan & F Raquel 'Sovereign debt' in GM Grossman & K Rogoff (eds) (1995*)* *Handbook of international economics* (1995).

26 WM Weidemaier & M Gulati 'Market practice and the evolution of foreign sovereign immunity' (2018) 43 *Law and Social Inquiry* 496; *NML Capital Ltd v po Central de la Republica Argentina* 652 F.3d 172 (2d Cir 2011).

sovereign debt litigation can be categorised into two categories, namely, (i) immunity from suit; and (ii) immunity from execution.[27] Immunity from suit is the bedrock of the international principle that sovereign states should not be taken to foreign courts against their will.[28] On the other hand, immunity from execution stems from the long-standing concerns about disruptions and political ramifications that can result from the seizure of a foreign state's property.[29] A state's immunity from execution is only available for sovereign non-commercial property. This means that sovereign commercial property can be the subject of attachment. In *Connecticut Bank of Commerce v Republic of Congo*[30] the American court was of the view that a sovereign's property could not be attached when there is no evidence of it being used commercially. The court further elaborated that the term 'commercial activity' should be interpreted narrowly. Finding this hurdle of locating commercially-used sovereign property, creditors then turned to the property of state agencies or corporations. This also has been difficult as courts have ruled that these agencies or corporations should have their separate legal personality apart from that of the state respected.[31]

Apart from litigation, the global community has invented different mechanisms to deal with sovereign debt default. These mechanisms include the Debt Service Suspension initiative (DSSI) (although mainly used to temporarily help debtor states preserve resources for other emergencies; it can also be viewed as a mechanism to halt default referring to Nyerere's concerns above); rescheduling and restructuring of debts. Rescheduling or restructuring entails changing the principal amount of the debt, extending maturity time and/or interest payment deferment, and also changing the interest rate on the debt. Restructuring initiatives can be instituted before or after the default. Restructuring before default aims to avoid a total default. For example, when Zambia missed a payment of a $42,5 million coupon on its sovereign bonds in October 2020, the government made a restructuring request to its creditor to defer interest payments for six months. Creditors rejected the request and Zambia remained with a 30-day grace period to make payment or enter a default. The grace period expired and Zambia defaulted, becoming the first pandemic-era African

27 J Blackman & R Mukhi 'The evolution of modern sovereign debt litigation: Vultures, alter egos, and other legal fauna' (2010) 73 *Law and Contemporary Problems* 47, http://www.jstor.org/stable/25800669 (accessed 19 January 2021).

28 *The Schooner Exchange v M'Faddon* 11 US 11, 114 (1812).

29 Blackman & Mukhi (n 27).

30 309 f.3d 240.

31 See *First National City Bank v Banco Para El Comercio Exterior De Cuba (Bancec)* 462 US 611, 626 (1983).

country to default. After a default, states still continue with restructuring initiatives. For example, following a default in 2017, Mozambique in 2019 swapped its debt by exchanging its Euro-denominated bond valued at $726,5 million for a new $900 million bond to cover missed principal and interest payments and extended the maturity time from 2023 to 2031. When bond holders and states do not reach an agreement on restructuring of the debt, bond holders look for other avenues to recover their debts, including the use of bilateral investment treaties (BITs).

7.2.2 Bilateral investment treaties

Bilateral investment treaties (BITs) are treaties between two states for the protection and promotion of investments. BITs have been used by bond holders to initiate arbitration cases under the investor-state dispute settlement (ISDS) mechanism. There currently are 2 298 BITs in force worldwide, and it is not the scope of this chapter to scale how these BITs have addressed sovereign debts. As will be discussed later, a small variation in the BIT provision has far-reaching interpretative and legal implications. An investment tribunal's findings in one case should not be generalised to apply in other cases or BITs. The true implication of a tribunal decision depends on the facts of the case and the exact formulation of the BIT. In one BIT sovereign bonds may qualify as an investment while in other BIT sovereign bonds may not qualify as investments.

To date there have been only four sovereign debt investment cases (SDIC). The first three cases were the results of the Argentina 2000s sovereign debt default (the *Abaclat,*[32] *Ambiente*[33] and *Giovanni*[34] cases). The fourth case was the result of the Greece sovereign default (*Poštová Banka*).[35] In the first three cases which involved the Argentina-Italy BIT, the tribunals accepted that sovereign bonds were investments. In the fourth case which involved the Slovakia-Greece BIT, the tribunal concluded that

32 *Abaclat & Others v Argentina* ICSID Case ARB/ 07/5, Annex A, Settlement Agreement (29 December 2016). The *Abaclat*, *Ambiente* and *Giovanni* cases all concerned claims arising out of Argentina's enactment of legislation concerning the restructuring of its public debt, leading to the government's default in sovereign bonds in late 2001.

33 *Ambiente Ufficio SpA & Others v Argentina* ICSID Case ARB/ 08/9, Order of Discontinuance of the Proceeding (4 May 2015).

34 *Giovanni Alemanni & Others v Argentina* ICSID Case ARB/ 07/8, Order of the Tribunal Discontinuing the Proceeding (14 December 2015).

35 *Poštová banka, as and ISTROKAPITAL SE v Greece* ICSID Case ARB/13/8, Award (9 April 2015). The case concerned claims arising out of the enactment of legislation that amended sovereign bond terms retroactively and unilaterally by the government, allegedly allowing the imposition of new terms upon bond holders against their consent if a supermajority of other bond holders consented, in the context of Greece's 2012 sovereign debt restructuring.

sovereign bonds did not qualify as investments under the Slovakia-Greece BIT. It is important to highlight that none of the above cases reached the merit stage. The *Abaclat* case was settled; the *Ambiente* and *Giovanni* cases were discontinued for non-payment of tribunal's fees; and in the *Poštová Banka* case the tribunal lacked jurisdiction. It therefore is unclear which substantive protection sovereign bonds enjoy under international investment law.[36] Although the cases did not reach to the merit stage, they do raise concerns over the scope and jurisdictional mandate of investment tribunals over investment cases involving sovereign debts.

The major issues of discussion in the *Abaclat* case were (i) how the term 'investment' should be construed and defined; and (ii) whether an investor can bring contract claims (emanating from sovereign bonds) before an investment tribunal. The tribunal ruled that when defining the term 'investment', the focus should be on the contracting parties' agreement and not criteria developed by case law. According to the tribunal, criteria such as the *Salini* case criteria on investment[37] are useful but they cannot be used to create a limit, which neither the ICSID convention's drafters and state parties nor the contracting parties to a specific BIT intended to create.[38] In relation to contract claims, the tribunal held that in this case the arbitral tribunal had no jurisdiction where the claim at stake is a pure contract claim. The tribunal will only have jurisdiction over investment disputes where the acts of a state are purely acts of a sovereign power and not acts of the state as a party to a contract. This means that when the act of the state can be construed as acts that any party to a contract can do, then the dispute is termed a normal contractual dispute to be settled in the normal contractual dispute settlement mechanism. This can further be elaborated by making reference to the *Biwater Gulf (Tanzania) Limited* case against Tanzania.[39] When deciding whether a contract termination by the government of Tanzania amounted to expropriation, the tribunal ruled that the termination in itself did not constitute expropriation. However, the Tanzanian government press release, in which Prime Minister Lowassa announced the termination of the contract, was an unreasonable disruption of the contractual mechanisms existing between the investor and the government, and motivated by political considerations. As such, these actions were inconsistent with the Republic's obligations under the

36 UNCTAD 'Sovereign debt restructuring and international investment agreements 2 IIA Issue Note (2011) 4-5.

37 *Salini Construttori SpA and Italstrade SpA v Kingdom of Morocco* ICSID Case ARB/00/4, Decision on Jurisdiction of 23 July 2001, § 52, 42 ILM 609, 622 (2003) (*Salini*).

38 *Abaclat* (n 32) para 360.

39 *Biwater Gauff (Tanzania) Limited v United Republic of Tanzania* ICSID Case ARB/05/22, Award (24 July 2008).

treaty. Taken alone, they had a concrete effect on the investor's contractual rights, and taken together with the acts that followed (of which it formed part) ultimately contributed to an expropriation.[40] The investor state dispute settlement (ISDS) is not meant to replace contractual remedies.[41]

In the *Ambiente* case the area of contention was whether the term 'investment' encompasses sovereign bonds. The tribunal was of the opinion that the ordinary meaning of the term 'investment' certainly does not restrict the scope of the notion so as to exclude bonds or security entitlements.[42] States have the possibility of restricting economic operations and assets that they consider to constitute investments, by giving or not giving consent or by qualifying their consent with certain restrictions, be it via their domestic investment legislation or via the applicable BIT.[43] According to the tribunal, the definition of the term 'investment' should be a literal meaning plus any restrictions imposed by the host state to the meaning of investment. Such restrictions include (i) notifications under article 25(4); (ii) the definition of investment within the national investment legislations; and (iii) the definition in the applicable BITs.[44]

In the *Postova Banka* case the tribunal considered article 1 of the Slovakia-Greece BIT, which defined 'investment' as 'every kind of asset'. The tribunal concluded that the list of examples provided under article 1 of the Slovakia-Greece BIT must be considered within the context of the treaty. If the interpretation focuses only on the phrase 'every kind of asset' as an investment, the examples in article 1 will be redundant. The tribunal distinguished the Argentina-Italy BIT language because it contained the phrase 'independent of the legal form adopted' which was not equally available in the Slovakia-Greece BIT. It also distinguished the Argentina-Italy BIT because it contained examples of 'obligations' and 'public titles' compared to the Slovakia-Greece BIT reference to 'loans, claims to money or to any performance under contract'. The tribunal's conclusion was that the Argentina-Italy BIT contained a wider definition of investment as compared to that of the Slovakia-Greece BIT. The *Postova Banka* case is a clear illustration of how varying constructions of provisions in BITs can have different interpretations and implications.

The emergence of the sovereign debt investment cases (SDIC) has been the result of a lack of a comprehensive, binding international

40 *Biwater Gauff* (n 39 para 500.

41 As above.

42 *Ambiente* (n 33) para 456.

43 *Ambiente* para 452.

44 *Ambiente* para 453.

legal framework for the resolution of sovereign debt crises.[45] Holdout creditors find investment arbitration advantageous as states usually pay upon award in order to avoid reputational damage.[46] From the four cases above, the substantive standards of sovereign debts under BITs remain at the interpretative mandate of arbitral tribunals. If sovereign debts are not excluded from the BITs legal framework, states are under unpredictable pressure to face SDIC litigation.

Although there have never been SDIC cases in Africa, the possibility cannot be ruled out. The risks of leaving the Pandora's box open are higher. States, in particular SADC member states, should provide a clear stance on the scope of BITs in relation to sovereign debt. The negative implication posed by SDIC is that it hinders the ability of states to solve debt problems. Bond holders are likely to ignore sovereign debt restructuring (SDR) initiatives if they know that they can get even higher compensation by undertaking SDIC. Moreover, the existence of SDIC as an alternative to SDR gives bond holders an upper hand during SDR negotiations. Although the same can be true for waiver of sovereign immunity, SDIC have more effect, because courts have been reluctant to accept sovereignty immunity waivers. This makes it more difficult for states to put forth a successful SDR proposal.

On the other hand, as for the positive aspect of SDIC, it discourages 'opportunistic defaults' of sovereign debt, that is, that states deliberately do not make payment of their debts while they are able to pay. More than half of defaults by middle-income countries occur at levels of external debt relative to GDP below 60 per cent which, under normal circumstances, is usually viewed as an important indicator of debt sustainability.[47] Under opportunistic default, states enjoy the luxury of paying less than the bonds' face value by demanding a haircut. Together with the states' desire to be considered a good borrower, SDIC puts more pressure on states to comply and pay rather than default on their debts. However, this argument should not romanticise SDIC because opportunistic defaults are rare, as explained by the reputational and punishment theories of sovereign debt default. The reputational theory assumes that a debtor's sole incentive to make repayments is to preserve its reputation as a good borrower.[48]

45 G Anna 'Sovereign debt: Now what?' (2016) *Yale Journal of International Law Online* 45.

46 M Waibel 'Opening Pandora's box: Sovereign bonds in international arbitration' (2007) 101 *American Journal of International Law* 711-715.

47 CM Reinhart & KC Rogoff *This time is different: Eight centuries of financial folly* (2009).

48 J Bulow & R Kenneth R 'A constant recontracting model of sovereign debt' (1989) 97 *Journal of Political Economy* 155, also see J Eaton, M Gersovitz & JE Stiglitz 'The pure theory of country risk' (1986) 30 *European Economic Review* 481; H Grossman, H Van & B John B *Sovereign debt as a contingent claim: Excusable default, repudiation, and reputation*

The punishment theory theorises that a country pays their debt to avoid the threat of direct sanctions that lenders can impose which can cost the defaulting debtor's ability to transact freely in the financial and goods markets.[49]

7.3 The interplay between BITs and sovereign debt with particular focus on the SADC Model BIT

The relevance of BITs in sovereign debt default is on (i) the definition of 'investment' in relation to sovereign debt; (ii) the non-discrimination obligation (national treatment (NT) and most-favoured nation (MFN)) and how states can treat different bond holders differently; (iii) the fair and equitable treatment and whether SDRs impairs bond holders' legitimate expectations; and (iv) the utilisation of the investor-state dispute settlement mechanism by bond holders.

7.3.1 The definition of investment in relation to sovereign bonds

It is the definition provision that demarcates the applicability of a treaty. In BITs, the definition section has serious implications for the host state, as it mirrors the host state's exposure to investor-state claims. There are three forms of defining an investment. The first is an enterprise-based definition; the second is a closed-list asset-based definition; and, lastly, an open-list asset-based definition.

An enterprise-based definition is the narrowest option for outlining an investment. It requires the establishment or acquisition of an enterprise for the aim of making a remote investment. The definition then lists the assets of the investor that are covered because they form an element of the enterprise. However, this illustrative list is not the test for investment, but rather an illustration of the styles of assets of the investor that are covered by the treaty. For example, in the Morocco-Nigeria BIT

> investment means an enterprise within the territory of one state established, acquired, expanded or operated, in good faith, by an investor of the other state in accordance with law of the party in whose territory the investment is made

(1987).

49 As above. Also see B Eichengreen *Till debt do us part: The US capital market and foreign lending, I 920-I 955* (1987); PH Lindert & PJ Morton 'How sovereign debt has worked' Working Paper 45 Davis:.

taken together with the asset of the enterprise which contribute sustainable development.[50]

A closed-list asset-based definition is an intermediate approach to defining an investment. This definition is partially analogous to the enterprise-based definition. It provides a closed list which 'starts from an enterprise approach, but expands this to include assets like property rights, whether or not they're associated with an existing enterprise within the host state'. For example, in the Tanzania-Canada BIT '[i]nvestment means (a) an enterprise; (b) shares, stocks and other forms of equity participation in an enterprise; (c) bonds, debentures, and other debt instruments of an enterprise; (d) a loan to an enterprise'.[51]

An open-list asset-based definition provides for the broadest coverage. The definition is characterised by the use of broad language such as 'every kind of asset' or 'every kind of investment', followed by a non-exhaustive list of the investments covered. This approach is more favourable to investors and less predictable for host states. Arbitral tribunals can interpret this definition widely to include assets not usually considered to be investments. The shortage of limitations of this definition therefore is its biggest challenge. This notwithstanding, this has been the foremost widely-adopted definition in the old regime of BITs. For example, in the Germany-Zambia BIT '[t]he term "investment" shall comprise every kind of asset, and more particularly, though not exclusively …'[52]

All four SDICs involved an open-list asset-based definition of investment. Neither BIT (the Argentina-Italy BIT and the Slovakia-Greece BIT) expressly included bonds in the list of qualifying investments. The tribunal in the three Argentina cases held that Argentine sovereign bonds qualified as an 'investment' under the BIT because the BITs defined investment as every kind of asset and the illustrative list of assets contained assets similar to sovereign debt/bonds. However, the tribunal in *Postova Banka* held that the Greece sovereign bonds did not qualify as investments because, although investment was defined to mean every kind of asset, the illustrative list of investments did not contain anything similar to sovereign debt/bond. Whether a sovereign bond falls under the definition of investment depends on the precise wording of the treaty.

50 Reciprocal Investment Promotion and Protection Agreement Between the Government of the Kingdom of Morocco and the Government of the Federal Republic of Nigeria.

51 Art 1, Agreement between the Government of Canada and the Government of the United Republic of Tanzania for the Promotion and Reciprocal Protection of Investments.

52 Art 8, Treaty between the Federal Republic of Germany and the Republic of Zambia Concerning the Encouragement and Reciprocal Protection of Investments.

After considering the most used three options of defining 'investment', the SADC Model BIT recommends the enterprise-based definition and strongly advises against an open-list asset-based definition. The recommended definition reads as follows:

> Investment *means an enterprise within* the territory of one state party established ... An enterprise may possess assets such as ...
>
> For greater certainty, investment does not include:
> (1) debt securities issued by a government or loans to a government.

The SADC model BIT definition of investment specifically excludes sovereign bonds from the scope of the BITs by specifically excluding debt securities issued by the government as investment.

Apart from the three most used forms of defining investment in BITs, some other forms of defining the term 'investment' can be seen in investment treaties involving SADC member states. For example, the Brazilian-Angola Cooperation and Investment Facilitation Agreement (Brazil-Angola CIFA) leaves the definition of investment to be determined under the domestic law of the respective countries. Another is the Brazil-Mozambique CIFA which defines investment as a long-lasting enterprise producing goods and services, with the exclusion of portfolio investments, sovereign debts and money claims.

The discussions above have only addressed the definition of investment under BITs. However, for cases under the ICSID Convention framework,[53] the Convention requires that the transaction or asset should also qualify as investment under the ICSID Convention. The next paragraphs will discuss the relationship between the investment definition in the SADC Model BIT and in the ICSID Convention (Convention).

The ICSID Convention does not define the term 'investment'. The negotiation history reveals diverging views on what investment should be, leading to the non-inclusion of the definition of investment in the Convention. During the negotiations, delegates offered varying views on the inclusion of bonds and loans. Burundi underscored that money lent to a state should not be termed investment.[54] Austria rejected the inclusion of

53 Convention on the Settlement of Investment Disputes Between States and Nationals of Other States (International Centre for Settlement of Investment Disputes (ICSID)) 575 UNTS 159.

54 ICSID *The history of the ICSID Convention: Documents concerning the origin and the formulation of the Convention on the Settlement of Investment Disputes between States and Nationals of Other States* (1970) 261.

public bonds.[55] Australia was of the view that the Convention seemed to include cases where the host country borrows cash from foreign investors.[56]

After having reviewed dozens of cases[57] related to debt instruments and sovereign bonds, Waibel concluded that so far, ICSID tribunals had liberally accepted jurisdiction over debt instruments, despite the ambiguity of article 25.

There have been divergent views on the relationship between the BIT definition of investment and that of the Convention. The first view is to the effect that the ICSID Convention definition of investment takes supremacy over the BIT definition. This position was taken by the annulment committee in the *Mitchell v DRC* case, when it ruled that 'the ICSID Convention may only be applied to the type of investment that the multilateral ICSID Convention envisaged'.[58] This position has been cemented in other legal scholarships and case laws.[59] If this approach is taken, then member states to the ICSID Convention might find it difficult to enjoy the limited scope of the SADC Model BIT definition, in case the definition of investment under the ICSID Convention is found to include sovereign bonds.

The second approach gives the BIT definition supremacy over the ICSID Convention definition. The annulment committee in the *Malaysian Historical Salvors* case ruled that a BIT should be accorded supremacy over

55 ICSID (n 54) 709.

56 ICSID (n 54) 668.

57 The cases reviewed include *Fedax v Venezuela*; *CSOB v Slovakia* (Jurisdiction); *CSOB v Slovakia* (Jurisdiction); *SOABI v Senegal*; *Mytilineos v Serbia & Montenegro* (Jurisdiction); *Globex v Ukraine* (Award); *Joy Mining v Egypt* (Jurisdiction); *CDC v Seychelles* (Jurisdiction); *Booker v Guyana*; *ADC v Hungary* (Award); *OKO Pankki Oyj v Estonia* (Merits); *I&I Beheer v Venezuela*; *Skype v Venzuela* (2009); *Sempra v Argentina* (Award); *Renta 4 v Russian Federation*; *Asian Express v Greater Colombo Economic Commission*; *Mihaly v Sri Lanka* (Jurisdiction).

58 *Mr Patrick Mitchell v Democratic Republic of the Congo* ICSID Case ARB/99/7 (Decision on the Application for Annulment of the Award) para 25.

59 *Mitchell v DRC* (Annulment) para 25; Z Douglas *The international law of investment claims* (2009) 165; CL McLachlan & M Weiniger *International investment arbitration: Substantive principles* (2007) 170; R Dolzer & C Schreuer *Principles of international investment law* (2008) 61-62; *Fakes v Turkey* (Award) para 111; *Globex v Ukraine* (Award) paras 43-44.

the ICSID Convention.'[60] The *Malaysian Historical Salvors* case position echoes the *Biwater Gauff* flexible approach to investment.[61]

The third approach requires that both the BIT and the Convention be given equal weight. The tribunal in the *SGS* case ruled that the jurisdiction of the Centre should be determined by jointly evaluating the BIT and the Convention.[62]

In order to ensure coherence, a two-tier approach is desirable. The tribunal should first evaluate whether the dispute meets the investment criteria under article 25 of the Convention and then undertake a second assessment of whether the investment in dispute is also an investment under the BIT in question.[63] This is so because, first, the question of 'investment definition' is a question of jurisdiction and admissibility of the case. The ICSID tribunal should first assess jurisdiction and admissibility of the case before it starts to deliberate the case. The main or primary document governing the ICSID tribunal jurisdiction and admissibility of case is the ICSID Convention. After the ICSID Convention, the BIT becomes a secondary document for the ICSID tribunal assessment of jurisdiction particularly when answering the question of whether the dispute concerns an investment within the meaning of the BIT under consideration.

It can therefore be concluded that different BITs define investment differently. The variations in the definition of investment are the deciding factors on whether a sovereign debt should be covered as investment or not. The SADC Model BIT defines investment by specifically excluding sovereign debts within the BIT scope of coverage.

7.3.2 Non-discrimination (national treatment and most-favoured nation provision)

Non-discrimination has become the key protection afforded to investors in the treaty system. The thrust of this principle is that states cannot discriminate among investors on the basis of nationality. In international investment law, non-discrimination is exemplified within the national treatment (NT) and the most-favoured nation (MFN) treatment standards.

60 'It is those bilateral and multilateral treaties which today are the engine of ICSID's effective jurisdiction. To ignore or depreciate the importance of the jurisdiction they bestow upon ICSID, and rather embroider upon questionable interpretations of the term 'investment' as found in Article 25(1) of the Convention, risks crippling the institution.' *Malaysian Historical Salvors* (Annulment) para 73.

61 *Malaysian Historical Salvors* para 79.

62 *SGS v Philippines* (Jurisdiction) para 154.

63 M Waibel *Sovereign defaults before international courts and tribunals* (2013).

The NT obligation requires states to treat foreign investors in the same way it treats its own nationals. The problem with this obligation is that debtor states often have a legitimate reason to treat domestic bond holders differently. For example, the insolvency of certain banks or pension funds might hit a country disproportionately hard. However, sovereign bonds nowadays are held by a myriad of creditors, nationals and non-nationals. It therefore seems difficult to discriminate against non-nationals.[64] Therefore, under this sub-part the focus will only be on the MFN standard.

The MFN provisions are designed to prevent trade distortions and promote trade liberalisation.[65] However, the challenges posed by the MFN provisions have led to it being rejected by SADC Model BIT. MFN provisions have been criticised by investment tribunals for their wide interpretation. It has been interpreted as to apply in dispute settlement,[66] and it can also attract a state's obligation from other treaties to be applicable in another treaty which does not contain those obligations.[67] It has allowed investors to free-ride on benefits granted to other investors in other treaties. The MFN clause therefore, as the SADC Model BIT notes, had the unintended consequence of multilateralisation of the international investment regime. In the *Maffezini* case[68] under the Argentine-Spain BIT the tribunal agreed with the investor to import and use the jurisdiction provision available in the Chile-Spain BIT. The Argentine-Spain BIT had a waiting period requirement while it was not the case for the Chile-Spain BIT. The tribunal used the Argentine-Spain BIT's MFN clause to import the ISDS clause from the Chile-Spain BIT. In another case, the *RosInvest Co* case,[69] the tribunal used the MFN clause to broaden claims by incorporating coverage of a wide range of claims available in another BIT.

There was therefore a compelling reason for the SADC Model BIT to omit the MFN clause, irrespective of its benefits. The SADC Model BIT

64 Waibel (n 63) 740.

65 M Ahmad, R Blanpain & B Flodgren *Corporate and employment perspectives in a global business environment* (2006).

66 A Tanzi *International investment law in Latin America: Problems and prospects/Derecho internacional de las inversiones en America Latina: Problemas y perspectivas* (2016).

67 D Collins *An introduction to international investment law* (2017).

68 *Emilio Agustín Maffezini v The Kingdom of Spain* ICSID Case ARB/97/7 (Award) (13 November 2000).

69 *RosInvestCo UK Ltd v The Russian Federation,* Arbitration Institute of the Stockholm Chamber of Commerce Case V079/2005, Final Award (12 September 2010).

recommends that the MFN provision should not be included in a treaty because it has the unintended effect of multilaterisation.

7.3.3 Fair and equitable treatment and the impairment of bond holders' legitimate expectations

While at first glance it seems in order to promise 'fair and equitable treatment' to an investor and his investment, ISDS arbitrators have interpreted this standard of treatment to incorporate as nearly anything negatively impacting investment. The alleged breach of the 'FET provision' remains one of the most used standards of treatment in ISDS cases.[70] It protects legitimate expectations – a notion that has received many, partly diverging interpretations.[71] It will therefore depend on the specific circumstances of a case whether tribunals will recognise a violation of the FET standard. In *CMS* the tribunal held that the host state needed to ensure a stable business environment.[72] It has been ruled that regular insolvency proceedings do not violate the FET standard.[73]

The SADC Model BIT recommends against the inclusion of a provision on fair and equitable treatment and opts instead for an alternate formulation of the availability on fair administrative treatment (FAT), if it is deemed necessary to include this clause. The special note provides that the fair and equitable treatment provision is a highly controversial provision. The drafting committee recommended against its inclusion due to very broad interpretations accorded to it by ISDS tribunals, as explained above. It [FET] has been interpreted to almost include anything negatively impairing an investor's investment. The fair administrative treatment (FAT) provides:

> The State Parties shall ensure that their administrative, legislative, and judicial processes do not operate in a manner that is arbitrary or that denies administrative and procedural [justice][due process] to investors of the

70 J Bonnitcha, LN Poulsen & M Waibel *The political economy of the investment treaty regime* (2017).

71 UNCTAD 'Fair and equitable treatment' UNCTAD Series on Issues in International Investment Agreements (2012) 63.

72 *CMS Gas Transmission Co v Argentina* ICSID Case Arb/01/8 (Award) (12 May 2005) para 274.

73 *Noble Ventures Inc v Romania* ICSID Case ARB/01/11 (Award) (12 October 2005) paras 177-178.

other State Party or their investments [taking into consideration the level of development of the State Party].

According to the commentary the alternative provision seeks to avoid the most controversial elements of FET.[74] However, it is important to note that some of the key words that have been used in the FAT provision have also been interpreted in relation to FET. As Waibel notes, the FET requires governments to act in conformity with the international standards of transparency, non-arbitrariness, due process and proportionality to the policy aims involved.[75] In the same way the FAT provides that 'administrative, legislative, and judicial processes do not operate in a manner that is arbitrary ...[76] ... improve the transparency, efficiency, independence and accountability'.[77]

Waibel lists five possible claims of FET in relation to sovereign bonds: first, a lack of transparency undermining legitimate expectations;[78] second, a take-it-or-leave-it exchange offer violates due process;[79] third, SDR carried out without good faith; fourth, profound transformation of the business environment; and, fifth, SDR undermines the legal framework of the sovereign bonds.[80]

The first and second forms of possible claims set out by Waibel might equally fall within the ambit of FAT. As for the first possible claim of lack of transparency, the FAT clause requires states to progressively improve transparency. Although progressive sounds like a soft obligation, borrowing from the jurisprudence of the protection of international economic human rights, progressive is an obligation that is capable of being violated if the state does not undertake concrete steps towards the goal.[81] It therefore falls that bond holders can show that the government was not transparent enough and it did not take affirmative steps to achieve that goal to the violation of the FAT obligation. However, in sovereign

74 South African Development Community Model Bilateral Investment Treaty Template with Commentary (SADC Model BIT) (July 2012).

75 Waibel (n 46) 711.

76 SADC Model BIT 5.1.

77 SADC Model BIT 5.5.

78 *Metalclad v Mexico* (Merits) para 76; *Maffezini v Spain* para 83; *CME v Czech Republic* para. 611; *Tecmed v Mexico* (Merits) para 152.

79 Waibel (n 63) 295.

80 Waibel (n 63) 296.

81 S Fukuda-Parr, T Lawson-Remer & S Randolph 'An index of economic and social rights fulfilment: Concept and methodology' (2009) 8 *Journal of Human Rights* 195.

bonds a transparency argument is unlikely to succeed due to the complex nature of the sovereign bonds market and restructuring.[82]

Another form of transparency concern is intrinsic to the sovereign debt management and not necessarily transparency in relation to the legal and regulatory framework. In Mozambique the International Monetary Fund (IMF) had to suspend its cooperation in 2016, after discovering a hidden debt of around $1,2 billion, following its first default in 2013. This raises a concern when it comes to the transparency of the Mozambiquan government.[83]

As to the second possible claim of a lack of due process of law, the SADC FAT provides to the effect that administrative or legislative action should not be operated in a way that denies administrative and procedural [justice][*due process*] to investors. By adopting a take-it-or-leave-it approach, bond holders can argue that the government act is a unilateral confrontational act without regard to due process.[84] To comply with this, the government should at least engage with bond holders in good faith.[85] This mirrors the situation in Zambia. The initiative of the Zambian government to engage with bond holders by requesting a six-month repayment holiday while it drafts its debt-restructuring plan, can be viewed as delaying tactic but it can also be viewed as an initiative of transparency by engaging with bond holders. On the other hand, creditors are raising concerns that the Zambian government is not acting in good faith, and any relief granted by Zambia would be designed to favour Chinese lenders, who account for the utmost amount of debt.[86]

7.3.4 The investor-state dispute settlement

The investor-state dispute settlement (ISDS) is the gateway for the investment arbitration case between an investor and the state. However, this mechanism has been losing its popularity due to concerns over the impartiality of arbitrators and the subjection of a sovereign state on equal footing with an individual person.

82 Fukuda-Parr et al (n 81) 295.

83 'Mozambique: Debt crisis despite Eurobond restructuring', https://www.fxstreet.com/analysis/mozambique-debt-crisis-despite-eurobond-restructuring-202001150911 (accessed 3 November 2020).

84 Waibel (n 63) 295.

85 As above.

86 T Mitimingi 'Zambia's missed Eurobond payment prompts default call by S&P' (23 October 2020), https://www.bloombergquint.com/markets/s-p-cuts-zambia-to-default-after-eurobond-payment-missed (accessed 3 November 2020).

The SADC Model BIT rejects the incorporation of ISDS provisions in BITs and recommends domestic and regional forum frameworks in the settlement of investment disputes. According to the model, investors should vindicate their rights in domestic courts or arbitration within the host country's institutions. However, this option is likely to jeopardise the quality of awards as most SADC countries lack strong arbitration institutions and capacity domestically. The independency of the judiciary remains an issue of concern in most SADC member states.

7.4 Conclusion

SADC Model BIT has significantly succeeded to limit the sovereign debt concept to fall within the BIT legal framework. It has limited the definition of investment to exclude sovereign debt. Hence, for countries adopting the SADC model's investment definition will be under no danger of facing sovereign debt investment cases (SDIC) litigation in case of default.

By excluding the MFN standard, the Model resolves the danger of bond holders importing more favourable terms from other BITs in order to accommodate their interests. For example, if the definition of investment under country A's BIT with country B excludes sovereign debt and country A's BIT with country C does not exclude sovereign debt as investment; then country B's bond holders can demand the definition of investment under country A's BIT with country C be applicable to them if country A's BIT with country B contains a typical old regime MFN clause. This type of importation makes reform useless if they do not address the practical implications of MFN provisions.

However, considering the important role that sovereign debt plays in providing states with needed finance, the global community should undertake coordinated efforts in creating a comprehensive framework to deal with sovereign debt defaults outside the BITs framework.

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