CHAPTER 11

State Immunity and Sovereign Bonds

Jürgen Bröhmer

1 Introduction

The title of this chapter, State Immunity and Sovereign Bonds, requires some clarification. When speaking of “sovereign” bonds, the attribute does not suggest that the bonds in question are privileged in any way as sovereign. In fact, the opposite is true as such bonds, more precisely the placing of such bonds on the capital markets, from the perspective of international immunity law, are regarded as private or commercial acts, i.e. as *acta iure gestionis* for which the state does not enjoy immunity. The attribute sovereign refers to the state as one of the parties in the commercial transactions that underlie the issuance of bonds.

Secondly, the chapter cannot just concern itself with state immunity. As will be shown below this question is well settled. When states issue bonds to finance their debt, they act commercially because it is the nature of the act rather than its purpose which determines whether states are protected from legal action in foreign fora. Whereas the purpose of such transactions will usually be a public one because the states are trying to obtain funds to exercise their public functions, the transactions to obtain these funds are no different from those engaged in by a commercial enterprise seeking to raise finance. In other words states are only engaging in a type of transaction in which any individual could also engage in.

It is therefore necessary to assume a broader perspective and ask how the international community deals with disputes that arise from states engaging in commercial transactions to secure financing. The issues of interest here are not the technical details of the financial instruments and any disputes arising, for example, from conflicting interpretations of contractual terms in the narrow sense. The issue here is that states sometimes default on their debt thus leaving those investors that have given them money in the lurch. There are several possibilities of addressing this problem legally. Protecting states from law suits in foreign fora brought by creditors is only one such potential option. This option comes in two guises. The first one is the question of whether states enjoy immunity from adjudication, which, as already indicated, has to
be answered in the negative. The second one is whether states enjoy immunity from execution, i.e. whether states can protect all or at least some of their assets from the grasp of creditors who were successful with their law suits. Other ways to address these issues could be through classical international law pathways such as diplomatic protection, where a state takes up concerns of its citizen creditors, or international negotiations through international financial institutions such as the International Monetary Fund (IMF) to alleviate the situation. The IMF, the European Central Bank and the European Commission, with indirect involvement of states (not only member states of the European Union) are currently engaged in this type of negotiation in an attempt to control the sovereign debt crises that has engulfed a number of member states of the European Union. The result of these negotiations can be informal, ad hoc and tailored debt restructuring, for example by prescribing what has become known as “haircuts”. All of this must be seen against the background of a lack of rules governing sovereign bankruptcy. Bankruptcy norms are the ultimate resort for addressing financial problems of private legal entities, but all efforts for the creation of a general and formal sovereign debt restructuring mechanism (SDRM) for states have so far been unsuccessful. Finally there are recent attempts to invoke investment arbitration as a means for creditors to retrieve outstanding monies.

1.1 Historical Excursion
Sovereign debt is nothing new as was shown impressively by Reinhart and Rogoff in 2009. Two events are particularly interesting because they reflect fundamental change in international law and show that it is not always such countries as Greece, Portugal or South American countries that have difficulties with their debt.

---

1 See Anne O. Krueger, Struggling with Success: Challenges Facing the International Economy (Singapore: World Scientific, 2012), 165 et seq.
3 See ibid., 99–100 for a table listing the cumulative tally of default and rescheduling around the world between the year of independence (where applicable) or the year 1800 and 2008. Spain (13), Germany (8) and Austria (7) are among the countries with most defaults. A number of South American countries look back at 8–10 defaults. Belgium, Denmark, Finland, Norway, Sweden, the UK, Canada, USA, Australia, and New Zealand are the countries without defaults in that list.