ODIOUS SECURITIZATION

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This debt has been "imposed upon the people . . . without their consent."[1] *It has not been "incurred for the benefit of the people."*[2] *Furthermore, "the creditors, from the beginning, took the chances of the investment."*[3] *Thus, claims to enforce the debt are "inapplicable, legally and morally."*[4]

This is not Jawaharlal Nehru upon the stroke of midnight on August 15, 1947. Nor is this Nelson Mandela on May 10, 1994. Nor even am I quoting the People's Republic of China, which renounced in 1949 all debt previously incurred, but on different grounds. Rather I quote diplomats of the *United States* as they sought to repudiate Spanish claims in 1898 that the United States or Cuba accept the external debts incurred while Spain ruled the island.

This U.S. action offers a precedent for modern assertions that an international debt is odious, and thus "inapplicable, legally and morally." Of course, precedent alone—even one involving the United States—does not constitute international law. I invoke the U.S. correspondence not as a binding declaration of law, but rather as a template for understanding the doctrine of odious debt, a doctrine with an unsteady history but a compelling rationale.

Borrowing from the correspondence quoted above, we might identify the following criteria for such debt; such debt must be:

(1) without the consent of the people;

(2) not for the benefit of the people; and

(3) both of the above with the knowledge of the creditors.

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1 *On Public Debts*, *in* 1 JOHN BASSETT MOORE, MOORE'S DIGEST OF INTERNATIONAL LAW § 97, at 359 (1906).

2 *Id*. at 358.

3 *Id*. at 368.

4 *Id*. at 359.

I will offer three specific suggestions about the doctrine: (1) that odious debt must be conceived broadly to cover not just traditional forms of indebtedness, but also other long-term obligations invented by modern finance; (2) that an obligation might be beneficial, yet still odious; and (3) that bondholders should not be presumed innocent in the face of immoral investments. Each of these observations tracks, respectively, the criteria established above for odious debt.

I. CONSENT AND ODIOUS SECURITIZATIONS

A. Debt "imposed upon the people . . . without their consent"

This first criterion for odious debt has special significance today. Debts taken on by occupying powers are likely to satisfy this criterion. Indeed, humanitarian law limits occupying powers to usufructuary occupation. Article 55 of the Hague Regulations of 1907 provides that the "occupying State shall be regarded only as administrator and usufructuary of public buildings, real estate, forests, and agricultural estates . . . situated in the occupied country."[5] International law has long interpreted this mandate as covering natural resources such as oil.[6]

[5] Convention Between the United States and Other Powers Respecting the Laws and Customs of War on Land, Oct. 18, 1907, art. 55, 36 Stat. 2277, 2309, 205 Consol. T.S. 277.

[6] There remains some controversy as to whether the mandate extends to movable property, but oil has long been established to be immovable property for these purposes, subject to Article 55 of the Hague Regulations. *See* N.V. De Bataafsche Petroleum Maatschappli & Ors. v. The War Damage Comm'n, 22 MALAYAN L.J. 155 (1956) (Ct. App. 1956) (Sing.), *reprinted in* 51 AM. J. INT'L L. 802 (1957) (Singapore Oil Stocks case); *see also* Eyal Benvenisti, *Water Conflicts During the Occupation of Iraq*, 97 AM. J. INT'L L. 860, 864 (2003) (arguing that although the United States would be entitled to utilize the public resources of Iraq, such use must benefit the people of Iraq); *id*. at 869 (explaining that since oil is considered immovable property the laws of usufruct apply to its use and require that while the fruits may be used, the capital must be maintained); *id*. at 870 (describing the use allowed by the principle of *usufructus* as involving protection "against overuse and diminution of the resource's quality and quantity"); R. Dobie Langenkamp & Rex J. Zedalis, *What Happens to the Iraqi Oil? Thoughts on Some Significant, Unexamined International Legal Questions Regarding Occupation of Oil Fields*, 14 EUR. J. INT'L L. 417, 434 (2003) (suggesting the rules of usufruct constrain an occupier by requiring the use of economically sound judgments made in good faith and not for the occupier's own enrichment); *id*. at 435 (arguing that the United States must handle Iraqi oil fields in a way that "facilitat[es] the evolution of a valued and productive member of the community of nations"); Harold Dichter, Comment, *The Legal Status of Israel's Water Policies in the Occupied Territories*, 35 HARV. INT'L L.J. 565, 582 (1994) (suggesting that oil is an immovable asset and therefore governed by the rules of usufruct of Hague Article 55); Meredith DuBarry Huston, Comment, *Wartime Environmental Damages: Financing the Cleanup*, 23 U. PA. J. INT'L ECON. L. 899, 902 (2002) (interpreting Article 55 as prohibiting military occupiers from "permanently alter[ing] or destroy[ing] enemy territory," or "act[ing] irresponsibly or maliciously in using the natural resources [such as oil] found therein") (internal quotation marks omitted).

Modern finance has invented a number of ways to alienate the economic value of property, often without alienating the property itself. Concessions—transferring the control over the resource, but not the title—offer one possibility. Securitizations—converting assets that generate an income stream into tradable securities capable of being sold in the capital markets—offer another innovative mechanism.[7]

Could an occupying power then cleverly confound the Hague Regulations through a financial arrangement that avoided the language of permanent divestiture, but that neatly transferred the economic value of natural resources from the occupied state to another entity—say, a foreign oil company? The answer is likely to be "no." Under Roman and civil law, "usufruct" requires that the person making use of another's property do so "for a time without damaging or diminishing it."[8] Transferring the long-term economic benefits of a resource would indeed damage or diminish that resource, at least from the perspective of those to whom the resource is "returned" at occupation's end.

It remains possible, of course, that such a nonusufructuary use might benefit the local population—perhaps a benign governor might exploit the natural resources for long-term gain for the people of the land? Yet, this claim is exactly what Article 55 denies. Recognizing that the occupier will often claim a long-term benefit for the local population, humanitarian law wisely excludes this claim from the outset. The assumption underlying this rule must be that obtaining the consent of the governed to long-term obligations involving natural resources is not feasible in the case of an occupying power, or that altruistic foreign occupiers are hard to come by.

Thus, despite various calls during the last year to privatize Iraqi oil fields as a means to raise the funds for Iraqi reconstruction,[9] the United States has refused to do so. But the planned repatriation of sovereignty scheduled for June 30, 2004,[10] might lead some to be less shy. After all, with Iraq now back in the hands of Iraqis, humanitarian limits on occupiers will no longer apply.

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[7] STEVEN L. SCHWARCZ, STRUCTURED FINANCE, A GUIDE TO THE PRINCIPLES OF ASSET SECURITIZATION (3d ed. 2002).

[8] BLACK'S LAW DICTIONARY 1542 (7th ed. 1999).

[9] *See* Holman W. Jenkins, Jr., *How to Lift the Curse of Iraqi Oil*, WALL ST. J., May 14, 2003, at A15; Susan Lee, *An Oil-for-People Program*, WALL ST. J., Apr. 30, 2003, at A16.

[10] *See* Jeffrey Gettleman & Dexter Filkins, *Pending Vote, Some Iraqis See Larger Council*, N.Y. TIMES, Feb. 20, 2004, at A1; Robin Wright & Colum Lynch, *Plan for Caucuses in Iraq Is Dropped*, WASH. POST, Feb. 20, 2004, at A1; *see also* Warren Hoge, *Annan Is Said to Have Doubt On Iraq Voting,* N.Y. TIMES, Feb. 19, 2004, at A1; Daniel Williams, *Fallujah Insurgents Find a New Focus;* WASH. POST, Feb. 8, 2004, at A20.

Or at least that will be the argument. But consent of the governed will still remain a significant stumbling block, unless the democratic machinery is more firmly in place than it seems to be at the time of this writing.

This discussion reveals the utility of conceiving of odious debt broadly—not just as bank loans or other forms of debt, but also other long-term obligations of the state, typically with respect to that state's natural resources or other assets capable of generating long-term income streams.

B. Debt not "incurred for the benefit of the people"

The second criterion for odious debt seems to establish a nearly impossible standard. It limits the possibility of odious debts to those cases where the government has truly squandered every penny or every rupiah or every peso. But this is not the usual case, even of corruption. There is typically some effort, however marginal, for social benefit. Even Saddam Hussein's palaces likely served some public function. But even where there is a local benefit, that benefit must be measured against the cost. The portion of the debt that dramatically exceeds the expected benefit might be seen as odious.

C. "The creditors from the beginning took the chances of the investment": Knowledge and Bondholder Morality

This final criterion requires that those lending monies know of the illicit purposes to which the monies will be put. Certain players in international finance are more likely to have knowledge of the uses of borrowed funds than others. Lee Buchheit writes that "banks [have] branches or representative offices in the debtor countries and they [are] thus in a position to assess first-hand the local political and economic scene. A similar presumption cannot be made about bondholders."[11]

Is bond lending therefore superior to bank lending because it is immune from attack as "odious debt"—because one cannot prove the requisite state of knowledge for the doctrine to apply? Is ignorance truly bliss? What are the moral obligations of a bondholder?

Perhaps the burden should not be on the bondholder, but on intermediaries—principally the underwriters.[12] Or alternatively perhaps we should simply

[11] Lee C. Buchheit, *Cross-Border Lending: What's Different This Time?*, 16 NW. J. INT'L L. & BUS. 44, 48 (1995).

[12] Even if ignorance is bliss, the underwriter at least might still face Section 11 liability under U.S. law

opt for cheaper credit by eliminating as much risk as possible for investors in debt.

My own view is that bondholding should not be devoid of moral obligation. The broad, deep, and faceless capital markets should not offer an escape from culpability for the financiers of international delicts. It is certainly clear that the capital markets are used at times by bondholders intentionally to support activity they desire.[13] Even if bondholders cannot be charged with aiding and abetting, they might at least be denied the right to enforce their credit when that credit was likely to be deployed in illegitimate ways by the debtor nation's government.

CONCLUSION

The doctrine of odious debt exposes a fundamental dilemma in international finance—the desire not to saddle a population with a debt to which it did not consent and from which it did not benefit, coupled with the practical need to ensure that capital continues to flow. Lenders do not want to be in the position of evaluating the morality of their borrowers' choices. But in the international context, the plenipotentiary representing the borrower may be clothed with the legal authority to enter into long-term obligations but yet not have in mind the interests of the people for whom it purports to speak. In such a context, it seems appropriate to require of lenders a basic standard of care.

for failing to inform investors of the risk of repudiation of the debt by a successor regime. 15 U.S.C. § 77(k) (2000).

[13] Consider the case of bonds used by a diaspora to support its homeland. *See* Anupam Chander, *Diaspora Bonds*, 76 N.Y.U. L. REV. 1005, 1060-62, 1069-71 (2001).