

# Mozambican Illegal Debts: Testing the Odious Debt Doctrine

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## ABSTRACT

*In June 2019, the Constitutional Council of Mozambique delivered a judgment declaring a financial transaction arranged by the government in violation of the parliamentary prerogatives in budgetary matters unconstitutional. This was only the tip of an iceberg consisting of a series of transactions tainted with corruption. In the face of this illegality, many antidebt campaigners have invoked the application of the odious debt doctrine to block the enforcement of contractual claims and the availability of restitutionary remedies. Under the odious debt doctrine, a debt is odious if, in the awareness of the creditors, it is contracted without the consent of and not for the benefit of the population. The operation of the odious debt doctrine presupposes an inquiry into its legal status. Lacking a proper normative characterization, the doctrine is to be understood more as a matter of policy than as a matter of law. As a result, its ideal systematic placement would be under the umbrella of transnational public policy. Transnational public policy establishes universal principles to serve the common interests of mankind. The key point, then, is to ascertain whether and to what extent the values enshrined into the odious debt doctrine may belong to the realm of the transnational public policy. In this context, the controversy on the validity of the Mozambican debt can become the touchstone for testing the legal status and operation of the odious debt doctrine.*

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## I. INTRODUCTION

In June 2019, the Constitutional Council of Mozambique declared a financial transaction made in contravention of constitutional norms related to the national budget invalid.<sup>1</sup> The transaction concerned a loan of \$850 million contracted by Ematum, a Mozambican state-owned fishing company, with Credit Suisse and guaranteed by the Mozambican government.

The judgment of the Mozambican Constitutional Council was just the tip of the iceberg of a complicated financial scheme articulated in three separate transactions to state-owned enterprises arranged by two banks: the Russian VTB Capital PLC and the Swiss Credit Suisse.<sup>2</sup> In addition to the Ematum loan, there were two other loans to state-owned enterprises: a \$622 million loan to ProIndicus to perform coastal surveillance (from Credit Suisse) and a \$535 million loan to the

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1. República de Moçambique Conselho Constitucional [Republic of Mozambique Constitutional Council], June 3, 2019, Acórdão n° 5/CC/2019 (Mozam.) [hereinafter Constitutional Council Judgment].

2. Rodrigo Olivares-Caminal, *Why Does Mozambique Need to Pay Its Non-Odious Debt?*, FIN. TIMES ALPHAVILLE (April 13, 2019), <https://ftalphaville.ft.com/2019/04/04/1554350405000/Why-does-Mozambique-need-to-pay-its-non-odious-debt/> [https://perma.cc/SA6H-E3M2] (arch-ived Sept. 21, 2020).

Mozambique Asset Management company (MAM) to build and maintain shipyards (from VTB).<sup>3</sup> All these loans were backed by guarantees from the Mozambican government. Of the three loans, only the one made to Ematum was publicly disclosed and subsequently converted into loan participation notes (LPNs). These LPNs were, in turn, legally extinguished in April 2016 through an exchange for \$727 million of eurobonds issued by the Mozambican government.<sup>4</sup>

Following the disclosure by the Mozambican government of the existence of these debts, the International Monetary Fund (IMF) and bilateral donors suspended their financial support to Mozambique. As a result, the local currency depreciated by about 65 percent within six months and economic growth plummeted to 3.8 percent in 2016 from 6.6 percent the previous year.<sup>5</sup> In this context, the Mozambican government announced its intention to restructure all its external commercial debt.<sup>6</sup> Since then, no payment on this debt has been made, causing the country's credit profile to be downgraded and the cost of financing to rise.<sup>7</sup>

Making matters even more complicated, in 2016 and in 2017 the country's administrative court (*Tribunal Administrativo*) declared the state guarantees of the Ematum, ProIndicus, and MAM loans illegal for violating the Constitution and budgetary laws.<sup>8</sup> A special commission within Parliament arrived at a similar conclusion, and an independent audit report was subsequently published highlighting numerous irregularities in borrowing and using funds.<sup>9</sup> In December

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3. See *id.*; see also ALED WILLIAMS, THE MOZAMBIQUE HIDDEN LOANS CASE: AN OPPORTUNITY FOR DONORS TO DEMONSTRATE ANTI-CORRUPTION COMMITMENT 1 (2018) (citing tuna fishing and maritime security as supposed reason for loans).

4. See Olivares-Caminal, *supra* note 2.

5. See *id.*; see also Press Release, IMF, IMF Executive Board Concludes 2017 Article IV Consultation with the Republic of Mozambique, Press Release No. 18/77 (Mar. 7, 2018), <https://www.imf.org/en/News/Articles/2018/03/07/pr1877-imf-executive-board-concludes-2017-article-iv-consultation-with-the-republic-of-mozambique> [<https://perma.cc/R2AC-FULM>] (archived Aug. 28, 2020).

6. The government emphasized that “while the external commercial debt represented only 13 per cent of total external debt, it accounted for over 40 per cent of debt service,” Olivares-Caminal, *supra* note 2.

7. *Id.*

8. *Moçambique Pode Agora Recusar Pagar a Dívida Oculta, Dizem os Analistas, e Ganhará com Isso*, CIP 2 (2019), [https://cipmoz.org/wp-content/uploads/2019/02/CIP\\_-Mozambique-can-now-refuse.pdf](https://cipmoz.org/wp-content/uploads/2019/02/CIP_-Mozambique-can-now-refuse.pdf) [<https://perma.cc/V4A2-AEHT>] (archived Sept. 14, 2020).

9. See ASSEMBLEIA DA REPUBLICA VIII LEGISLATURA, RELATÓRIO DA COMISSÃO PARLAMENTAR DE INQUÉRITO PARA AVERIGUAR A SITUAÇÃO DA DÍVIDA PÚBLICA 36-7 (Nov. 30, 2016), [https://reflekt.ch/wp-content/uploads/2019/09/2016\\_Bericht-Parlamentarische-Untersuchungskommission-Moçambique-port.pdf](https://reflekt.ch/wp-content/uploads/2019/09/2016_Bericht-Parlamentarische-Untersuchungskommission-Moçambique-port.pdf) [<https://perma.cc/YHU4-SKWH>] (archived Nov. 20, 2020); see also KROLL ASSOCS. U.K. LTD., INDEPENDENT AUDIT RELATED TO LOANS CONTRACTED BY PROINDICUS S.A., EMATUM S.A. AND MOZAMBIQUE ASSET MANAGEMENT S.A. (June 23, 2017), <https://www.open.ac.uk/technology/mozambique/sites/www.open.ac>.

2018, several charges for indictment were brought before the District Court for the Eastern District of New York against multiple individuals, including a former Mozambican minister, for having allegedly conspired to defraud investors through numerous material misrepresentations and omissions.<sup>10</sup> Further, Mozambique brought a lawsuit against Credit Suisse and VTB in the English High Court alleging the invalidity of the secret loans.<sup>11</sup>

The judgment rendered by the Constitutional Council in June 2019 must be seen in this framework. It was based on a claim filed by the Budget Monitoring Forum, the Platform of Civil Society Organizations, and another two thousand citizens to declare the Ematum transaction unconstitutional. This request was based on Article 179(2)(p) of the Mozambican Constitution,<sup>12</sup> under which Parliament has the exclusive competence to authorize the contraction of loans and other financial transactions and fix the upper limits of state guarantees. The Ematum transaction, instead, was arranged by the government and merely approved by the Mozambican Parliament by means of an *ex post* resolution.

The Mozambican Parliament opposed the claim of the applicants, arguing that the resolution was a political act and, thereby, was not justiciable before the Constitutional Council. The Constitutional Council, however, rejected this argument emphasizing that the government had acted in violation of the constitutional competence of Parliament in budgetary matters (Article 179) and had not inscribed the transaction in the state budget in violation of Law Number 9/2002.<sup>13</sup> In this way, the Constitutional Council put the violation not so much on the side of Parliament, but rather on the side of the government. On these bases, the Constitutional Council declared null the assumption of the loans and the provision of the guarantees, relying not only on constitutional norms, but also on some articles of

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uk.technology.mozambique/files/files/2017-06-23\_Project%20Montague%20%20In  
dependent%20Audit%20Executive%20Summary%20English%20(REDACTED%20FOR  
%20PUBLISHING).pdf [https://perma.cc/CC5X-29CS] (archived Aug. 28, 2020).

10. Indictment, *United States v. Boustani*, 356 F. Supp. 3d 246 (E.D.N.Y. 2019) (No. CR 18 681). For a comment, see Press Release, U.S. Attorney's Office E. Dist. N.Y., *Three Former Mozambican Government Officials and Five Business Executives Indicted in Alleged \$2 Billion Fraud and Money Laundering Scheme That Victimized U.S. Investors*, DEPT JUST. (Mar. 7, 2019), <https://www.justice.gov/usao-edny/pr/three-former-mozambican-government-officials-and-five-business-executives-indicted> [https://perma.cc/SVK6-DFL8] (archived Aug. 28, 2020).

11. *Mozambique Sues in UK to Cancel Debt in Secret Loan Case*, JUBILEE DEBT CAMPAIGN (Jan. 20, 2020), <https://jubileedebt.org.uk/press-release/mozambique-sues-in-uk-court-to-cancel-debt-in-secret-loan-case> [https://perma.cc/Z2G3-K6H9] (archived Aug. 28, 2020).

12. CONST. OF THE REPUBLIC OF MOZAMBIQUE Nov. 16, 2004.

13. In this respect, the Government also violated the ordinary laws that discipline the inscription of expenditures in the budgetary law. Constitutional Council Judgment, *supra* note 1, at 17.

the *Código Civil*.<sup>14</sup> To complete the picture, in May 2020 the same Constitutional Council declared the nullity of the MAM and ProIndicus loans and the related guarantees.<sup>15</sup> The impact of these declarations of nullity by the Constitutional Council on the financial transactions is still to be appreciated in full.

Against this background, the purpose of this work is to ascertain whether and to what an extent the much invoked, but scarcely applied, odious debt doctrine may play a role in the lawsuits related to the Mozambican loan transactions. Part I analyzes the national norms coming into play before domestic courts, with particular reference to two issues: the effects on the loan and guarantee agreements of the declarations of invalidity rendered by the Mozambican Constitutional Council; and the availability of the restitutionary remedies in relation to the enforceability of contracts tainted with corruption. As the application of national laws may result in piecemeal decisions, a solution can be to have recourse to a uniform benchmark like the odious debt doctrine. Part II effectuates a reconstruction of the odious debt doctrine to understand what legal status it possesses and concludes that it would be reasonable to qualify the doctrine under transnational public policy. Part III explores the notion of transnational public policy and its applicability in relation to international contracts before domestic fora. In this context, the Mozambican transactions may become a benchmark to test the scope of the odious debt doctrine beyond the traditional arena of state succession.

## II. LEGAL PROBLEMS

The three Mozambican financial transactions present certain specificities. The ProIndicus and MAM loans were arranged under a cloak of secrecy as their proceeds were used to acquire military equipment for the security services and the Ministry of Defense. By contrast, contracting the Ematum financing was not hidden: the existence of the Ematum LPNs was discussed in various IMF country reports, had been included in the country's public debt statistics, and these notes were publicly traded and included in JPMorgan's emerging market bond index.<sup>16</sup> When the LPNs were extinguished and replaced with sovereign eurobonds, they were fully disclosed and approved by

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14. The Constitutional Council made reference to the combined provisions of Articles 294 (nullity of transactions infringing mandatory rules of law), 286 (nullity demanded at any time by the interested party and declared *ex officio* by the seized court), and 289 (retroactive effect of nullity and retrogression of what has been given). *Id.* at 17–18.

15. República de Moçambique Conselho Constitucional [Republic of Mozambique Constitutional Council], May 8, 2020, Acórdão n° 7/CC/2020 (Mozam.).

16. Olivares-Caminal, *supra* note 2.

the Mozambican Parliament. Nevertheless, for various reasons, all these loans and guarantees may be challenged in court.

A. *The Internal Validity of the Transactions*

Both the judgments of the Mozambican Constitutional Council and the decision of the Mozambican administrative court cast doubt on the authority of the Mozambican government to provide guarantees. Broadly speaking, the question of the capacity of a government to enter into financial transactions does not depend on the law governing the transaction, but on the internal law of the state. In the last century, the act of borrowing was viewed as an expression of sovereignty on the same footing as the printing of currency.<sup>17</sup> Currently, Parliamentary authorization has lost its sovereign characterization and can be considered a step in the borrowing process.<sup>18</sup> The capacity of a government to bind the state must be appreciated in two regards: the authority of the government to enter into a financial transaction and the formal requirement to do so.<sup>19</sup>

Under the financial practice, when the borrower or the guarantor is a sovereign state or a state-controlled entity, the loan or guarantee agreement is completed by a condition precedent under which the transaction cannot become operative until the government has provided documentary evidence that the transaction is valid and enforceable and that it has the power and the authority to enter into the agreement.<sup>20</sup> Generally, the declaration on the validity of the transaction is encapsulated in the representations and warranties made by the borrower.<sup>21</sup> Its inclusion in the conditions precedent also emphasizes that the transaction cannot be carried out until the borrower gives evidence of what it has represented and warranted. Normally, the documentation of the borrower is completed by a legal

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17. Luis M. Drago, *State Loans in Their Relation with International Policy*, 1 AM. J. INT'L L. 692, 695–696 (1907). The internal invalidity of the loan transactions was often used as a means to repudiate the loans. This is what occurred in the second half of the nineteenth century in relation to the debt contracted by certain US southern states; in particular, North Carolina and South Carolina. In both cases, the debts were incurred in plain violation of the state constitution and were later repudiated. REGINALD C. MCGRANE, *FOREIGN BONDHOLDERS AND AMERICAN STATE DEBTS* 334–54 (1935).

18. Georges van Hecke, *Problèmes Juridiques des Emprunts Internationaux*, XVIII BIBLIOTHECA VISSERIANA 1, 20 (1964).

19. Charles Cheney Hyde, *The Negotiation of External Loans with Foreign Governments*, 16 AM. J. INT'L L. 523, 525–26 (1922).

20. ANDREW MCKNIGHT, *THE LAW OF INTERNATIONAL FINANCE* 112 (2008).

21. RAVI C. TENNEKON, *THE LAW & REGULATION OF INTERNATIONAL FINANCE* 71 (1991).

opinion made by a lawyer belonging to the jurisdiction of the borrower that the transaction at hand is valid and binding.<sup>22</sup>

This practice is now reinforced by the United Nations Conference on Trade and Development (UNCTAD) Principles on Promoting Responsible Sovereign Lending and Borrowing.<sup>23</sup> Pursuant to Principle Number 3, lenders have a specific responsibility to determine whether the financial transaction has been duly authorized and is valid and enforceable under the relevant jurisdictions. If these conditions are not met, the lenders should refrain from concluding the agreement. However, the rule that loans to public borrowers are always invalid unless properly authorized does not amount to a general principle of law. At most, it may be qualified as an emerging principle that reflects a good and reasonable practice. By contrast, it is an accepted general principle of law that, for a contract to be valid, the borrower needs to have at least *prima facie* authority, while the lender must not behave in bad faith in this respect.<sup>24</sup>

### 1. Ostensible Authority

The ostensible authority of the agent to bind his principal must be appreciated in the light of the law applicable to the contract that, in the case of the Mozambican guarantees, corresponds to English law.<sup>25</sup> Under English law, the doctrine of apparent authority stipulates that when a “person by words or conduct represents to a third party that

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22. G.A. PENN, A.M. SHEA & A. ARORA, 2 BANKING LAW: THE LAW AND PRACTICE OF INTERNATIONAL BANKING 101–03 (1987).

23. U.N. Conference on Trade & Development, Principles on Promoting Responsible Sovereign Lending and Borrowing 6 (Jan. 10, 2012), [https://unctad.org/system/files/official-document/gdsddf2012misc1\\_en.pdf](https://unctad.org/system/files/official-document/gdsddf2012misc1_en.pdf) [<https://perma.cc/ZP9W-XLM6>] (archived Dec. 19, 2020) [hereinafter UNCTAD, *Principles on Promoting*]. The Principles constitute the outcome of the UNCTAD Project on Promoting Responsible Sovereign Lending and Borrowing. *See id.* at 3–4.

24. Matthias Goldmann, Responsible Sovereign Lending and Borrowing: The View from Domestic Jurisdictions 18–19 (Feb. 2012), [https://unctad.org/en/PublicationsLibrary/gdsddf2012misc3\\_en.pdf](https://unctad.org/en/PublicationsLibrary/gdsddf2012misc3_en.pdf) [<https://perma.cc/H4XW-EVSU>] (archived Sept. 21, 2020).

25. ASSEMBLEIA DA REPUBLICA VIII LEGISLATURA, *supra* note 9, at 36–37. The matter does not fall within the purview of the Rome I Regulation that excludes from its scope the “question whether an agent is able to bind a principal, or an organ to bind a company or body corporate or incorporate, to a third party” (art. 1(2)(g)), with the result that the criterion to determine the applicable law is left to common law. Regulation of the European Parliament and of the Council Regulation (EC) 593/2008 of 7 June 2008 on the Law Applicable to Contractual Obligations (Rome I), 2008 O.J. (L 177) 6 [hereinafter Rome I Regulation]. In regard to this, common law establishes that the issue whether an agent is able to bind the principal to contract with a third party is governed by the law applicable to the contract. *See* DICEY, MORRIS & COLLINS, 2 THE CONFLICT OF LAWS 2122 *et seq.* (Lord Collins of Mapesbury ed., 14<sup>th</sup> ed. 2012).

another has authority to act on his behalf, he may be bound by the acts of that other as if he had in fact authorised them.”<sup>26</sup>

The doctrine of ostensible authority was applied by the Queen’s Bench in a case concerning the failure to pay certain Ukraine bonds held by Russia.<sup>27</sup> One of the arguments raised by Ukraine to justify the default was that the Minister of Finance, who signed the loan agreement, lacked the proper authorization to do so.<sup>28</sup> On the one hand, the loan agreement disregarded the budgetary limits contained in the annual budget law that could be amended only in force of an act of Parliament. On the other hand, the Council of Ministers did not follow all of the procedural rules for borrowing. All in all, this has brought the capacity of Ukraine to enter into a valid loan agreement with Russia into question. The Queen’s Bench dismissed this defense giving a different view of the capacity to borrow and ostensible authority. In terms of the capacity of Ukraine to borrow, the court espoused the argument that was laid down by the trustee of the bonded loan, under which restrictions on state activity cannot be presumed.<sup>29</sup> In doing so, the court did not pay much attention to the fact that the trustee was referring to the *Lotus* case (*France v. Turkey*) that dealt with an interstate dispute, while in the case at hand the dispute was with the trustee.<sup>30</sup> In terms of the ostensible authority to sign the contract by the Ukraine government, the court held that the issue was to be assessed under English law that was the law governing the transaction. In this context, the court emphasized that the transaction documents clearly recorded that Ukraine was represented by the Minister of Finance acting upon the instructions of the Cabinet of

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26. Francis M.B. Reynolds, *Agency*, in 2 CHITTY ON CONTRACTS 1, 35–36 (Hugo G. Beale ed., 31st ed. 2012).

27. Following the deflagration of the USSR, Ukraine adopted a policy of close relations with the EU that culminated in a proposal to enter into an Association Agreement with the EU (2013). Russia vigorously opposed this possibility and in the end the Ukraine government was obliged to renounce to the EU agreement. In exchange for that renunciation, Russia granted financial support to Ukraine in the form of \$15 billion. The first tranche of the loan consisted of \$3 billion, secured by Ukrainian bonds issued under a trust deed governed by English law. Following the Russian annexation of Crimea and the intestine war, the Ukraine government decided to stop servicing the bonds. In the face of a default, the trustee—instructed by Russia—applied to the English High Court for a summary judgement in relation to the payment on the bonds. *Law Debenture Tr. Corp. v. Ukraine* [2017] EWHC 655 (QB), [2017] 1 CLC 298, [298], [304]–[06], [341]–[46] (Eng.).

28. *Id.* at [330].

29. *Id.* at [336].

30. The trustee referred to RUSTEL SILVESTRE J. MARTHA, THE FINANCIAL OBLIGATION IN INTERNATIONAL LAW 203 (2015), which considers the tenet enunciated in the *Lotus* Case applicable to the field of international financial law, under which the rules of law binding upon states derive from their own free will as expressed in conventions or by usages generally accepted as reflecting principles of law and restrictions cannot be presumed. *Id.* at [328–31]; see *S.S. Lotus (Fr. v. Turk.)*, Judgement, 1927 P.C.I.J. (ser. A) No. 10, at 18 (Sept. 7).



Ministers. Moreover, there were previous instances of signature by the Minister of Finance of bond issuances under the same trust. Hence, the ostensible authority of the Minister of Finance to sign this type of document was plainly established.<sup>31</sup>

The ruling of the Queen's Bench constitutes a precedent in relation to the validity of the Mozambican guarantees, especially since English courts are the competent forum and English law is the applicable law. Also, in this case, the key point is the ostensible or usual authority by the government to sign financial agreements in the name of and on behalf of the Mozambican state. This point is to be appreciated in the light of the criteria laid down in the decision mentioned above. In this case, the Minister of Finance signed the documents upon instructions of the government and the signature regarded all the guarantee agreements. Moreover, the Ematum transaction was endorsed by a resolution of the Mozambican Parliament. The elements of an ostensible authority may be found.

## 2. Overriding Mandatory Rules

The doctrine of ostensible authority generally preserves the whole transaction from being affected by the internal invalidity of the loan. Nevertheless, the issue of the internal validity might still come into play in the form of an overriding mandatory rule of Mozambique.

Under Article 9(1) of the Rome I Regulation,<sup>32</sup> overriding mandatory rules are those provisions, the respect for which is regarded as crucial by a country for safeguarding its public interests, such as its political, social, or economic organization, to be applied irrespective of the law applicable to the contract.<sup>33</sup> This notion must be appreciated in three respects. First, not all of the mandatory provisions of a foreign state can qualify themselves as overriding mandatory provisions and prevail over the mandatory rules of the forum.<sup>34</sup> Second, respect for these provisions must be crucial to preserve a public interest that involves the political, economic, and social organization of a country.

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31. *Law Debenture Tr. Corp.* [2017] 1 CLC at [336]–[37].

32. Rome I Regulation, *supra* note 25.

33. This notion reflects the judgment rendered by the European Court of Justice in *Arblade* under which “[t]he fact that national rules are categorised as public-order legislation does not mean that they are exempt from compliance with the provisions of the Treaty. . . . The considerations underlying such national legislation can be taken into account by Community law only in terms of the exceptions to Community freedoms expressly provided for by the Treaty and, where appropriate, on the ground that they constitute overriding reasons relating to the public interest.” Joined Cases C-369/96 & C-376/96, *Criminal Proceedings Against Jean-Claude Arblade*, 1999 E.C.R. I-8453, ¶ 31.

34. Overriding mandatory rules of the applicable law take precedence over the mandatory rules of the forum. See Andrea Bonomi, *Art. 9: Overriding Mandatory Provisions*, in 2 EUROPEAN COMMENTARIES ON PRIVATE INTERNATIONAL LAW: ROME I REGULATION - COMMENTARY 599, 620 (Ulrich Magnus & Peter Mankowski eds., 2017).

Antitrust regulations, embargoes and economic sanctions, regulations of the stock exchange, and exchange controls fall into this category.<sup>35</sup> Third, these provisions must have an overriding effect, which means they are to be applied regardless of the normal rules on conflict-of-laws.

Under the Rome I Regulation, overriding mandatory rules of a third country may come into play indirectly on the basis of the *lex fori* and directly as part of the law of the third country.<sup>36</sup> With reference to the *lex fori*, the overriding mandatory rules of a third country would come into play not so much *per se*, but under the public policy of the forum (Article 9(2)).<sup>37</sup> With reference to the law of a third country, the application of overriding mandatory rules is subjected to many conditions (Article 9(3)). First of all, the overriding mandatory provisions can be applied only if they render the performance of the contract unlawful. Second, the mandatory provisions must belong to the country where the obligations arising out of the contract have to be or have been performed. However, even though these conditions are met, the seized court enjoys a wide range of discretion in deciding whether or not to apply the overriding mandatory rules in question. In this process, the seized court is called to consider the nature and purpose of the overriding mandatory provisions and the consequences of their application or nonapplication.<sup>38</sup> This assessment involves striking a balance between all the interests at stake: those of the parties, those of the forum, those of the state of the overriding mandatory rules, and those of the state of the law governing the contract.<sup>39</sup>

Against this background, the Mozambican constitutional norms on the internal invalidity of the loan can be easily categorized as overriding mandatory rules, as they partake of the political, social, and economic order of the state. These constitutional norms can come into play indirectly under the *lex fori* to the extent that it prohibits the enforcement of contracts that involve the performance of an illegal act pursuant to the laws of a friendly foreign state. It is up to the English

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35. *Id.* at 621.

36. On this distinction see Adeline Chong, *The Public Policy and Mandatory Rules of Third Countries in International Contracts*, 2 J. PRIV. INT'L L. 27, 40–47 (2006).

37. In *Regazzoni v. K.C. Sethia* [1958] A.C. 301 (HL), the foreign mandatory rule was not applied *per se*, but because it was against English public policy to enforce contracts that involved the performance of an illegal act according to the laws of a friendly foreign state. See Chong, *supra* note 36, at 41–42 (discussing *Regazzoni v. K.C. Sethia*).

38. Jonathan Harris, *Mandatory Rules and Public Policy Under the Rome I Regulation*, in *ROME I REGULATION: THE LAW APPLICABLE TO CONTRACTUAL OBLIGATIONS IN EUROPE* 269, 325–30 (Franco Ferrari & Stefan Leible eds., 2009).

39. This is a sort of comity doctrine assessment. To the extent that the interests of the state of the overriding mandatory rules are deemed to prevail, the foreign act is enforced provided that this is consistent with the laws and policies of the forum. See Joel R. Paul, *Comity in International Law*, 32 HARV. INT'L L. J. 1, 43–44 (1991).

judge to operate such an appreciation that would displace the rules on ostensible authority. These constitutional norms can also come into play directly under the law of a third country, provided that a series of conditions are met. The first condition is that these norms must belong to the state where the contractual obligations are to be performed and are capable of making the performance unlawful. In the present case, the loan transactions have been performed in Mozambique and are illegal under the law of Mozambique, as emphasized by the Mozambican Constitutional Council. The second condition is that the seized forum is required to make an evaluation of all the interests at stake, in particular of the consequences of the application of the Mozambican overriding mandatory rules. In this regard, however, the English judge might conclude that the necessity of preserving the binding nature of the loan contracts and the orderly functioning of financial markets for sovereign debt constitute prevailing interests of the forum.<sup>40</sup>

### 3. Novation

Even though Mozambican constitutional norms should apply, and the invalidity would affect the performance of the transactions, it is questionable whether and to what extent this invalidity would affect the bonded loan issued by the Mozambican government. This is particularly true with reference to Ematum, because the Ematum loan underwent a restructuring process.<sup>41</sup> From a substantive standpoint, a restructuring operation consists of a debt conversion under which the old debt is exchanged for bonds of minor nominal value issued by the same debtor. The forerunner of these restructuring operations was the auction organized by Mexico in 1988, at which holders of syndicated debts tendered their credits in exchange for Mexican bonds secured by twenty-year zero-coupon US Treasury bonds held in escrow at the Federal Reserve Bank of New York.<sup>42</sup> From a formal standpoint, this operation amounts to an objective novation. Novation is a civilian institute that permits the extinction of the original obligation and its replacement with another between the same or new parties (or some of them).<sup>43</sup> In this context, the bonds issued under the restructuring of the Ematum loan amount to a completely new obligation with different terms and conditions and a new debtor (here, the Republic of

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40. Such an outcome would be consistent with the fact that London is one of the major financial centers.

41. See *supra* Part I.

42. Michael Chamberlin, Michael Gruson & Paul Weltchek, *Sovereign Debt Exchanges*, 1988 U. ILL. L. REV. 415, 450–51.

43. Andrew S. Burrows, *Assignment*, in 1 CHITTY ON CONTRACTS 1495, 1515–16 (Hugo G. Beale ed., 31st ed. 2012).

Mozambique).<sup>44</sup> Hence, the Mozambican bonded loan should not be affected by the invalidity of the Ematum loan transaction that has been wholly extinguished.<sup>45</sup> Nevertheless, a recent amendment to the French Civil Code may question this assumption. New Article 1331 of the French Civil Code provides that, if the obligations are not valid, their novation does not produce any effect.<sup>46</sup> In this connection, it is worth considering that the ways of extinguishing the obligations are governed by the law governing the original contract,<sup>47</sup> in this case English law. Although French law is not the governing law, it may nonetheless constitute a benchmark for a common law judge to understand a civilian notion like novation.

### B. *Corruption and Enforceability of Contracts*

There is a strong claim that the Mozambican financial transactions were tainted, though at different degrees, with corruption.<sup>48</sup> It is certainly true that globalization, including financial globalization, is often combined with transnational bribery.<sup>49</sup> This is a harmful phenomenon that produces economic, systemic, and social damages<sup>50</sup> and is capable of threatening the rule of law, property rights, and the enforcement of contracts, and of contributing to undermining the legitimacy of a tainted government.<sup>51</sup> Since it is a transnational phenomenon touching on economic connecting points, corruption has progressively become the object of international conventions, the most far-reaching of which is the (2003) UN

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44. Olivares-Caminal, *supra* note 2.

45. *See id.* But see JEFF KING, THE DOCTRINE OF ODIOUS DEBT IN INTERNATIONAL LAW 188 (2016).

46. New Art. 1331 of the French Civil Code was introduced by Ordonnance No 131-2016. CODE CIVIL [C. CIV.] [CIVIL CODE] art. 1331 (Fr.). In this way, French law has acknowledged the old rule “*ce qui est nul ne peut être susceptible d’aucun effet*” laid down by Robert Joseph Pothier in his *Traité des Obligations*, in 1 OEUUVRES DE POTHIER, sect. 589 (ed. 1824).

47. *See* Rome I Regulation *supra* note 25, Art. 12(1)(d); *see also* DICEY, MORRIS & COLLINS, *supra* note 25, at 1860.

48. *Cf. supra* Part I (discussing the irregularities and covert nature of some of the loans).

49. According to the World Economic forum statistics, the global cost of corruption is at least \$2.6 trillion, or 5 percent of the global gross domestic product (GDP), and, according to the World Bank, businesses and individuals pay more than \$1 trillion in bribes every year. *See* Press Release, Security Council, Global Cost of Corruption at Least 5 Per Cent of World Gross Domestic Product, Secretary-General Tells Security Council, Citing World Economic Forum Data, U.N. Press Release SC/13493 (Sep. 10, 2018).

50. *See* Philip M. Nichols, *Regulating Transnational Bribery in Times of Globalisations and Fragmentation*, 24 YALE J. INT’L L. 257, 270–279 (1999).

51. *See* Christiana Ochoa, *From Odious Debt to Odious Finance: Avoiding the Externalities of a Functional Odious Debt Doctrine*, 49 HARV. J. INT’L L. 109, 144 (2008).

Convention Against Corruption.<sup>52</sup> Article 16 of the UN Convention imposes the criminalization of active bribery by foreign public officials and invites the signatory states to criminalize the passive bribery of these public officials. The UN Convention, in addressing the consequences of an act of corruption, enables the signatory states to consider corruption a relevant factor in legal proceedings to annul or rescind contracts, withdraw a concession or other similar instrument, or take any other remedial action (Article 34).<sup>53</sup> This option implies that the enforceability of a contract tainted with corruption is still mainly left to the norms of the domestic legal orders.

Under the English doctrine of illegality and public policy, “no court will lend its aid to a man who founds his cause of action upon an immoral or illegal act.”<sup>54</sup> This doctrine is essentially a procedural rule that precludes the enforcement of a contract and the provision of other remedies.<sup>55</sup> Broadly speaking, a contract is illegal when it contravenes the law in terms of formation and performance.<sup>56</sup> Illegality may concern not only the contract to which it is directly related, but also collateral transactions connected to this contract.<sup>57</sup> Against this background, if an upstream corruptive activity could be proved, the downstream Mozambican financial transactions would follow its fate.<sup>58</sup>

### 1. Restitutionary Remedies

Even though the doctrine of illegality would bar the enforceability of a contract, it could still be possible to recover money under the law of restitution that is meant to reverse unjust enrichment. The core of this branch of law consists of the fact that no one can be enriched at

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52. G.A. Res. 58/4 (Oct. 31, 2003).

53. Juan Bautista Justo, *UNCTAD's Principles on Public Debt and the United Nations Convention against Corruption: Links and Common Strategies*, in *SOVEREIGN FINANCING AND INTERNATIONAL LAW*, 189, 206–07 (Carlos Esposito, Yeufen Li, Juan Pablo Bohoslavsky eds., 2013).

54. The courts follow this route “not for the sake of the defendant, but because they will not lend their aid to such a plaintiff”; moreover, “where both are equally in fault, potior est condicio defendentis,” *Holman v. Johnson* [1775] 1 Cowp. 341, 343 (Lord Mansfield) (Eng.).

55. See Dan D. Prentice, *Illegality and Public Policy*, in 1 *CHITTY ON CONTRACTS* 1223, 1228 (Hugo G. Beale ed., 31st ed. 2012). The rule goes back to *Evert v. Williams* (1725) where the Court of Exchequer refused to enforce a contract meant to share the profits of armed robbery between two highwaymen. The text of the judgment is lost, but it is possible to read an account in the *Law Quarterly Review*. See 9 *L. Q. REV.* 197 (1893).

56. See Prentice, *supra* note 55, at 1229–30.

57. See *id.* at 1325–26; A discussion of connected transactions can be found in *Nayyar v. Denton Wilde Sapte*. See [2009] EWHC 3218 (QB) (Eng.).

58. It is also a general principle of law that contracts resulting from acts of corruption are void. See *Goldmann*, *supra* note 24, at 34.

the expense of another without a justification.<sup>59</sup> In civil law systems, unjustified enrichment is usually categorized as a *quasi ex contractu* obligation, while in common law systems it is the basis of the law of restitution.<sup>60</sup>

However, restitution cannot be granted if doing so would have the same effect as enforcing unenforceable contracts.<sup>61</sup> In these cases, no court will give assistance to either party for restitution. This implies that the illegality of a contract may operate not only to bar the enforcement of that contract, but also to disqualify the claimant's right to restitution of the benefits transferred under the contract.<sup>62</sup>

With regard to this, the UK Supreme Court in *Patel v. Mirza* laid down some criteria that should guide the judge in deciding whether and to what extent the public interest would be harmed in enforcing a claim to recover money under an illegal agreement.<sup>63</sup> The case concerned the provision of money to trade in shares under an insider dealing scheme. The illegal activity did not take place, and the plaintiff brought a lawsuit to have his money back based, *inter alia*, on unjust enrichment. Lord Toulson, delivering the opinion with which the majority agreed, highlighted that illegality may provide a defense to civil claims of every sort. In civil claims, there are two discernible policies underlying the doctrine of illegality: first, a person should not be allowed to profit from his wrongdoing; second, the law should be coherent and not self-defeating, "condoning illegality by giving with the left hand what it takes with the right hand."<sup>64</sup> As a matter of principle, a person should not be debarred from recovering what was transferred under an unlawful consideration, unless some public interest is seriously harmed. In this context, three criteria may come into consideration. First, it is necessary to consider the underlying purpose of the provision that has been infringed and whether this purpose can be reinforced by the denial of the claim; second, it is necessary to consider other public policies on which the denial of the claim may have

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59. According to Lord Mansfield "the defendant, upon the circumstances of the case, is obliged by the ties of natural justice and equity to refund the money." *Moses v. Macferlan* (1760) 2 Burr 1005, 1012 (Eng.). In other words, the defendant has been enriched, this enrichment occurred at the expense of the plaintiff, and it is unjust to permit him to retain this benefit. See ROBERT GOFF & GARETH JONES, *THE LAW OF RESTITUTION* 14–16 (1st ed. 1966).

60. See Paolo Gallo, *Unjust Enrichment: A Comparative Analysis*, 40 AM. J. COMP. L. 431, 436 (1992); Daniel P. O'Connell, *Unjust Enrichment*, 5 AM. J. COMP. L. 2, 2–3, 14 (1956).

61. See RICHARD A. BUCKLEY, *ILLEGALITY AND PUBLIC POLICY* 265 (2nd ed. 2009).

62. See William J. Swalding, *The Role of Illegality in the English Law of Enrichment*, in UNJUSTIFIED ENRICHMENT: KEY ISSUES IN COMPARATIVE PERSPECTIVES 289, 298 (David Johnston & Reinhard Zimmerman eds., 2002).

63. See *Patel v. Mirza* [2016] UKSC 42 [120] (appeal taken from EWCA (Civ)); see also Andrew Burrows, *Illegality after Patel v. Mirza*, 70 CURRENT LEGAL PROBS. 55, 59 (2017).

64. *Patel*, [2016] UKSC 42 at [99].

an impact; and, third, it is necessary to consider whether the denial of the claim would be a proportionate sanction, considering that punishment is a matter for the criminal court.<sup>65</sup> Although the effective acknowledgment of these criteria in lower courts is still uncertain,<sup>66</sup> Lord Toulson warned that there may be rare cases where the enforcement of claims based on unjust enrichment might be considered as “undermining the integrity of the justice system.”<sup>67</sup>

The issue of proportionality has been also acknowledged in the US legal system, where the *Restatement 2d of Contracts* stipulates that a party has no claim in restitution for the performance he has made under or in return of a promise that is unenforceable for public policy, unless this would involve a disproportionate forfeiture.<sup>68</sup> The disproportion of the forfeiture must be appreciated in the light of the public interest involved and the extent of the contravention: “if the claimant has threatened grave social harm, no forfeiture will be disproportionate.”<sup>69</sup>

Once corruption is proved in relation to the Mozambican transactions, the availability of a restitutionary remedy must be tested in the light of the three criteria laid down in *Patel v. Mizra*. In terms of underlying purpose of the infringed prohibition, the aim is to ensure market integrity and fair competition among lenders. In terms of additional public policy, the denial of the claim would lead lenders to reinforce internal mechanisms of audit and compliance. In terms of proportionate response, the issue will be evaluated in light of the consequences of the fraudulent activity. Nevertheless, even though these three criteria should be cumulatively satisfied, the final warning of Lord Toulson to bar the defense only in “rare cases” could tip the scales in favor of granting the remedy.

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65. *See id.* at [120].

66. *See* Matthias Goldmann, *The Law and Political Economy of the Mozambique’s Odious Debt*, in HOW TO AVOID THE REPETITION OF “ODIOUS” DEBTS? 6 (2019).

67. Patel, [2016] UKSC 42 at [121] (Toulson, LJ). However, the granting of the restitutionary remedies cannot amount to a stultification of the law. *See* GOFF & JONES: THE LAW OF UNJUST ENRICHMENT 897–900 (Charles Mitchell, Paul Mitchell & Stephen Watterson eds., 9th ed. 2016).

68. RESTATEMENT (SECOND) OF CONTRACTS § 197 (AM. LAW INST. 1981). Sections 198 and 199 provide some temperaments to this rule when a party has not engaged in serious misconduct and he has withdrawn from the transaction before the purpose had been implemented, when allowing the claim would put an end to a continuing situation in contrast with the public interest, or when a party was excusably ignorant of the facts or of a legislation of minor importance or he was not equally involved in the promise. *See id.* §§ 198–99.

69. *Id.* § 197 cmt. b.

## 2. Unclean Hands

The *Restatement 3d of Restitution and Unjust Enrichment*, reformulating the rules of the *Restatement 2d of Contracts*, has stipulated that there is no claim when the allowance of restitution would defeat the policy of the law that makes the agreement unenforceable.<sup>70</sup> In this context, two competing policies come into play: the policy against unjust enrichment and the policy prohibiting the underlying transaction. If these policies are incompatible, the public policy against the enforcement of the transaction prevails over the private claims based on unjust enrichment. In these cases, the restitutionary remedy can also be denied on the basis of the inequitable conduct of the claimant that is the source of the asserted liability: “he who comes into equity must come with clean hands.”<sup>71</sup>

A meaningful application of the defense of “unclean hands” is given in *Adler v. Nigeria* where the plaintiff became involved in a series of false transactions in which he should have received some money under over-invoiced contracts with Nigeria.<sup>72</sup> Under the fraudulent scheme, Adler, the plaintiff, provided \$5 million to the Nigerian officials in exchange for transactions worth \$60 million. As that fraudulent scheme broke down, Adler did not receive anything and sued Nigeria before the federal courts of California to reclaim the sums given to the Nigerian officials. On appeal, the court rejected the argument submitted by the plaintiff that denying the remedy would involve an unjust enrichment to Nigerian officials. The court underscored that, although the fraudulent scheme was concocted by Nigerian officials, Adler had freely joined it. In this context, granting the remedy when the bribe had not reached the hoped-for result would encourage individuals like the plaintiff to take part into these schemes.<sup>73</sup>

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70. RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 31 (AM. LAW INST. 2011).

71. The defense of the “unclean hands” comes from a maxim elaborated by the English Barrister Richard Francis in his book *MAXIMS OF EQUITY* (1728): “he who hath committed iniquity shall not have equity.” RICHARD FRANCIS, *MAXIMS OF EQUITY* 5 (1728). Later, it was acknowledged by the United States Supreme Court. *See generally* *Talbot v. Jansen*, 3 U.S. 133 (1795). The defense has the purpose of preserving the integrity of the judicial system that would be undermined by the allowing a claimant with unclean hands to recover. *See* T. Leigh Aneson, *Announcing the “Clean Hands” Doctrine*, 51 U.C. DAVIS L. REV. 1827, 1841 (2018).

72. *See generally* *Adler v. Federal Republic of Nigeria*, 219 F.3d 869 (9th Cir. 2000).

73. In substance, the Federal Court weighted the competing policies of discouraging frauds like that suffered by Adler and of discouraging individuals like Adler from participating in such an operation and considered the latter prevailing. *See id.* at 877.



In light of the decision rendered in the Adler case, the policy of discouraging fraudulent operations seems to prevail over the policy of avoiding unjust enrichment. Once corruption can be proved, the same rationale could plainly apply to the Mozambican loans with even more strength: in this case, the fraudulent operation was accomplished.

### III. THE ODIIOUS DEBT DOCTRINE

The multifaceted question of the validity of the Mozambican financial transactions will be decided in domestic courts on the basis of domestic laws. This involves a fragmentation in the outcomes of the lawsuits. To correct this flaw, at least partially, the solution is to have recourse to a uniform legal benchmark. In the absence of a proper international convention on the phenomenon of sovereign debt, this benchmark might be provided by the so-called “odious debt doctrine.” In this context, the key point is to ascertain the legal status of this doctrine.

#### A. *The Emergence of the Doctrine*

In the 1920s, the Russian “*émigré*” Alexander Sack elaborated a doctrine under which odious debt constituted an exception to the rule of the passage of public debt in cases of state succession and of government succession. To qualify itself as odious, a debt must be contracted by a despotic regime, not in the interest of the nation, but as a means to strengthen its power and in the lenders’ awareness of all that (“*a su des créanciers*”).<sup>74</sup>

In terms of state succession, the general rule is that local debt (i.e., debt contracted by a territorial entity of the state) and localized debt (i.e., debt contracted by the central government for local projects or areas) pass to the successor state, while in relation to national debt (i.e., debt contracted by governments for general purposes) the picture is more complicated. In the case of absorption or merger, the absorbing or newly created state shall assume the debt of the extinguished state. In the case of secession or separation, however, where the predecessor state continues its existence, the national debt will remain with the predecessor state, even though the successor state may assume a portion of the debt on an equitable basis.<sup>75</sup> In the view of Sack, an

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74. See ALEXANDER N. SACK, *LES EFFETS DES TRANSFORMATIONS DES ETATS SUR LES DETTES PUBLIQUES* 157–184 (1927). For a comment on the evolution of this concept, see ROBERT HOWSE, *THE CONCEPT OF ODIIOUS DEBT IN PUBLIC INTERNATIONAL LAW* 2 (2007), [https://unctad.org/en/docs/osgdp20074\\_en.pdf](https://unctad.org/en/docs/osgdp20074_en.pdf) [https://perma.cc/5VP2-C2YP] (archived Aug 23, 2020).

75. MALCOLM N. SHAW, *INTERNATIONAL LAW* 996–98 (6th ed. 2008).

exception to this rule concerns debts that are odious to the population or to the successor state.<sup>76</sup>

With reference to debts odious to the population, a first example concerns the controversy surrounding the Cuban debt following the Spanish–American War (1898). Towards the end of the nineteenth century, the Spanish Crown had contracted bonded debt secured by certain fiscal revenues of Cuba, the proceeds of which were used to suppress the struggle for the independence of the island.<sup>77</sup> During the peace negotiations following the defeat of Spain, the US delegation successfully pleaded the argument of the nonpassage of those debts, arguing that they were not contracted in the interest of the population.<sup>78</sup> Although the peace treaty reflected the position of the United States, the traditional rule of the passage of the debt to the annexing state was formally maintained through an *escamotage*, under which Cuba was not ceded but abandoned by the Spanish Crown.<sup>79</sup> By the same token, the Treaty of Versailles (1919) stipulated that the debt incurred by Germany and Prussia for the forced colonization of Polish lands should not have passed to Poland (Article 255).<sup>80</sup> For similar reasons, after the “*Anschluss*” of Austria (1938), the German Reich refused to assume the Austrian bonded loans organized by the League of Nations, as the guarantee agreement that backed those loans contained a clause concerning the independence of Austria from other nations that was considered against the interest of the Austrian people.<sup>81</sup> With reference to debt odious to the successor state, a first

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76. SACK, *supra* note 74, at 158–71.

77. See ERNST FEILCHENFELD, PUBLIC DEBT AND STATE SUCCESSION 329–43 (1931).

78. Although it was aware of the fact that not all the debt had been contracted for “odious” purposes, see *id.* at 339–40, the American delegation insisted that “[t]he decrees of the Spanish government itself show that these debts were incurred in the fruitless endeavors of government to suppress the aspirations of the Cuban people for greater liberty and freer government.” 1 JOHN BASSETT MOORE, A DIGEST OF INTERNATIONAL LAW 377 (1906).

79. The Treaty of Peace between Spain and the United States (signed December 10, 1898) established that Cuba was “relinquished” and not “ceded” to the United States. See Treaty of Paris art. I, Dec. 10, 1898, Spain-U.S., 187 C.T.S. 101 (“Spain relinquishes all claim of sovereignty over and title to Cuba.”). This is in contrast to the case of Puerto Rico, which was explicitly the object of cession (art. II). See SACK, *supra* note 74, at 143–44. In this way, the debt did not pass either to the United States, as the possession of the island was acquired *a non domino*, or to Cuba, as it was already occupied by US troops and so deprived of sovereignty. See FRANTZ DESPAGNET, COURS DE DROIT INTERNATIONAL PUBLIC 125 (1910).

80. The Treaty of Peace with Germany was concluded at Versailles on 28 June 1919. See Treaty of Versailles, Jun. 28, 1919, 225 C.T.S. 189; SACK, *supra* note 74, at 159–60.

81. Although the financial arrangements were made with the purpose of meeting the objective necessities of the population, the guarantor states had a clear political intent. See James L. Foorman & Michael E. Jehle, *Effects of State Succession and Government Succession on Commercial Bank Loans to Sovereign Borrowers*, 1982 U. ILL.

example concerns the debts contracted by the Boer Republics to finance warfare against the United Kingdom (1899–1902). At the time of the annexation of the defeated Boer Republics, Great Britain declared its unwillingness to recognize those obligations, arguing that debt incurred by the enemy could not pass to the victorious power.<sup>82</sup> A similar approach had already been acknowledged in the Fourteenth Amendment to the US Constitution, which excludes the debt incurred by the Confederate States to finance their rebellion (1861–1867) from the rule of maintenance.<sup>83</sup>

In terms of government succession, the general rule is that a change of government does not affect the obligations contracted by the previous government.<sup>84</sup> The exception depicted by Sack concerns the so-called *dettes de regime*. They are debts contracted by a despotic regime not for the benefit of the population, but to strengthen its power.<sup>85</sup> This type of debt may be regarded as a personal debt of the government, as found by Chief Justice Taft in the Tinoco arbitration,<sup>86</sup>

L. REV. 1, 21–22. In force of Art. 88 of the Treaty of Peace between the Allied Powers and Austria (signed 10 September 1919), the defeated country was deprived of the power to alienate its independence without the consent of the Council of the League of Nations. See Treaty of Saint-Germain art. 88, Sep. 10, 1919, 226 C.T.S. 36. This undertaking was solemnly restated by Austria in connection with the two League Loans: explicitly in Protocol No. I for Economic and Financial Assistance to Austria and implicitly in the Austrian Protocol. See Protocol No. I for Economic and Financial Assistance to Austria, Oct. 4, 1922, XII L.N.T.S. 387; Austrian Protocol, July 15, 1932, CXXXV L.N.T.S. 285.

82. See JOHN WESTLAKE, INTERNATIONAL LAW, PART I: PEACE 78 (1904) (noting a traditional understanding that a successor is not liable for loans that a predecessor took out for the purposes of funding war). In doing so, the UK government was not invoking a rule of law but rather a rule of expediency. See ARTHUR B. KEITH, THE THEORY OF STATE SUCCESSION, WITH SPECIAL REFERENCE TO ENGLISH AND COLONIAL LAW 65 (1907). In effect, under the Agreement between Great Britain and the Orange Free State and the South African Republic as to the Terms of Surrender of the Boer Forces in the Field (signed May 31, 1902), the notes issued as a war loan would have been regarded as evidence of war losses of the original holders as long as they were issued for valuable considerations (art. 10). See Peace of Vereeniging, May 31, 1902, 191 C.T.S. 234. The official position of His Majesty's government was acknowledged by Lord Alverstone. See *West Rand Gold Mining Co. Ltd. v. The King* [1905] 2 KB 391, 401–06.

83. U.S. CONST. amend. XIV, § 4; see Lee C. Buchheit, G. Mitu Gulati & Robert B. Thompson, *The Dilemma of Odious Debts*, 56 DUKE L. J. 1201, 1213, n. 29 (2007).

84. “Public debts, whether due to or from the revolutionised State, are neither cancelled nor affected by any change in the constitution or internal Government of a State.” HENRY W. HALLECK, HALLECK'S INTERNATIONAL LAW 76 (Sir Sherston Baker ed., 1878). Following the French Revolution, the Constitution of 1791 established that “[s]ous aucun prétexte, les fonds nécessaires à l'acquittement de la dette nationale . . . ne pourront être ni refusés ni suspendus.” 1791 CONST. tit. V, art. 2 (Fr.).

85. SACK, *supra* note 74, at 157, justified this position by arguing that creditors in this case “ont commis un acte ostile à l'égard du peuple; ils ne peuvent donc pas compter que la nation affranchie d'un pouvoir despotique assume le dettes 'odieuses', qui sont des dettes personnelles de ce pouvoir.”

86. “The bank knew that this money was to be used by the retiring president . . . for his personal support after he had taken refuge in a foreign country. It could not hold his own government for the money paid to him for this purpose.” Aguilar-Armory & Royal

or as a personal debt of a particular class of citizens, as highlighted by the Soviet institute of international law with particular reference to the debts incurred by the Czarist regime.<sup>87</sup> In more recent times, the doctrine was advanced by the People's Republic of China in an *aide-mémoire*,<sup>88</sup> which was submitted in a lawsuit before the Northern District Court of Alabama regarding the payments on defaulted bonds issued in 1911 by the Chinese Imperial government.<sup>89</sup>

The Jubilee 2000 campaign has led many antidebt activists to invoke the application of the odious debt doctrine beyond the narrow boundaries of state succession and government succession. As a further step, they have systematically put odious debt under the wider category of illegitimate debt that includes debt against national law, debt against public policy, and unfair or objectionable debt.<sup>90</sup> The category of illegitimate debt would cover loans to oppressive regimes (Argentina and South Africa), loans bearing usurious interest (Latin American countries), loans for bad projects (Tanzania, Nigeria, and Indonesia), loans for self-enriching regimes (The Philippines), and loans to unreliable governments (Zaire).<sup>91</sup> The motivation behind the creation of the category of illegitimate debt and the subsumption of odious debt under it is that an odious/illegitimate debt should not be repaid.<sup>92</sup> Nevertheless, the flaw in this argumentation is that the odious debt doctrine and the wider illegitimate debt doctrine lack proper legal underpinnings.<sup>93</sup>

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Bank of Canada (Gr. Brit. v. Costa Rica), 1 R.I.A.A. 369, 394 (1923); *see also infra* Part IV.E.

87. *See* Evgeny A. Korovin, *Soviet Treaties and International Law*, 22 AM. J. INT'L L. 753, 762–63 (1928) (discussing the characterization of the October Revolution as a radical change of government); Boris Mirkin-Guetzevitch, *La Doctrine Soviétique du Droit International*, 32 REVUE GÉNÉRAL DE DROIT INTERNATIONAL PUBLIQUE 313, 320–321 (1925). However, most of the Czarist debt was contracted for development purposes. *See* HAROLD G. MOULTON & LEO PASVOLSKY, *WORLD WAR DEBT SETTLEMENTS* 60 (1929).

88. On the general assumption that “it is a long-established principle of international law that odious debts are not to be succeeded to,” the aide memoire argued that, in China, a radical change of régime took place and that the railways bearer bonds constituted a means through which the previous government strengthened its oppression of the Chinese people. *See* People's Republic of China, *Aide Memoire of the Ministry of Foreign Affairs*, 22 I.L.M. 81 (1983). It concluded that “[t]his position of the Chinese Government fully conforms to the principles of international law and has a sound basis in jurisprudence.” *See id.*

89. The point was dismissed implicitly by the United States District Court for the Northern District of Alabama on the assumption of the irrelevance of political changes for the continuity of the states in international law. *See Jackson v. People's Republic of China*, 550 F. Supp. 869, 872 (N.D. Ala. 1982).

90. *See* Joseph Hanlon, *Defining “Illegitimate Debt”: When Creditors Should Be Liable for Improper Loans*, in *SOVEREIGN DEBT AT THE CROSSROADS* 109, 109–11 (Chris Jochnick & Fraser A. Preston eds., 2006).

91. *See id.* at 118–25.

92. *See* Christoph G. Paulus, *The Evolution of the “Concept of Odious Debt”*, 68 HEIDELBERG J. INT'L L. 391, 393–94 (2008).

93. Buchheit, Gulati & Thompson, *supra* note 83, at 1228–30.

With reference to the odious debt, currently the odiousness of a debt should be appreciated against three criteria, that are a reformulation of those previously identified by Sack and enfranchise the doctrine from the arena of state/government succession. These criteria are the absence of consent by the population, the absence of benefit for the population, and the awareness of this on the part of the creditors.<sup>94</sup> In terms of the absence of consent, a democratic government is presumed to have the consent of the population to govern a country and thereby also the consent to raise loans. By contrast, a nondemocratic government is not presumed to have consent to govern a country and, implicitly, to borrow. Nevertheless, in both cases this is a rebuttable presumption. On the one hand, a nonelected government may also enjoy some general consent within the population and some specific consent in relation to particular loans. On the other hand, it is questionable that under a democratic government a loan should reflect the consent of the population only because constitutional requirements have been satisfied. In this respect, the formalistic criterion of the validity of the loan is not sufficient: it is necessary to consider the benefit to the population.<sup>95</sup> In terms of the absence of benefit, it is necessary to draw a distinction between loans for general purposes and loans for specific purposes. While the odiousness can be easily established for loans related to specific projects, the beneficial impact of loans contracted for general purposes on the population must be ascertained from time to time. Under a dictatorial regime, loans for general purposes may be odious as far as they can serve to reinforce an illegitimate government, while loans for specific projects that are objectively beneficial for the population are nevertheless odious because they free funds that can be used for odious purposes.<sup>96</sup> In terms of creditors' awareness, the key point is whether it is necessary to have an actual knowledge or whether a reckless ignorance suffices. Both cases presuppose that creditors are burdened with the responsibility to make inquiry into the purpose of the loans.<sup>97</sup>

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94. SABINE MICHALOWSKY, UNCONSTITUTIONAL REGIMES AND THE VALIDITY OF SOVEREIGN DEBT 49–59 (2007).

95. *See id.* at 51.

96. *See* Juan Pablo Bohoslavsky & Veerle Opgenhaffen, *The Past and Present of Corporate Complicity: Financing the Argentinean Dictatorship*, 23 HARV. HUM. RTS. J. 157, 174 (2010). Nevertheless, “To demonstrate that the loan contributed to the violation is essential, as there would be no reason to regard a loan as invalid because of an *ius cogens* violation committed by one of the parties, the borrowing state, unless this violation bears a relation to the contract.” MICHALOWSKI, *supra* note 94, at 82.

97. MICHALOWSKY, *supra* note 94, at 58. This is feasible as far as a loan is related to a specific project, as explained in Principle No. 5 of the UNCTAD Principles on Promoting Responsible Sovereign Lending and Borrowing. *See* UNCTAD, *Principles on Promoting*, *supra* note 23, at 7. Broadly speaking, creditors should have evidence that the proceedings are used for the benefit of the population in all international development agreements. *See* Günter Frankenberg & Rolf Knieper, *Legal Problems of*

This picture should be completed by a sanction mechanism in force of which, once debts have been designated as odious/illegitimate by a specific institution, municipal courts should not enforce the loan contracts and international financial institutions should deny further financing to debtors that decide to repay those debts.<sup>98</sup> To avoid all these problems, a proposal has been formulated regarding the creation of a framework for accountable sovereign debt financing articulated into an *ex ante* component and an *ex post* component. The first component should focus on the initial assessment and continuous monitoring of the loan, while the second component should focus on the establishment of a tribunal to assess compliance with the *ex ante* obligations.<sup>99</sup>

### B. *The Doctrine and its Qualification.*

In the view of its supporters, the odious debt doctrine should invalidate a loan and neutralize the enforcement of the underlying claims. All this presupposes that the doctrine is normatively characterized. The flaw is that an intense doctrinal debate is not enough to turn policy into law.<sup>100</sup> Hence, the legal status of the doctrine is still an open question and deserves a thorough analysis.

#### 1. The Doctrine as International Law

A first approach consists of qualifying the doctrine as an international law norm. With respect to customary law, Article 38 of

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*the Overindebtedness of Developing Countries: The Current Relevance in the Doctrine of Odious Debt*, 12 INT'L J. SOC. L. 415, 434 (1984).

98. Anna Gelpern, *What Iraq and Argentina Might Learn from Each Other*, 6 CHI. J. INT'L L. 391, 413 (2005).

99. The *ex ante* component is based on the registration of sovereign contracts by foreign lenders/investors on a dedicated website to signal the purported benefits to the population and the international community. In this way, lenders are called upon to disclose their engagements with the sovereign counterpart, to require as a condition precedent that the debtor should indicate the use of the funds, to conduct an audit on the debtor government and the impact of the contract, and to monitor periodically the execution of the contract. The *ex post* component is based on the establishment of a tribunal to assess whether or not *ex ante* obligations have been fulfilled. The tribunal will be composed of independent individuals and shall adjudicate claims filed even by private persons not party to the transaction. The weak points of this proposal are the voluntary nature of the registration and the effects of the findings of the tribunal. See YVONNE WONG, SOVEREIGN FINANCE AND THE POVERTY OF NATIONS 134–65 (2012). The idea to establish an international tribunal to assess the odiousness of a debt had been already envisaged by SACK, *supra* note 74, at 163.

100. See Emily F. Mancina, *Sinners in the Hands of an Angry God: Resurrecting the Odious Debt Doctrine in International Law*, 36 GEO. WASH. INT'L L. REV. 1239, 1252–53 (2004) (“To assert, or even prove, that odious debt is bad for the Third World is not tantamount to a logical integration of the principle into international law.”).

the ICJ Statute stipulates that it amounts to “a general practice accepted as law.”<sup>101</sup> In relation to the material element, the ICJ has ruled that there must be a constant and uniform usage practiced by states,<sup>102</sup> while in relation to the psychological element two approaches have emerged. First, the existence of this element may be inferred from the very general practice, the literature, or previous judgments.<sup>103</sup> Second, the existence of this element must effectively be proved.<sup>104</sup> However, with reference to the phenomenon of state succession, since 1945, practice has not recorded significant instances of nonpassing debt on the basis of the odious debt doctrine.<sup>105</sup> There is an exception, perhaps, of the debts relating to the Dutch administration of Indonesia (1949) and the French administration of Algeria (1962).<sup>106</sup>

With respect to treaty law, the issue arose within the draft articles on succession of states in respect of state debt.<sup>107</sup> In his Report on the nontransferability of odious debt, Professor Bedjaoui singled out two definitions of odious debt: debt contracted by the antecessor state to serve purposes contrary to the major interests of either the successor state or the transferred territory; and debt contracted for purposes not in conformity with international law and, in particular, with the principles of the United Nations.<sup>108</sup> With specific reference to this second point, Professor Bedjaoui emphasized that, in terms of ethics, the odiousness of a debt must be appreciated in relation to human rights and the right to self-determination, on the one hand, and to the unlawful recourse to war, on the other.<sup>109</sup> Once it has been established

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101. See, e.g., SHAW, *supra* note 75, at 72–93.

102. Asylum (Colom. v. Peru), Judgment, 1950 I.C.J. 266, at 276–77 (Nov. 20).

103. See Delimitation of the Maritime Boundary in the Gulf of Maine Area (Can./U.S.), Judgment, 1984 I.C.J. 246, ¶ 90 (Oct. 12).

104. See North Sea Continental Shelf (Ger./Neth.), Judgment, 1969 I.C.J. 3, at 32–41 (Feb. 20).

105. See Andrew Yianni & David Tinkler, *Is There A Recognized Legal Doctrine of Odious Debt?*, 32 N.C. J. INT'L L. & COM. REG. 749, 766-67 (2007) (The lack of invocation was surprising considering the post-colonization process and the disaggregation of the Soviet Union and the Federation of Yugoslavia).

106. KING, *supra* note 45, at 80–82.

107. See Vienna Convention on Succession to State Property, Archives and Debts, pt. 4, Apr. 8, 1983, 22 I.L.M. 306; 1983 Vienna Convention on the Succession of States in Respect of State Property, CENTRE FOR INTERNATIONAL LAW, <https://cil.nus.edu.sg/database/cil/1983-vienna-convention-on-the-succession-of-states-in-respect-of-state-property-archives-debt> (last visited Sept. 6, 2020) [<https://perma.cc/XG37-AYSY>] (archived Sept. 6, 2020) (demonstrating that the Convention has never entered into force due to its lack of signatory parties).

108. Mohammed Bedjaoui (Special Rapporteur), *Ninth Report on Succession of States in Matters Other than Treaties*, [1977] 2 Y.B. Int'l L. Comm'n. 45, U.N. Doc. A/CN.4/301 [hereinafter Bedjaoui, *Ninth Report*].

109. Bedjaoui made specific reference to debt incurred to purchase arms to violate human rights through genocide and racial discrimination, to debt incurred to subjugate peoples and colonize their territories, and to debt incurred to finance a war of aggression. *Id.* at 69.

that a debt is odious, the natural consequence is its nonpassage to the successor state. Regarding to this, Professor Bedjaoui distinguished between war debt and subjugation debt. War debt comprised the debt incurred by the Boer Republic to fight Britain and the debt contracted by the German Empire after the outbreak of World War I; subjugation debt comprised the Spanish debt secured by Cuban revenues and the German debt incurred for the colonization of Polish lands.<sup>110</sup> However, the proposal of Bedjaoui was not acknowledged in the final text of the 1983 Vienna Convention; Article 33 simply stipulates that “state debt” means any financial obligation of a predecessor state arising in conformity with international law toward another state, an international organization, or any other subject of international law. Nevertheless, the clause “in conformity with international law” would leave some room of maneuvering for the odious debt doctrine.<sup>111</sup>

The odious debt doctrine was raised before the Iran–United States Claims Tribunal<sup>112</sup> in relation to the enforceability of a contract concerning the provision of military equipment to Iran.<sup>113</sup> The Tribunal rejected the submission that supply would not have been beneficial to Iran as when the contract was made the country was not involved in war activities. Further, the Tribunal found that the odious debt doctrine was not applicable to the case as it could be invoked only in situations of state succession and not of *change de régime*.<sup>114</sup> Apart from any other consideration, the key point was that, in the view of the Tribunal, the odious debt doctrine could play a role in relation to state succession but not to government succession.

## 2. The Doctrine as a Doctrine

Under a doctrinal perspective, two primary issues arise. The former concerns the position of Sack’s doctrine within the international law scholarship, and the latter concerns the status of the odious debt doctrine as an international law doctrine.

With respect to the position of Sack’s doctrine within the international law scholarship, it is worth highlighting that, before the late 1990s, Sack’s work was not much regarded among the international law scholars. In his much-praised book on public debt

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110. *Id.* at 72–74.

111. *See* REX J. ZEDALIS, CLAIMS AGAINST IRAQI OIL AND GAS 42–43 (2010).

112. *See generally* CHARLES N. BROWER & JASON D. BRUESCHKE, THE IRAN–UNITED STATES CLAIMS TRIBUNAL 3–10 (1998).

113. U.S. v. Islamic Republic of Iran, 32 Iran-U.S. Cl. Trib. Rep. 162 (1996).

114. *Id.* at 176 (“The Tribunal does not take any stance in the doctrinal debate on the concept of ‘odious debt’ in international law. In any event, the Tribunal will limit itself to stating that the said concept belongs to the realm of the law of State succession. The revolutionary changes in Iran fall under the heading of State continuity, not State succession.”).



and debt succession, Professor Ernst Feilchenfeld reported two instances of odious debt that justified an exemption from the rule of maintenance: the Spanish debt incurred for taming insurgencies in Cuba and the German debt incurred for the colonization of lands held by Polish owners.<sup>115</sup> Both these diversions from the rule of maintenance had already been reported in Sack's book, but Professor Feilchenfeld did not feel it necessary to refer to the Russian *émigré* as an authority to reinforce his position. Along the same lines, Professor Mohammed Bedjaoui did not mention Sack's work when discussing the doctrine of odious debt in his Report on the Succession of States in Matters other than Treaties.<sup>116</sup> This exclusion is surprising as Sack's work was referred to in the book by Professor Daniel O'Connell on state succession in relation to the description of odious debt.<sup>117</sup> Nevertheless, Sack's exclusion from the Bedjaoui Report may be explained by the fact that, in his work on public debt and state succession, Feilchenfeld did not refer to Sack as an international lawyer, but as an international financial lawyer.<sup>118</sup> In effect, in his time the Russian *émigré* was praised more by economists than by lawyers.<sup>119</sup> The fortune of Sack's work changed when in an article written on the eve of the First Mexican Debt Crisis (1983) Professor Michael Hoeflich indicated Sack as a leading scholar in the field of public debt succession.<sup>120</sup> Sack's odious debt doctrine was resumed and further developed by the debt abolitionist Patricia Adams<sup>121</sup> and has since become topical among antidebt activists, especially in connection with the Jubilee campaign and the Iraqi debt reduction.<sup>122</sup> What is still lacking is a thorough acknowledgement of it by international lawyers.<sup>123</sup>

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115. See FEILCHENFELD, *supra* note 77, at 329 *et seq.*, 450 *et seq.*

116. Bedjaoui, *Ninth Report*, *supra* note 108, at 67–74.

117. DANIEL P. O'CONNELL, STATE SUCCESSION IN MUNICIPAL LAW AND INTERNATIONAL LAW 458–59 (C.J. Hamson & R.Y. Jennings eds., 1967).

118. See FEILCHENFELD, *supra* note 77, at 574–75, 590–92; see also SACK, *supra* note 74, at 133–34 (In fact, with reference to state debt succession, Sack underscored that “*Le principe de la succession des dettes publiques est donc un principe, non de droit international public réglant les rapports entre Etats, mais de droit financier et de droit public général*”; prophetically he added that “*la succession de dettes publiques semble être une institution de droit supra-étatique (überstaatliches Recht) qu'il appartient à l'avenir de formuler et d'établir d'une façon définitive*”).

119. See Sarah Ludington & Mitu Gulati, *A Convenient Untruth: Fact and Fantasy in the Doctrine of Odious Debt*, 48 VA. J. INT'L L. 595, 624–28 (2008).

120. See Michael Hoeflich, *Through a Glass Darkly: Reflections on the History of Public International Law on Public Debt in Connection with State Succession*, 1982 U. ILL. L. REV. 39, 45.

121. See PATRICIA ADAMS, ODIUS DEBTS: LOOSE LENDING, CORRUPTION, AND THE THIRD WORLD ENVIRONMENTAL LEGACY 164–67 (1991).

122. See Ludington & Gulati, *supra* note 119, at 603–04.

123. See KING, *supra* note 45, at 27–28; Margot E. Salomon & Robert Howse, *Odius Debt, Adverse Democracy and the Democratic Ideal*, in SOVEREIGN DEBT AND

With respect to the status of the odious debt doctrine in international law, the issue is whether and to what extent the doctrine, as such, has become source of law. Article 38 of the ICJ Statute enumerates legal scholarship among the sources of international law. In detail, it stipulates that the teachings of the most highly qualified publicists of the various nations constitute a subsidiary means for the determination of the rules of law.<sup>124</sup> The mention of academic writings has a double meaning. On the one hand, it plays the role of filling the lacunae embedded in international law that is a legal system without a law-making process comparable to that of national states.<sup>125</sup> On the other hand, it reflects the fact that international law has its origin in the writings of celebrated scholars—the so-called founders of modern international law.<sup>126</sup> With the rise of legal positivism the influence of scholars' writings as a source of international law declined in favor of custom and treaty where states are the actors of the law-making process.<sup>127</sup> Although in some ambit of international law, scholars' writings occasionally still have an influence on the formation of the law,<sup>128</sup> currently they are mainly referred to in arbitral tribunals and in national courts to reinforce argumentation.<sup>129</sup> As an international law doctrine, the odious debt doctrine should be pled before international courts and tribunals.<sup>130</sup> However, because of its unclear legal contours and its capacity to impair the rule of keeping to agreements, the doctrine might be confined to cases where the court or the tribunal are called on to decide *ex aequo et bono*.<sup>131</sup>

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HUMAN RIGHTS 425, 436 (Ilias Bantekas & Cephas Lumina eds., 2018). *Contra* WONG, *supra* note 99, at 16–18.

124. See Statute of the International Court of Justice art. 38, ¶ 4; *see also* Perm. Ct. Arb. Arbitration Rules art. 35, ¶ 1(a)(iv).

125. International law has no single body capable of producing laws and a machinery of compulsory jurisdiction to enforce it. This reflects the anarchic status of world affairs and the conflict between states. *See* SHAW, *supra* note 75, at 70.

126. The number counts first all Hugo Grotius, author of the celebrated *DE JURE BELLI AC PACIS* (1625), but also Albericus Gentili, Franciscus de Vitoria, Franciscus Suarez, Johannes Althusius, and Samuel von Pufendorf, to name a few. *See* ARTHUR NUSSBAUM, *A CONCISE HISTORY OF THE LAW OF NATIONS* 58–177 (1947).

127. SHAW, *supra* note 75, at 112–13.

128. This is the case, for example, with GILBERT GIDEL, *LE DROIT INTERNATIONAL PUBLIC DE LA MER* (1932), which exerted a great influence on the development of the concept of “contiguous zone” within the law of the sea.

129. They are used more rarely in the ICJ judgments and opinions to avoid problematic selection of citations. IAN BROWNLIE, *PRINCIPLES OF PUBLIC INTERNATIONAL LAW* 24–25 (7th ed. 2008).

130. The only arbitral tribunal before which the odious debt defense was unsuccessfully raised was the United States-Iran Claims Tribunals in the case *U.S. v. Islamic Republic of Iran*, 32 Iran-U.S. Cl. Trib. Rep. 162 (1996).

131. Under the ICJ the application of the *ex aequo et bono* rule is an exceptional event and depends on the explicit provision of the parties. *See generally* Free Zones of the Upper Savoy (Fr. v. Switz.), Judgment, 1930 P.C.I.J. (ser. A) No. 24, at 10 (Dec. 6).

### 3. The Doctrine as Soft Law

The present international law picture contains an objective lacuna in terms of rules applicable to the phenomenon of sovereign debt: there are neither international conventions regulating this subject<sup>132</sup> nor established rules in this field.<sup>133</sup> To fill this gap, certain international agencies have produced some pieces of soft law.

In January 2012, the United Nations Conference on Trade and Development (UNCTAD) adopted the Principles on Promoting Responsible Sovereign Lending and Borrowing.<sup>134</sup> This adoption implemented a Resolution by the UN General Assembly stressing the importance of responsible financing in which both public and private creditors and sovereign debtors share responsibility for preventing unsustainable debt situations.<sup>135</sup> The UNCTAD Principles have not been formally incorporated into a binding instrument for two reasons: first, this choice is consistent with the soft law characterization of international financial law;<sup>136</sup> second, the purpose of the Principles is not so much to establish rights and obligations, but rather to identify basic rules and best practices. This second reason reflects the dynamic and flexible nature of the Principles<sup>137</sup> and their nonuniform legal status.<sup>138</sup> Although some incremental acknowledgement of these

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132. *But see* Vienna Convention on Succession to State Property, Archives and Debts, *supra* note 107, at 306.

133. This gap may be filled by having recourse to Art. 96 of the UN Charter under which the General Assembly may request from the ICJ an opinion on any issue of international law, including sovereign debt. So far, such a step has not been taken. Although not formally binding, the interpretative activity of the court may contribute to promote the progressive development of international law. *See* Legal Consequences of the Construction of a Wall in the Occupied Palestinian Territory, Advisory Opinion, 2004 I.C.J. Rep., 136, 213 (Higgins, J.). A set of rules may nevertheless be doctrinally inferred. *See* MAURO MEGLIANI, SOVEREIGN DEBT: GENESIS, RESTRUCTURING, LITIGATION 430-61 (2015).

134. *Supra* note 23.

135. G.A. Res. 65/144, ¶ 3 (Dec. 20, 2010). However, the UN General Assembly could have adopted a Declaration on Principles of Sovereign Debt, but such a step would have required a nearly unanimous consent that lacked and still lacks. *Cf.* HENRY G. SCHERMERS & NIELS M. BLOKKER, INTERNATIONAL INSTITUTIONAL LAW 789-90 (5th rev. ed. 2011).

136. Chris Brummer, *Why Soft Law Dominates International Finance—and not Trade*, 13 J. INT'L ECON. L. 623–24 (2011).

137. *See* Juan Pablo Bohoslavsky & Carlos Esposito, *Principles Matter: The Legal Status of the Principles on Responsible Sovereign Financing*, in SOVEREIGN FINANCING AND INTERNATIONAL LAW, *supra* note 53, at 73, 86.

138. The Principles have been derived by analogy from domestic legal systems. Only a few reflect customary law (corruption, necessity), while the rest of them may be classified as general principles of law (agency, authorization, bindingness), emerging principles (assessment of a borrower's capacity, lender's due diligence), guiding principles (audits, disclosure of information), or structural principles (avoiding overborrowing). *See* Goldmann, *supra* note 24, at 8.

Principles in restructuring and litigation may be recorded, it is too early to qualify them as proper body of legal rules.<sup>139</sup>

The UNCTAD Principles do not make specific reference to the odious debt doctrine. This absence is consistent with the fact that they aim to be an objective benchmark for responsible sovereign financing. This aim would be undermined by the acknowledgment of the odious debt doctrine, the status of which is still unclear. However, a closer analysis of the Principles may lead to a different conclusion. Under Principle Number 1, lenders are called to recognize that government officials responsible for a financial transaction are acting in the name and on the behalf of the population and hence must refrain from corrupting them to breach that duty. Moreover, under Principle Number 2, lenders are required to inform the borrowers of the risks and benefits of the financial transaction. Further, under Principle Number 5, lenders financing a specific project are responsible for making an *ex ante* investigation of its impact. All this indicates that the three updated elements of the doctrine are in some way embedded in these Principles.

By contrast, the updated elements of Sack's doctrine are straightforwardly acknowledged in the Human Rights Council (HRC) Guiding Principles on Foreign Debt and Human Rights.<sup>140</sup> The Guiding Principles, *inter alia*, push for the establishment of an international debt workout mechanism to restructure unsustainable debts and resolve debt disputes in a fair, transparent, efficient, and timely manner (¶ 84).<sup>141</sup> This mechanism should have the mandate to rule on the "odiousness" or "illegitimacy" of particular external debts. The criteria to be used in assessing the odiousness or illegitimacy of a debt should be defined by national legislation on the basis of the following elements: the absence of consent by the debtor state's

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139. See, e.g., Juan Pablo Bohoslavsky & Matthias Goldmann, *An Incremental Approach to Sovereign Debt Restructuring: Sovereign Debt Sustainability as a Principle of Public International Law*, 41 YALE J. INT'L L. ONLINE 13, 38–42 (2016) (noting that these principles "complement, rather than replace, existing mechanisms").

140. The HRC Guiding Principles are centered on the primacy of human rights, in particular economic, social and cultural rights, and on their non-retrogression in relation to state indebtedness. See Human Rights Council Res. 20/23, U.N. Doc. A/HRC/20/23, at 11–16 (Apr. 10, 2011).

141. *Id.* at 20, ¶ 84. The input for the establishment of a debt workout mechanism reflects the failure of many proposals for the creation of a machinery for sovereign debt restructuring, from the IMF Sovereign Debt Restructuring Mechanism to the IIF Principles for Stable Capital Flows and Fair Debt Restructuring in Emerging Markets. See MEGLIANI, *supra* note 133, at 569–79. The HRC Guiding Principles stress the necessity of filling this lacuna. The UNCTAD is currently working to a Debt Workout Mechanism to be designed by a Working Group. *Sovereign Debt Workout Mechanism*, UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT, <https://unctad.org/en/Pages/GDS/Sovereign-Debt-Portal/Sovereign-Debt-Workout-Mechanism.aspx> (last visited Sept. 6, 2020) [<https://perma.cc/K23C-E2UH>] (archived Sept. 6, 2020).

population, the absence of benefit to the debtor state's population, and the creditors' awareness of this (¶ 86d).<sup>142</sup> However, this reference must be correctly appreciated in the light of the nature, aim, and scope of the HRC Guiding Principles. In fact, the Guiding Principles are more political in character than the UNCTAD Principles; they neither pursue the creation of new rights or obligations under international law, nor do they replace other mechanisms designed to address aspects of the sovereign debt problem. Rather, their normative contribution consists of identifying existing basic human rights standards applicable to sovereign debt and related policies, as well as in elaborating the implications of these standards (¶ 17).

#### 4. The Doctrine as a Matter of Politics

The odious debt doctrine has been used as a political argument—with different outcomes—in the dynamics of debt restructuring. Some cases can be inferred from the practice.

At the beginning of the new century Argentina was on the edge of an economic crisis. Economic growth was stagnant, and the cost of borrowing increased. To meet these imbalances, Argentina requested the assistance of the IMF against the implementation of a huge package of fiscal reforms.<sup>143</sup> However, the cure was not able to defeat the disease. In late 2001, the economic and political situation precipitated, and, in December 2001, Argentina declared default on its debt estimated at \$180 billion. Bonded debt, which amounted to nearly half the outstanding debt, was technically difficult to restructure as it was articulated in 152 series of bonds, governed by eight different laws, and held by over 700,000 holders around the world.<sup>144</sup> The restructuring of the Argentine debt was characterized by a sharp unilateralism both in form and in substance. First, the debtor did not

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142. According to the commentary, debt restructuring mechanisms should have the authority to adjudicate claims of invalid or illegitimate debts. The rationale is that the people of a debtor country should not be required to repay loans from which they have not benefitted. In alternative, there has to be some form of auditing of the external debts at the commencement of any restructuring process to ensure that only valid and legitimate external debts will be included in the restructuring plan and, in that context, repaid. Human Rights Council Res. 20/23, *supra* note 140, at 20, ¶ 86(d).

143. Conditions on which the disbursement of the resources depends are attached to the letter of intent signed by the minister of finance of the requesting state. Formally, it is a unilateral act of the government; substantively, it is the outcome of intense negotiations between the staff of the government and the staff of the IMF. This implies that in case of non-compliance with the conditions, a breach of obligation does not arise, even though the drawing of resources ceases. See ANDREAS F. LOWENFELD, *INTERNATIONAL ECONOMIC LAW* 614–15 (2008).

144. José García-Hamilton Jr., Rodrigo Olivares-Caminal & Octavio M. Zenarruza, *The Required Threshold to Restructure Sovereign Debt*, 27 *LOY. L.A. INT'L & COMP. L. REV.* 249, 256–57 (2005).

encourage the formation of negotiating committees and refused to have contacts with those formed at the initiative of some bondholders;<sup>145</sup> second, the debtor formalized a “take-it-or-leave-it” proposal of restructuring, which involved huge losses for creditors. In September 2003, Argentina launched a first restructuring proposal providing for the cancellation of 75 percent over the nominal value of the outstanding debt without any recognition of the accrued interest. Facing strong opposition by the holders, Argentina reconsidered the proposal and, in January 2005, launched the final exchange offer involving a reduction of 75 percent over the nominal value of the outstanding debt but with a partial recognition of the accrued interest.<sup>146</sup> This unilateral approach has many explanations. Among them is the argument that the debt had been incurred by the dictatorship and thereby was illegitimate and worthy of repudiation.<sup>147</sup>

Another situation where the odious debt doctrine came into play was the restructuring of the Iraqi debt. Following the Iraq War and the overthrow of Saddam Hussein (2003), the issue of debt relief arose not out of a sense of humanity or justice, but because of the necessity to relieve the new Iraq from a heavy burden and so buttress the democratic process. Although the Iraqi government grounded its request for debt restructuring on the incapacity to repay the debt, the US Administration and many debt-abolitionist associations claimed the debt was to be reduced as it was incurred to finance the war against Iran and the lavish way of life of Saddam Hussein and his entourage.<sup>148</sup> In this context, the US Administration exerted a significant pressure over its allies for a substantial relief of the Iraqi bilateral debt that amounted to \$120 billion.<sup>149</sup> This reduction took place mainly within the machinery of the Paris Club,<sup>150</sup> where the Iraqi debt enjoyed

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145. Arturo C. Porzecanski, *From Rogue Creditors to Rogue Debtors: Implications of Argentina's Default*, 6 CHI. J. INT'L L. 311, 323–24 (2005).

146. This massive debt reduction has few precedents in the recent financial history and those few involved poor countries, smaller sums, and bank creditors. RODRIGO OLIVARES-CAMINAL, LEGAL ASPECTS OF SOVEREIGN DEBT RESTRUCTURING 256–59 (2009); see Porzecanski, *supra* note 145, at 325.

147. To tell the truth, most of the debt was contracted or restructured under the democratic presidency. See Gelpert, *supra* note 98, at 408; MICHALOWSKY, *supra* note 94, at 91–92.

148. Detlev F. Vagts, *Sovereign Bankruptcy: In Re Germany (1953), In Re Iraq (2004)*, 98 AM. J. INT'L L. 302, 303 (2004).

149. Half of the debt was due to Arab nations. See Ross P. Buckley, *Iraq's Sovereign Debt and Its Curious Global Implications*, in BEYOND THE IRAQ WAR: THE PROMISES, PITFALLS AND PERILS 141, 141–42 (Michael Heazle & Iyanatul Islam eds., 2006).

150. The Paris Club ([www.parisclub.org](http://www.parisclub.org)) is the general forum for the restructuring at multilateral level of bilateral debt owed to industrialized countries. It is an international conference that has undergone a process of institutionalization: the elements of institutionalization can be identified in the Secretariat (composed of staff provided by the French Treasury), the methodological sessions, and *tours d'horizon*. The final act of the Paris Club negotiations is the agreed minutes, the typical final act of an

generous treatment. In this context, the Iraqi debt should have been rescheduled under the so-called Classical Terms that involve rescheduling at market rate.<sup>151</sup> Instead, this debt benefitted from an *ad hoc* treatment implying a cancellation of nearly \$30 billion thanks to diplomatic activism by the United States.<sup>152</sup> The United States' pressure for a significant debt relief was not confined to Paris Club participants; it extended to those bilateral creditors that did not participate in the Club workouts as well as to commercial creditors.<sup>153</sup> Although it is unclear to what extent the odious debt doctrine played an effective role in the debt restructuring process, it is certainly true that it entered the public debate as a political argument for a significant debt reduction.<sup>154</sup>

The odious debt doctrine was also evoked in connection with the restructuring of the Ecuadorian debt. During his campaign for the presidential election, candidate Rafael Correa promised not to pay some of the country's external debts, but rather to spend the sums intended for payment on public sector projects. He affirmed that Ecuador would be justified in doing so because the bonded debt represented obligations that had been illegally incurred by previous oppressive regimes and was therefore unfair and illegitimate.<sup>155</sup> Once elected in 2007, President Correa kept his promise and created a Public Debt Audit Commission to evaluate the country's obligations incurred between 1976 and 2006.<sup>156</sup> The Commission took into consideration

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international conference, which are not published. The Paris Club in its activity follows six principles: solidarity, consensus, information sharing, case-by-case, conditionality, and comparability of treatment. See Mauro Megliani, *Paris Club*, in MAX PLANCK ENCYCLOPEDIAS OF INT'L L., <https://opil.oup.com/view/10.1093/law:epil/9780199231690/law-9780199231690-e2176?rskey=x1hvc4&result=1&prd=MPIL> (last updated July 2015) [<https://perma.cc/GL6L-Q7JU>] (archived Aug. 25, 2020).

151. See *Classic Terms*, PARIS CLUB, <https://clubdeparis.org/en/communications/page/classic-terms> [<https://perma.cc/3FMJ-JF3D>] (arch-ived Aug. 25, 2020) (calling the classic terms the "standard terms" for countries seeking assistance from the Paris Club).

152. See Buckley, *supra* note 149, at 146–47 (explaining how vigorous diplomatic efforts by the United States led creditor countries to forgive 80 percent of Iraqi sovereign debt).

153. For a detailed description of the Iraqi sovereign debt saga, see WONG, *supra* note 99, at 52–64.

154. According to Jai Damle, the most compelling argument for a sharp debt reduction was based not so much on the odious debt doctrine but rather on the stagnancy of the Iraqi economy and the instability of the Middle-East, as it was necessary to avoid setting a precedent in this field. See Jai Damle, *The Odious Debt Doctrine After Iraq*, 70 L. & CONTEMP. PROBS. 139, 148, 150–51 (2007).

155. Adam Feibelman, *Ecuador's Sovereign Default: A Pyrrhic Victory for Odious Debt?*, 25 J. INT'L BANKING L. & REG. 357, 358 (2010).

156. WONG, *supra* note 99, at 93–94. The Commission was composed of academic and anti-debt activists in some way connected to the European Network on Debt and Development (EURODAD). *Id.*

various aspects of Ecuador's external obligations. It found that the proceeds of various borrowings and restructurings had been used to unfairly benefit certain internal and external subjects. The international bonds were found to be invalid because the government had ceded to oppressive terms of the loan (waiving sovereign immunity, submitting to foreign law, etc.). Moreover, the service on the debt in 2007 was found to be greater than the public expenditure on health, welfare, urban development and housing, the environment, and education.<sup>157</sup> On the basis of the findings of the Commission, President Correa made a selective default and declared two out of three international bonded loans illegal; he also stopped paying coupons without formally repudiating the loans.<sup>158</sup> Neither the Audit Commission nor President Correa, however, made any specific reference to the odiousness of the debts, possibly because the three criteria of odiousness were not met.<sup>159</sup>

##### 5. The Doctrine as Domestic Law

The Guiding Principles on Foreign Debt and Human Rights, in laying down the three elements of the odious debt doctrine, underscore that odiousness and illegitimacy should be defined by national legislation (¶ 86(d)). This is far from being surprising, considering that one of the major sources of sovereign indebtedness is private loans that are governed by a domestic legal system usually coinciding with English law and New York law.<sup>160</sup>

Both the UNCTAD Principles and the HRC Guiding Principles, in their respective ways, stimulate national legislation to acknowledge the notion of odious debt in their jurisdictions. A significant step in this direction might be the elaboration of a sort of model law capable of constituting a benchmark for national legislation.<sup>161</sup> This model law might be elaborated within UNCTAD as a follow-up to the Principles

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157. Feibelman, *supra* note 155, at 358.

158. WONG, *supra* note 99, at 94–95. Following the default, the Ecuadorian government started buying back the bonds at a risible price. Arturo C. Porzecanski, *When Bad Things Happen to Good Sovereign Debt Contracts: The Case of Ecuador*, 73 *LAW & CONTEMP. PROBS.* 251, 266–267 (2010). The success of the Ecuador operation was also due to the behavior of the trustee of the issuance, which decided not to accelerate the loan and enforce the bondholder's claims. See Lee C. Buchheit & G. Mitu Gulati, *The Coroner's Inquest*, 28 *INT'L FIN. L. REV.*, Sept. 2009, at 22, 24–25.

159. The Audit Commission did not find that the debts were not contracted for the benefit of the population or that the creditors knew of this hypothetical fact; moreover, the borrowing government was not a dictatorship. See Feibelman, *supra* note 155, at 360.

160. Michael Gruson, *Controlling Choice of Law*, in *SOVEREIGN LENDING: MANAGING LEGAL RISK* 51, 59 (Michael Gruson & Ralph Reisner eds., 1984).

161. The benchmark is constituted by the UNCITRAL Model Law on Arbitration. See generally U.N. COMM. ON INT'L TRADE L., *MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION*, U.N. DOCS. A/40/17, annex I & A/61/17, annex I, U.N. Sales No. E.08.V.4 (1985) (amended 2006).



on Responsible Sovereign Borrowing and Lending. As such, the model law is not binding; nevertheless, states may freely incorporate the whole of it or some of its provisions in their legislation. Such a step may contribute to fill an objective lacuna.

In this context, it is worth noting that some states have enacted legislative measures to curb vulture funds' activism<sup>162</sup> in recovering their claims.<sup>163</sup> The issue of the illegitimate/odious debt, though, has not yet become the object of specific legislation. The only exception is perhaps the US Iraqi Freedom from Debt Act,<sup>164</sup> which underscored that international precedents exist under which

debts incurred by dictatorships for the purposes of oppressing their people or for personal purpose may be considered "odious". In cases where borrowed money is used in ways contrary to the people's interest, with the knowledge of the creditors, the creditors may be said to have committed a hostile act against the people.<sup>165</sup>

This stipulation constitutes a plain acknowledgment of the Sackian odious debt doctrine in relation to government succession, but was confined to the exceptional situation of post-war Iraq. Moreover, the Act emphasized that such debts might be questioned, but not that they were *per se* illegal.

In the absence of specific national legislation addressing this phenomenon, the only solution is to have recourse to existing norms, such as abuse of rights,<sup>166</sup> unjust enrichment,<sup>167</sup> and agency.<sup>168</sup>

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162. Vulture funds are investment funds specializing in purchasing the debts of sovereigns in distress at a price below face value with the purpose of obtaining the nominal amount in court. On their disruptive activism, especially in connection with the saga of the Argentine sovereign bonds, see generally Tim R. Samples, *Rogue Trends in Sovereign Debt: Argentina, Vulture Funds, and Pari Passu Under New York Law*, 35 NW. J. INT'L L. & BUS. 49 (2014).

163. The most significant of these initiatives is perhaps the 2010 UK Parliament Debt Relief (Developing Countries) Act. See generally Debt Relief (Developing Countries) Act 2010, c. 22. Under this Act, a UK court cannot render a judgment, or enforce a foreign judgment or arbitral award, against a "heavily indebted poor country" under which private creditors would be enabled to recover their credits in excess of the sustainable level as calculated under the Heavily Indebted Poor Country Initiative. *Id.* §§ 3(1), 4(2), 5(1), (3).

164. See generally Iraqi Freedom From Debt Act, H.R. 2482, 108th Cong. (2003).

165. *Id.* § 2(3).

166. See Frankenberg & Knieper, *supra* note 97, at 428 (describing "abuse of rights" as being against the interests of the population or exceeding the sovereign's natural resources).

167. See Jeff A. King, *Odious Debt: The Terms of the Debate*, 32 N.C. J. INT'L L. & COM. REG. 605, 643 (2007) (arguing that unjust enrichment has questionable applicability to the odious debt doctrine because, by definition, odious debt requires there be no benefit to the state and thus no enrichment).

168. See Buchheit, Gulati & Thompson, *supra* note 83, at 1237-45 (describing that agency law may relieve a "principal" state's obligation to repay a debt in only some

However, this piecemeal approach does not ensure coverage for all the elements of the doctrine and is also too dependent on the applicable law and the seized forum. Against this background, the solution is then to accept that the odious debt doctrine lacks a proper normative status. Nevertheless, because the doctrine reflects values and values are traditionally protected by public policy, it can come into play in the form of public policy.

## 6. The Doctrine as Public Policy

Under the law of contracts, a contract cannot be enforced if it is against public policy. Public policy is usually understood as the “whole body of laws and legal instruments whose principles cannot be set at naught either by special conventions or by a conflicting foreign law.”<sup>169</sup> Although it reflects the fundamental economic, social, moral, and political values of a given country, the content of public policy is subject to variation at different times and in different places.<sup>170</sup> The judge plays a key role in appreciating the meaning and operation of these values. In this process, the judge should not follow mass opinion when it is clearly in error. He is called to direct it, not so much on the basis of personal convictions, but rather on the ground of the convictions of the healthy elements of the population that are able to combine respect for tradition with acceptance of social change.<sup>171</sup>

Against this background, the key point is, first, to understand whether and to what extent the values protected by the odious debt doctrine may be subsumed under the umbrella of public policy and, second, under which category of public policy they may fall. Normally, contracts are appreciated in the light of the municipal public policy of the forum. Unfortunately, the values that traditionally come into play under this policy are the domestic values of the forum. This fact makes municipal public policy unsuited to acknowledge international values like those protected by the odious debt doctrine. These values are better served under transnational public policy.

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circumstances, such as when a lender is aware of the “agent” regime’s self-dealing motives).

169. Application of Convention of 1902 Governing Guardianship of Infants (Neth. v. Swed.), Judgment, 1958 I.C.J. 55, 102 (Nov. 28) (separate opinion by Moreno, J.).

170. *Evanturel v. Evanturel*, [1874] UKPC 58, 68 (Can.). Public policy is a “conception the definition of which in any particular country is largely dependent on the opinion prevailing at any given time in such country itself . . .” *Payment of Various Serbian Loans Issued in France (Fr. v. Yugoslavia)*, 1929 P.C.I.J. (ser. A) No. 20, at 46.

171. DENNIS LLOYD, *PUBLIC POLICY: A COMPARATIVE STUDY IN ENGLISH AND FRENCH LAW* 125–26 (1953).

## IV. TRANSNATIONAL PUBLIC POLICY

The existence of a transnational public policy (or transnational public order) has been envisaged in certain international commercial arbitrations and has formed the object of intense doctrinal debate. From a substantive point of view, transnational public policy transcends the boundaries of national states.<sup>172</sup> Its values come from many sources: natural law, principles of universal justice, *jus cogens*, and general principles of morality and public policy accepted in civilized countries.<sup>173</sup> In addition to the prohibition of corruption that can be considered a sort of “*noyau dur*” of the transnational public policy,<sup>174</sup> these values include abhorrence of slavery, discrimination, kidnapping, murder, piracy, and terrorism, the promotion of fundamental human rights, and the acknowledgement of uniform laws and codes of practice.<sup>175</sup> However, to reflect a universal moral standard, a truly international public order value does not necessarily have to be accepted in all the jurisdictions.<sup>176</sup> From a systematic point of view, transnational public policy poses itself alongside municipal public policy and international public policy.

A. *The Notion of Public Policy*

Juristic elaboration has progressively distinguished three types of public policy: municipal, international, and transnational. Municipal public policy has the effect of rendering a contract void and unenforceable. Under common law, a contract with public policy makes a contract illegal and thereby unenforceable,<sup>177</sup> while under civil law a contract with public policy makes the consideration unlawful and the contract void.<sup>178</sup> In any case, contracts infringing on public policy do

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172. Michael Pryles, *Reflections on Transnational Public Policy*, 24 J. INT'L ARB. 1, 3 (2007).

173. JULIAN D.M. LEW, APPLICABLE LAW IN INTERNATIONAL COMMERCIAL ARBITRATION 534 (1978).

174. JEAN-BAPTISTE RACINE, L'ARBITRAGE COMMERCIAL INTERNATIONAL ET L'ORDRE PUBLIC 393–94 (1999).

175. LEW, *supra* note 173, at 535.

176. The condemnation of racial discrimination, corruption, or drug trafficking is not necessarily unanimous, FOUCHARD, GAILLARD, GOLDMAN ON INTERNATIONAL COMMERCIAL ARBITRATION 853, 863–864 (Emmanuel Gaillard & John Savage eds., 1999). In this context, the elaboration of the transnational public policy takes place along the same lines as that of the general principles of law. RACINE, *supra* note 174, at 360.

177. Illegality may affect both the formation and the performance of the contract. See Prentice, *supra* note 55, at 1224.

178. Article 1131 of the French *Code Civil* stipulates that “*l'obligation . . . sur une cause illicite, ne peut avoir aucun effet*,” Code Civil [C. CIV.] [CIVIL CODE] art. 1131, while Article 1133 provides that “*la cause est illicite . . . quand elle est contraire . . . à l'ordre public*.” *Id.* art. 1133.

not give rise to claims for specific performance or damages.<sup>179</sup> From a substantive standpoint, it is possible to distinguish between political public policy and economic public policy. The former prohibits those contracts that openly conflict with the social order; the latter prohibits those contracts that, without infringing on the fundamental values of the society, affect economic relations.<sup>180</sup>

International public policy consists of values that are regarded as so fundamental by the seized forum that their infringement can block the application of a foreign law or the enforcement of a foreign act.<sup>181</sup> This policy is stricter in scope and mandate than municipal public policy; otherwise, the whole private international law system would be seriously impaired.<sup>182</sup> In this respect, international public policy is a misnomer, as it concerns those fundamental, moral, economic, social, and political interests of the seized forum.<sup>183</sup> As a result, domestic courts are less inclined to apply public policy in cases involving an international element than they are in cases of purely domestic characterization.<sup>184</sup> That implies that “not every rule which belongs to the *ordre public interne* is necessarily part of the *ordre public externe ou internationale*.”<sup>185</sup> This narrowness is reflected in the EU conflict-of-laws system. Under the Brussels I Regulation, the recognition and enforcement of a foreign judgment may be refused as far as it is “manifestly” contrary to the public policy of the seized forum (Articles 45 and 46).<sup>186</sup> In the same vein, under the Rome I Regulation, the application of a provision of the law of a foreign country may be refused only if that application is “manifestly” incompatible with the public policy of the forum (Article 21).<sup>187</sup>

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179. See KONRAD ZWEIGERT & HEIN KÖTZ, INTRODUCTION TO COMPARATIVE LAW 380–81 (T. Weir trans., 3rd ed. 1998) (describing the unenforceability of contracts contrary to public policy in the western world).

180. EUROPEAN CONTRACT LAW 142–43 (Bénédicte Fauvarque-Cosson & Denis Mazeaud eds., 2008).

181. Mathias Forteau, *L'ordre public « Transnational » ou « Réellement International »*, 138 J. DROIT INT'L 3, 5 (2011).

182. *Vervake v. Smith* [1982] 2 All ER 144 (HL) 157 (Lord Simon of Glaisdale) (appeal taken from EWHC Fam.) (UK).

183. JULIAN D.M. LEW, TRANSNATIONAL PUBLIC POLICY: ITS APPLICATION AND EFFECT BY INTERNATIONAL ARBITRAL TRIBUNALS 20 (2018).

184. See *Loucks v. Standard Oil Co.*, 120 N.E. 198, 202 (N.Y. 1918) (“The courts are not free to refuse a foreign right at the pleasure of the judges, to suit the individual notion of expediency or fairness. They do not close their doors unless help would violate some fundamental principle of justice, some prevalent conception of good moral, some deep-rooted tradition of common weal.”).

185. DICEY, MORRIS & COLLINS, *supra* note 25, at 1874 (internal quotation marks omitted).

186. Regulation (EU) No. 1215/2012 of the European Parliament and of the Council of 12 December 2012 on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters, 2012 O.J. (L 351) 1.

187. Rome I Regulation, *supra* note 25, art. 21.

Still, international public policy is wider in content than municipal public policy as it acknowledges some values of the international community.<sup>188</sup> In *Oppenheimer v. Cattermole*, the House of Lords refused to apply a foreign law, which constituted a grave infringement of fundamental human rights.<sup>189</sup> In *Kuwait Airways v. Iraqi Airways*, the House of Lords refused to enforce a foreign act which was adopted under a *jus cogens* violation.<sup>190</sup> In *Yukos Capital Sarl v. OJSC Rosneft Oil Co*, Lord Justice Rix, delivering the judgment of the Court of Appeal, which dealt with the public policy exception to the act of state doctrine,<sup>191</sup> drew a distinction between

the act of State which cannot be challenged for its effectiveness despite some alleged unfairness, and the act of State which is sufficiently outrageous or penal or discriminatory to set up the successful argument that it falls foul of clear international law standards or English public policy and therefore can be challenged.<sup>192</sup>

Conceptually speaking, these international elements of international public policy belong to the realm of transnational public policy or the truly international public order, that “is the one that establishes universal principles, in various fields of international law and relations, to serve the higher interests of the world community, the common interests of mankind, above and sometimes even contrary to the interests of the individual nations.”<sup>193</sup>

### *B. The Emergence of Transnational Public Policy*

The existence of a truly international public order has been the object of an intense doctrinal debate. In a course delivered at the Hague Academy of International Law in 1932, Professor Niboyet evoked the existence of an “*ordre public international*.” The justification for this peculiar form of public policy lies in the fact that the international judge has no territorial forum and, therefore, no territorial public policy to enforce. Substantively, this “*ordre public international*” would correspond to the public policy of civilized countries capable of

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188. International public policy has undergone a process of internationalization. Forteau, *supra* note 181, at 9–10.

189. *Oppenheimer v. Cattermole* [1976] AC 249 (HL) 278 (appeal taken from EWHC (Ch)) (UK).

190. *Kuwait Airways Corp. v. Iraqi Airways Co.* [2002] UKHL 19 [114], [2002] 2 AC (HL) 883 (UK).

191. See *Yukos Capital Sarl v. OJSC Rosneft Oil Co* [2012] EWCA (Civ) 855 [68]–[69] (Eng.).

192. *Id.* at [110].

193. Jacob Dolinger, *World Public Policy: Real International Public Policy in the Conflict of Laws*, 17 TEX. INT'L L.J. 167, 172 (1982).

displacing, in case of contrast, the application of municipal law.<sup>194</sup> Professor Rolin took this point further and specified that the *ordre public international* would prevent not only the application of a conflicting municipal substantive rule but also the application of a conflicting municipal public policy rule.<sup>195</sup>

Currently, the view that identified truly international public order with the common principles of civilized nations is no longer tenable.<sup>196</sup> In this respect, Maury spoke of an “*ordre public de la société internationale*” based on customary norms and the general principles of law,<sup>197</sup> while Goldman specified that truly international public order was to be understood as the public policy of the international community and not as a mere juxtaposition of the common public policy of civilized nations.<sup>198</sup>

This approach was substantively endorsed in 1986 at the Eighth Congress of the International Chamber of Commercial Arbitration (ICCA). In that context, it was acknowledged that not only international arbitrators, but also municipal judges had in a number of cases referred to a notion of a transnational public policy capable of encompassing both the territorial values of the forum and the fundamental values of the international community.<sup>199</sup> The existence of a truly international public order was further acknowledged in the International Law Association (ILA) Interim Report on Public Policy as a Bar to Enforcement of International Arbitral Awards (2000). On that occasion, it was affirmed the existence of a transnational public policy with universal application that consists of “fundamental rules of natural law, principles of universal justice, *jus cogens* in public international law and the general principles of morality accepted by what are referred as ‘civilised nations.’”<sup>200</sup>

From an axiological point of view, the application of the values of the international community can be justified by the fact that they reflect the establishment of a world public order based on respect for

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194. Jean-Paul Niboyet, *Le Rôle de la Justice Internationale en Droit International Privé: Conflit de Lois*, 40 RECUEIL COURS 157, 178 (1932).

195. HENRI ROLIN, *Vers un Ordre Réellement International*, in HOMMAGE D'UNE GÉNÉRATION DE JURISTES AU PRÉSIDENT BASDEVANT 441, 444 (1960).

196. PHILIPPE FOUCARD, *L'ARBITRAGE COMMERCIAL INTERNATIONAL* 399 (1965).

197. JACQUES MAURY, *L'ÉVICTION DE LA LOI NORMALMENT COMPÉTENTE: L'ORDRE PUBLIC INTERNATIONAL ET LA FRAUDE A LA LOI* 141 (1952).

198. See Berthold Goldman, *La Protection Internationale des Droits de l'Homme et l'Ordre Public International dans le Fonctionnement de la Règle de Conflit de Lois*, in 1 RENÉ CASSIN AMICORUM DISCIPULORUMQUE LIBER 449, 464 (1969).

199. See Pierre Lalive, *Ordre Public Transnational (ou Réellement International) et Arbitrage International*, *REVUE DE L'ARBITRAGE* 329, 329–30 (1986) (Fr.) [hereinafter Lalive, *Ordre Public Transnational et Arbitrage International*].

200. ALAN REDFERN, MARTIN HUNTER, NIGEL BLACKBY & CONSTANTINE PARTASIDES, *LAW AND PRACTICE OF INTERNATIONAL COMMERCIAL ARBITRATION* 420 n. 8 (2004) (citing INTERNATIONAL LAW ASSOCIATION, INTERIM REPORT ON PUBLIC POLICY AS A BAR TO ENFORCEMENT OF INTERNATIONAL ARBITRAL AWARDS (2000)).

human dignity.<sup>201</sup> Nevertheless, jurists in developing countries have occasionally perceived these values as a new form of legal colonization by jurists of developed countries.<sup>202</sup>

### 1. Early Cases

Traditionally, the emergence of the doctrine of truly international public order can be traced back to the ICC Award Number 1110 (1963), in which Judge Lagergren held that a contract that had as its object bribery infringed the law of nations.<sup>203</sup> Although the approach used by Judge Lagergren was quite innovative, it was not the first time that truly international public policy, in some way, had emerged. This point was highlighted by Professor Lalive, who recalled two old cases referred to by Professor Niboyet where the existence of a transnational public policy, in some way, had been foreshadowed.<sup>204</sup> The key point is that, in these two cases, national mandatory rules were applied as reflecting principles of universal justice that mirrored an emerging transnational public policy.

The *Créole Case* concerned the release by British authorities of slaves embarked on a US ship that entered the port of Nassau (1840).<sup>205</sup> The ship was sailing from Virginia to New Orleans when, along the coast of Florida, some of the slaves took control of the ship and forced the captain to dock at the port of Nassau, a British colony. As slavery was forbidden by the Slavery Abolition Act of 1833, which had abolished slavery throughout the British Empire,<sup>206</sup> the British authorities released the slaves. The United States authorities protested against this release, and the case was submitted to the British–US Mixed Commission (1855). The Commission heard the claim, and, based on the findings, Subarbiter Bates accorded an indemnity to the US claimants. In his line of reasoning, the Subarbiter acknowledged, as a matter of principle, that slavery was against the

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201. This is the backbone of the so-called New Haven School. See W. Michael Reisman, Siegfried Wiesner & Andrew Willard, *The New Haven School: A Brief Introduction*, 32 YALE J. INT'L L. 575, 576 (2007).

202. With specific reference to the issue of transnational public policy, Andrew I. Okekeifere, *The Enforcement and Challenge of Foreign Awards in Nigeria*, 14 J. INT'L ARB. 223, 237 (1997), underscored that “[j]ust like the concepts of international law of contract and international mercantile law this new concept is hardly anything short of an ego trip by a few writers of the developed world eager to impose, for the advantage of their countries and regions, rules that they are conversant with on the poor less-heard nations without caring about the sensibilities of the latter's local setting and peculiar dynamics.”

203. See *infra* note 214.

204. Lalive, *Ordre Public Transnational et Arbitrage International*, *supra* note 199, at 335–36.

205. Niboyet, *supra* note 194, at 181–87.

206. Slavery Abolition Act 1833, 3 & 4 Will. 4 c. 73 (Eng.). The Slavery Abolition Act was anticipated by the celebrated case *Somerset v. Stewart* (1772) 98 Eng. Rep. 499.

principles of justice and humanity, but he concluded that, as slavery was accepted in various countries, it was not against the law of nations. In other words, the fact that slavery was accepted in a number of countries prevented the formation of general consent against it.<sup>207</sup>

A different conclusion was reached in relation to the *Maria Luz Case*. The *Maria Luz* was a Peruvian ship sailing from China to Peru with a certain number of “coolies” on board. Following the progressive abolition of the slave trade, labor-intensive industries—such as cotton and sugar plantations, mines, and railway construction—were left without a supply of cheap manpower. To fill this gap, a large-scale slavery-like trade in Asian (primarily Indian and Chinese) indentured laborers—the coolies—emerged.<sup>208</sup> Technical problems obliged the *Maria Luz* to enter the Japanese port of Kanawaga (1872). The Japanese authorities asked the coolies whether they preferred to be freed or to continue their travel to Peru. The coolies chose the first option and were embarked on a ship to China at the expense of the Japanese government. Nevertheless, a dispute arose between Peru and Japan regarding the behavior of the Japanese authorities, which was later submitted to the arbitration of the Czar Alexander II (1875). The Czar ruled that the Japanese government bore no responsibility for the release of the coolies as it had simply applied its own laws and customs without infringing general rules of international law or particular treaties.<sup>209</sup> In other words, the Czar, in his award, endorsed the application of the overriding mandatory rules of the forum,<sup>210</sup> that displaced the law governing the contract of the semi-enslavement of the coolies. With reference to international law, the Czar did not say

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207. In practice, the legal problem was solved by giving precedence to the *lex navis* (the slaves on the ship were under US jurisdiction) over the *lex loci* (the port of Nassau was under British jurisdiction). In this respect, Subarbiter Bates failed to apply the customary rule of the jurisdiction of the coastal state on its internal waters. See GILBERT GIDEL, *LE DROIT INTERNATIONAL PUBLIC DE LA MER: TOME II LES EAUX INTÉRIEURES* 93-94 (1932). The decision of the Mixed Commission is reprinted in French in ALBERT DE LAPRADELLE & NICOLAS POLITIS, *1 RECUEIL DES ARBITRAGES INTERNATIONAUX* 704-5 (1905).

208. Coolies replaced slaves for masters who were gradually losing their labor force because of the anti-slavery laws. Some of these laborers signed contracts based on misleading promises, some were kidnapped and sold into the trade, some were victims of clan violence and sold to coolie brokers, while others sold themselves to pay off gambling debts. Workers from China were mainly transported to Peru and Cuba. The Peru coolies were mainly employed in silver mines and guano collecting industry. See ELLIOTT YOUNG, *ALIEN NATION: CHINESE MIGRATION IN THE AMERICAS FROM THE COOLIE ERA THROUGH WORLD WAR II* 46-58 (2014).

209. See the text of the arbitration in FERDINAND PERELS, *MANUEL DE DROIT MARITIME INTERNATIONAL* 93-94 (L. Arendt trans., 1884).

210. See *supra* Part II.A.2.



that the law of nations imposed the liberation of the coolies, but he implied that that it did not forbid it.<sup>211</sup>

### C. Arbitral Awards

Arbitral practice has provided a significant contribution to the emergence of the notion of transnational public policy in relation to transnational contracts.<sup>212</sup> In this context, two different conceptions of public policy have arisen. The first requires that public policy in arbitration should coincide with that of the seat of arbitration and the country where the arbitral award is to be enforced. The second may provide a better solution. This considers that the power of arbitrators to adjudicate a dispute derives from all the jurisdictions that are ready to recognize the award under certain conditions, with the result that arbitrators should not focus on the public policy of a specific forum, but should be guided by fundamental requirements of justice.<sup>213</sup>

In the ICC Award 1110 (1963), the claim concerned the failure to pay services for a bribing activity under a contract between an Argentine wheeler-dealer and a German firm.<sup>214</sup> The object of the contract was the bribery of high officials of the Argentine government by the Argentine wheeler-dealer to secure, on behalf of the German firm, a contract for the building of an electric power station. Since the German firm refused to pay the Argentine wheeler-dealer for his services, the dispute was submitted to ICC arbitration. Judge Lagergren, the sole arbitrator, declined to hear the case on the assumption that “corruption is an international evil; it is contrary to good morals and to an international public policy common to the community of nations.”<sup>215</sup> In the view of Judge Lagergren, cases involving gross violations of good morals and international public law could not have countenance in any court of a civilized country or

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211. Cf. *infra* notes 227–31 and accompanying text (discussing the judgment of the Japanese court).

212. Stephen Jagusch, *Issues of Substantive Transnational Public Policy*, in INTERNATIONAL ARBITRATION AND PUBLIC POLICY 23, 29 (Devin Bray & Heather L. Bray eds., 2015).

213. An arbitral tribunal sitting in a country where racial or religious discrimination is part of public policy should not depart from the fundamental rules of justice embedded in transnational public policy to comply with the rules of the seat, FOUCHARD, GAILLARD, GOLDMAN ON INTERNATIONAL ARBITRATION, *supra* note 165, at 862.

214. Argentine Engineer v. British Company, ICC Case No. 1110, Award (1963), reprinted in 10 ARB. INT'L 282 (1994).

215. *Id.* ¶ 20. Judge Lagergren did not declare the contract null and void, as he followed the non-separability doctrine between the claim submitted to arbitration and the arbitral agreement. *See id.*

arbitral tribunal.<sup>216</sup> Judge Lagergren could have taken an easier road and simply declared that the claim was against Argentine law (the law governing the performance of the contract) and French law (the law governing the arbitration). Nevertheless, he took the road less travelled and founded his decision on the public policy of the community of nations.<sup>217</sup>

The issue of a truly international public order has come into play again in more recent times.<sup>218</sup> In *World Duty Free Company Ltd v. Kenya* (2006), the claim was based on an act of expropriation of duty-free complexes at the Nairobi and Mombasa airports by the Kenyan government.<sup>219</sup> During the proceedings, however, evidence emerged that the agreement for the construction and maintenance of the duty-free complexes had been tainted with corruption.<sup>220</sup> Since the ICSID tribunal found that corruption was contrary to the international public policy of most countries or, in other words, to transnational public policy, the claims could not be heard. In the view of the ICSID tribunal, public policy consists of “an international consensus as to universal standards and accepted norms of conduct that must be applied in all fora.”<sup>221</sup> The ICSID tribunal did not declare the contract null and void but upheld the decision by the Kenyan government to do so.<sup>222</sup> Although the result would have been the same under the domestic public policy of the applicable (Kenyan and English) laws, the arbitrators consciously implied that transnational public policy takes precedence over municipal public policy.<sup>223</sup>

The World Duty Free award gained some followers. In 2009, in *EDF v. Romania*, the ICSID tribunal held that the request for a bribe by a state agency amounted to a violation of not only the fair and equitable treatment rule contained in the Romania–United Kingdom BIT (1995), but also truly international public order.<sup>224</sup> Also, in this case, the arbitral tribunal felt it necessary to bring corruption under the scope of transnational public policy.

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216. *Id.* ¶ 23.

217. *Id.* The view of Lagergren reflected values of universal justice. *See id.*

218. *See* ICC Case No. 3913, Award (1981) & ICC Case No. 8891, Award (1981); Pierre Lalive, *L'Ordre Public Transnational et l'Arbitre International*, in NUOVI STRUMENTI DI DIRITTO INTERNAZIONALE PRIVATO – LIBER FAUSTO POCAR 598, 605 (Gabriella Venturini & Stefania Bariatti eds. 2009) [hereinafter Lalive, *L'Ordre Public Transnational et l'Arbitre International*] (referring to ICC Case No. 3913).

219. *World Duty Free Co. v. Republic of Kenya*, ICSID Case No. ARB/00/7, Award, ¶ 62 (Oct. 4, 2006).

220. *See* Cecily Rose, *Questioning the Role of International Arbitration in the Fight Against Corruption*, 31 J. INT'L ARB. 183, 202–04 (2014).

221. *See World Duty Free*. ICSID Case No. ARB/00/7, ¶ 139.

222. *Id.* ¶¶ 179, 183.

223. *See* Moritz Renner, *Towards a Hierarchy of Norms in Transnational Law?*, 26 J. INT'L ARB. 533, 547 (2009).

224. *EDF (Servs.) Ltd. v. Romania*, ICSID Case No. ARB/05/13, Award, ¶ 221 (Oct. 8, 2009).

Arbitral tribunals evoked, rather than applied, transnational public policy in these arbitral awards, because of the nonseparability doctrine between contracts and arbitration.<sup>225</sup> Once these constraints were definitively overcome, arbitrators could straightforwardly declare the contracts on which the claims are based null and void.

#### D. *International Contracts in Domestic Fora*

In domestic fora, truly international public order values generally come into play under the umbrella of international public policy, to block the enforcement of foreign laws, acts, and decisions. This does not occur with reference to the enforcement of contractual claims, because the illegality of contracts is traditionally appreciated in the light of the municipal public policy of the forum that is scarcely permeable by international values. Nevertheless, in relation to international contracts cases, the presence of an international connecting factor would justify the acknowledgment of certain transnational public policy values into the domain of the municipal public policy of the forum. This process would take place along the same lines as in relation to conflict-of-laws cases where the presence of an international connecting factor has justified the gradual introduction of certain transnational public policy values into the international public policy of the forum. Such a scenario would imply a radical change in the content and operation of the municipal public policy, but it also would introduce a certain degree of uniformity across domestic fora.<sup>226</sup>

In this context, a useful benchmark may be constituted by the decision rendered by the Japanese court of Kanawaga in the above-mentioned case of the liberation of the coolies.<sup>227</sup> The Japanese court dealt with two specific issues: whether and to what extent the contract was, first, valid and enforceable and, second, against *bonos mores*. With reference to the first issue, the judge held, as a matter of principle, that a foreign contract should be construed and enforced in accordance with the *lex loci contractus*. Nevertheless, the judge stressed that when the *lex fori* and the *lex loci contractus* collide, the latter must yield to the

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225. See Ronán Feehily, *Separability in International Commercial Arbitration; Confluence, Conflict and the Appropriate Limitations in the Development and Application of the Doctrine*, 34 *ARB. INT'L* 355, 355–57 (2018).

226. See Martin Hunter & Gui Conde e Silva, *Transnational Public Policy and Its Application in Investment Arbitration*, 4 *J. WORLD INV.* 367, 368 (2003).

227. See *supra* Part IV.B.1. The decision rendered by the Kanawaga Kencho on 27 September 1872 is available in English in 1 *PAPERS RELATING TO THE FOREIGN RELATIONS OF THE UNITED STATES* 548–52 (1873) [hereinafter *Kanagawa Kencho Decision*]. For a historical account see Igor R. Saveliev, *Rescuing the Prisoners of the Maria Luz: The Meiji Government and the 'Coolie Trade', 1868–75*, in *TURNING POINTS IN JAPANESE HISTORY* 71 (Bert Edström ed., 2002).

former. In this case, Japanese law forbade not only any kind of enslavement in Japan, but also the importation and exportation of slaves in and from Japan. As a result, the contracts entered into between the Peruvian masters and the coolies were in contrast with the overriding mandatory rules of the forum, and thereby not enforceable.<sup>228</sup> With reference to the second issue, the judge found that, although there was no universal law that made these contracts void *ab initio*, they contained features that could not be favorably acknowledged by countries other than those strictly concerned. As the condition of slavery was “so repugnant to all sense of natural justice” that it could be recognized only under a specific law, there was no obligation under either international law or international comity by a sovereign state to provide assistance to it.<sup>229</sup> In effect, in delivering his decision, the judge clearly stated that he had been guided by “broader principles of natural justice and equity which are of universal application.”<sup>230</sup> In this way, the judge founded his decision on not only the territorial rules of the forum, but also the broader values reflecting transnational public policy. Although these values were not so far-reaching to affect the validity of the semi-enslavement contracts, they were sufficiently strong to justify the liberation of the coolies.<sup>231</sup>

Although the decision of the Japanese court could be represented more as a forgotten case than an effective precedent, practice has recorded some scattered instances where transnational public policy was applied by municipal courts in relation to international contracts. In this context, however, it is not always clear whether the national judge is applying international law norms or referring to international values. The point is well highlighted in a judgment delivered in 1966 by the *Cour d'appel* of Paris.<sup>232</sup> The case concerned a contract, entered into in Geneva by two corporations based in Luxembourg, that had as its object the sale of weapons abroad. The court held that such a contract was contrary to both French and international public policy

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228. The Kanawaga Kencho underscored that these rules reflected an established policy of the empire under which “no laborers or other persons subject to this government of enjoying its protection shall be taken beyond its jurisdiction against their free and voluntary consent, nor then without the express consent of the government.” See Kanawaga Kencho Decision, *supra* note 227, at 549.

229. *Id.* at 550. The Japanese decision echoes *Somerset v. Stewart*, *supra* note 206, at 510, where Lord Mansfield held that the status of slavery was so odious that nothing could be suffered to support it except for positive law, and the laws of England did not approve it.

230. Kanawaga Kencho Decision, *supra* note 227, at 548.

231. This humanitarian gesture raised Japan’s status in the eyes of the international community. See DOUGLAS HOWLAND, INTERNATIONAL LAW AND JAPANESE SOVEREIGNTY 33–37 (2016).

232. Cour d’appel [CA] [regional court of appeal] Paris, 5 ch., Feb. 9, 1966, Favier C. Soc. Anderssen, note Pierre Louis-Lucas (Fr.), in 55 REVUE CRITIQUE DE DROIT INTERNATIONAL PRIVE 264 (1966) (Fr.).

(namely, transnational public policy). The difficulty in appreciating this reference to truly international public order is that its sources were identified with pieces of international legislation in force rather than with international values. Nevertheless, a closer analysis demonstrates that the pieces of international legislation were not considered in their normative characterization. Rather, they were regarded in their capacity of expressing—notably but not exclusively—transnational public policy in the context of the sale of weapons.<sup>233</sup>

This issue has been better highlighted in a couple of cases concerning the sale abroad of works of art. In 1982, the *Tribunale* of Turin delivered a judgment regarding the restitution of Peruvian works of art illegally brought into Italy. Based on the criterion of the *lex rei sitae*, the court found that the law governing the transaction was Peruvian law. Since Peruvian law forbade the transfer abroad of works of art in the absence of an authorization, the works of art were to be returned to the Peruvian authorities. In its line of reasoning, the court held that applying Peruvian law was consistent not only with Italian public policy, but also with international public policy (namely, transnational public policy). In detail, the court referred to the rules contained in the 1970 UNESCO Convention on the Illicit Import, Export, and Transfer of Ownership of Cultural Property.<sup>234</sup> These rules, though, came into play not so much as applicable norms—as at the time of the purchase of the Peruvian artefacts the Convention had not yet entered into force—but rather as principles reflecting the common values of the international community in the field of transfer of cultural properties.<sup>235</sup> This Italian judgment did not remain completely isolated. In 1997, the Swiss *Tribunal Fédéral*, in a case concerning the restitution of a picture stolen abroad, came to the conclusion that, although the above mentioned 1970 UNESCO Convention and the 1995 UNIDROIT Convention on Stolen or Illegally Exported Cultural Objects<sup>236</sup> were not technically applicable, as they

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233. “[C]e trafic est contraire à l’ordre public international, tel que celui-ci est révélé notamment par l’acte général de la Conférence de Bruxelles du 2 juillet 1890, article 8, par l’arrangement conclu le 13 décembre 1906 entre la France, la Grande-Bretagne et l’Italie, enfin à la Convention internationale, conclue le 17 juin 1925, sous les auspices de la Société des Nations sur la répression de trafic d’armes . . .” See *id.* at 265.

234. UNESCO Convention on the Means of Prohibiting and Preventing the Illicit Import, Export and Transfer of Ownership of Cultural Property Nov. 14, 1970, 823 U.N.T.S. 231, [http://portal.unesco.org/en/ev.php-URL\\_ID=13039&URL\\_DO=DO\\_TOPIC&URL\\_SECTION=201.html](http://portal.unesco.org/en/ev.php-URL_ID=13039&URL_DO=DO_TOPIC&URL_SECTION=201.html) [<https://perma.cc/WNY7-Z85E>] (archived Nov. 20, 2020).

235. See Judgment of 25 marzo 1982, *Casa della Cultura Equadoriana c. Damusso e Altri*, 18 RIVISTA ITALIANA DI DIRITTO INTERNAZIONALE PRIVATO E PROCESSUALE 615 (1982).

236. UNIDROIT Convention on Stolen or Illegally Exported Cultural Objects, Jun. 24, 1995, 2421 U.N.T.S. 457, <https://www.unidroit.org/instruments/cultural-property/1995-convention> (last visited Sept. 6, 2020) [<https://perma.cc/BC7J-KLXU>] (archived Sept. 6, 2020).

had not yet been ratified by Switzerland, their norms “relèvent d’une commune inspiration [et] constituent autant d’expressions d’un ordre public international en vigueur ou en formation.”<sup>237</sup>

Despite their scantiness, these cases indicate that municipal judges have not hesitated to acknowledge a wider notion of public policy capable of embracing the fundamental values of the international community and to deny the enforcement of international contracts infringing these values.<sup>238</sup> In this context, it is worth highlighting that international contracts, nowadays, are a wide notion not confined to contracts between parties in different countries, but excluding only those situations where no international element is involved or, in other words, where all elements are connected to a single country.<sup>239</sup>

Applying this empirical approach to sovereign loans involves overcoming the traditional division between the economic and the legal definition of sovereign debt. The economic definition focuses on the residency of the creditors: the debt is internal when creditors are resident within the borrowing state; it is external when they are resident outside. The legal definition impinges on the characterization of the loan contract: the debt is foreign when the loan is denominated in a foreign currency, launched on foreign markets, submitted to a foreign law or jurisdiction; it is domestic when none of these connecting factors is present.<sup>240</sup> The result is that only domestic loans in the hands of internal creditors would escape from being qualified as international loan contracts. This picture, potentially, would enlarge the operation of transnational public policy in relation to sovereign debt.

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237. Lalive, *L'Ordre Public Transnational et l'Arbitre International*, *supra* note 218, at 604 (quoting UNIDROIT Convention on Stolen or Illegally Exported Cultural Objects, *supra* note 236).

238. Pierre Lalive, *Transnational (or Truly International) Public Policy and International Arbitration*, in *COMPARATIVE ARBITRATION PRACTICE AND PUBLIC POLICY IN ARBITRATION* 257, 286 (Pieter Sanders ed., 1986).

239. The international character of a contract may be defined in a great variety of ways. The solutions adopted in both national and international legislation range from a reference to the place of business or habitual residence of the parties in different countries to the adoption of more general criteria, such as the contract having “significant connections with more than one State,” “involving a choice between the laws of different States”, or “affecting the interests of international trade”. Although the UNIDROIT Principles of International Commercial Contracts do not expressly acknowledge any of these criteria, the general assumption is that the concept of “international” contracts should be given the broadest possible interpretation, so as ultimately to exclude only those situations where no international element at all is involved; i.e., where all the relevant elements of the contract in question are connected with one single country. See UNIDROIT, *UNIDROIT PRINCIPLES OF INTERNATIONAL COMMERCIAL CONTRACTS* 1 (2016).

240. See MEGLIANI, *supra* note 133, at 4–5.

### E. *Odious Debt and Transnational Public Policy*

In terms of illegitimate/odious debt, two connected issues arise: whether the odious debt doctrine can be subsumed under the umbrella of transnational public policy, and whether, once a debt is declared illegitimate/odious, restitutionary remedies are available.

In relation to subsumption under transnational public policy, the Sackian view pursuant to which a debt must be odious not only in the view of a government, but also in that of the family of nations, ideally places the odious debt doctrine in this context.<sup>241</sup> Nevertheless, this qualification is to be tested. In this respect, it is necessary to draw a distinction between situations where the financial transaction is tainted with corruption and situations where no corruptive activity emerges. In the first case, the financial transaction is considered collateral to the corruptive activity and follows its fate.<sup>242</sup> In the second case, it is questionable whether transactions not affected by corruption but by mere “odiousness” may be declared illegal and unenforceable.

The reading of the World Duty Free arbitration may offer some guidance in this regard. In the view of the arbitral tribunal, bribery was contrary to transnational public policy “[i]n light of domestic laws and international conventions relating to corruption, and in light of the decisions taken in this matter by courts and arbitral tribunals.”<sup>243</sup> These are the benchmarks against which to ascertain the subsumption of the values protected by the odious debt doctrine under transnational public policy. In terms of national law, some pieces of legislation are specifically aimed at curbing the judicial activism of vulture funds,<sup>244</sup> but this is a very different issue from considering a loan contracted without the consent of the population, not for its benefit and in the awareness of the creditors to be illegal. In terms of international conventions, no international instrument regulating this phenomenon has so far been drafted, even though two pieces of soft law can be recorded: the UNCTAD Principles Promoting Responsible Sovereign Lending and Borrowing and the HRC Guiding Principles on Foreign Debt and Human Rights (¶ 86(d)).<sup>245</sup> In the first, the three elements of the odious debt doctrine are in some way embedded in the text; in the second, the odious debt doctrine is expressly mentioned, but with the

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241. See SACK, *supra* note 74, at 162.

242. “[C]laims based on contracts of corruption or on contracts obtained by corruption cannot be upheld by this Arbitral Tribunal,” World Duty Free Co. v. Republic of Kenya, ICSID Case No. ARB/00/7, Award, ¶ 157 (Oct. 4, 2006).

243. *Id.*

244. See Debt Relief (Developing Countries) Act 2010, c. 22 (U.K.). Further, there is a 2008 Belgian law meant to prevent funds appropriated by the Belgian government for development co-operation from becoming an object of attachment by creditors of recipient states. See DEVI SOOKUN, STOP VULTURE FUNDS LAWSUITS 88 (2010).

245. *Supra* Part III.B.3.

indication that it should be formalized through national legislation. On the one hand, this picture reflects the failure of a proper normative characterization of the doctrine; on the other hand, it indicates an emerging principle capable of gaining progressive acceptance.

In terms of arbitration, the only case in which the doctrine has been applied is the so-called Tinoco arbitration.<sup>246</sup> The case concerned the validity of a loan contracted by Frederico Tinoco, President of Costa Rica, with the Royal Bank of Canada following the *coup d'état* of 1917. In January 1917, Tinoco was Secretary of War under President Alfredo Gonzalez. On the grounds that Gonzalez was seeking presidential reelection in violation of a constitutional limitation, Tinoco used the army and navy to seize the government and assume the provisional headship of the Republic. He, then, called a presidential election and became the new president of Costa Rica, but soon he lost the favor of the population and was obliged to relinquish power. Over this period, the sums provided under the loan contracted with the Royal Bank of Canada were used for the personal expenses of President Tinoco and his kinship. Because of this, the successor government did not recognize the loan, and the United Kingdom, acting in diplomatic protection on behalf of the Canadian bank, agreed with Costa Rica to submit the controversy to arbitration. Umpire Taft, the Chief Justice of the U.S. Supreme Court at the time, held that the Canadian Bank did not behave in good faith in its lending activity and thereby Costa Rica had been right in repudiating the loan.<sup>247</sup> The Tinoco arbitral award, however, does not contain all three of the traditional elements of the doctrine, as Tinoco was democratically elected.<sup>248</sup> Moreover, this is a “vintage” case, too old and isolated in the arbitral practice to constitute a precedent.<sup>249</sup>

All this picture indicates that, to this day, the acknowledgment of the odious debt doctrine within transnational public policy is not well established but is still a process in formation. Nevertheless, this does not preclude courts and tribunals from applying the doctrine and contributing to its formalization.

In relation to the availability of restitutionary remedies, it is again necessary to draw a distinction between cases in which the transaction

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246. See Aguilar-Armory & Royal Bank of Canada (Gr. Brit. v. Costa Rica), 1 R.I.A.A. 369, 394 (1923).

247. “The case of the Royal Bank depends not on the mere form of the transaction but upon the good faith of the bank in the payment of money for the real use of the Costa Rican Government under the Tinoco régime. It must make out its case of actual furnishing of money to the government for its legitimate use. It has not done so.” *Id.* at 394.

248. See Sarah Ludington, Mitu Gulati & Alfred L. Brophy, *Applied Legal History: Demystifying the Doctrine of Odious Debts*, 11 THEORETICAL INQUIRIES IN L. 247, 262–63 (2010).

249. See Lee C. Buchheit & G. M. Gulati, *Odious Debts and Nation-Building: When the Incubus Departs*, 60 ME. L. REV. 477, 482 (2008).



is tainted with corruption and cases in which it is not. When a transaction is tainted with corruption, the doctrine of the unclean hands bars the recovery of what has been transferred under the contract, as the policy of discouraging corruptive activity is considered prevailing over the policy of avoiding unjust enrichment. In this case, it is superfluous to make an inquiry into the legal status of the odious debt doctrine. By contrast, when the transaction is not tainted with corruption, the availability of the restitutionary remedies depends on the legal status of the doctrine. Even assuming that the doctrine may have some public policy characterization, the general rule is that a claim for the recovery of money lent based on unjust enrichment can be barred only in rare cases.

However, the sanction of denying restitutionary remedies can be reasonable to the extent that creditors coincide with those who have partaken in the corruptive activity or the odious transaction. This is certainly the case of transactions with bankers, just like those declared invalid by the Mozambican Constitutional Council. By contrast, this can scarcely be the case of bonded loans where the holders of the bonds do not coincide with those who have taken part in the corruptive or odious activity. This involves that restitutionary remedies can hardly be refused to bondholders.

## V. CONCLUSION

The controversy surrounding the Mozambican loans has opened the Pandora's box on the validity and enforceability of sovereign loans and guarantees lacking a proper authorization and tainted with corruption as well as on the availability of restitutionary remedies. As these transactions are contracts with private parties, these issues should be appreciated in the light of domestic law and before national courts. These two factors would determine the outcome of lawsuits. To avoid fragmentation, a possible solution is to have recourse to a uniform benchmark: the odious debt doctrine.

Under the odious debt doctrine, a sovereign loan or guarantee is invalid as long as it is incurred without the consent of the population and not in its interest with the awareness of the creditors. The legal status of this doctrine, though, is still uncertain. Failing a proper normative characterization, it may come into play in the form of public policy. Normally, public policy is meant to protect the fundamental values of the forum. As the odious debt doctrine protects international values, its ideal collocation could be under the umbrella of transnational public policy that serves the common interests of mankind.

In the case of international contracts, to the realm of which sovereign loans and guarantees with private parties belong, the presence of an international connecting factor can justify the

contamination of the parochial public policy of the forum with the values protected by the transnational public policy. In this context, it is plainly acknowledged that when an odious debt is incurred on the basis of an upstream corruptive activity, the illegality of this latter impinges upon the former and restitutionary remedies are unavailable. What remains an open question is whether and to what extent the values protected by the odious debt doctrine are *per se* subsumable under transnational public policy. The conclusion is that, to this day, this process of subsumption is still at an early stage. Nevertheless, this does not preclude courts and tribunals from applying the doctrine and contributing to its formalization.