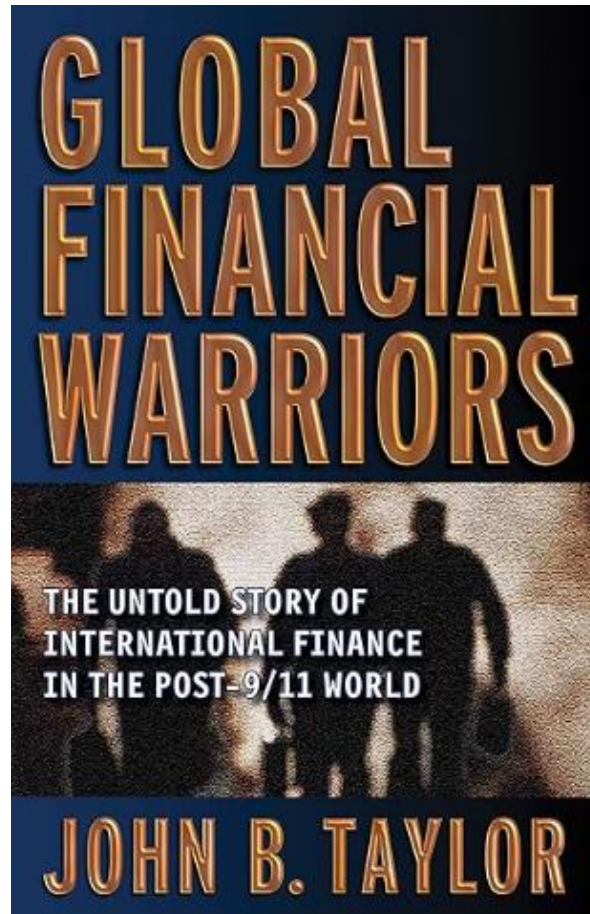


International Cooperation in the Age of Taylor: A CAC/EAP Story

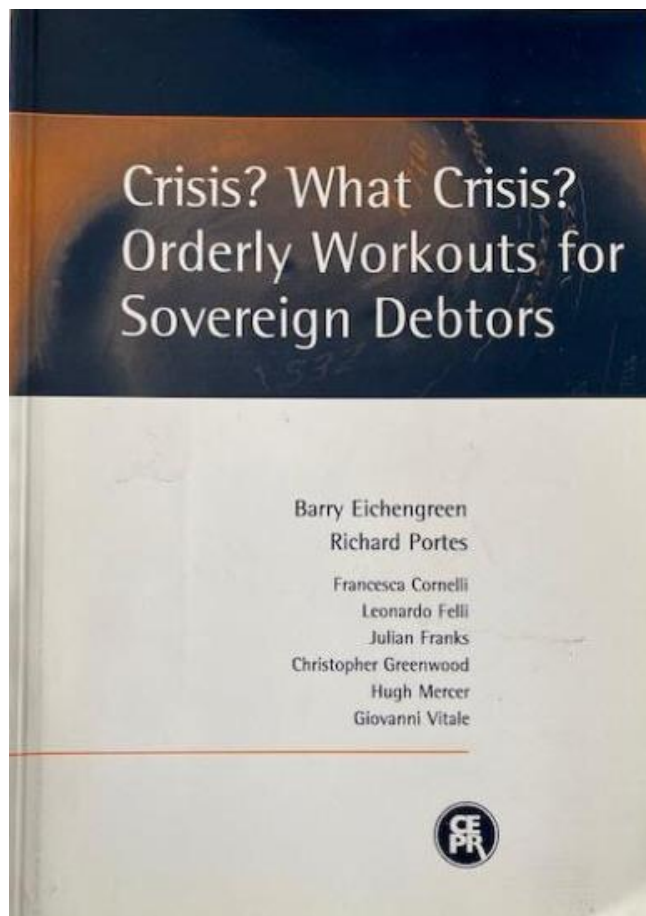
Barry Eichengreen
University of California, Berkeley
May 8, 2025

- CACs = Collective Action Clauses
- EAP = The IMF's Exceptional Access Policy

JBT tells the story of both in Chapter 4 of his book



Self-servicing remark: One of the first two authors (1995)



The date (1995) provides the context

- Mexican crisis.
- Unprecedentedly large IMF program.
- Worries about moral hazard.
 - For reckless EM policymakers.
 - For reckless creditors who got bailed out.
- Solution: make it easier to restructure as an alternative to bailouts.
- Solution: in turn it becomes possible to limit exceptionally large programs



Obstacles Undersecretary Taylor had to overcome

- Fear of higher borrowing costs limited willingness of EMs to issue.
- Novelty premium.
 - First movers would also be sending a negative signal about their own creditworthiness.
- Alternative IMF proposal (SDRM).
 - Temptation for the press to set up the two Stanford professors and golfing partners as rivals and even enemies.

Negotiations and achievements

- March 14, 2002 Taylor memo to Treasury Secretary O'Neill.
- April 2, 2002 speech at IMF Spring Meetings announcing Treasury "Action Plan."
- April 19, 2002, G7 signs on to Action Plan.
- Summer 2002: Treasury leads international effort to develop model clauses.
- IMF Fall Meetings 2002: Bringing all stakeholders, both private and public, together in Treasury Cash Room, but no agreement.
- January 2003: Mexico (with impetus from Carstens) agrees to go first.
- Scores of other countries then follow.

Assessment: Impact on borrowing costs depends who you are

The Economic Journal, 114 (April), 247–264. © Royal Economic Society 2004. Published by Blackwell Publishing, 9600 Garsington Road, Oxford OX4 2DQ, UK and 350 Main Street, Malden, MA 02148, USA.

DO COLLECTIVE ACTION CLAUSES RAISE BORROWING COSTS?*

Barry Eichengreen and Ashoka Mody

We compare launch spreads on emerging-market bonds subject to UK governing law, which typically include collective action clauses, with spreads on bonds subject to US law, which do not. Collective-action clauses reduce the cost of borrowing for more creditworthy issuers, who appear to benefit from the ability to avail themselves of an orderly restructuring process. Less creditworthy issuers, in contrast, pay higher spreads. It appears that for less creditworthy borrowers the advantages of orderly restructuring are offset by the moral hazard and default risk associated with the presence of renegotiation-friendly loan provisions. We draw out the implications for the debate over whether to encourage the wider utilisation of these provisions as part of the effort to strengthen the international financial architecture.

For nearly a decade, since the outbreak of the Mexican crisis, there has been a steady stream of proposals for 'strengthening the international financial architecture' – that is, for more effectively preventing and resolving financial crises.¹ Encouraging the more broad-based use of collective action clauses (CACs) in loan contracts is a prominent initiative on the crisis resolution front. Collective action clauses specify who represents the creditors in negotiations, detail majority-voting procedures for altering the financial terms of the contract and limit the incentive or ability of individual creditors to initiate legal action against a borrower in arrears. They are seen as a useful way of streamlining and simplifying the process of debt restructuring.

While such clauses have long been included in syndicated bank loan contracts, they are absent from roughly two thirds of emerging market debt issued between 1991 and 2001 (where we measure debt by value). In particular, international bonds issued in the US and subject to the law of the State of New York require the unanimous consent of the bondholders to any restructuring, complicating efforts to alter payment terms. US-style bonds also typically lack clauses specifying who represents the bondholders and making provision for a bondholders committee or assembly. In addition, they lack sharing clauses designed to restrain individual creditors from utilising lawsuits as a way of holding up settlements in an effort to extract side payments. Bonds subject to German and Japanese law have the same

* The World Bank's Research Committee and the Ford Foundation (through the Berkeley Project on New International Financial Architecture) provided financial support for this research. Manzoor Gill and Himmat Kalsi provided the updated data on bond spreads and guidance on their interpretation. Gabin Ho, Galina Hale, and Anindita Sen helped us assemble the data and develop the documentation. For helpful comments and advice, we thank Daniel Bond, Michael Buchanan, David Card, Thomas Duvall, participants at an IMF seminar, and two referees of this JOURNAL. The views expressed in this paper are not necessarily those of the World Bank or the International Monetary Fund.

¹ Two reviews of these proposals are Kenen (2001) and Eichengreen (2002).

Assessment: Impact of enhanced clauses depends on who you are

Is Aggregation a Problem for Sovereign Debt Restructuring?

By BARRY EICHENGREEN AND ASHOKA MODY*

Reform of the mechanisms and procedures through which problems of sovereign debt sustainability are resolved is at the center of the effort to make the international financial system more resilient and less prone to crisis. Governments that default on their debts must embark on lengthy and difficult negotiations. Lenders and borrowers, uncertain of one another's willingness to compromise, may engage in costly wars of attrition, delaying agreement on restructuring terms. Even if disagreements about the debtor's willingness and ability to pay are put to rest, dissenting creditors may continue to block agreement until they are bought out on favorable terms.

In the interim, the creditors receive no interest, and the borrowing country loses access to international capital markets. The exchange rate may collapse, and banks with foreign-currency-denominated liabilities may suffer runs. To avert or delay this costly and disruptive crisis, the International Monetary Fund will come under intense pressure to intervene, provoking all the controversy that IMF intervention typically entails. Officials of the borrowing country, for their part, will go to great lengths to avoid seeing the country placed in this difficult situation. They may raise interest rates, run down their reserves, and put their economy through a deflationary wringer, all at considerable cost to society.

These costs could be reduced if countries with unsustainable debt reorganized sooner and if debtors and creditors could agree more easily on restructuring terms. But a necessary condition for this is a more efficient mechanism for debt workouts that addresses the information asymmetries and coordination problems that stand in the way of prompt debt reorganization.

Debt restructuring involves two conceptually

similar but procedurally different problems, those of intra-issue and inter-issue coordination. The first problem, restructuring a single debt instrument with multiple holders, can be facilitated by writing into each of those instruments provisions known as collective-action clauses. John Taylor (2002a, b) has recommended adding to all international loan agreements an engagement clause that would designate a trustee to represent the holders of that instrument at the outset of the restructuring, a representation clause that would provide for the creation of a creditors committee to serve as a communications channel and coordinate relations with the sovereign during restructuring negotiations, an initiation clause that would give only that trustee the power to initiate litigation on the instruction of a specified fraction of the bondholders, and a majority action clause under which a qualified majority vote of the bondholders accepting changes in the financial terms of the issue would become binding on all its holders. A combination of moral suasion and regulatory and financial incentives would be used to encourage lenders and borrowers to adopt these provisions.

However, collective action clauses, which are specific to the individual debt contract, might not suffice to deal with the broader problems of information-sharing and creditor coordination that arise when the government in default has multiple debt obligations, as is typically the case. Collective-action clauses provide for a bondholder assembly and qualified majority voting, debt instrument by debt instrument, on whether to accept a restructuring offer, but they do not specify a way of aggregating the preferences of creditors holding different issues. If the holders of some issues refuse the government's offer, they may have to be paid in full or bought out at par. The government will have fewer resources to share with other issue-holders, who may then reject its restructuring offer. This may create a first-mover problem.

To address these additional complications, Anne Kruger (2001, 2002) has a proposed a

* Department of Economics, University of California, Berkeley, CA 94720, and International Monetary Fund, respectively. The opinions expressed here are not necessarily the official views of any organization with which the authors are affiliated.

More recent evidence suggests that enhanced clauses lower borrowing costs across the board



WP/20/162

IMF Working Paper

**Do Enhanced Collective Action Clauses Affect
Sovereign Borrowing Costs?**

by Kay Chung and Michael G. Papaioannou

I N T E R N A T I O N A L M O N E T A R Y F U N D

And Exceptional Access Policy? Approved in September 2002

- John writes how he preferred rules over discretion.
- Influenced by you know who
 - (Kydland and Prescott 1977).
- This was referred to as “constrained discretion.”

BOX 1. KEY ELEMENTS OF THE EXCEPTIONAL ACCESS POLICY

The key elements of the Exceptional Access Policy (EAP)—including its original (2002) and current (2016) iteration—and its associated procedures for access to the General Resources Account in excess of NA limits for members facing exceptional needs are as follows:

Criteria to Justify Exceptional Access

CRITERIA	ORIGINAL EAP (2002)	CURRENT EAP (2016)
EAC1: BOP Needs	The member is experiencing exceptional balance of payment (BOP) pressures on the capital account resulting in a need for Fund financing that cannot be met within the NA limits.	The member is experiencing or has the potential to experience exceptional BOP pressures on the current account or the capital account, resulting in a need for Fund financing that cannot be met within the normal limits.
EAC2: Debt Sustainability	A rigorous and systematic analysis indicates that there is a high probability that debt will remain sustainable.	A rigorous and systematic analysis indicates that there is high probability that the member's public debt is sustainable in the medium term. Where the member's debt is assessed to be unsustainable ex ante, exceptional access (EA) will only be made available where the financing being provided from sources other than the Fund restores debt sustainability with a high probability. Where the member's debt is considered sustainable but not with a high probability, EA would be justified if financing provided from sources other than the Fund—although it may not restore sustainability with high probability—improves debt sustainability and sufficiently enhances the safeguards for Fund resources. For purposes of this criterion, financing provided from sources other than the Fund may include, inter alia, financing obtained through any intended debt restructuring. This criterion applies only to public (domestic and external) debt. However, the analysis of such public debt sustainability will incorporate any potential contingent liabilities of the government, including those potentially arising from private external indebtedness.
EAC3: Market Access	The member has good prospects of regaining access to private capital markets within the time Fund resources would be outstanding, so that the Fund's financing would provide a bridge.	The member has prospects of gaining or regaining access to private capital markets within a timeframe and on a scale that would enable the member to meet its obligations falling due to the Fund.
EAC4: Program Success	The policy program of the member country provides a reasonably strong prospect of success, including not only the member's adjustment plans but also its institutional and political capacity to deliver that adjustment.	The policy program of the member country provides a reasonably strong prospect of success, including not only the member's adjustment plans but also its institutional and political capacity to deliver that adjustment.

Decision-making procedures. (i) A higher burden of proof is needed in EA program documents—including thorough discussion of need and the proposed level of access, a rigorous analysis of debt sustainability, and an assessment of risks to the Fund arising from the exposure and its effect on the Fund's liquidity. (ii) There are enhanced requirements and expectations regarding early Board consultations for EA cases.

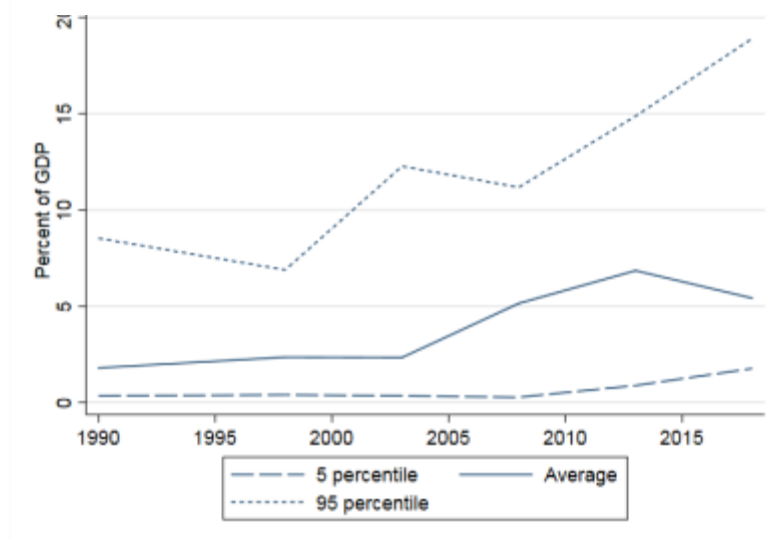
Assessment

- EAP policy succeeded in encouraging “deliberate and systematic consideration” of large programs.
- But lack of clear numerical or other benchmarks has raised questions about “evenhandedness.”
- Repeated ad hoc changes in the framework as “special cases” arise (the “Systemic Exemption” for example).
- Staff is said to have reverse engineered whether cases qualify for Exceptional Access to allow programs to go forward (which is staff’s preference).
- Still no support in the institution for a binding rule.



Assessment

Distribution of IMF arrangement sizes



But then there is also this

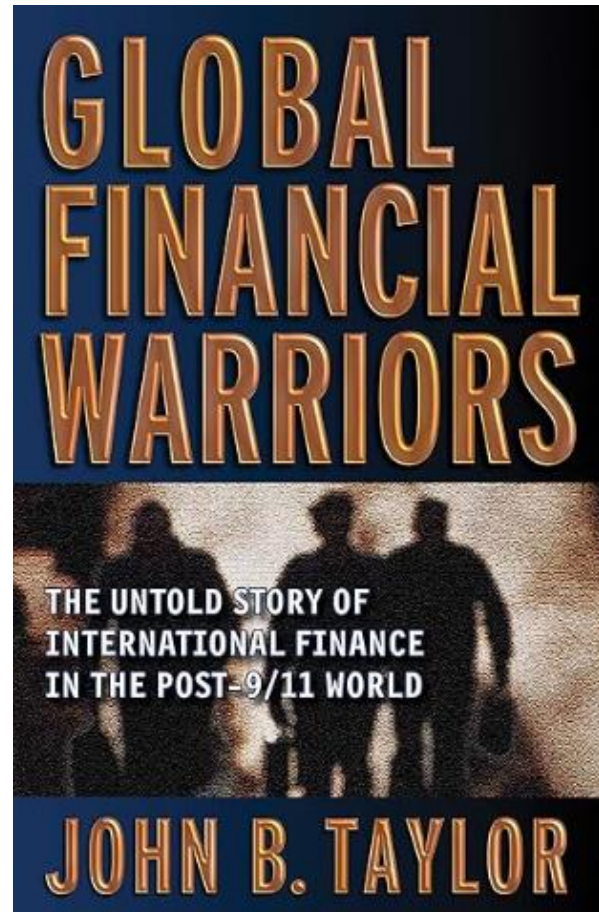
- Which is not very encouraging when one thinks about a systematic process for encouraging exceptional access to IMF resources.



Argentina secures IMF loan and ends most capital controls in key milestones for President Milei

Conclusion

- The undersecretary's achievements were considerable.



- Thank you.