

# The potential of trust law in sovereign debt restructuring.

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## **The Potential of Trust Law in Sovereign Debt Restructuring Unveiled**

The interplay between sovereign debt defaults and legal frameworks has long been a subject of scholarly discourse and practical concern. Navigating this labyrinthine arena necessitates a rigorous understanding of various legal paradigms, one of which is trust law. In a new [article](#), I aim to shed light on the utility of trust law in dealing with sovereign debt defaults. The article delves into the core principles of trust law – impartiality and independence – and evaluates their applicability in reconciling the often-divergent interests of creditors and sovereign debtors. While acknowledging the roles of other legal mechanisms, such as national insolvency laws and contractual agreements, the article posits that trust law offers unique advantages in fostering equitable and just resolutions. Nevertheless, this paradigm is not without its limitations, which also warrant a thoughtful discussion. Ultimately, the article calls for an integrated approach to assess the broader implications of trust law within the financial system, advocating for its potential role in stabilizing global markets and enhancing international relations.

The article accentuates the inherent fairness of trust law. It offers an impartial arena where the divergent interests of multiple stakeholders, such as creditors and sovereign debtors, find resolution. Devoid of political or economic predispositions, trust law functions as an essential agent in resolving financial disagreements. In the practical realm, the utility of trust law in sovereign debt defaults is not merely theoretical. For instance, the 2001 Argentine debt crisis offers an illuminating example. A trust structure was set up, managed by The Bank of New York Mellon, serving as a neutral trustee to oversee fund distribution to creditors. By adhering to the core principles of trust law, this arrangement contributed significantly to an equitable settlement, mitigating conflicts and facilitating a fair distribution of assets. This case underscores the burgeoning relevance of trust law as an efficient and equitable instrument for resolving complex financial disputes in the international sphere.

Yet, trust law is not a universal remedy for debt defaults. National insolvency laws may apply domestic remedies, but they are often impeded by international enforcement difficulties and disparate legal interpretations. Contractual frameworks offer negotiated settlements, though they often include consent requirements and involve the potential for disputes.

The merits of trust law in managing sovereign debt defaults are numerous. Trust law could reconcile the conflicting interests of both sovereign debtors and creditors by establishing a fiduciary relationship that includes rigorous duties. Specifically, a trustee serves as a neutral arbiter between creditors and a debtor. The trustee, bound by fiduciary duties, is obligated to act in the best interests of the creditors while also honouring the terms of the trust deed, which may include conditions for restructuring debt. This fiduciary responsibility mitigates unilateral actions that can exacerbate conflicts and so cuts through streamlines disagreements and fosters resolution.

Trust law's detachment from external influences allows it to avoid political interference. For example, a trustee in a sovereign debt scenario is not subject to governmental policies of the debtor nation. The role is purely fiduciary, ensuring that decisions are made based on the legal agreement and not external political considerations.

Furthermore, the inherent flexibility of trust law enables tailor-made settlements. The structure of a trust can be customized to suit the particularities of a sovereign debt default scenario. Specific clauses can be incorporated into the trust deed to address unique challenges posed by the debtor's economic conditions, thereby making the mechanism adaptable to a variety of situations. This flexibility enhances its efficacy.

This legal mechanism is also cost-effective and accessible to stakeholders of varying financial means. Trust law minimizes litigation costs by centralizing the administration of debt repayments through a single trustee rather than requiring multiple parties to engage in separate legal actions. Additionally, the process is relatively straightforward, minimizing legal fees and making the mechanism more accessible to parties with limited financial resources.

However, trust law has limitations. A significant one is the enforcement of trust terms, which presents a formidable challenge due to ambiguities in legal interpretation, the complexities of international law, and varying jurisdictional authorities. Additionally, the absence of a clear legal framework may restrict its utility. The success of trust law in resolving sovereign debt defaults is contingent upon several factors, including the proper establishment of the trust, the prevailing legal landscape, and the willingness of all parties to engage in the process.

The broader implications of applying trust law extend beyond the financial sphere. Its use of collaborative strategies might reduce the frequency of future defaults, contribute to the stabilization of global financial markets, and even serve as a blueprint for its application in other sectors of international finance. To counteract the challenges related to enforcement, the article recommends the creation of a standardized legal framework and the fortification of enforcement mechanisms. This could also have ripple effects on international relations, underscoring the critical need for global financial collaboration.

The article posits trust law as an emergent, promising instrument for managing the complexities of sovereign debt defaults due to its intrinsic qualities of fiduciary responsibility, transparency, and asset protection. These qualities can ensure that stakeholders' interests are more equitably balanced, thereby mitigating the adversarial tensions often present in debt negotiations. Despite its limitations, it has great potential to serve as an unbiased and equitable mediator. The article does not merely call for further study but advocates for the practical integration of trust law into the management of sovereign debt defaults. Such an integration may be a harbinger of its usefulness in future default resolutions. The article thus offers insights for an array of professionals, including policymakers, legal experts, and individuals dealing with sovereign debt defaults.

*This post comes to us from Charles Ho Wang Mak, a lecturer in law at Robert Gordon University, a PhD Candidate in Law at University of Glasgow, and a research associate at Oxford University. It is based on his recent article, "Debts unravelled: trust law's unbiased approach to resolving sovereign defaults," available [here](#).*

*The article was also previously featured in a post on September 29, 2023 in Columbia Law School's [CLS Blue Sky Blog](#).*