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## Is There a Recognized Legal Doctrine of Odious Debts

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## Is There a Recognized Legal Doctrine of Odious Debts

### Cover Page Footnote

International Law; Commercial Law; Law

# Is There A Recognized Legal Doctrine of Odious Debts?

Andrew Yianni† & David Tinkler††

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### I. Introduction

The issue of “odious debts” requires consideration from time to time in the context of sovereign debt claims, and it has recently become topical again. The purpose of this article is to review the literature on odious debt to determine whether there is an established doctrine of odious debt.

Whether a doctrine of “odious debt” exists and, if it does, what

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the term “odious debt” means are contentious questions. Even among the supporters of such a doctrine there is disagreement over its scope. There is an important distinction to make between the two types of supporters in order to guide the analysis of the odious debt issue.

## II. The Legal and Political Approaches

The supporters of the odious debt doctrine can be divided into two groups: those who take the legal approach and those who take the political approach. Supporters of the Legal Approach seek to demonstrate that there is a customary rule of international law that defines and governs odious debt. Supporters of the Political Approach do not use legal techniques to try to show the existence of a doctrine of odious debt; instead, they make an argument based on political principles.

### A. *The Political Approach*

Professor Alexander Sack formulated the classic political definition in 1927.<sup>1</sup> The elements of the definition are: (i) debts are incurred contrary to the interests of the State; (ii) the creditor knows that the debt is contrary to the interests of the State; and (iii) the funds were not spent in the interests and needs of the State.<sup>2</sup> Sack believed that there are two types of odious debt: debts that are incurred by a despotic power “to strengthen its despotic regime [in order to] repress the population that fights against it,”<sup>3</sup> and debts which are “loans incurred by members of the government or by persons or groups associated with the government to service interests manifestly personal—interests that are unrelated to the interests of the State.”<sup>4</sup>

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<sup>1</sup> See generally ALEXANDER SACK, *THE EFFECTS OF STATE TRANSFORMATIONS ON THEIR PUBLIC DEBTS AND OTHER FINANCIAL OBLIGATIONS* (1927) (writing on the principle that a state should not be bound to debts which are created against the state's interest.).

<sup>2</sup> PATRICIA ADAMS, *ODIOUS DEBTS: LOOSE LENDING, CORRUPTION AND THE THIRD WORLD'S ENVIRONMENTAL LEGACY* 164-66 (1991) (citing SACK, *supra* note 1, at 157-58).

<sup>3</sup> *Id.* at 165.

<sup>4</sup> Patricia Adams, *The Doctrine of Odious Debts: Using the Law to Cancel Illegitimate Debts*, Address at the Germany Jubilee Network Seminar (June 21, 2002) (transcript available at <http://www.odiousdebts.org/odiousdebts/print.cfm?Content>).

Patricia Adams suggests that bribes are an example of this second type of odious debt because they are a “manifestly personal interest.”<sup>5</sup> Jeff Rudin adds to the definition of odious debt that “debts from loans made in breach of international law are automatically odious.”<sup>6</sup> Rudin explains:

[T]he reason for this is that international jurisprudence now imposes a duty on governments to uphold a core of fundamental rights or prohibitions. Pre-eminent amongst the prohibitions are acts of aggression, slavery, genocide and racial discrimination.<sup>7</sup>

Adams suggests that an international tribunal be established to deal with odious debt claims.<sup>8</sup> Adams believes that Indonesia should commence arbitration proceedings against the World Bank in respect of the \$30 billion lent to the Suharto government between 1966 and 1998 as up to \$10 billion of that served “manifestly personal” interests.<sup>9</sup>

Odious debt is considered an exception to the general principle that a new government “automatically and unconditionally”<sup>10</sup> accepts debts contracted by its predecessor. Sack suggested that a new government would be required to prove that the debt satisfied these conditions, which would create a presumption that the debt was odious.<sup>11</sup> It would then be open to the creditor to demonstrate to an international tribunal that the funds were used to benefit the territory.<sup>12</sup> A debt is odious, and, therefore, non-transferable “if the previous regime was any form of dictatorship acting contrary to the needs and wishes of the subjugated population.”<sup>13</sup> This is a

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ID=4909).

<sup>5</sup> *Id.* at 2.

<sup>6</sup> Jeff Rudin, *Odious Debt Revisited*, Jubilee South 6 (2002), available at <http://www.jubileesouth.org/news/EpFVuVkkFlkCCnpoKE.shtml>.

<sup>7</sup> *Id.* at 6. Although a rule with strong support, it is not yet clear that the prohibition on racial discrimination is a rule of *jus cogens*. See, e.g., Convention on the Prevention and Punishment of the Crime of Genocide art. 7, Dec. 9, 1948, 78 U.N.T.S. 277.

<sup>8</sup> See ADAMS, *supra* note 2, at 167.

<sup>9</sup> See Adams, *supra* note 4.

<sup>10</sup> See Rudin, *supra* note 6, at 2.

<sup>11</sup> See ADAMS, *supra* note 2, at 166.

<sup>12</sup> See ADAMS, *supra* note 2, at 167.

<sup>13</sup> Rudin, *supra* note 6, at 2.

significant difference from the Legal Approach which requires state—not merely government—succession to trigger an odious debt classification.<sup>14</sup> This difference makes the Political Approach immediately much wider because situations such as post-invasion Iraq in 2003 would certainly be within the scope of the theory. Rudin also suggests that South Africa's conversion from apartheid in 1994 would be covered.<sup>15</sup>

### III. Is There an Established Doctrine of Odious Debt?

The Political Approach is not a theory that can be subjected to serious legal analysis because it is not based on legal principles. In this context, it is instructive to consider how new legal rules can be made. It is not contentious to state that any individual country is free to change its law to make odious debts irrecoverable. For example, the United States could pass a Federal law to this effect although it would need to reconcile that law with constitutional rules protecting property rights (that is, no expropriation without compensation, as the creditors' rights would be taken away). However, ultimately Congress could amend the Constitution if necessary.

In the United Kingdom, Parliament could effectively do the same by passing a law that all odious debts, however defined, are irrecoverable. The United Kingdom has no written constitution but is subject to the European Convention on Human Rights.<sup>16</sup> However, as a matter of national law, Parliament could make the necessary amendments to the Convention.

As alternative approach on the public international law level, all sovereign nations, or a significant subset of them such as the G7 and others, could enter into a convention or treaty under which odious debts are void or could be made void. This is what Sack wanted.<sup>17</sup>

The real point is that neither of these steps, national nor international, have been taken. Interestingly, there has been a half-hearted attempt by some to pursue the second route in the form of

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<sup>14</sup> See *infra* Part III.A.

<sup>15</sup> See Rudin, *supra* note 6, at 9.

<sup>16</sup> The UK signed the Convention as a treaty and has incorporated it into domestic law through an act. Human Rights Act, 1998, c. 42, pt. I, arts. 2-12 (Eng.).

<sup>17</sup> See Adams, *supra* note 4, at 2.

the 1983 Vienna Convention on Succession of States in respect of State Property.<sup>18</sup> Article 38 of this Convention provides that no debt passes to successor states unless there is a positive agreement to this effect.<sup>19</sup> This Convention will be discussed in detail below, but it should be noted that it has not entered into force and that it is focused on state succession, rather than regime change.<sup>20</sup> Also, it deals predominantly with public international law type debts that are owed by one state to another state or by a state to an international institution, such as the International Monetary Fund.<sup>21</sup>

In the absence of a convention or treaty or changes in the law on a national level, subject to a point that will be considered below, what is left?

The answer is other sources of public international law. For Europeans, that immediately leads to consideration of the United Nations and in particular, its judicial arm, the International Court of Justice (ICJ).

### A. *The Legal Approach*

Some supporters of the odious debt doctrine apply more sophisticated legal analysis to attempt to prove that a customary rule of international law exists in respect of odious debt.<sup>22</sup> In order to discuss whether the doctrine is a rule of international law, it is helpful to briefly consider how the rules of international law are made.

#### 1. *Sources of International Law*

Article 38(1) of the Statute of the International Court of Justice is accepted as an authoritative statement of the sources of international law.<sup>23</sup> There are four categories:

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<sup>18</sup> Vienna Convention on Succession of States in Respect of State Property, Archives and Debts, Apr. 8, 1983, 22 I.L.M. 306 (1983).

<sup>19</sup> *Id.*

<sup>20</sup> *Id.*

<sup>21</sup> *Id.*

<sup>22</sup> Charles Abrahams, *The Doctrine of 'Odious Debts'* (Aug. 2002) (unpublished LL.M. thesis, University Lieden, The Netherlands), available at <http://www.odiousdebts.org/odiousdebts/publications/ApartheidDebtThesis.pdf>.

<sup>23</sup> Statute of the International Court of Justice art. 38(1), June 26, 1945, 59 Stat.

- a. international conventions, whether general or particular, establishing rules expressly recognized by the contesting states;
- b. international custom, as evidence of a general practice accepted as law;
- c. the general principles of law recognized by civilized nations;
- d. subject to the provisions of Article 59, judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determination of rules of law.<sup>24</sup>

The supporters of the Legal Approach argue that there is a customary rule of international law, so there must be “evidence of a general practice accepted as law.”<sup>25</sup> The Court has developed the requirements for a customary rule to be formed in its jurisprudence.<sup>26</sup>

The requirements can be summarized as follows:

- The rule must be “in accordance with a constant and uniform usage practised by the States in question”;<sup>27</sup>  
 an indispensable requirement would be that within the period in question, short though it may be, state practice, including that of states whose interests are specially affected, should have been both extensive and virtually uniform in the sense of the provision invoked, and should moreover have occurred in such a way as to show a general recognition that a rule of law or legal obligation is involved;<sup>28</sup>
- it is “sufficient that the conduct of states should, in general, be consistent with such rules, and that instances of state conduct inconsistent with a given rule should generally have

1055, 1060, 3 Bevens 1179, 1187, *available at* <http://www.icj-cij.org/documents/index.php?p1=4&p2=2&p3=0> [hereinafter I.C.J. Statute].

<sup>24</sup> *Id.*

<sup>25</sup> *Id.*; *see, e.g.*, Arrest Warrant of 11 April 2000 (Dem. Rep. Congo v. Belg.), 2002 I.C.J. 121 (Feb. 14) (separate opinion of Judge Koroma), *available at* <http://www.icj-cij.org/docket/files/121/8134.pdf> (last visited May 1, 2007).

<sup>26</sup> *See* I.C.J. Statute, *supra* note 23

<sup>27</sup> Asylum (Colom. v Peru), 1950 I.C.J. 266, 276-77 (Nov 20, 1950).

<sup>28</sup> North Sea Continental Shelf (F.R.G. v. Den.; F.R.G. v. Neth.), 1969 I.C.J. 3, 43 (Feb. 20).

been treated as breaches of that rule, not as indications of the recognition of a new rule”,<sup>29</sup>

for a new customary rule to be formed, not only must the acts concerned “amount to a settled practice,” but they must be accompanied by the *opinio juris sive necessitates*. Either the States taking such action or other States in a position to react to it must have behaved in such a way that their conduct is evidence of a belief that this practice is rendered obligatory by the existence of a rule of law requiring it. The need for such a belief, i.e. the existence of a subjective element, is implicit in the very notion of the *opinio juris sive necessitate*;<sup>30</sup>

- “only if . . . abstention were based on their [the states] being conscious of having a duty to abstain would it be possible to speak of an international custom”;<sup>31</sup>

if an individual state consistently objects to the application of a rule to its affairs, a specific exemption may be created. The ICJ has stated in the context of a matter affecting Norway that “in any event[,] the . . . rule would appear to be inapplicable as against Norway inasmuch as she has always opposed any attempt to apply it to the Norwegian coast.”<sup>32</sup>

For a doctrine of odious debt to be accepted as a customary rule of international law, it must be demonstrated that there is extensive and virtually uniform state practice, as well as *opinio juris* supporting such a rule.<sup>33</sup>

## 2. *The Literature*

The doctrine of odious debt has been defined as follows: “odious debts are those contracted against the interests of the population of a state, without its consent and with the full

<sup>29</sup> Military and Paramilitary Activities (Nicar. v U.S.), 1986 I.C.J. 14, 98 (June 27).

<sup>30</sup> *Id.* at 108-09.

<sup>31</sup> S.S. “Lotus” (Fr. v. Turk.), 1927 P.C.I.J. (ser. A) No. 10 (Sept. 7, 1927).

<sup>32</sup> Anglo-Norwegian Fisheries (U.K. v. Nor.), 1951 I.C.J. 116, 131 (Dec. 18).

<sup>33</sup> See Ashfaq Khalfan, Jeff King & Bryan Thomas, *CISDL Working Paper: Advancing the Odious Debt Doctrine 1* (Centre for Int’l Sustainable Dev. L., Mar. 11, 2003), available at [http://www.odiousdebts.org/odiousdebts/publications/Advancing\\_the\\_Odious\\_Debt\\_Doctrine.pdf](http://www.odiousdebts.org/odiousdebts/publications/Advancing_the_Odious_Debt_Doctrine.pdf) [hereinafter CISDL].

awareness of the creditor.”<sup>34</sup>

The three limbs of the test are explained further as:

- (i) *Absence of consent*—the population must not have consented to the transaction in question;<sup>35</sup>
- (ii) *Absence of benefit*—there must be an absence of benefit to the population in two ways:<sup>36</sup>
  - a. the debt is contracted against the interests of the state; and
  - b. the proceeds are spent against the interests of the state; and
- (iii) *Creditor Awareness*—a subjective test of the knowledge of the absence of consent and the absence of benefit.<sup>37</sup>

The Legal Approach allows for the odious debt theory to be invoked only when the legal personality of a state changes, for instance as a result of decolonization, annexation, or dissolution.<sup>38</sup> Merely a change of government is insufficient.<sup>39</sup>

Under this approach, once a debt is classified as odious a right accrues to the debtor state to repudiate the debt unilaterally.<sup>40</sup> In practice, most likely, the creditor has no option other than to use available dispute resolution mechanisms to protect its rights.<sup>41</sup> The question of whether such a creditor would have a right of set off against the debtor is not addressed.

#### IV. The Three Types of Odious Debts

Three types of odious debt are identified, and some state practice has been identified:

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<sup>34</sup> *Id.*

<sup>35</sup> *Id.*

<sup>36</sup> *Id.*

<sup>37</sup> *Id.*

<sup>38</sup> *See id.*, *supra* note 33, at 2.

<sup>39</sup> *See* CISDL, *supra* note 33, at 31, 47; *see also* Abrahams, *supra* note 22, at 53.

<sup>40</sup> *See* CISDL, *supra* note 33, at 47; *see also* Abrahams, *supra* note 22, at 87.

<sup>41</sup> *See* CISDL, *supra* note 33, at 6-9.

### A. *The First Type of Odious Debt*

The first type of odious debt that will be considered is hostile debt: debts that are aggressively against the interests of a population, such as debts raised to fund conquest, colonization, war, or suppressing secessionist attempts.<sup>42</sup> Three main examples of hostile debts are cited as evidence of state practice: the Cuban debts of 1898,<sup>43</sup> Article 254 Treaty of Versailles regarding the colonization of Poland,<sup>44</sup> and the Treaty of Peace with Italy 10 February 1947.<sup>45</sup>

#### 1. *The Cuban Debts of 1898*

Cuba was a Spanish colony until the Spanish-American War in 1898.<sup>46</sup> The Spanish government raised a six percent loan of 620,000,000 pesetas in May 1886 to be serviced and repaid from the annual budget of Cuba.<sup>47</sup> New bonds were issued in 1890 to cover debts raised between 1886 and 1890 and were sold on the international market.<sup>48</sup> These debts were owed by Spain and contracted under Spanish law but were secured on, and paid out of, the revenues of Cuba.<sup>49</sup>

The American Commissioners at the peace conference that lead to the Treaty of Paris 1898 argued that the debts were not chargeable to Cuba because the debts were created by the Spanish government for its own purpose, through its own agents and without consultation with Cuba.<sup>50</sup> Creditors knew that the revenues were pledged to opposing Cuban independence so they took the risk inherent with security of that nature.<sup>51</sup> Spain argued that the obligations passed to the successor along with

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<sup>42</sup> *Id.* at 17.

<sup>43</sup> *Id.* at 25; *see also* Abrahams, *supra* note 22, at 35.

<sup>44</sup> *See* CISDL, *supra* note 33, at 27; *see also* Abrahams, *supra* note 22, at 34.

<sup>45</sup> *See* Abrahams, *supra* note 22, at 34.

<sup>46</sup> *See* Europa World Plus, Cuba: History, <http://www.europaworld.com> (last visited May 1, 2007) (requires subscription) [hereinafter Cuba History].

<sup>47</sup> *See id.*

<sup>48</sup> *See id.*

<sup>49</sup> *See id.*

<sup>50</sup> *See id.*

<sup>51</sup> *See id.*

sovereignty.<sup>52</sup>

As a result of the Treaty, Cuban sovereignty passed to the United States, but the United States did not assume obligations for this debt under the Treaty of Paris and the creditors were not fully repaid.<sup>53</sup> It is instructive to apply the definition of odious debt to this example. If it is accepted that colonial peoples are disenfranchised and cannot be deemed to consent to any exercise of sovereignty by the colonial power, the first limb of the definition is satisfied. It was agreed between the Spanish and American Commissioners that, before 1860, part of Cuban revenue had been sent to Madrid and used for national expenses.<sup>54</sup> The Spanish did not deny that an increase in Cuban debt between 1861 and 1880 was to fund attempts to secure San Domingo, to pay for expeditions in Mexico, and to suppress Cuban uprisings between 1868 and 1878.<sup>55</sup> The second limb of the odious debt definition clearly states that the debt must be contracted and spent against the interests of the state. Therefore, it would be insufficient if the debt were not contracted and spent in the interests of the state; rather, the debt must be actively against the interests of the state.<sup>56</sup> It is questionable whether the first two of the three purposes were actively against the interests of Cuba, either when contracted or spent, so whether there is an absence of benefit is unclear.<sup>57</sup> There are also doubts over whether the bondholders who bought the consolidation issue in 1890 could be said to know that the funds they provided were put to use refinancing the debt raised to counter insurgency in Cuba.<sup>58</sup> In 1890, Cuba was still part of the Spanish Empire, therefore, particularly in view of contemporaneous European colonial empires, it would not be extraordinary for Spain to use revenue from its colonies to secure debt.<sup>59</sup> Thus, it is unclear whether the third limb of the definition—creditor awareness—is satisfied by

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<sup>52</sup> See Cuba History, *supra* note 46.

<sup>53</sup> See *id.*

<sup>54</sup> See *id.*

<sup>55</sup> See Abrahams, *supra* note 22, at 39.

<sup>56</sup> See Cuba History, *supra* note 46.

<sup>57</sup> See *id.*

<sup>58</sup> See *id.*

<sup>59</sup> See *id.*

the Cuban debt, as part payment of creditors may represent a political rather than legal settlement.

## 2. *Article 254 Treaty of Versailles*

In 1866, significant funding was given to the Prussian government to purchase Polish estates, followed by additional funding in 1898 and 1902.<sup>60</sup> In 1908, the Prussian government legislated to allow the expropriation, with compensation, of Polish-owned estates; an extra 25,000,000 marks were paid into the fund and an issue of bonds was authorized.<sup>61</sup>

Following the First World War, under the Treaty of Versailles, Poland, as a successor state to Germany, assumed only the German public debts contracted before 1 August 1914.<sup>62</sup> Debts which, in the opinion of the Reparation Commission, were attributable to measures taken by the Prussian or German governments to colonize Poland were not assumed by Poland.<sup>63</sup>

Again, to apply the odious debt test is instructive. It is arguable that the first limb—lack of consent—would be satisfied because the debts were incurred during a colonization process. With regard to the second limb, the absence of benefit, it is unclear that the purpose of the fund was against the interests of Poland as distinct from the interests of individual Poles whose property was expropriated. To accept that it was against the interests of Poland for estates to be owned by ethnic Germans is to take a position that is racially discriminatory, which is impossible to justify as a basis for a rule of law. It is not possible to say whether there was creditor awareness of the purpose of the funds for either the initial or subsequent payments into the fund.

## 3. *Treaty of Peace with Italy 1947*

The Franco-Italian Conciliation Commission, under the Treaty of Peace with Italy that followed the Second World War, ruled that Ethiopia would not have to assume the expenses incurred by Italy

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<sup>60</sup> See CISDL, *supra* note 33, at 27.

<sup>61</sup> *Id.*

<sup>62</sup> See art. 254 of Treaty of Versailles, June 28, 1919.

<sup>63</sup> *Id.* at art. 255.

in subjugating Ethiopia.<sup>64</sup>

The first limb, absence of consent, would be satisfied because funds were used to colonize Ethiopia.<sup>65</sup> As it is accepted that colonization does not benefit the colonized peoples, the second limb, absence of benefit, may also be satisfied. However, the major question of whether the definition applies is whether the creditors knew of the purpose for the funds. If it is not possible to identify precisely the funds that were used to subjugate Ethiopia, it would not be possible to classify the rights of one group of creditors as 'odious' while leaving the rights of other creditors unaffected. It is very unclear whether the third limb, creditor awareness, would be satisfied because of the lack of a clear purpose for the funds subsequently applied to subjugate Ethiopia at the time the debt was issued.

### *B. The Second Type of Odious Debt*

The second type of odious debt is war debt: those debts which are contracted by the losing state during war, or where war is imminent.<sup>66</sup>

The main example of state practice cited as evidence for war debts being odious is the British refusal to take on war debts of the Boer Republics after annexation in 1900.<sup>67</sup>

Following the Boer War, 1899-1902, the Boer Republics became British colonies.<sup>68</sup> Initially, the Supreme Court of the Transvaal took the straight state succession approach and held that the Boer debts raised to fund the war devolved upon Britain as the new sovereign.<sup>69</sup> However, Britain refused to accept legal responsibility for public debts incurred in relation to the war as they were different than other debts.<sup>70</sup> Yet, the British government did ultimately pay ten percent *ex gratia* of the value of the bonds.<sup>71</sup>

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<sup>64</sup> See Rudin, *supra* note 6, at 4.

<sup>65</sup> *Id.*

<sup>66</sup> See CISDL, *supra* note 33, at 26; see also Abrahams, *supra* note 22, at 29.

<sup>67</sup> See CISDL, *supra* note 33, at 26.

<sup>68</sup> *Id.*

<sup>69</sup> *Id.*

<sup>70</sup> *Id.*

<sup>71</sup> *Id.*

The transfer of debts in the context of the Boer War was further considered by the English courts.<sup>72</sup> The South African Republic had seized gold belonging to the claimant in a manner alleged to be unlawful under the South African laws in force at the time.<sup>73</sup> The claimant sought to recover the gold or compensation from Britain.<sup>74</sup> The court held that Britain had no liability because a “conquering Sovereign, when making peace, can make any conditions he thinks fit respecting the financial obligations of the conquered country, and it is entirely at his option to what extent he will adopt them.”<sup>75</sup>

Any attempt to apply the definition must fall at the paradox created by its first and second limbs, absence of consent and absence of benefit. If the debts contracted by a colonial power on behalf of a colony, such as the Cuban debts above, are deemed to lack necessary consent from, and be hostile towards, the population, then it cannot follow that debts contracted by a state prior to colonization are also deemed to lack consent and are hostile to the population. It is possible that the third limb, creditor awareness, was satisfied because of the situation at the time the debt was raised.

The British position is based upon the rights of a conquering sovereign.<sup>76</sup> There is no attempt to apply the definition of odious debt and the position taken is much broader as it is not limited to debts that satisfy all limbs of the definition.<sup>77</sup> Accordingly, these debts cannot be classified as odious within the definition suggested by the Legal Approach.

### *C. The Third Type of Odious Debt*

The third type of odious debt is developing world debt not in the interests of the population: modern “dictators’ debts” including proceeds spent on personal items, used to fight unjust

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<sup>72</sup> *West Rand Central Mining Co., Ltd. v. The King*, (1905) 2 L.J.K.B. 391 (Eng.).

<sup>73</sup> *Id.* at 391-93.

<sup>74</sup> *Id.* at 393.

<sup>75</sup> *Id.* at 402.

<sup>76</sup> *Id.*

<sup>77</sup> *See id.* The court says that conditions can be made by a conquering Sovereign concerning the general financial obligations, without limiting those financial obligations to any sort of definition. *See id.*

wars or distributed in a discriminatory fashion.<sup>78</sup> The writers who take the Legal Approach do not cite any examples of state practice to support this category because of the limitation that a doctrine of odious debt can only be invoked on state succession rather than regime change.<sup>79</sup> However, dictators' debts have been considered by arbitration tribunals in *Costa Rica v. Great Britain* and *World Duty Free Limited v. Republic of Kenya*.<sup>80</sup>

### 1. *Costa Rica v Great Britain (1923)*

The arbitration in *Costa Rica v. Great Britain* concerned banking transactions by the government of President Tinoco.<sup>81</sup> Bills drawn by the Finance Minister on Banco Internacional de Costa Rica were paid in to the credit of the government with the Royal Bank of Canada.<sup>82</sup> Based on these bills the Royal Bank paid several checks drawn by the Tinoco government.<sup>83</sup> After the fall of the Tinoco government, Costa Rica refused to honor the debt.<sup>84</sup> This set of facts looks like corruption: Tinoco wanted the funds for himself and the Royal Bank of Canada knew or should have known of this intent.

Chief Justice Taft found in favor of Costa Rica. He held that the position of the Royal Bank depended upon its good faith in the payment of money for the real use of the Costa Rican government under the Tinoco regime.<sup>85</sup> The Royal Bank had to show that it provided the money to the government for its legitimate use.<sup>86</sup> The claim failed because the Royal Bank knew the money was to be used by Tinoco for his personal support after he had taken refuge in another country, so the money was not for legitimate government use.<sup>87</sup>

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<sup>78</sup> See CISDL, *supra* note 33, at 19.

<sup>79</sup> See generally *id.* at 47 (noting the difference between state succession and governmental succession in the context of discussions concerning odious debt).

<sup>80</sup> See *id.* at 28, 41; see also Abrahams, *supra* note 22, at 46.

<sup>81</sup> Tinoco Case (Gr. Brit. v. Costa Rica), 2 ANN. DIG. 34 (1923).

<sup>82</sup> *Id.* at 34-35.

<sup>83</sup> *Id.* at 35.

<sup>84</sup> *Id.*

<sup>85</sup> *Id.* at 36-39.

<sup>86</sup> *Id.* at 39.

<sup>87</sup> Tinoco Case, *supra* note 81, at 39.

Applying the legal definition, the first limb—absence of consent—may be satisfied because public money was applied for private purposes by those in power. The second limb—absence of benefit—would be satisfied because the funds were not put to a legitimate use. The tribunal held that the third limb, creditor awareness, was satisfied because the Royal Bank of Canada knew that the money was to be used by Tinoco for his personal support.<sup>88</sup> However, the trigger event of state succession for invoking the legal definition did not occur.<sup>89</sup> Therefore, this decision cannot be considered to support the Legal Approach definition of odious debt as currently formulated. In this context, it is worth noting that there is separate jurisprudence concerning corruption.<sup>90</sup>

## 2. *World Duty Free Limited v. Republic of Kenya (2006)*

As the most recent award concerning dictators' debts it is worth discussing *World Duty Free* in detail.<sup>91</sup> In 1989, Kenya concluded a contract with House of Perfume for the construction, maintenance and operation of duty-free complexes at Nairobi and Mombassa Airports.<sup>92</sup> This agreement was amended in 1990 to substitute World Duty Free (WDF) for House of Perfume.<sup>93</sup>

WDF claimed that Kenya breached the Agreement by illegally expropriating its properties and destroying its rights under the Agreement.<sup>94</sup> WDF sought restitution under a contractual complaint exclusively arising from the House of Perfume contract, or in the alternative, compensation.<sup>95</sup> Kenya submitted that the Agreement was procured by paying a bribe of \$2 million to the then President of Kenya, Daniel arap Moi. Payment of such a

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<sup>88</sup> *Id.*

<sup>89</sup> There was no state succession because the Tinoco government was not a recognized government and was in fact actively non-recognized. *Id.* at 37-38.

<sup>90</sup> See *infra* Part IV.C.2 (discussing *World Duty Free Limited v. Republic of Kenya*, a case deciding that a contract based on corruption is unenforceable).

<sup>91</sup> *World Duty Free Ltd. v. Rep. of Kenya*, ICSID (W. Bank) Case No. ARB/00/7 (Oct. 4, 2006), <http://ita.law.uvic.ca/documents/WDFv.KenyaAward.pdf>.

<sup>92</sup> *Id.*

<sup>93</sup> *Id.*

<sup>94</sup> *Id.*

<sup>95</sup> *Id.*

bribe was criminal so the resulting contract does not have the force of law.<sup>96</sup> It is unenforceable and the claims cannot be heard as a matter of public policy. In addition, as a matter of applicable law, the contract was voidable and was validly avoided by Kenya.<sup>97</sup>

The International Centre for Settlement of Investment Disputes (ICSID) Tribunal discussed the existence of a bribe.<sup>98</sup> The CEO and shareholder of WDF met the President to discuss establishing the duty-free complexes.<sup>99</sup> He had been told by his contact that he would be required to make a personal donation of \$2,000,000 to the President.<sup>100</sup> He took a briefcase containing \$500,000 in cash to the first meeting.<sup>101</sup> The briefcase was placed against a wall and when he opened the briefcase in the car after the meeting he found it now contained maize.<sup>102</sup> His contact told him that was a sign the President liked the proposal.<sup>103</sup>

Kenya submitted that the payment was a bribe.<sup>104</sup> WDF submitted that it was a gift of protocol or a personal donation made to the President to be used for public purposes within the framework of the Kenyan system of Harambee.<sup>105</sup>

The Tribunal held that the payments made on behalf of House of Perfume could not be considered as a personal donation for public purposes.<sup>106</sup> They were made to obtain an audience with the President and, above all, to obtain during that audience the agreement of the President on the contemplated investment.<sup>107</sup> The Tribunal held that it was a bribe.<sup>108</sup>

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<sup>96</sup> *Id.*

<sup>97</sup> *World Duty Free*, ICSID (W. Bank) Case No. ARB/00/7 (Oct. 4, 2006), <http://ita.law.uvic.ca/documents/WDFv.KenyaAward.pdf>.

<sup>98</sup> *Id.*

<sup>99</sup> *Id.*

<sup>100</sup> *Id.*

<sup>101</sup> *Id.*

<sup>102</sup> *Id.*

<sup>103</sup> *World Duty Free*, ¶ 131, ICSID (W. Bank) Case No. ARB/00/7 (Oct. 4, 2006), <http://ita.law.uvic.ca/documents/WDFv.KenyaAward.pdf>.

<sup>104</sup> *Id.* ¶ 133.

<sup>105</sup> *Id.*

<sup>106</sup> *Id.* ¶ 136.

<sup>107</sup> *Id.* ¶ 135.

<sup>108</sup> *Id.* ¶ 136.

The Tribunal discussed treatment of corruption in previous arbitral awards, in treaties and by the General Assembly of the United Nations.<sup>109</sup> It concluded that even where corruption was common practice and the award of a contract without it was difficult or impossible, tribunals had always refused to condone the practice, and this Tribunal endorsed the same approach.<sup>110</sup> The Tribunal stated that bribery is contrary to international public policy so claims based on contracts of corruption or on contracts obtained by corruption cannot be upheld by the Tribunal.<sup>111</sup> The Tribunal then considered English and Kenyan law and public policy and found that neither system permitted corruption.<sup>112</sup>

WDF argued that the bribe was a collateral contract or was at least severable from the Agreement.<sup>113</sup> The Tribunal rejected that it was a collateral contract on the facts and in principle because the bribe formed an intrinsic part of the transaction; without the bribe there would have been no contract. It was irrelevant that the bribe was not wholly initiated by WDF.<sup>114</sup>

The President acted corruptly, to the detriment of Kenya and in violation of Kenyan law.<sup>115</sup> There was no mechanism in English or Kenyan law for attributing knowledge to the state (as the otherwise innocent principal) of a state officer engaged as its agent in bribery.<sup>116</sup>

If the tests are applied, the first limb, absence of consent, is satisfied, as the bribe was held to be in violation of Kenyan law. The second limb, absence of benefit, may not be satisfied as, in the absence of the bribe, it would be difficult to argue that a contract to build substantial facilities at two major airports would be against the interests of Kenya, and with the associated job creation for the Kenyan people. The third limb, creditor awareness, would

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<sup>109</sup> *World Duty Free*, ¶¶ 138-155, ICSID (W. Bank) Case No. ARB/00/7 (Oct. 4, 2006), <http://ita.law.uvic.ca/documents/WDFv.KenyaAward.pdf>.

<sup>110</sup> *Id.* ¶ 156.

<sup>111</sup> *Id.* ¶ 157.

<sup>112</sup> *Id.* ¶ 179.

<sup>113</sup> *Id.* ¶ 111.

<sup>114</sup> *Id.* ¶ 174-75.

<sup>115</sup> *World Duty Free Ltd. v. Republic of Kenya*, ¶ 185, ICSID (W. Bank) Case No. ARB/00/7 (Oct. 4, 2006), <http://ita.law.uvic.ca/documents/WDFv.KenyaAward.pdf>.

<sup>116</sup> *Id.* ¶ 185.

be satisfied as the CEO of WDF knew that he was expected to make a personal donation.

As *World Duty Free* does not satisfy all three limbs of the test, it does not meet the odious debt criteria. The Tribunal held that it was the bribe that rendered the contract voidable, not that the contractual debt was odious.<sup>117</sup> As with *Tinoco*, *World Duty Free* does not support the Legal Approach definition of odious debt because there was no state succession.

## V. Is a Doctrine of Odious Debt a Customary Rule of International Law?

The proponents of the Legal Approach argue that there is (a) sufficient state practice and (b) *opinio juris* to establish odious debt as a customary rule of international law.<sup>118</sup> These arguments must be able to discharge the burdens described by the ICJ necessary to become a customary rule of international law. This returns us to the discussion of Article 38(1) of the Statute of the ICJ.

### A. State Practice

The ICJ has established that the threshold for state practice is that there is a uniform and extensive practice regarding odious debt amongst the states concerned, with exceptions treated as breaches of the rule.<sup>119</sup> Any abstention from seeking to recover a debt must be from a belief that recovery would be unlawful, unless the abstention is by one state that has consistently refused to apply the rule.<sup>120</sup>

The examples cited in support of the Political Approach are the same as those cited for the Legal Approach so the same criticisms of sparse and antique evidence must be addressed again.<sup>121</sup> The first example cited is Cuba 1898 and the most recent before *World Duty Free* is the Franco-Italian Conciliation Commission decision of 1947. These examples cover some fifty years. However, there

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<sup>117</sup> *Id.* ¶ 183.

<sup>118</sup> *See, e.g.*, Abrahams, *supra* note 22, at 50.

<sup>119</sup> MALCOLM N. SHAW, *INTERNATIONAL LAW* 70 (5th ed., 2003)

<sup>120</sup> *Id.* at 71.

<sup>121</sup> *See* discussion *supra* part III.

is virtually no state practice cited for the sixty years since World War II.

The lack of examples since 1945 is surprising given that the decolonization and the dissolutions of the Soviet Union, Yugoslavia, and Czechoslovakia have all occurred during this time. There were numerous opportunities for a doctrine to be applied, with most examples falling within the hostile debts category, but a lack of practice. Set against this silence is the restructuring activity of the Paris Club and the London Club.<sup>122</sup>

The number of post-decolonization dictators also presented opportunities for successor governments to develop and invoke a doctrine of odious debts. Indonesia and Nigeria are examples of states that might have tried to invoke a doctrine but did not.<sup>123</sup> Again this reluctance can be contrasted against restructuring activity involving both states, with Nigeria involved in five Paris Club treatments since 1986<sup>124</sup> and Indonesia in eight since 1966.<sup>125</sup>

Creditor states have also consistently sought to recover debts. There have been 405 Paris Club restructuring deals since 1956 involving 83 debtor states.<sup>126</sup> None of the examples cited can be placed without doubt into the Legal Approach definition of odious debt. The most convincing example on its facts, *Tinoco*, is excluded because there was no state succession and the Cuban and

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<sup>122</sup> The Paris Club and London Club are known for many sovereign debt restructurings. Most recently, in 2004, the Paris Club decided to write-off the debts of Iraq. Press Release, Club de Paris, The Paris Club and the Republic of Iraq Agree on Debt Relief (Nov. 21, 2004), [www.clubdeparis.org](http://www.clubdeparis.org) (click on "Press Releases" hyperlink, then scroll down to find "Iraq" hyperlink).

<sup>123</sup> Much of Nigeria's debt can be considered odious given the fact that the original loans were made to authoritarian regimes, many of which were then looted. Rather than pursue an odious debt resolution, the countries decided to work through the restructuring activity of the Paris and London club. See Lles Leba, *Compassionate Debt Relief or Paris Club 419*, VANGUARD (Lagos), Dec. 12, 2005, available at <http://www.odiousdebts.org/odiousdebts/index.cfm?DSP=content&ContentID=14357>. See generally Description of the Paris Club, <http://www.clubdeparis.org/sections/qui-sommes-nous> (describing the restructuring activities of the club in general).

<sup>124</sup> Paris Club, Nigeria: List of the Debt Treatments, <http://www.clubdeparis.org/sections/pays/nigeria> (last visited May 1, 2007).

<sup>125</sup> Paris Club, Indonesia: List of the Debt Treatments, <http://www.clubdeparis.org/sections/pays/indonesie> (last visited May 1, 2007).

<sup>126</sup> Paris Club, Key Figures, <http://www.clubdeparis.org/sections/services/chiffres-cles>.

Boer debt examples create such a paradox that they appear to be mutually exclusive. There are fundamental questions against at least one limb of the definition for the other examples cited so that it appears that there is no state practice to support the definition as formulated.<sup>127</sup>

It can be concluded confidently that the threshold of state practice has not been met. The absence of states asserting a doctrine of odious debts, the lack of state practice that can be shown to support the Legal Approach definition, combined with the evidence of creditor states seeking to assert claims, shows that the overwhelming state practice is that sovereign debt is recoverable. The examples cited are therefore best viewed as isolated exceptions arising from peculiar circumstances which have not been followed as precedents.

### *B. Opinio Juris*

Supporters of the Legal Approach must also show that states have acted consistently with a doctrine of odious debt because this practice is rendered obligatory by the existence of a rule of law requiring it.<sup>128</sup> The same criticisms of the examples cited as state practice can be levelled at those cited as *opinio juris*; they are isolated examples of mainly historic interest.<sup>129</sup> Even staunch supporters, such as Abrahams, accept that "it has to be admitted that proof of *opinio juris* is difficult to produce."<sup>130</sup>

Others cite such evidence as Article 38 of the Vienna Convention on Succession of States in Respect of State Property 1983,<sup>131</sup> which provides that no debt passes to successor states unless there is a positive agreement to that effect.<sup>132</sup> However, the Convention has not entered into force and an express reference to

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<sup>127</sup> See CISDL, *supra* note 33, at 1-2 (the three limbs of the test are absence of consent, absence of benefit, and creditor awareness.)

<sup>128</sup> See IAN BROWNLIE, PRINCIPLES OF PUBLIC INTERNATIONAL LAW 5-11 (1998).

<sup>129</sup> Of all the restructuring deals discussed *supra* note 137 that could possibly be used to argue the strength of an *opinio juris* approach to odious debt, each is an isolated incident giving no clear cut support for this perspective.

<sup>130</sup> See Abrahams, *supra* note 22, at 50.

<sup>131</sup> See Vienna Convention, *supra* note 18, at 306.

<sup>132</sup> *Id.*

odious debt was removed from the first draft.<sup>133</sup> Reference is also made to international materials on corruption.<sup>134</sup> However, the ICSID Tribunal in *World Duty Free* did not even discuss a doctrine of odious debt nor is it mentioned in the reported submissions, despite an extensive discussion of international policy on bribery.<sup>135</sup>

The Tribunal left open the possibility for a non-contractual, proprietary, or restitutionary claim, as WDF had not pleaded those claims.<sup>136</sup> The existence of any of these claims would not be consistent with the suggested doctrine of odious debt, as it would allow the creditor some protection rather than the right of the debtor unilaterally to walk away from the debt.

The Legal Approach definition of odious debt is not accepted as a rule of international law; as has been demonstrated, it does not even come close to satisfying the requirements in this respect. As discussed above, the consistent practice through the last sixty years has been for sovereign debts to be repaid.<sup>137</sup> Even in *World Duty Free* the Tribunal suggested that a financial remedy would be available to the claimant, despite the bribe, had it made the correct pleadings.<sup>138</sup> The uniformity of practice, especially when considered in the context of the erosion of absolute state immunity to allow sovereigns to be pursued through the courts, is persuasive evidence of an *opinio juris* that sovereign debt obligations should be respected and protected.

This approach is also consistent with the established rule of international law that foreign property cannot be appropriated by a state without appropriate compensation.<sup>139</sup> Since a debt is a choice in action it is a form of property, so the rights of the creditor are protected by international law.<sup>140</sup> The award in *World Duty Free*

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<sup>133</sup> See CISDL, *supra* note 33, at 33.

<sup>134</sup> *Id.* at 34.

<sup>135</sup> *World Duty Free*, ¶ 107, ICSID (W. Bank) Case No. ARB/00/7 (Oct. 4, 2006), <http://ita.law.uvic.ca/documents/WDFv.KenyaAward.pdf>.

<sup>136</sup> *Id.* ¶ 179.

<sup>137</sup> See discussion, *supra* Part V.A.

<sup>138</sup> *World Duty Free*, ¶ 179, ICSID (W. Bank) Case No. ARB/00/7 (Oct. 4, 2006), <http://ita.law.uvic.ca/documents/WDFv.KenyaAward.pdf>.

<sup>139</sup> SHAW, *supra* note 119, at 905.

<sup>140</sup> *Id.* (indicating that private rights obtained by foreign nationals continue after

tests a limit of that right when the right was acquired through bribery. The right was held to be severely curtailed but the Tribunal left open only the possibility of a non-contractual, proprietary or restitutionary claim, and so rights of the creditor were not totally extinguished.<sup>141</sup> The protection of property rights from sovereigns is further evidence of *opinio juris* requiring sovereigns to honor obligations.

The Centre for International Sustainable Development argues that the relationship between government and state is that of agent and principal, so the actions of the corrupt agent should not be attributable to the innocent principal.<sup>142</sup> The ICSID Tribunal in *World Duty Free* used an agency analogy to avoid imputing knowledge of the bribe to Kenya.<sup>143</sup> The agency analogy may have a practical application to situations such as that in *World Duty Free* where a contract was won through bribery.<sup>144</sup>

The final observation is that most jurisdictions in developed countries have made corruption and bribery unlawful. Where corruption is involved in a contractual arrangement, the purported "rights" of the parties are adversely affected whether there is a debt claim or not. This is established law in many jurisdictions, but it has nothing to do with odious debts in legal terms. Most cases are between private parties and have been applied in a sovereign context.

## VI. Conclusion

A review of the literature on odious debt reveals two approaches: the Political Approach and the more sophisticated Legal Approach. The Political Approach is not a theory that can be subjected to serious legal analysis because it is not based on legal principles. The Legal Approach is the product of a more sophisticated legal analysis to attempt to prove that a customary rule of international law exists in respect to odious debt. After considering Article 38 of the Statute of the ICJ and the jurisprudence of the Court on the formation of customary rules of

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state succession and can be enforced against the new sovereign).

<sup>141</sup> *World Duty Free*, *supra* note 91, at 179.

<sup>142</sup> See CISDL, *supra* note 33, at 36.

<sup>143</sup> *World Duty Free*, *supra* note 91, paras. 184-85.

<sup>144</sup> *Id.*, para. 174.

international law, it must be concluded that neither the threshold for state practice nor *opinio juris* have been met. Consequently, it has been demonstrated that the Legal Approach definition of odious debt is not accepted as a rule of international law.

A separate, established body of law exists in many jurisdictions in relation to corruption and bribery. Where corruption is involved in a contractual arrangement, the purported “rights” of the parties are adversely affected. This body of law has nothing to do with odious debts, but has been applied in a sovereign context, notably by the ICSID Tribunal in *World Duty Free*.

The question of whether there is a recognized legal doctrine of odious debt, therefore, must be answered in the negative. If there is no rule of odious debt in international law, there can be no scope for legitimate repudiation of sovereign debt as odious.

