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Legal Aspects of the Latin American External Debt and its Ramifications for the Development and Integration of the Americas

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I. INTRODUCTION

Latin America is currently in the throes of an external debt crisis. The effects of this crisis reach far beyond the immediate lenders and debtors involved. From the unemployed in industries that can no longer sell their goods, to the Latin American children who go hungry due to increased food costs, there are many people throughout the world being hurt by the current situation. If the parties fail to work out solutions to this crisis, the result may be disastrous for the global economy, the world banking system, international relations and the development of Latin America.

This comment will examine: 1) some historic aspects of lending to Latin American nations; 2) the reasons for the current external debt crisis; 3) current stop-gap solutions to the problem; 4) the legal aspects of loan defaults; and 5) the legal, economic and political ramifications of the debt crisis for the development and integration of the Americas. Its primary focus will be on Latin American loans classified by the Inter-American Development Bank (IDB) as external public debt.[1]

The legal issues cannot be understood apart from their historical and economic contexts. A grasp of this background information is also essential for testing whether enforcement of existing loan contracts in the present legal framework is viable.

II. Reasons for the External Debt Crisis

A. *Illiquidity*

Bank loans to the major borrowing countries in Latin America increased at a rapid rate which accelerated further in the mid-1970's. The expansion in lending to Latin America is evidenced by the following figures (in millions of dollars):

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1. The IDB defines external public debt as follows:

The external public debt includes all external debt with an original or extended maturity of one year or more, repayable in foreign currency and contracted directly by public bodies or by private entities with a guarantee of payment by any of the following public institutions:

1. Central government or its departments;
2. Political subdivisions such as states, provinces, departments or municipalities;
3. Central bank;
4. Autonomous institutions (such as corporations, development banks, railways, utilities, etc.) where

(a) the budget of the institution is subject to the approval of the government of the reporting country; or where

(b) the government owns more than fifty percent of the voting stock or more than half of the members of the Board of Directors are government representatives; or where

(c) in the case of default the state would become liable for the debt of the institution.

Consequently, the following are not registered as public debt: obligations with a maturity of less than one year, loans contracted with option of repayment in local currency, private sector debt without the guarantee of the public sector, "purchase" and "repurchase" operations with the International Monetary Fund, and "swap" transactions between central banks. Inter-American Development Bank, Economic and Social Progress in Latin America 380 (1983) [hereinafter cited as IDB (1983)].

1960	1970	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981
7,205	20,792	29,868	37,123	49,094	59,094	77,432	96,852	121,847	145,171	160,071	181,156[2]

These loans provided money for purchases of goods and construction of new projects, as well as for the liquidity needed to service the accumulating debts. In mid-1982, the ability of Latin American nations to borrow freely in the Eurodollar market was sharply curtailed in response to Mexico's near default. For example, during the first half of 1982, Brazil's borrowing averaged $1.5 billion a month. This amount was cut in half after the Mexican default, and by the fourth quarter of 1982, the prior availability of automatic borrowing had disappeared. By October 1982, Brazil had lost about $4 billion in interbank deposits and approximately $2 billion in trade-related lines of credit.[3]

The contraction of credit has caused severe liquidity problems. It is one reason Latin American borrowers have confronted problems in servicing their loans.[4]

B. *World Recession*

Past borrowing appeared to be supportable in light of the conditions that existed when the loans were made.[5] The borrowing countries were experiencing a steady growth in GNP. The volume of exports was increasing and brought in growing amounts of hard currency to service the loans. Unfortunately, world economic conditions changed abruptly from expansion to recession.[6] This resulted in a decline in the volume of exports.

In 1982, a steep drop in commodity prices caused export unit values for goods from Latin America to drop by ten percent.[7] The drop in prices, coupled with the decline in volume, significantly reduced total export receipts. For example, Argentina's 1980 exports of $7.82 billion fell to $3.4 billion in 1982 (56% decline); Brazil's 1980 exports of $10.60 billion fell to $8.06 billion in 1982 (24% decline); Chile's 1981 exports of $3.54 billion fell to $2.01 billion in 1982 (43% decline); Mexico's 1981 exports of $24.91 billion fell to

2. IDB, *supra* note 1, at 381.

3. Langoni, *The Way Out of the Country Debt Crisis*, Oct. 1983 EUROMONEY 20.

4. Bance, *Brazil's O.K. - But The Others?*, Nov. 1983 EUROMONEY 23.

5. Sandberg, *Stop Breast-Beating on LDC Debt*, Oct. 1983 EUROMONEY 34.

6. *See* IMF Survey, Sept. 5, 1983 at 261, col. 3.

7. IDB, *Supra* note 1, at 134. For example, sugar, which is exported by most Latin American nations, suffered the most drastic drop in prices. From 1980 to 1982, the price per metric ton dropped from $632 to $130. *Id.*

$16.56 billion in 1982 (44% decline); Peru's 1981 exports of $3.18 billion fell to $2.46 billion in 1982 (33% decline).[8] Thus, by 1982, most Latin American nations had a severe shortage of hard currency from exports and had difficulty servicing their mounting debts.

C. *Interest Rates and Spreads*

Most international bank loans have floating interest rates. Euro-currency interest rates are usually based on the London Interbank Offered Rate (LIBOR)[9] for the currency of the loan. Other Latin American loans are tied to the U.S. prime rate. Loan interest rates are periodically adjusted to reflect changes in LIBOR or the U.S. prime rate. The LIBOR and U.S. prime rate which were at 6-7% levels in 1976, rose to over 18% in mid-1981.[10] When most of the loans were negotiated, interest rates were relatively low. In some cases, they were actually negative in real terms when viewed against the expanding economies. Due to the fiscal policies of the United States, interest rates became unusually high, especially in light of the world recession.

The high level of interest rates is the most significant cause of the external debt crisis. Each 1% increase in the LIBOR increases current account deficits by approximately $900 million in Brazil; $300 million in Argentina; $150 million in Chile; $750 million in Mexico; $90 million in Peru; and $350 million in Venezuela.[11]

Borrowers also pay a premium or spread over LIBOR or the U.S. prime rate. This spread is the basis of the bank's profit and is negotiated in light of the relative risks involved. Since 1979, the average spreads charged to developing nations increased from approximately .8% to over 1%, while spreads to developed nations hovered around the .5% range.[12] For the Latin American nations with serious loan problems, the spreads are currently even higher, ranging from 1 ¾% to 2 ⅜%. The higher spreads are also being attached to loans that are being restructured, thus increasing the burden.

8. International Monetary Fund, Directory of Trade Statistics 4 (1983).

9. LIBOR is the interest rate on various currencies in the Euro-dollar Market that London banks offer to other banks.

10. International Monetary Fund, International Capital Markets and Prospects 6, *Occasional Paper* 23 (1983). [hereinafter cited as IMF.]

11. *Capitalism Under Stress*, Oct. 1983 Euromoney 64.

12. IMF *supra* note 9, at 6.

The increase in spreads on new loans and renegoiated loans, coupled with sharply increased interest rates, have caused loan service payments to rise at a faster rate than the total outstanding principal of these loans.[13]

From 1974 to 1981, annual service payments on the external public debt increased in Argentina from $792 million to $2,150 million (272%); in Brazil from $1,219 million to $8,611 million (706%); in Chile from $278 million to $1,662 million (597%); in Mexico from $1,196 million to $8,482 million (709%) and in Venezuela from $506 million to $3,048 million (602%). The total annual service payments by Latin American countries rose from $5,564 million to $29,481 million (530%).[14] Service payments have spiraled upward to the point where it is impossible to meet the payments with the amount of dollars available.[15]

The rapid growth of the servicing costs and the debt signifies that greater percentages of new loans must be used to service existing loans instead of financing imports and development projects.[16]

III. The Current Solution

In mid-1982, Mexico was on the brink of a major default that would have produced significant economic, legal and political repercussions throughout the world. To avert this crisis, and to avoid subsequent defaults by other nations, the International Monetary Fund (IMF) formulated emergency credit programs that enabled debtor nations to cope with the current illiquidity problems. These IMF programs, however, are conditioned on debtor nations agreeing to enact harsh economic austerity measures.

In exchange for IMF assistance and loans, lender banks must commit additional funds according to a quota system, which is based on each bank's exposure in the debtor country. The additional loans are stop-gap measures that will hopefully hold off defaults until the debtors' ability to service their loans improves markedly. Such improvement would result from a fall in interest

13. Bance, *Brazil's O.K.—But the Others?* Nov. 1983 Euromoney 23.

14. *Id.*

15. IBD, *supra* note 1, at 381.

16. *Banks Must Acquire Equity in Debtor Countries*, The Wall Street Journal, Sept. 30, 1983, at 31, col. 3.

rates, an increase in the value of exports, or a decline in the value of imports.

As of late 1983, the IMF program, together with Mexico's self-imposed austerity measures have drastically improved Mexico's economic plight.The first half of 1983 produced a $6.5 billion trade surplus; the government deficit was down 24% from the same period in 1982.[17] However, in human terms, the price was high. Food prices and unemployment shot up dramatically, causing hardships for most Mexicans.[18]

Brazil is experiencing the effects of the IMF measures. The social costs have been tremendous. Food prices skyrocketed, wages were reduced and employment fell as Brazil adopted austerity measures to meet the IMF's conditions for new loans. Throughout the fall of 1983, newspapers and magazines graphically documented strikes, food riots, supermarket looting and protests directly aimed at the IMF.[19] Some Brazilian supermarkets resorted to the use of armed guards to prevent lootings from desperate Brazilians caught in the economic "adjustments."[20]

To control resistance to the austerity programs, emergency measures were enacted in Brazil on October 19, 1983, for 60 days, and later rescinded. These measures included a ban on public discussions of the government's actions, arrests, house searches and the government take-over of unions in Brasilia.[21]

In an era when Brazil is being encouraged to promote democracy, this overreaction to the IMF conditions resulted in the loss of IMF conditions resulted in the loss of recent gains and renewed use of government repression.[22]

The IMF measures can only attempt to remedy a debtor coun-

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17. Robinson, *The IMF vs. The People*, Oct. 1983 EUROMONEY 90, 93. Mexico voluntarily imposed additional corrective measures. *Id.*

18. Dolgar, *Why Mexico Remains Poor*, The Miami Herald, Sept. 25, 1983, at 1E, col. 4.

19. Brooke, *Economic Crisis Strains Brazil's Stability*, The Miami Herald, Oct. 2, 1983, at 30A, col. 1.

20. Brooke, *Brazils' Hunger Stalks Rio Slums as Mobs Fight Police to Loot Food*, The Miami Herald, Sept. 20, 1983, at 18A, col. 1.

21. *Brazilian Emergency Measures*, The Wall Street Journal, Nov. 25, 1983 at 17, col. 2.

22. Prior to this decree, Brazil was viewed on the "road back to democracy from military dictatorship". Ulman, *Brazil's Rough Road Back to Democracy*, The Wall Street Journal, Oct. 21, 1983 at 29, col. 4. But the emergency measures were seen as giving President Figueiredo "near dictatorial powers in the capital district". *Brazilian Decree Draws Protests, Miring Debt Plan*, The Wall Street Journal, Oct. 21, 1983 at 33, col. 4.

try's internal economic problems, while providing stop-gap funds until the anticipated recovery. The major reasons for the current situation are, however, external to the debtor nations and largely outside of their control. Yet, Latin American nations must now suffer the social and political consequences.

IV. The Threat of Defaults

Loan defaults are the greatest threat to jeopardizing the precarious balance that currently exists amongst borrowers and lenders. Default is *de facto* when declared by borrowers, and can range from suspension of principal and/or interest payments to formal repudiation. Default is *de jure* when declared by creditors.[23]

The risk and occurrence of international loan defaults is not a new situation. The most recent series of defaults by Latin American borrowers occurred in the 1930s due to the Great Depression.[24] However, the character of previous credit was different. Bonds with fixed-interest rates were issued with banks merely serving as underwriters and promoters. Therefore, the assets of the individual investors were at risk, rather than the assets of banks. The individual creditors lacked bargaining power, so debtor countries in financial trouble would usually suspend payments. nations would attempt to give partial payment on the bonds when they tried to get back into the bond markets.[25] However, on several occasions, bond defaults resulted in the extreme remedy of military intervention.[26]

After World War II, significant changes occurred in international lending. Today, banks are responsible for most of the loans. Due to the strength and interrelationship of the banking system, as well as the dependency of both developing and industrial nations on international credit, the bank creditors now have greater negotiating strength than did individual bond holders. Due to the apparent reduction in risk, bank spreads are much lower than the risk premiums bond purchasers previously demanded. However, a nation's payments on the bonds was predictable since the interest

23. R. Dale & R. Mattione, *Managing Global Debt* 2 (1983) (a staff paper from The Brookings Institute) [hereinafter cited as Brookings.]

24. *Id.* at 3.

25. *Id.*

26. *Id.*

rates were fixed.[27] Today's system of variable rate financing can throw the best planning into disarray.

Banks also respond differently to financial difficulties. To prevent book losses, banks prefer to reschedule loan repayments in a longer repayment time frame rather than accept a partial payment of the debt. When this method is used during inflationary periods, the banks benefit since the loans are renegotiated at current interest rates.[28]

In spite of the negotiating positions that banks have, write-offs quietly occur on international loans, just as they do on domestic loans. One hundred major U.S. banks reported that from 1975 to 1980 loans to debtors in Latin American countries were charged-off in the following amounts: Venezuela - $17.4 million; Mexico - $57.9 million; Brazil - $31.0 million; Nicaragua - $34.6 million; Argentina - $17.2 million; Honduras $8.1 million; Guatemala - $7.5 million; Costa Rica - $7.2 million; Jamaica - $22 million; and El Salvador - $2.2 million.[29] The majority of these loans were to private parties and were written off the same way domestic loans to private parties are written off.

Charge-offs to Mexico and Nicaragua also included charge-offs to the government-owned banks and agencies.[30] For some of the charged-off loans, banks may not have properly investigated whether the debtors were actually part of the government that the banks believed would ultimately be responsible for the loans. The banks also may have failed to get third-party guarantees from the governments. Where the write-offs were on loans to governments, government agencies or government-owned banks, the amount of the loans in jeopardy was dwarfed by the amount of outstanding government placed loans the banks had in each country. Since external public loans are generally linked by cross-default agreements[31] and guarantees by the central government on foreign loans, a bank exposes all the external public debt of that country

27. *Id.*
28. *Id.*
29. A. Porzencanski, *Profitability of International Banking*, in International Banking, 139 (E. Roussakis ed. 1983) [hereinafter cited as International Banking] citing Robert Morris Associates, *Report on Domestic and International Loan Charge-Offs* (Philadelphia, various years).
30. *Id.*
31. A cross-default clause enables a lender to declare its loans to a country in default if the country has defaulted on just one outstanding loan.

to possible default by declaring a relatively small loan in default.[32] Banking regulators would then require banks to increase loan loss reserves or write-off the loans.[33] The survival of some major banks would have been jeopardized due to the enormous sums of money involved.

Apparently, the banks surveyed prefer to suffer small losses rather than face the possible consequences of a large simultaneous default of other loans. The potential problems with defaults demonstrate that the negotiating position of international banks is more precarious that generally realized.

V. Sovereign Immunity

When the legal posture of the banks in relation to their government debtors is examined, particular attention is focused on the protection government debtors will receive under the doctrine of sovereign immunity. Sovereign immunity is a likely defense whenever a creditor seeks a judgment against a government borrower or guarantor. Under the absolute theory of sovereign immunity, a sovereign cannot be forced, without its consent, to answer in the courts of another nation. In the United States, the Supreme Court first followed this theory in *The Schooner Exchange v. McFaddon.*[34] In 1952, the absolute theory was officially rejected in the "Tate" letter, which stated that the United States Department of State would follow the restrictive theory of sovereign immunity.[35] Under the latter theory, sovereign immunity is recognized only when a sovereign acts in a public capacity, but not when it acts in a private or commercial capacity. The adoption of the restrictive theory resulted from the recognition that governments have become more involved in commercial activities. Such activities are beyond the scope of traditional governmental activities, and it is viewed as unjust to deprive private parties, who deal commercially with governments, a legal means of resolving disputes.[36] Now, both the United Kingdom and the United States have codified the re-

32. Porzencanski, *supra*, note 28.

33. Clarke & Farrar, *Rights and Duties of Managing and Agent Banks in Syndicated Loans to Government Borrowers*, 1978 V. Ill. L. Rev. 229, 232 (1978).

34. 11 U.S. (7 Cranch) 116 (1812).

35. 26 State Dept. Bulletin 984 (1952).

36. Nichols, *Legal Issues in International Lending: General Consideration*, International Banking *supra* note 28, at 155.

strictive theory.[37]

An understanding of the sovereign immunity statutes in the United States and United Kingdom is important because the majority of loans made to Latin America originate in these two countries. Since banks have had leverage in their negotiations, they have insisted that their local laws apply and that debtors consent to the creditor's jurisdiction.[38] Some lenders from other countries also require that the law of either the United States or the United Kingdom apply since the legal systems and case law in these countries appear to be more predictable. This comment will now address on the treatment of sovereign immunity in the United States.

In the United States, the Foreign Sovereign Immunities Act of 1976 (FSIA) codified existing case law pertaining to sovereign immunity. The general rule is found in Section 1609 which states:

> Subject to existing international agreements to which the United States is a party at the time of enactment of this Act the property in the United States of a foreign state shall be immune from attachment arrest and execution except as provided in sections 1610 and 1611 of this chapter.[39]

Section 1611 (b)(1) recognizes that this immunity can be expressly waived. The section provides:

> (b) Notwithstanding the provisions of section 1610 of this chapter, the property of a foreign state shall be immune from attachment and from execution, if—
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> (1) the property is that of a foreign central bank or monetary authority held for its own account, unless such bank or authority, or its parent foreign government, has explicitly waived its immunity from attachment in aid of execution, or from execution, notwithstanding any withdrawal of the waiver which the bank, authority or government may purport to effect except in accordance with the terms of the waiver.[40]

The waiver of immunity exception is also found in section 1605 (a)(1) which states:

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37. The State Immunity Act of 1978 is the statute in the United Kingdom. *Id.* at 168.

38. F. Nattier, *Handling Disputes Outside The Inter-American and the United Nations Conventions*, in Current Legal Aspects of Doing Business in Latin America (S. Stairs, ed. 1981).

39. 28 U.S.C. § 1609 (1976).

40. 28 U.S.C. § 1611(b)(1) (1976).

> (a) A foreign state shall not be immune from the jurisdiction of courts of the United States or of the States in any case—
>
> (1) in which the foreign state has waived its immunity either explicitly or by implication, notwithstanding any withdrawal of the waiver which the foreign state may purport to effect except in accordance with the terms of the waiver;[41]

Thus, if a proper waiver of immunity is attained from the foreign bank or the foreign government, as either debtor or guarantor, and the dispute is governed by United States law, it is possible to attach and execute on the central bank's assets held in the United States. Most, if not all public loan agreements with Latin American countries contain such waivers, because they are highly recommended by the attorneys who draft the contracts for banks,[42] and because banks have occupied the dominant negotiating position.

The sovereign immunity protection of the FSIA applies only to a government's non-commercial activities. Section 1605(a)(2) states:

> (a) A foreign state shall not be immune from the jurisdiction of courts of the United States or of the States in any case—
>
> (2) in which the action is based upon a commercial activity carried on in the United States by the foreign state; or upon an act performed in the United States in connection with a commercial activity of the foreign state elsewhere; or upon an act outside the territory of the United States in connection with a commercial activity of the foreign state elsewhere and that act causes a direct effect in the United States;[43]

The foreign state has the burden of proving that it is entitled to immunity because its claim does not fall within the § 1605(a)(2) commercial exception.[44]

Not only is immunity denied when the activity is commercial, but also when the suit involves "rights in property taken in viola-

41. 28 U.S.C. § 1605(a)(1) (1976).

42. Nichols, *supra* note 23, at 159-160.

43. 28 U.S.C. § 1605(a)(2) (1976).

44. De Sanchez v. Banco Central de Nicaragua, 515 F. Supp. 900, 903 (1981), [hereinafter cited as *De Sanchez*], citing House Judiciary Comm. Report, Doc. No. 94-1487, *reprinted in* 1976 U.S. Code Cong. & S. Admin. News 6604, 6615; Arango v. Guzman Travel Advisors Corp., 621 F.2d 1371, 1378 (5th Cir. 1980); Behring International, Inc. v. Imperial Iranian Air Force, 475 F. Supp. 396, 405 n.9 (D.N.J. 1979).

tion of international law"[45] and

> that property or any property exchanged for such property is present in the United States by the foreign state; or that property or any property exchanged for such property is owned or operated by an agency or instrumentality of the foreign state and that agency or instrumentality is engaged in a commercial activity in the United States;[46]

Under this section, a Nicaraguan citizen living in the United States was able to recover $150,000 on a check that the central bank of Nicaragua issued in her favor on its account in an American bank.[47] The court acknowledged that the stop payment imposed on the plaintiff's check in order to regulate foreign exchange controls was a non-commercial government activity entitled to immunity. Nevertheless, the plaintiff could still sue the bank for its noncommercial governmental activity because the central bank of Nicaragua conducted commercial activities in the United States.[48]

A foreign government's assets on deposit in the United States are only entitled to immunity if: 1) the government has not waived immunity in its contract; and, 2) the bank in which it deposits its money does not engage in any commercial activity in the United States. Hence, the FSIA actually offers little protection for a debtor nation's assets on deposit in the United States.

VI. Actual Default

The international media has focused much attention on the external debt problems in Latin America and the dire potential of default on the mounting debts. It is curious, therefore, that a recent suit involving such a default escaped much publicity by the media and banking commentators. The case of *Libra Bank Ltd. v. Banco National de Costa Rica, S.A.*, involves Costa Rica's default on a loan of forty million dollars. The court held that the assets of the central bank of Costa Rica on deposit in the United States could be attached.[49]

The *Libra Bank* case presents a lengthy examination of the

45. *See De Sanchez*, 475 F. Supp. at 900.
46. 28 U.S.C. § 1605(a)(3) (1976).
47. *De Sanchez*, 475 F. Supp. at 910.
48. *Id.*
49. Libra Bank Ltd. v. Banco Nacional de Costa Rica, S.A., No. 81-7624 slip op. (S.D.N.Y. July 11, 1983) [hereinafter cited as *Libra*].

legal issues involved in a suit to seize a central bank's assets in the United States when a loan default occurs. In December 1980, a consortium of sixteen banks[50] loaned forty million dollars to the Banco Nacional of Costa Rica, which is wholly-owned by the Costa Rican government. This loan was to be completely repaid during 1981 in quarterly installments. The first installment was satisfied, but after August 18, 1981, no further interest payments were made. The Banco Nacional stated that it could not honor the re-payment agreement and pay the second payment due August 30, 1983, because of a resolution of the Central Bank of Costa Rica. The resolution was adopted on August 27, 1981, only authorized foreign currency repayments to multilateral agencies.

The Central Bank denied Banco Nacional's requests for foreign currency to pay the loan installment. In addition, on November 24, 1981, the President of Costa Rica and the Minister of Finance declared that the government and its public sector entities could not pay interest or principal in foreign currencies on external debts without official approvals. After the defendant defaulted, an order of attachment was granted. The defendant's various bank accounts in New York were levied upon, and approximately $800,000 was attached. Months later, a United States Marshall was authorized to levy upon a number of additional banks. By this time, the accounts of Banco Nacional were no longer maintained at these banks or at any other banks in New York. At least two and half million dollars had been withdrawn from the accounts.

The court reviewed the act of state doctrine noting that it "reflects at least in part the realization that in most cases there is nothing an American court can do to rectify a foreign seizure which has been fully effected within the territory of the expropriating state. . ."[51] The doctrine did not apply in this case because the situs of the debt was New York and the New York court had jurisdiction over it. Thus, the court held the loan agreement enforceable and the defendants liable for attorneys' fees under the terms of the contract. Banco Nacional subsequently made an un-

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50. Other plaintiffs were: Libra Bank Ltd. (agent for the sixteen banks), Libra International Bank S.A., Banco Espirito Santo e Commercial de Lisboa, Banco de Viscaya, S.A., Banque Internationale. A Luxembourg, S.A., Banque Rothschild, and The National Bank of Washington and Banco de La Provencia de Buenos Aires (itself from a critically debt-strapped country).

51. *Libra* citing United Bank, Ltd. v. Cosmic International, Inc., 542 F.2d 868, 874(2d Cir. 1976), which cites Tabacalera Severiano Jorge, S.A. v. Standard Cigar Co., 392 F.2d 706, 715 (5th Cir.) *cert. denied*, 398 U.S. 924 (1968).

successful motion "to re-argue," based on Article VIII, Section 2(b) of the Bretton Woods Agreement[52] claiming that this Agreement, to which the United States and Costa Rica are signatories, overrode the act of state doctrine. Section 2(b) states that exchange contracts are unenforceable. The court held that the loan agreement was not an exchange contract and, therefore, the Bretton Woods Agreement was not applicable.[53]

Throughout the proceedings, Costa Rica acknowledged that it owed the money on the loans and would eventually repay it. The only problem was the country's shortage of foreign currency and its self-preserving action of placing priorities on the use of its existing foreign currency. The Libra Bank consortium was successful in seizing a mere $800,000 and a judgment for the balance of the loan. However, without assets to attach in the United States, the judgment left the plaintiffs in the same position as before the suit; they would have to wait until Costa Rica was able to obtain the foreign currency to repay the loan.

For problems concerning the Latin American external debt, judgments granting attachments provide an unrealistic solution. Due to the cross-default clauses on the loan agreements, all the lending banks could be parties to a legal assault on the assets of a Latin American nation that was declared to be in default. Due to the economics of the situation, banks which could have declared their loans to Costa Rica in default apparently did not do so. Libra Bank attached what assets it could. Even if it had been successful in attaching the $2.5 million that had been in the country's New York accounts, this would still not have satisfied the amount due on the loan.

Thus, the legal situation of the Latin American external debt crisis is vastly different from that of previous attempts by one or more claimants to attach the assets of a foreign sovereign. Since hundreds of lending banks involved are intertwined by the cross-default clauses in their loan contracts, it is possible that a declaration of default by one bank could result in a "crisis of confidence" as well as rapid declarations of default by other banks on all their loans. As a result of all the banks pressing their claims *en masse* against limited and inadequate assets, each claimant would receive

52. Libra Bank Ltd. v. Banco Nacional de Costa Rica, S.A., No. 81-7624 slip op. (S.D.N.Y. Aug. 12, 1983).
53. *Id.*

too little to make legal recourse a viable solution.[54]

Furthermore, if significant numbers of banks pressed their claims against debtor nations and tried to attach their foreign currency assets, such actions would have grave political ramifications and would affect the United States' economy and foreign policy. All nations in difficulty would probably withdraw their assets held in United States banks (or in the foreign banks that were subject to attachment), due to fear for the safety of these assets. Such a mass withdrawal would result in an unstable position for the United States and the international banking system. The drastic action of attaching what assets a country has would lead to political animosities by the affected country and its sympathizers since the causes of the problem were mainly outside of the control of the debtor nation, which had been acting in good faith.

This could ultimately result in intervention by the President of the United States to resolve the situation. According to *Restatement (Second) of Foreign Relations Law of the United States* § 213: "The President may waive or settle a claim against a foreign state based on the responsibility of the foreign state for an injury to a United States national, without the consent of such national."[55] This section was cited in the case of *Dames & Moore v. Regan*,[56] which upheld the power of the Executive branch to invalidate attachments.

VII. Development and Integration of the Americas

All of the countries of the Western Hemisphere have a vested interest in the legal, economic, political, and social ramifications of the external debt situation. Our nations are bound by the ties of trade, monetary interdependence, immigration, and efforts for regional political stability.

When one nation suffers, the effects ripple to other nations.

54. As of August, 1983 banks in the United States reported liabilities payable in U.S. dollars to the following countries: Argentina - $4,249 million; Brazil - $3,078 million; Chile - $1,465 million; Colombia - $1,674 million; Cuba - $1,674 million; Ecuador - $12 million; Guatemala - $718 million; Jamaica - $106 million; Mexico - $9,444 million; Panama - $5,925 million; Peru - $1,127 million; Uruguay - $1,050 million; Venezuela - $8,575 million. Some of this money is being held by individuals and other non-governmental entities and thus would not be subject to attachment. Federal Reserve Bulletin Oct. 1983, at A59-A60.

55. Restatement Second of the Foreign Relations Law of the United States § 213 (1965).

56. 453 U.S. 654, 680 (1981).

Although the focus of the problem in the United States is on the economic ramifications of a potential default on its banking system, other serious effects have already taken place. The Federal Reserve Bank of New York reported that a decline of exports to Latin America cost the United States an estimated 250,000 jobs in 1982. United States exports to Latin America were $38.95 billion in 1981, $30.09 billion in 1982, and dropped to $10.93 billion in the first half of 1983 ($21.86 billion annualized).[57]

The impact on Latin America is equally disturbing. Per capita income has declined for the third straight year and is 8% below its peak in 1980.[58] In more and more Latin American nations, increasing percentages of the GNP are being used solely to continue servicing the external debt. In the short term, it will be difficult for these countries to develop economically at the previous pace unless there is a significant increase in their exports and GNP to offset these costs.

Due to the social pressures caused by the austerity measures needed to cope with the situation, populist political pressures could force Latin American governments to default on their loans. Increased dictatorial control could result as the nations struggle to force the measures on the population. The grave implications of this situation demand the close scrutiny and cooperation of the political leaders of the Western Hemisphere, as well as the banking community, since the costs of this problem affect nations as a whole.

VIII. Conclusion

The external debt problem of Latin America is of enormous political, social and economic importance to all of the Americas. It also affects other parts of the world. The major causes of the debt crisis are due to 1) illiquidity; 2) world recession and decreased exports; and 3) high interest rates and spreads. These factors are mainly outside of the control of the affected debtor nations.

Legal proceedings declaring the existing loans in default and attaching the hard currency assets that exist outside of the territory of the debtor nations are not a viable solution. Such judgments would be a hollow victory for the creditors, because the

57. The Wall Street Journal, Nov. 16, 1983, at 33, col. 2.
58. *Id.* at col. 3.

shortage of such assets would be inadequate to satisfy outstanding debts. Creditors would be in a similar position to that of one who holds a judgment against a judgment-proof debtor. These assets are also vulnerable to withdrawal by debtor nations. Furthermore, attachment proceedings would alienate the debtor nations from the creditor nations both politically and economically.

Since the legal solution is inadequate and the problem deeply troubles the nations involved, cooperation to remedy the situation must transcend the immediate self-interests of those who are parties to the loans. Programs, such as those of the IMF, should be supported, but always with sensitive evaluations of the social and political ramifications on the nations that must conform to the austerity measures. Nations in better economic positions must take the responsibility of aiding those nations with debt problems by contributing excess food and by facilitating trade. International cooperation, not legal confrontation, is the key to an effective resolution of this problem.

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