Monetary Policy, Fiscal Dominance, Contracts, and Populism

Sebastian Edwards

Most populist experiences in Latin America, including the best known ones—Peru (1985–90), Argentina (2003–17), and Venezuela (2002–present)—have been characterized by "fiscal dominance."[1] Monetary policy is dominated by fiscal policy, and the central bank finances (very) large increases in public expenditures. The central bank purchases national and subnational debt (municipalities and provinces) and provides loans to state-owned enterprises. In this way, it finances large transfers to the lower and middle classes, provides funds to huge public investment projects, and helps pay for the nationalization of large firms. Fiscal dominance has been behind the explosion of inflation in the vast majority of Latin American populist episodes. Peru under President Alan García ended up with hyperinflation of 7,000 percent in 1990, and Venezuela is on its way to 1,000,000 percent. Argentina under the Kirchners avoided hyperinflation, but in 2016, the last full year of President Cristina Fernández de Kirchner in office, the consumer price index increased at an annual rate of 41 percent.

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Sebastian Edwards is the Henry Ford II Distinguished Professor of International Economics at UCLA and a Research Associate at the National Bureau of Economic Research. He thanks Doug Irwin, Ed Leamer, Alejandra Cox, José De Gregorio, Leonidas Montes, and Al Harberger for helpful discussions and comments. In the early 2000s, he was an expert witness in some of the Argentine arbitration cases discussed in this article.

[1]On populism in Latin America, see Dornbusch and Edwards (1990, 1991).

There are instances, however, when fiscal dominance is not possible. The most obvious case is when a country does not have a currency of its own, either because it is dollarized—that is, it uses another nation's currency as a medium of exchange—or when it belongs to a monetary union. In those occasions, inflation is mostly kept in check. In Latin America, Ecuador provides an interesting case study of a populist regime—Rafael Correa, 2007–17—without fiscal dominance. In March 2000, in the aftermath of a major macroeconomic crisis that resulted in 100 percent inflation and debt default, Ecuador decided to eliminate its domestic currency, the sucre, and to adopt the U.S. dollar as its currency. During Correa's 10 years in office, Ecuador averaged 3.8 percent inflation, significantly below that of other populist experiments in the Latin American region. However, in order to finance his populist program, Correa ran a very expansive fiscal policy:

- Between 2008 and 2017, the structural fiscal balance in Ecuador averaged −5.4 percent of GDP.
- During Correa's last five years in office (2012–17), the deficit amounted to 8.7, 9.4, 7.8, 7.9, and 4.6 percent of GDP.
- Starting in 2009, debt dynamics moved into an unsustainable path. Gross government debt went from 23 percent of GDP in 2010 to a projected 54 percent of GDP in 2020.[2]

Other instances of countries that, in principle, cannot adopt a fiscal dominance regime include those that have a currency board system, where the central bank cannot issue high-powered money, unless it is (fully) backed by international reserves. However, the degree of precommitment of this type of system is lower than in nations without a currency of their own.

Countries that give up their currency and dollarize or join a monetary union, always have the option of reintroducing domestic money at some point in the future. This was, for example, the case of Liberia in the 1990s. Indeed, Ecuador's Rafael Correa insinuated that he would go in that direction when in 2016 he stated: "Very few countries in the world have committed a *monetary suicide* like Ecuador, adopting a foreign currency that behaves exactly in the opposite way

[2]These figures come from the International Monetary Fund's *World Economic Outlook*, April 2018, data set.

we want it to." Noting that Ecuador could not devalue, he compared the situation with that of neighboring countries: "Colombia devalued, Peru devalued, but we could not respond to anything" (see Telesur 2016).[3]

More recently, there has been talk about the possibility that Italy would leave the eurozone and reintroduce the lira as legal tender, an option that was also discussed seriously in 2013–15 in Greece. It has been argued that by abandoning the monetary union, Italy (or any periphery country that follows this route) would gain two policy tools: monetary policy, and the possibility of devaluing the currency as a way to gaining international competitiveness. This notion is based on the idea that a very strong euro, driven by Germany's rapid productivity growth, exacerbated the eurozone's periphery problems immediately after the 2008–10 financial crisis.

However, reintroducing a domestic currency is not easy. Some of the important issues that have to be addressed include the rate of conversion between the international currency (euro) and the new national money (lira), mechanisms for establishing credibility for the new regime, the creation of a full-fledged central bank with the appropriate staff, and negotiating with international institutions such as the IMF. In addition, there are logistical problems, including printing notes for the new-old national currency. But perhaps the most important difficulty—and one that tends to be overlooked in discussions on this topic—has to do with converting contracts denominated in the international currency (euros) into contracts denominated in domestic currency (liras or drachmas).

There have been some cases of contract conversions in history, and none of them has been easy. For example, after the devaluation of 2002, Argentina had to convert most contracts, which were written in terms of U.S. dollars, into pesos. In this case, the transition was not from an international to a domestic currency, but from a currency board with a fixed exchange rate (one dollar = one peso) to an adjustable currency system. Pesification was done at arbitrary rates. Some contracts (bank deposits) were converted using a 1.4 pesos per dollar rate, while the rest were rewritten at the old one-to-one

[3]Ecuador responded to the drop in the price of oil in mid-2014 by imposing import duties surcharges. On Ecuador's dollarization, see Calderón de Burgos (2014).

exchange rate. The result was a barrage of lawsuits and legal cases in domestic and international courts, and in arbitration tribunals.[4]

But perhaps the most interesting—and, surprisingly, least known—case of contract conversion happened in the United States between 1933 and 1935, when President Franklin D. Roosevelt decided to abandon the gold standard and devalue the U.S. dollar relative to gold. At the time, most contracts in the United States were written in "gold currency." That is, the debtor committed himself to paying a specified amount in "gold equivalent." This meant that if the official price of gold was increased, as happened in January 1934, the dollar value of the debt would rise proportionally. As a consequence, a large number of companies would go bankrupt, and the value of the public debt would increase drastically. In June 1933, Congress decided to deal with this issue by passing a Joint Resolution that abrogated the gold clause in contracts in a retroactive fashion. Not surprisingly, a large number of lawsuits followed. The Supreme Court heard the "gold cases" in early January 1935.[5]

In this article, I analyze the U.S. episode in the 1930s and compare it with the case of Argentina in the early 2000s. The discussion shows many similarities, as well as important differences between the two events. An important goal of this discussion is to provide some clues on the likely consequences of decisions to ditch a monetary regime that constrains discretionary monetary policy, replacing it by one that allows, at least in principle, for the emergence of some form of fiscal dominance.

The Devaluation of the U.S. Dollar and the Abrogation of the Gold Clauses

On April 19, 1933, President Franklin D. Roosevelt announced that the United States was abandoning the gold standard. From that point onward, paper dollars were not convertible into gold at the historical (almost 100 years old) rate of $20.67 per ounce. Gold could not be held by individuals, banks, or corporations, or shipped internationally, except to settle trade balances and under authorization by

[4]For an analysis of the Argentine case, within the Latin American context, see Edwards (2010).

[5]Edwards (2018) provides a detailed analysis of the abrogation of the gold clauses in the United States.

the Treasury. At that time no announcement was made regarding an official devaluation of the currency with respect to gold.

On May 12 of that year, Congress approved the Agricultural Adjustment Act (AAA). It included a provision known as the Thomas Amendment, which gave the president the authority to devalue the dollar by up to 50 percent with respect to gold. Roosevelt believed that by doing so commodity prices would increase rapidly. This idea had come to him through Cornell University Professor George F. Warren, who had developed a theory of a close and immediate correspondence between the price of gold and that of agricultural commodities. The theory was presented in a long book (coauthored with Frank A. Pearson), replete with tables and graphs, titled *Prices* (Warren and Pearson 1933). FDR was also influenced by the British experience after the devaluation of sterling in September 1931; in his view, by abandoning the gold standard, the United Kingdom had begun to recover. During May and June of that year Roosevelt pondered by how much the dollar should be devalued in order for the price level to return to approximately its 1926 level.

Deciding by how much to devalue was not the only problem addressed by the administration during late May 1933. A pressing issue was what to do with the fact that most debt—all of the federal debt, most of the local governments' debt, and a very large proportion of private debts—included gold clauses. That meant that the debtor committed him or herself to paying the dollar equivalent of the gold value of the debt at the time of issuance. From a practical point of view this meant that if the dollar was devalued substantially, public and private debts would experience an abrupt jump, and most public utilities and other corporations would go bankrupt. It was estimated that in 1933 debt totaling approximately $120 billion was subject to the gold clause (this figure includes private and public debt). In order to put things in perspective, GDP was approximately $70 billion.

On June 5, 1933, Congress passed a Joint Resolution abrogating the gold clauses in public and private contracts, retroactively. This meant that when, and if, the dollar was officially devalued, debtors would not have to adjust their debts up by the amount of the devaluation. They would be required by law to pay only the amount of paper dollars stipulated in the original debt contracts. Passing this Joint Resolution was extremely controversial. While the Democrats claimed that all it did was clarify that there was only one type of legal money in the United States, Republicans argued that it set in motion major income redistribution from the creditor class to the debtor class. After the Joint Resolution almost every analyst and observer predicted that once the dollar was officially devalued, a large number of lawsuits would be filed by creditors who held securities with a gold clause.[6]

During the next few months, and although the official price of gold continued to be $20.67 per ounce, the dollar depreciated relative to other currencies, and especially with respect to the French franc, which continued to be rigidly attached to gold. The dollar also depreciated relative to the pound sterling.

On January 15, 1934, and after a failed attempt to raise commodity prices through a limited "gold buying program," President Roosevelt announced plans to officially devalue the dollar with respect to gold. On January 30, the Gold Act of 1934 was signed into law, and the next day the president set a new official price of gold at $35 an ounce. The Treasury declared that it was buying and selling any amount of metal at that price internationally. However, U.S. residents were still not allowed to own gold. The Gold Act also created the Exchange Stabilization Fund at the Treasury, financed with the capital gains that stemmed from raising the price of gold from $20.67 an ounce to $35 an ounce.

The Gold Cases and the Supreme Court

As soon as the dollar was officially devalued on January 31, 1934, there was great confusion. Most debtors wanted to pay in paper dollars, and every creditor demanded payment in gold equivalent. There was also confusion in international markets. These stemmed from the fact that a number of European countries had issued dollar-denominated debt in the United States, subject to the gold clause. The question at hand was whether these foreign powers should pay

[6]The issue of finding a new and stable value for the dollar relative to gold and major currencies (sterling and the French franc) occupied negotiators from the United States, United Kingdom, and France during the early weeks of the London Monetary and Economic Conference that opened during the second week of June 1933. In early July, and to everyone's surprise, President Roosevelt announced to the conference that the United States would not seek to stabilize the exchanges. According to the president, doing so before finding a way to increase agricultural prices and put an end to disinflation was a mistake. See Edwards (2018) for details.

in gold terms, or if they should take advantage of the abrogation of the gold clause and the devaluation, and pay in depreciated paper dollars. This led to the peculiar situation where the prices of some foreign bonds increased significantly, with yields tightening below those of U.S. equivalent securities. At the end, the Swiss and the French continued to pay in gold terms, while the Germans and the Italians decided to discharge their debts using depreciated paper dollars.

During the first half of 1934, a multitude of lawsuits was filed in different courts. On June 20, 1934, a Federal Court in St. Louis ruled that the joint resolution abrogating the gold clause was constitutional and that private debtors did not have to pay in gold equivalent. A similar ruling was handed down by a District Court in New York on July 3, 1934 (*Baltimore and Ohio Railway* case). As soon as the decision was delivered, the lawyer for the plaintiff declared that he would take the case all the way to the Supreme Court.

As a way to avoid generalized confusion, the administration decided to ask the Supreme Court to consolidate a number of gold cases, and to hear them together. On November 18, 1934, J. Crawford Briggs, the solicitor general, announced that the Supreme Court had agreed to hear four cases on January 8. Two of them referred to private debts and two to public debts. The administration became part of one of the private cases, involving the bankruptcy of the Iron Mountain Company, a subsidiary of the Missouri & Pacific Railroad. This case was known as the *Bankers Trust Case*. The two public debt cases referred to a Liberty Bond and a gold certificate. The Court of Claims asked whether the government could be sued by holders of these securities.

During the final weeks of 1934, an army of lawyers worked preparing the government cases. It was decided that Homer Cummings, the attorney general, would argue in front of the Supreme Court during the first day of the proceedings. In terms of legal strategy, the administration decided to follow a multipronged approach. The principal argument was that, according to Article I, Section 8, of the Constitution, Congress had the power "to coin money" and "to regulate the value thereof." Thus, Congress could "pass a law prohibiting gold clauses." In addition, the administration argued that Congress had not violated the Fifth or Fourteenth Amendments, since there had been no "taking." The government had not questioned the "validity" of public debt. It was further argued that if there had been any "taking" this would have happened on June 5, 1933, the day the Joint Resolution annulling the gold clauses was passed. According to the data, however, government bonds were "worth just as much with that right [the gold clause] withdrawn or abrogated as it was worth when that provision still formed part of the obligation" (MacLean 1936: 250).

A key argument made by the government was that in 1933 Congress faced the "necessity" to take action. This required devaluing the dollar with respect to gold, and the only way to do that without damaging the economy in an irreparable way was by first abrogating the gold clauses. Assistant Solicitor General Angus MacLean, one of the government lawyers who argued in front of the Supreme Court, pointed out in an article published shortly after the ruling that, "if the gold clauses were maintained, . . . this meant bankruptcy on a national scale. . . . The Supreme Court was virtually obliged to sustain the action of Congress . . . in order to save the country" (MacLean 1936: 250–51). Administration lawyers believed that the Supreme Court would be sympathetic toward this necessity argument. After all, in January 1934, the Court had ruled that a Minnesota statute declaring a moratorium on mortgages, based on the argument of "emergency" and "necessity," was constitutional (Edwards 2018: 142).

The government also relied on a "secondary argument," grounded on two ideas. First, it was thought that it would be impossible to pay all debts in gold because holdings of the metal around the globe were only a fraction of the amount involved in these cases. The weakness of this idea was evident: the plaintiffs were not asking for physical gold, but to be paid in "gold equivalent" at the new exchange rate of $35 per ounce. Second, it was contended that there were no damages involved in the abrogation of the gold clause because generalized disinflation meant that the same amount of paper dollars in 1934 bought more goods than a decade earlier.

The Supreme Court heard the gold cases on January 8, 9, and 10, 1935. The opening argument for the government was delivered by Attorney General Homer Cummings. No questions were asked by the justices, as was the tradition when the nation's top lawyer appeared in front of the Court. During the next two days some of his deputies and the chief lawyer for the Reconstruction Finance Corporation made presentations in front of the Court. All deference was set aside, as the justices asked one question after the other, introducing what the press considered to be significant holes into the government's arguments. At the end of the third day there was general sense among observers, reporters, and legal experts that the government had done rather poorly. Suddenly there was fear that the court was going to declare that the abrogation of the gold clauses was unconstitutional. A key question within the ranks of the administration was what to do if that was indeed the case. On January 13, three days after the argument in front of the Court was over, the *New York Times* reported that, because of "the speculative fever for gold" stemming from the government lawyers' poor performance, the price of Liberty Bonds had reached their highest since their issuance in 1917. The *Times* added, "Should the gold clause case now before the United States Supreme Court go against the government, a complete reclassification of prices of gold and nongold state and municipal bonds would be in order" (New York Times 1935: 2).

From today's perspective, perhaps the most surprising action considered by the White House, in case of a negative decision, was for the president to deliver a speech, explaining why he was not going to abide by the Supreme Court decision. In that speech he would tell the American people that his administration would take any action necessary in order not to pay past debts in gold terms. The draft, which may be found in the FDR presidential archives, said toward the end:

> Every individual or corporation, public or private, should pay back substantially what they borrowed. That would seem to be a decision in accordance with the Golden Rule, with the precipice of Scripture and the dictates of common sense. . . . In order to attain this reasonable end, I shall immediately take such steps as may be necessary, by proclamation and by message to the Congress of the United States [quoted in Maglioca 2012: 35].

The Rulings

The Supreme Court ruled on February 18, 1935. There were two rulings, one regarding the private debt cases, the second one regarding the Liberty Bond and the gold certificate. Both decisions were five to four, with the conservative bloc of the Court—a group known as the Four Horsemen—in the minority. The rulings were written by Chief Justice Charles Evans Hughes. With respect to private debts, the Supreme Court ruled that since the Constitution gave Congress authority to coin money and determine the value thereof, it was constitutional to change the nature of the private debt contracts, if that was needed for Congress to exercise its power and to conduct the type of monetary policy that the country needed.[7]

The ruling regarding the public debt was more complex and very controversial. According to the majority of the Court, although Congress had the power to coin currency, it also had the power to issue debt on behalf of the United States. This second power carried with it the obligation of paying back that debt. According to the Court, one power could not be used to annul the other power. Consequently, the abrogation of the gold clause in government debts was unconstitutional. However, the Court continued, there were no damages involved. Because of deflation, the same amount of paper dollars used to purchase the Liberty Bond at the time of issue (1917), would buy in 1935 a larger amount of goods and services than what it could buy originally.

The combination of these two rulings meant that the Roosevelt administration had won on all accounts. The process, however, was long, costly, and nerve racking; it generated great uncertainty and encouraged speculation. According to Friedman and Schwartz (1963: 699), although the devaluation of the dollar had a positive effect, by allowing the Federal Reserve to increase base money, "some of the measures accompanying it—in particular, the nationalization of gold, the abrogation of the gold clause, and the New Deal's program besides monetary policy—had the opposite effect by discouraging business investment."

Argentina: Currency Board, Devaluation, and Contracts

On December 23, 2001, Argentina defaulted on its debt. Two weeks later the peso was devalued by 30 percent, and a 10-year experiment with a currency board and a fixed exchange rate (one peso equal to one dollar) came to an end. The next few years were difficult for Argentina: GDP collapsed, unemployment exploded, and the peso continued to sink. By 2005 the currency had lost two-thirds of its value (at the time of this writing the exchange rate is 36 pesos per dollar). The road to devaluation and default

[7] For details, see Edwards (2018) and the literature cited therein.

was traumatic: the year 2001 was characterized by massive demonstrations, riots, bank runs, a suspended IMF program, and a bank deposits freeze. On December 9, 2001, President Fernando de la Rúa resigned, and five months later, Nestor Kirchner, the former governor of the province of Entre Ríos, was elected president. When he took over, growth was negative, unemployment exceeded 20 percent, the public debt was in arrears, relations with the IMF were strained, and the currency continued to depreciate at a rapid clip.[8]

On January 6, 2002, the Economic Emergency Law was passed by the Argentine Congress. This Act put an end to the 1991 Convertibility Law, which had provided the legal backbone for the currency board and the one-to-one peso/dollar fixed exchange rate regime. The new legislation converted contracts that were written in dollars into depreciated pesos. In the financial sector, pesification was asymmetrical. Dollar-denominated deposits were converted into pesos at a rate of 1.4 pesos per dollar; debts were converted at the one-peso-one-dollar rate. At that time the (parallel) market value of the U.S. dollar was close to 3 pesos. Other contracts, and in particular public service prices (telephony, electricity, sewage, toll roads), which were written in U.S. dollars, were converted into pesos at the old rate of one peso per dollar. This resulted in significant losses to international companies, many of which had invested large amounts during the privatization process initiated by President Carlos Menem.

In addition to converting contracts from dollars to pesos, the Kirchner government decided to restructure the external debt, which had been in arrears since late December 2001. In September 2003, the Argentine government made an offer to investors to exchange defaulted bonds for new ones. This proposal became known as the "Dubai Guidelines" and implied an average reduction of the face value of the debt of approximately 75 percent. Investors balked at the stiff losses and asked for better conditions. Negotiations ensued, and a new offer was formally made in June 2004 under the moniker of "Dubai Plus." The terms of this proposal were very similar to the original ones and implied losses (in present value terms) for bondholders of approximately 75 percent (see Edwards 2015).

[8]For the Argentine experiment with a currency board, see Edwards (2010).

Legal Arbitration Proceedings

Immediately after the conversion of contracts from dollars to pesos, investors sued Argentina in national and international courts. Although the Aurelius "holdouts" case, heard in New York, is the better-known one, there was a multitude of arbitration cases (almost 40) heard in Washington and Paris at the World Bank's International Centre for Settlement of Investment Disputes (ICSID). A detailed analysis of the different cases in U.S. courts and in arbitration tribunals may be found in Porzecanski (2016).

From early on, Argentina's legal strategy was based on the notions of "emergency" and "necessity." Government lawyers argued that Argentina had faced an economic "emergency" stemming from an unprecedented economic crisis unleashed from abroad. In particular, the Argentine economy was subject to a number of severe external shocks. The terms of trade declined markedly, global interest rates increased swiftly, the U.S. dollar (the currency to which the peso was fixed) strengthened in global markets, and capital inflows slowed significantly, in part as a result of contagion stemming from Russia and Brazil. The lawyers argued that these circumstances created a "perfect storm"—a unique negative situation that threatened the survival of the state. Faced with this external picture, there was no alternative but to devalue the peso with respect to the dollar. This action was required to increase the country's degree of international competitiveness, and in this way encourage exports, employment, and growth.

However, devaluation could not be undertaken if (most) contracts were in dollars, because it would result in massive bankruptcies, undue burdens to citizens, and a huge increase in the already high public-sector debt. Thus, the government faced the "necessity" to pesify and retroactively convert dollar-denominated contracts into pesos at the original rate of one-to-one. These arguments, of course, are very similar to those used by the Roosevelt administration in 1935. Argentine courts, including the nation's Supreme Court, accepted these premises and ruled that pesification was legal within the Argentine legal order.

By early 2017, ICSID had heard 37 Argentina-related cases. At each one of the hearings the Argentine legal team showed a video that depicted the political upheaval that affected the country in 2001. The film included scenes of violent demonstrations and riots, of mounted police officers charging on demonstrators, and of President de la Rua leaving the presidential palace in a helicopter, after resigning. The government insisted that the conversion of contracts was not a capricious measure, but one dictated by force majeure. In addition, and in case after case, Argentina's lawyers and their experts argued that the conversion of contracts had not created undue burdens to the plaintiffs, and that damages were either zero or very small. Again, this strategy seemed to be taken out of the FDR playbook in 1935.

One of the early arbitration cases was *Sempra Energy International v. Republic of Argentina* (ICSID Case No. ARB02/16), a case related to a gas distribution business. The award document issued by the tribunal summarizes clearly the arguments made by both the investor seeking reparation and by the government of Argentina.[9] This is the way the tribunal summarized the complaint by Sempra:

> The Claimant argues that a number of measures adopted by the Government of Argentina in the period 2000–2002 and thereafter have resulted in the permanent abrogation and repudiation of most of the rights it had under the regulatory framework. . . . The Claimant asserts that this is particularly so in the case of . . . the derogation of the calculation of tariffs in U.S. dollars.[10]

After calculating several breaches in the contract, Sempra asked for compensation totaling $300 million.

The tribunal described Argentina's position with respect to the circumstances that led to the annulment of dollar contracts and their conversion to pesos as follows:

> The Government has pleaded . . . an exemption from liability in the light of a national *emergency* or state of *necessity* under domestic law, general international law and the Treaty, all

[9]This award was later annulled by the tribunal on procedural grounds. The annulment tribunal claimed that the original tribunal had based its ruling on Customary International Law, while it should have relied on the language in the Bilateral Investment Treaty (BIT). Other awards, including that of the CSM gas case (ARB/01/8), were annulled for similar reasons. In spite of the annulment, the award granted by the original tribunal was maintained. For a discussion of the procedural aspects of the Argentine cases, see Alvarez and Brink (2012).

[10]The award document by the tribunal is available at www.italaw.com/sites/default/files/case-documents/ita0770.pdf.

> based on the severity of the crisis that has affected the country since 2000. . . . The Respondent [Argentina] has explained in detail the severity that characterized the crisis affecting the country, which in its view threatened the very existence of the State and its independence. The Respondent asserts in particular that the significant decreases in the Argentine Gross Domestic Product, consumption and investment during the crisis period, together with deflation and the reduction in value of Argentine corporations, resulted in widespread unemployment and poverty, with dramatic consequences for health, nutrition and social policy. Public institutions were also no longer functioning. . . . With a view to overcoming such difficulties, there was an urgent *need* to resort to *emergency*, described by the Respondent as a severe form of *necessity*, and which materialized in the 2002 Emergency Law. The Respondent explains in this respect that the Emergency Law [including pesification of contracts] was not the cause of the unfolding economic *emergency*, but rather the normative consequence of a situation that had become manifest in world financial markets. The Respondent maintains that the measures adopted were the remedy recommended by distinguished economists and led to the gradual recovery that is noticeable at present [ICSID 2007: 96, emphasis added].

The tribunal explained that in order for the necessity argument to be valid, a number of preconditions had to be met. In particular, Argentina had to prove that the actions taken, including the unilateral conversion of contracts, were the only options available to deal with the negative circumstances. In addition, these measures had to be temporary. Moreover, Argentina had to prove that it had not contributed, by its own actions, to the crisis.

With respect to the defendant's possible contribution to the unleashing of the crisis, the tribunal noted that Argentina's lawyers made the following point:

> The Respondent [Argentina] argues in particular that it has not contributed to the state of necessity since most of the relevant factors were exogenous, the measures adopted were the only means to safeguard an essential interest against a grave and imminent peril because otherwise the situation would have gone out of control, no essential interest of other States benefiting from the obligation or of the international

> community as a whole have been seriously impaired, and the Claimant . . . [has] not been treated differently from other investors in this sector [ICSID 2007: 99].

The Rulings

Although every case had its unique characteristics, in all of them Argentina made the necessity and emergency argument. The rulings were different in each case, but in most of them the tribunal did not agree with Argentina's emergency and necessity arguments. For example, in rendering its decision in the *Sempra* case, the tribunal wrote:

> The real issue . . . is whether the constitutional order and the survival of the State were imperiled by the crisis, or instead whether the Government still had many tools at its disposal to cope with the situation. . . . The Tribunal believes that the constitutional order was not on the verge of collapse, as evidenced by, among many examples, the orderly constitutional transition that carried the country through five different Presidencies in a few days' time, followed by elections and the reestablishment of public order. Even if emergency legislation became necessary in this context, legitimately acquired rights could still have been accommodated by means of temporary measures and renegotiation [ICSID 2007: 98].

Although the tribunal did not award the $300 million sought in the Sempra case, it did order Argentina to compensate the company in the amount of $128 million (ICSID 2007). In the majority of the arbitration cases Argentina was ordered to pay some damages to investors.

For years, Argentina ignored the ICSID rulings and did not pay the awards. This changed in 2016, after Mauricio Macri was elected president. Starting that year, and in an effort to regain access to international capital markets, settlements with several of the claimants that had prevailed at ICSID were pursued. A particularly important case was *Abaclat* (ICSID Case No. ARB/07/5), a case that involved thousands of Italian retail bond investors, with a very large award of approximately one billion euros.[11]

[11] In 2013 Argentina had settled five cases, involving total awards of approximately $650 million.

Comparison with the U.S. Gold Cases in 1935

In spite of the similarities of the legal arguments—namely, the reliance on "emergency" and "necessity"—the outcomes in the United States in 1935 and Argentina in the 2000s were very different. In the United States the Supreme Court ruled that there were no damages, and thus that no compensation had to be paid to the holders of public debts with a gold clause. In addition, after the forced conversion of contracts, the U.S. government continued to tap the capital markets. In fact, after the abrogation it had no problems rolling over the maturing debt, or selling new issues. Interestingly, after 1934 the government could place debt without the gold clause at longer maturities and lower interest rates than before contracts conversion (see Edwards 2018). Argentina, in contrast, had to pay major awards to debt holders and investors, and was excluded from the international capital markets for over 15 years. The country was only able to issue international debt after it had agreed to settle with the different plaintiffs that had prevailed in international courts.

There are a number of possible reasons for the differences in outcomes. First, in the case of the United States the abrogation of the gold clause was seen as a unique event with no historical antecedent. Moreover, investors and analysts did not expect it to set a precedent going forward. In many ways, it was considered a genuine case of an "excusable default," a unique situation that could be characterized as a true "emergency." In Argentina, in contrast, the devaluation, debt default, and contracts' rewriting were seen as one more step in a recurrent history of not playing by the rules of the game, and using the excuse of "emergency" not to pay what was owed to others. In addition, in many of the rulings the tribunal decided that Argentina had contributed to the crisis and that there were other policy options available to confront the negative situation, besides defaulting and abrogating contracts.

Second, the argument of necessity was significantly more persuasive during the Great Depression (1933) than in 2001–2, when many Latin American countries suffered shocks similar to those affecting Argentina but did not default on their debts or annulled contracts. In particular, and with respect to the "haircut" involved in the debt restructuring, many analysts and investors looked at the case of Uruguay, a country that suffered very similar (if not more severe) external shocks, and that imposed a very small loss on investors: 7 percent, compared with 75 percent in Argentina.

Third, in the United States the legal proceedings were exclusively domestic and culminated with the hearings at the Supreme Court in January 1935. In Argentina, in contrast, international tribunals were involved. The reason for this difference was that none of the U.S. government securities were marketed to foreigners (although some foreign national and investors did purchase them). This was very different in Argentina, where many securities were issued in London and New York and were expressly marketed to foreign investors, including retail investors in Italy. Furthermore, the government explicitly courted foreign companies to participate in the privatization process and to provide services in water supply, telephony, and power generation (see ICSID 2005, 2007).

Fourth, in the United States the abrogation was confined to debt securities. In Argentina, in contrast, it went beyond the financial sector and affected contracts in all sorts of businesses, including, as noted, prices for public services.

Conclusion

Undertaking a detailed cost-benefit analysis of these two contract-rewriting episodes is well beyond the scope of this article. What is clear, however, is that in both cases the conversion of massive contracts from one currency to another was cumbersome, logistically difficult, legally problematic, and, at the end of the road, costly for society. As the discussion clearly showed, it was significantly more costly for Argentina than for the United States.

Surprisingly, discussions on the possible abandonment of the eurozone by countries such as Italy or Greece tend to ignore the whole issue of contracts. This is also true of discussions regarding the possible reintroduction of a domestic currency in countries that have dollarized their economies, such as Ecuador, or other nations with populist governments that want to escape monetary discipline and move toward a fiscal dominance regime.

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