Carter Brod

Sovereign Entities Practice Guide

by Carter Brod, Morgan, Lewis & Bockius LLP

Overview

Question 1: What is a sovereign entity?

In the context of international securities transactions, a sovereign entity generally means a government or political subdivision thereof, which includes not only national governments and their ministries and departments but also sub-sovereign entities such as the governments of regions and municipalities. Securities issued or guaranteed by U.S. governmental entities are generally exempted securities under Section 3(a)(2) (15 U.S.C. §77c) of the U.S. Securities Act of 1933, as amended (the Securities Act). See Section 3 Exemptions from Securities Act Registration Checklist. Since this exemption does not apply to non-U.S. sovereign entities, their securities offerings must be registered with the U.S. Securities and Exchange Commission (SEC) unless another exemption applies. Registered U.S. offerings by non-U.S. sovereign entities are made under Schedule B to the Securities Act (Schedule B). While Schedule B is also permitted to be used by certain government owned or controlled companies and certain international organizations, the focus of this guide is on securities offerings by non-U.S. governments or political subdivisions thereof, and the term "sovereign entities" is used herein accordingly.

As governmental entities cannot issue equity securities, securities offerings by sovereign entities generally only include debt securities offerings.

Sovereign bond offerings can be domestic offerings or external offerings. Domestic sovereign bond offerings are offerings of local currency denominated bonds which are sold in the issuer's domestic market mainly to domestic investors. External sovereign bond offerings, on the other hand, are offerings of bonds denominated in U.S. dollars or another hard currency, which are offered in various jurisdictions outside of the issuing country and which trade internationally. Domestic sovereign bond offerings are different from external sovereign bond offerings in both the way they are conducted and the way they are documented. In particular, domestic bonds are typically sold via local auctions and with minimal disclosure or other documentation, whereas external sovereign bond offerings are generally conducted and documented in the same manner as other international debt securities offerings. This guide is focused on external offerings as opposed to domestic offerings.

Sovereign bonds have been issued by many countries around the world over many years. Sovereign entities that have issued bonds externally include developed countries, developing countries, offshore centers, and regions and municipalities. Some countries have been issuing sovereign bonds for many years and have a range of various series of bonds outstanding, whereas others may only have issued sovereign bonds once or a few times.

Similar to other international debt securities offerings, the main players in the sovereign bond offering market are investment banks, institutional investors, law firms, trustees, financial advisory firms, and other financial service providers. While international financial institutions such as the International Monetary Fund (IMF) and the World Bank play a key role in supporting and developing the sovereign debt markets generally, they are not directly involved in the process of offering sovereign bonds. For further information on the players in various securities offerings generally, see Parties to a Securities Offering Checklist and Identifying the Parties Involved in a Rule 144A/Regulation S Debt Offering and Their Roles.

Applicable Securities Laws and Regulations

Question 2: What are the relevant statutes and regulations governing securities offerings by sovereign entities?

The relevant laws and regulations for a sovereign bond offering are the domestic laws and regulations in the issuer's country, the governing law of the bonds and other transaction documents, and the securities laws in the jurisdictions into which the bonds are offered and sold.

Domestic Laws and Regulations

The domestic laws and regulations that are relevant for sovereign bond offerings will vary from country to country. See Getting the Deal Through: Debt Capital Markets. Particularly important domestic laws and regulations applicable to an external bond offering are those dealing with the authorization of the bond issue. For example, there are typically debt laws and budget laws that limit the level of governmental external debt that may be outstanding at a particular time or that may be incurred within a particular fiscal period. Parliamentary approvals and approvals from government ministries and the central bank may also be required for the transaction. For example, some countries' domestic laws allow the country to issue bonds directly, whereas in others the bonds must be issued via the country's central bank, its ministry of finance, or another governmental entity. Public procurement laws and regulations may also be applicable to the process of appointment of investment banks, lawyers, and other parties to the transaction.

External Laws and Regulations

External sovereign bonds are typically governed by English or New York law, in contrast with domestic bonds which are governed by local law. In international sovereign bond offerings, it is generally considered important that the bonds be governed by a law other than the law of the issuer's jurisdiction, because a sovereign issuer has the ability to change its own laws.

Regardless of the governing law of the bond documents, external bond offerings by sovereign entities, like other debt securities offerings, must be conducted in compliance with the securities laws of the jurisdictions into which the offering is made and where the securities are listed.

The following are certain statutes and regulations that are relevant for external sovereign bond offerings generally:

U.S. Securities Act

If a sovereign bond offering is made into the United States, it will need to be registered with the SEC or exempt from the U.S. registration requirements. Offerings outside the United States will need to be conducted in compliance with Regulation S (17 C.F.R. §§230.901-905) under the Securities Act (Regulation S). For SEC-registered offerings by non-US sovereign entities, a registration statement under Schedule B must be filed at the time of the offering, and annual reports must be filed thereafter on Form 18-K. The disclosure requirements under Schedule B are very limited compared to the disclosure requirements applicable to foreign private issuers, and in practice the disclosure in a sovereign bond prospectus goes significantly beyond the requirements set out in Schedule B for marketing reasons as well as general disclosure and liability considerations for the underwriters and the issuer. Offerings made pursuant to Rule 144A (17 C.F.R. §230.144A) under the Securities Act (Rule 144A) by sovereign entities customarily meet the same disclosure standards as SEC-registered offerings. For further information, see Understanding the Requirements of Rule 144A and Regulation S. Under Regulation S, securities that are backed by the full faith and credit of a foreign government are Category 1 securities and accordingly a pure Regulation S offering by a sovereign issuer must only comply with the "offshore transaction" and "no directed selling efforts" conditions in Regulation S. For additional information on Regulation S, see Regulation S Offering Representations and Covenants. For additional information on U.S. securities laws generally, see U.S. Securities Laws: An Overview.

U.S. Foreign Sovereign Immunities Act (FSIA)

The FSIA is important for sovereign bond offerings that are made into the United States. Among other things, the FSIA includes a "commercial activity" exception, which provides that a non-U.S. sovereign state does not have immunity from the jurisdiction of the U.S. courts where it is being sued based on a commercial activity carried on in (or having substantial contact with or a direct effect in) the United States (although there is uncertainty as to whether this exception extends to actions under the U.S. federal securities laws). While this exception (which has been held by the U.S. Supreme Court to apply to sovereign bonds) on its own may be sufficient to preclude a sovereign issuer from successfully claiming sovereign immunity from the jurisdiction of the U.S. courts with regard to its sovereign bond obligations, it is customary for a sovereign issuer also to execute, in its sovereign bond documentation, a waiver of any sovereign immunity it may have under the FSIA or on any other basis.

European Union Prospectus Directive (Directive 2003/71/EC, as amended) (the Prospectus Directive)

If a sovereign entity (including any regional or local authority of such a sovereign entity) that is not a European Economic Area (EEA) member state conducts a public offering of its securities in the EEA or lists its securities on an EEA regulated market, then that issuer generally is required to prepare a prospectus that meets the disclosure requirements of the Prospectus Directive and to have that prospectus approved by an EEA regulator and published. Such a prospectus would be subject to the disclosure requirements in Annex XVI to the Prospectus Directive ("Minimum Disclosure Requirements for the Registration Document for securities issued by Public International Bodies and for debt securities guaranteed by a member state of the OECD (schedule)"). EEA member states are exempt from the requirement to produce a Prospectus Directive-compliant prospectus under the Prospectus Directive, even if they are conducting a public offering in the EEA or listing their securities on an EEA regulated market. Nonetheless, both for marketing reasons as well as general disclosure and liability considerations for the underwriters and the issuer, EEA member states conducting sovereign bond offerings in the EEA customarily produce an offering circular that meets the general international disclosure standards for sovereign bond offerings. See Question 4.

U.S. Trust Indenture Act of 1939 (Trust Indenture Act)

Debt securities issued or guaranteed by a foreign government or its subdivisions are exempt from the requirements of the Trust Indenture Act pursuant to Section 304(a)(6) thereof. As a result, a non-U.S. sovereign entity conducting an SEC-registered bond offering can issue the bonds pursuant to a fiscal agency agreement instead of pursuant to an indenture that meets the requirements of the Trust Indenture Act.

Treaties or Conventions on Recognition and Enforcement of Judgments and Arbitral Awards

A sovereign entity will invariably be required to submit to the jurisdiction of certain external courts (such as English or New York courts) and/or to agree to resolution of disputes by an international arbitration tribunal in any proceedings arising out of its external sovereign bonds. However, it may not be possible to enforce in the issuer's country a judgment obtained in such an external court or an arbitral award from such tribunal unless there is an applicable bilateral or multilateral treaty in force regarding the reciprocal enforcement of judgments, or the issuer's country is a party to an applicable arbitration convention providing for recognition of such arbitral awards. Accordingly, it is important to determine what treaties or conventions may be relevant for the offering and to include appropriate disclosure in the disclosure document regarding the risks associated with recognition and enforcement of judgments or arbitral awards.

Securities Offering Process

Question 3: What is the typical process for securities offerings by sovereign entities, including general steps, timeline, key transaction documents, due diligence process and required regulatory and stock exchange filings?

Typical Offering Process

The typical offering process for sovereign bonds is similar to the offering process for other types of debt securities. For example, international sovereign bond offerings may be SEC-registered, issued to U.S. investors in a private placement exempt from the U.S. registration requirements, or conducted outside the United States pursuant to Regulation S under the Securities Act.

Certain differences between sovereign bond offerings and other offerings of debt securities include the following:

- Sovereign bond offerings do not involve financial statements, auditors, or auditor comfort letters.
- The authorization process for a sovereign bond offering may require approvals from government ministries and/or the parliament or the central bank in the issuer's country, whereas such types of approvals are generally not required for authorization of a corporate bond issue. See Question 2 above.
- The documentary due diligence process for a sovereign bond offering is largely based on official government documents and data, which are usually publicly available.
- There are special requirements for SEC-registered offerings of sovereign bonds under Schedule B, including special procedures (pursuant to SEC interpretive guidance and no-action letters) for shelf registrations of SEC-registered sovereign bonds which are different from the procedures applicable to shelf registrations by corporate issuers, as described below.

Sovereign bonds may be listed or unlisted. For an overview of listing requirements on U.S. exchanges, see Complying with NYSE and Nasdaq Listing Requirements. Sovereign bonds that are not SEC-registered are typically listed on a European stock exchange. In recent years, the Luxembourg Stock Exchange has been the most popular listing venue for sovereign bonds, although sovereign bonds are listed on many other stock exchanges. Stock exchange filings for sovereign bonds are similar to those that are required for other debt securities.

Key Transaction Documents

The principal documents used in external sovereign bond offerings, which are similar to those for other debt securities offerings, include:

- **Prospectus or other disclosure document.** The disclosure document may be referred to as a prospectus, offering circular, offering memorandum, or listing particulars, depending on the features of the offering. For further information on drafting disclosure documents, see Drafting an Offering Memorandum for a Rule 144A/Regulation S Securities Offering and Using Form S-3 Registration Forms.

- **Indenture, trust deed, or fiscal agency agreement.** Because sovereign entities are exempt from the Trust Indenture Act, sovereign bonds governed by New York law are often issued pursuant to a fiscal agency agreement rather than an indenture, even in SEC-registered offerings. English law governed sovereign bonds are issued pursuant to a trust deed or fiscal agency agreement. Certain ancillary documents may be required pursuant to the indenture, trust deed, or fiscal agency agreement, mainly relating to authentication and issuance of the bonds. For information on indentures in the context of a Rule 144A/ Regulation S offering, see Drafting an Indenture for a Rule 144A/Regulation S Issuance and Indenture (Rule 144A and/or Regulation S Debt Offering).

- **Terms and conditions of the bonds.** Many of the provisions in the terms and conditions of sovereign bonds are standard provisions which are found in debt securities generally. However, there are some provisions that are specific to sovereign bonds, such as waivers of sovereign immunity and collective action clauses (CACs). Sovereign bonds may bear interest at a fixed rate or a floating rate. They are typically unsecured but they may be secured or have other features. For example, a number of sovereign entities have issued Islamic bonds, which are structured to comply with Islamic law and are marketed to Islamic investors. The terms of sovereign bonds can vary considerably depending on whether they are issued as part of a restructuring (i.e., in exchange for existing bonds) or as part of a standalone capital raising. The terms of sovereign bonds issued in a standalone capital raising will typically be fairly simple and highly standardized, whereas the terms of sovereign bonds issued as part of a restructuring are typically heavily negotiated and can include tailored and innovative features.

- **Underwriting agreement.** Consistent with market practice in debt securities offerings generally, the underwriting agreement may be referred to as an underwriting agreement, a purchase agreement, or a subscription agreement, depending on the features of the offering.

- **Legal opinions.** In common with other international debt securities offerings, there will be a requirement for legal opinions under the issuer's local law and under the law governing the bond documentation to be delivered to the underwriters. 10b-5 statements will be delivered if the offering is SEC-registered or made pursuant to Rule 144A. Standard U.S. no-registration opinions will be provided in Rule 144A offerings. The local law legal opinion delivered by the issuer's counsel is often provided by the ministry of justice, the attorney general's office, or a senior lawyer within such a department. The underwriters will typically also have their own external local counsel, who will provide them with a local law legal opinion. For additional information, see Legal Opinions in Securities Offerings Checklist.

- **SEC registration documentation.** A registration statement under Schedule B and related SEC registration documentation will be required if the offering will be registered with the SEC.

- **Listing application.** A listing application and supporting documentation will be required if the bonds are to be listed on a stock exchange. See e.g., NYSE Information Submission Requirements Chart and NASDAQ Initial Listing Requirements Table.

- **DTC documentation.** DTC documentation will be required if the bonds will settle and clear through DTC.

As sovereign entities are not businesses and do not produce financial statements, sovereign disclosure documents do not contain financial statements or audit reports, and auditor comfort letters are not issued in sovereign bond offering transactions.

Certain certificates, authorizations, or other documents may also be required under the issuer's domestic law. The type of authorizations that are required, from what bodies they are obtained, and the type of documentation that evidences them will vary from one country to another depending on the features and requirements of its particular legal regime.

Provisions in the terms and conditions of sovereign bonds that are frequently negotiated include the following:

- **Negative pledge.** Common negotiating points in the negative pledge are the definition of the other debt to which the provision relates and the definition of permitted security interests.

- **Covenants.** Covenants tend to be minimal in sovereign bonds, and bonds of investment grade sovereign issuers frequently include only a negative pledge with no additional covenants. For developing country issuers or other sub-investment grade issuers, there may be a limited number of additional covenants, which will be negotiated. These covenants may include, for example, maintenance of the authorizations that are necessary for the issuer to comply with its obligations under the bonds, and maintenance of membership in and eligibility to utilize the general resources of the IMF (although these may sometimes be stated as in the form of events of default rather than covenants). For additional information on covenants, see Covenants: High Yield vs. Investment Grade.

- **Cross-default provision.** Common negotiating points in the cross-default provision are the definition of the type of debt that will be subject to the provision and the minimum level of debt that can trigger a cross-default.

- **Collective action clauses (CACs).** CACs are provisions that set out the bondholder voting requirements for approving amendments to the terms of the bonds, and provide that a specified percentage of bondholders (generally a super-majority) can agree to an amendment and the result will be binding on all holders, including those who did not vote or who voted against the amendment. CACs are designed to facilitate a relatively quick and orderly bond restructuring in the event of a sovereign bond default. In particular, they make it more difficult for a minority of dissenting bondholders (so-called "hold-out creditors") to obstruct or delay a sovereign bond restructuring. In the past, the inclusion of CACs and their format has been a topic for negotiation; however, in recent years CACs have become widely accepted in sovereign bonds. In 2013, it became mandatory for all euro-area sovereign bonds (i.e., sovereign bonds issued by countries that have adopted the euro as their national currency) to contain an agreed model form of CACs. In 2014 and 2015, the International Capital Market Association (ICMA) published recommended model forms of CACs, which since then have been included in the terms of most non-euro area sovereign bonds with minimal negotiation.

- **Creditor engagement provisions.** Sometimes referred to as bondholder committee provisions, these define the circumstances under which bondholders can appoint a committee to represent their interests and what that committee's powers and functions will be.

Timeline

The steps in a sovereign bond timetable will vary depending on the features of the offering including, for example, whether the offering is SEC-registered or conducted pursuant to Rule 144A or Regulation S, and whether the offering is a standalone offering or is instead being made pursuant to an existing shelf registration statement or issuance program. The key stages and steps in the timeline of a typical standalone sovereign bond offering are:

Preparation Stage

- Appointment of the parties, including underwriters, lawyers, trustee (if applicable), and agents

- Conducting the due diligence process

- Drafting the prospectus or other disclosure document, including comments from the working group and drafting sessions as required

- Drafting and negotiation of the transaction documents, including: trust deed, indenture, or fiscal agency agreement (as applicable); terms and conditions of the bonds; underwriting agreement; paying agency agreement (if applicable); and ancillary documentation

- Drafting and negotiation of the legal opinions

- Obtaining governmental authorizations, as required

- Applying for credit ratings for the bonds, which will typically be assigned from one or more of the main international credit rating agencies, Fitch, Moody's, and Standard & Poor's

- Beginning the process of review and approval by the SEC or other regulator or stock exchange for any registration or listing of the bonds being offered
- Finalizing and printing the preliminary prospectus or other disclosure document

Marketing and Pricing

- Launch and announcement of the offering
- Roadshow with investors, which typically is attended by senior representatives from the issuer's ministry of finance or similar department, together with representatives of the underwriters
- Agreeing the pricing terms (including the principal amount of the bonds to be sold, the interest rate, and the maturity date) following the completion of the roadshow
- Finalizing and printing the final prospectus or other disclosure document
- Signing the underwriting agreement

Closing and Settlement (typically between three and five business days after pricing)

- Executing the bond documents (trust deed, indenture or fiscal agency agreement, and global bond certificates)
- Delivering the legal opinions and other conditions precedent documents
- Issuing the bonds and delivering the net cash proceeds to the issuer

The overall length of time needed to complete a sovereign bond offering will depend on a variety of factors, including among others:

- Whether the issuer has done offerings previously and, if it has, how recent those offerings were
- The extent to which the issuer is able to complete authorizations and documentation steps (including providing information in the due diligence process) quickly and efficiently
- The complexity of the terms of the bonds (including the extent of any tailored or innovative features)
- The features of the offering (e.g., SEC-registered offerings generally take longer to complete than offerings made pursuant to Rule 144A and Regulation S, and offerings made pursuant to a shelf registration statement or under an existing issuance program can be done more quickly than standalone offerings)

As a rough indication of the time required to complete a sovereign bond offering, a typical standalone sovereign bond offering conducted pursuant to Rule 144A and Regulation S can be completed in approximately eight to ten weeks. However, as noted above, this time period may be longer or shorter depending on all of the characteristics of the issuer and the transaction. For an example of timing in an initial public offering context, see IPO Time and Responsibility Schedule.

Due Diligence Process

The due diligence process in a sovereign bond offering typically consists of documentary review as well as meeting with senior representatives of various ministries of the issuer, representatives of the issuer's central bank, and other key government entities. Unlike in a corporate bond offering, where documentary due diligence will often consist of reviewing a large volume of contracts and other internal corporate documentation provided in response to a detailed document request list, the documentary due diligence process for a sovereign bond offering is largely based on official government documents and data, much of which are publicly available. See Question 3 above. For additional information on due diligence in general, see Due Diligence Considerations for a Follow-on Offering, Due Diligence Interviews, Management Due Diligence Questions, Auditor Due Diligence Call Topics Checklist, and OFAC Due Diligence in Securities Offerings.

Required Regulatory and Stock Exchange Filings

Regulatory and stock exchange filings for offerings of sovereign bonds are similar to those that are required for other offerings of debt securities, and the requirements vary depending on the jurisdictions in which the offering is made and where the bonds are listed. See also Question 2 regarding approvals and authorizations that may be required in the issuer's own jurisdiction in connection with the issuance of the bonds.

For an SEC-registered offering by a sovereign entity, the issuer files a registration statement under Schedule B with the SEC for the offering, and annual reports on Form 18-K going forward. While Rule 415 under the Securities Act regarding delayed or continuous offerings does not apply to registration statements filed by sovereign entities, SEC interpretive guidance and no-action letters support that certain sovereign entities can conduct shelf registrations either (i) by filing a Schedule B shelf registration statement followed by prospectus supplements for each offering or (ii) by voluntarily filing an annual report on Form 18-K in advance of an offering (and updating it as necessary with filings on Form 18-K/A) and then incorporating by reference the Form 18-K and Form 18-K/A filings into a Schedule B shelf registration statement, with prospectus supplements filed for each offering. These shelf procedures are generally available only to "seasoned" issuers, which are issuers who have filed registration statements on Schedule B within the previous five years and which have not had any material defaults on their indebtedness in the previous five years. While the SEC staff has issued numerous no-action letters over a number of years supporting the foregoing shelf registration procedures, sovereign entities planning to effect shelf registrations should request a no-action letter from the SEC staff in advance if they have not done shelf registrations previously.

Stock exchange filings by sovereign entities listing their bonds generally consist of standard listing applications and submission of supporting documentation, similar to the documentation required for listings by corporate bond issuers.

Disclosure Obligations

Question 4: What information must be made available to potential investors in connection with securities offerings by sovereign entities?

There are minimal specific disclosure requirements applicable to sovereign entities from regulatory authorities (including SEC requirements under Schedule B) or stock exchanges. However, there is a well-established and highly standardized market practice regarding the content of disclosure documents in international sovereign bond offerings, as discussed below.

A. Risk Factors

Please describe the common risk factors that are specific or unique to issuers in this industry. Have there been any recent developments or changes that counsel should be aware of when preparing these risk factors?

Investment grade sovereign issuers tend to have limited risk factors sections, and some have no risk factors section at all. On the other hand, sub-investment grade sovereign issuers and those from emerging markets often have extensive risk factors sections similar to those that would be included in the disclosure documents for corporations in emerging markets or high yield corporate bonds. For further information on drafting risk factors in general, see How to Draft Risk Factors for a Registration Statement.

Risk factors that are common in sovereign bond disclosure documents include:

Risks Related to the Issuer

- **Vulnerability to adverse developments in the global economy.** Risk factors related to global economic conditions have become more common in light of recent global economic developments.
- **Dependencies in the economy.** For example, a risk factor may be included to address a dependency on budget revenues from the country's natural resources, such as oil or metals, or a dependency on revenues from tourism.
- **Other country-specific risk factors.** There may be other risk factors included to address any country-specific economic, monetary, political, or social risks.

Recent examples of risk factors related to the issuer include the following:

Adverse external factors, instability in international financial markets and adverse domestic factors could lead to reduced growth and decreased foreign investment in Mexico. High international interest rates could increase Mexico's expenditures, low oil prices could decrease the Mexican Government's revenues, and recession or low growth in Mexico's main trading partners could lead to fewer exports. A combination of these factors could negatively affect Mexico's current account. Instability or volatility in the international financial markets could lead to domestic volatility, making it more complicated for the Mexican Government to achieve its macroeconomic goals. This could also lead to declines in foreign investment inflows and portfolio investment in particular. Adverse domestic factors, such as domestic inflation, high domestic interest rates, exchange rate volatility and political uncertainty could lead to lower growth in Mexico, declines in foreign direct and portfolio investment and potentially lower international reserves. *(United Mexican States, Prospectus dated February 8, 2016)*

High inflation could have a material adverse effect on Ghana's economy and its ability to service its debt, including the Notes. Historically, inflation in Ghana has fluctuated significantly from year to year. The annual inflation rate increased from 8.8 per cent. as at 31 December 2012 to 17.0 per cent. as at 31 December 2014. The annual inflation rate subsequently increased to 17.7 per cent. as at 31 December 2015, primarily due to increased utilities tariffs and fuel prices and the depreciation of the Cedi over the period, but decreased to 16.7 per cent. in July 2016. For more information on historical inflation rates, please see "Monetary and Financial System—Monetary Policy—Inflation". Although tighter monetary and/or fiscal policies may help to curb inflation, the impact on inflation of higher food, fuel and other import prices is beyond Ghana's control. There can be no assurance that the inflation rate will not continue to rise in the future. Significant inflation could have a material adverse effect on the Republic's economy and the ability to service the government's debt, including the Notes. *(The Republic of Ghana, Prospectus dated September 13, 2016)*

Risks Related to the Bonds and the Offering

- **Enforceability of judgments.** This is a standard risk factor for sovereigns and is specific to sovereign issuers due to their status as sovereign entities. However, the specific wording of the risk factor will vary depending on the particular characteristics of the issuer, including the treaties or conventions to which it is a party for recognition and enforcement of judgments and/or arbitral awards. See Question 2.
- **Sovereign immunity.** While sovereign issuers will generally waive sovereign immunity in the bond documents, there will typically be certain limits to this waiver under domestic and other laws, which may warrant risk factor disclosure, depending on the extent of such limitations.
- **Collective action clauses (CACs).** A risk factor is sometimes included in order to caution the investor that the bonds contain CACs and accordingly the bonds may be amended without the consent of all bondholders, including the investor.
- **Reliability of statistics.** This risk factor is particularly relevant for sovereigns that are (or are political subdivisions of) developing countries, as much of the disclosure in a sovereign disclosure document is based on official statistics produced by the issuer, and the calculation and presentation methodology used may not be in line with international standards and may have risks of unreliability.

Recent examples of risk factors related to the bonds and the offering include the following:

The notes contain provisions that permit the Republic to amend the payment terms without the consent of all holders. The notes contain provisions regarding acceleration and voting on amendments, modifications, changes and waivers, which are commonly referred to as "collective action clauses". Under these provisions, certain key provisions of the notes may be amended, including the maturity date, interest rate and other payment terms, with the consent of the holders of 75% of the aggregate principal amount of the outstanding notes. *(Republic of Turkey, Prospectus Supplement dated January 18, 2017)*

Suriname is a sovereign state and, accordingly, it may be difficult to obtain or enforce judgments against us. Suriname is a sovereign state. As a result, it may be difficult or impossible for investors to obtain or enforce judgments against Suriname, whether in an investor's own jurisdiction or elsewhere. In particular, the Government has been advised by its Surinamese counsel that foreign judgments, including in respect of civil liabilities predicated upon applicable securities laws, cannot be enforced in Suriname unless there is a bilateral or multilateral treaty in force regarding the reciprocal recognition of judgments. Suriname currently has such a treaty only with the Netherlands. Even if an applicable treaty were in effect, the recognition and enforcement of a foreign judgment in Suriname will in all cases be subject to exceptions and limitations provided for in the laws of Suriname, including, for example, that assets that are meant for public service cannot be seized. Absent a treaty regarding reciprocal recognition of judgments, in order for a foreign judgment to be enforceable in Suriname, the case will need to be submitted to a Surinamese court, which will reconsider the merits of the case. Such a submission will require, among other things, the translation into Dutch of all documents related to the foreign judgment. As a result, it may be difficult to obtain recognition or enforcement in Suriname of a foreign judgment in respect of the Notes. *(Republic of Suriname, Offering Circular dated October 19, 2016)*

B. MD&A and Business

Please provide the key discussion points that counsel should consider when preparing the business and MD&A sections for issuers in this industry.

While there are no business or MD&A sections in a sovereign disclosure document, there are certain disclosure sections that are similar and which give rise to similar drafting considerations. These sections include Economy, Balance of Payments and Foreign Trade, Public Finance, Public Debt, and Monetary and Financial System. See Question 4(C) below. While some of the data presented in such sections may be calculated and presented in accordance with IMF methodology or other international standards, a substantial amount of data will typically be official data produced by the issuing country itself (or its central bank) using its own methodology. It is common for certain parts of the country disclosure to include an MD&A-style discussion and analysis of trends in economic and financial data. For example, some sovereign disclosure documents will include an MD&A-style discussion of gross domestic product (GDP) by economic sector across the years presented. For the discussion and analysis of trends in economic and financial data in a sovereign disclosure document, the same principles that underlie good MD&A drafting should be followed.

C. Other Prospectus Disclosure

Is there any other additional or special disclosure that should be included in the prospectus or registration statement for issuers in this industry, either required by the SEC or from market practice?

Based on market practice, the following are typical disclosure topics in sovereign bond disclosure documents (with variation as to terminology and locations of sub-topics within main sections):

- **Main country disclosure:** Population; demographics; geography; history; branches/structure of government, constitution, and political parties; international relations; memberships in international organizations; and anti-terrorism, anti-money laundering and anti-corruption institutions and initiatives
- **Economy:** Recent economic trends; economic policies; GDP by source; GDP by use; principal sectors of the economy (including industrial sectors and natural resources); inflation; employment/unemployment; wages and income; social benefits; education; healthcare; pension system; environment; state-owned enterprises; and privatization
- **Balance of payments and foreign trade:** Current account; capital account; financial account; composition of trade; direction of trade; and foreign direct investment
- **Public finance:** National budget process; fiscal policy; budgets and budget performance; sources of budget revenues (tax and non-tax); budget expenditure items; and relationship between national budget and local budgets
- **Public debt:** Debt management policy; external debt and debt service; domestic debt and debt service; relations with international financial institutions; debt ratings; and description of any prior defaults
- **Monetary and financial system:** Central bank; monetary policy; money supply; foreign reserves; interest rates; exchange rates; banking industry; financial performance of the banking sector; banking supervision and regulation; foreign exchange markets; and capital markets

Data in tables is typically presented for the past five completed fiscal years, together with any available interim data since the end of the most recent fiscal year.

D. Additional Disclosure Issues

Please discuss any other special disclosure issues or advice applicable to issuers in this industry.

Official data must be presented clearly and consistently, and the methodology for preparing and presenting such data must be clearly and accurately identified in the prospectus. Similar to good practice in drafting MD&A sections for corporate issuers, the prospectus should contain a meaningful discussion of monetary and economic trends and uncertainties, political factors that may impact the issuer's ability to make payments due on the bonds, and vulnerabilities in the issuer's economy.

Underwriting Agreements

Question 5: What types of underwriting arrangements are commonly used? What are some of the standard clauses and clauses that are heavily negotiated in an underwriting agreement in connection with an offering by a sovereign entity?

Underwriting arrangements in sovereign bond offerings are generally the same as they are in corporate bond offerings. In particular, one or more investment banks will act as lead underwriters and will manage the transaction and lead the marketing of the deal, as well as underwrite the offering on a firm commitment basis. As is the case in the corporate bond market, an initial purchase and resale structure is used in a Rule 144A offering of sovereign bonds, whereby the underwriters purchase the notes from the issuer at a discount to the offer price and then resell the notes to investors, with the discount representing the underwriting commission. See Drafting the Purchase Agreement for a Rule 144A/Regulation S Debt Offering and Drafting the Bond Purchasing Agreement. For a form of underwriting agreement, see Underwriting Agreement.

Sovereign bond underwriting agreements are very similar to underwriting agreements used in corporate bond offerings, with the style and content of the agreement varying depending on its governing law. Many of the business and financial representations and warranties that are customary in corporate bond underwriting agreements are not applicable to sovereign entities, and conversely there are some provisions that feature in sovereign bond underwriting agreements that are specific to sovereign issuers or that are tailored for sovereign issuers. For example, sovereign bond underwriting agreements usually include representations and warranties focused on the power and authority of the issuer to issue the bonds, the necessary governmental approvals being in place, compliance of the issuance of the bonds with the fiscal budget and borrowing limits, and enforceability of the issuer's obligations. Submission to jurisdiction and waiver of sovereign immunity provisions are often a focus of negotiations.

Continuous Disclosure and Corporate Governance

Question 6: What specific continuous disclosure and corporate governance requirements apply to sovereign entities?

For sovereign bonds that are registered with the SEC under Schedule B and listed on a U.S. stock exchange, the sovereign issuer will be required to file annual reports on Form 18-K with the SEC. Sovereign entities are not subject to the Sarbanes-Oxley Act of 2002 certification and auditor attestation requirements.

Sovereign issuers with bonds listed on a non-U.S. stock exchange need to consider the applicability of the ongoing obligations for listings on such stock exchange. For example, if the issuer becomes subject to the European Union Market Abuse Regulation (Regulation 596/2014) due to having its securities listed on a European stock exchange, the issuer would become subject to ongoing obligations regarding control and disclosure of inside information, the compliance with which may be difficult for a sovereign entity.

Stock Exchange Requirements

Question 7: Are there any special listing or corporate governance standards required by major stock exchanges, including NYSE and NASDAQ?

While the concept of corporate governance generally does not apply to sovereign issuers, there are some special listing and disclosure requirements that are applicable to sovereign entities that list on a U.S. stock exchange or a European stock exchange. See Questions 2 and 6.

Other Key Laws and Regulations

Question 8: What are other key laws and regulations that a securities lawyer working with a sovereign entity needs to be aware of?

If you are acting as counsel on a sovereign bond offering, you should be aware of, in particular:

- **Laws and regulations applicable to international securities offerings generally.** These may include, for example, the U.S. securities laws (in particular the Securities Act and the exemptions from the registration requirement thereunder), the Prospectus Directive, and the laws and regulations (as well as liability regimes) applicable to offerings in any other jurisdiction into which the bonds will be offered and sold.

- **Laws related to submission to jurisdiction and enforceability of judgments.** It is standard practice for a sovereign issuer to be required to submit to the jurisdiction of external courts (typically English or New York courts), or to agree to the resolution of disputes by arbitration, in the underwriting agreement and the terms of the bonds. Submission to the jurisdiction of English or U.S. courts requires the appointment of a process agent, which is often the embassy or consulate of the issuer in England or the United States, as the case may be. Arbitration provisions may be included if there are issues with regard to the enforceability of court judgments by the relevant issuer, depending on whether the issuer's country is a party to an applicable convention providing for recognition of arbitral awards. It is important to note that submission to jurisdiction and enforceability of judgments are two different things. It may be possible to obtain a judgment or an arbitral award against a sovereign issuer but it may be difficult to enforce that judgment or award against the issuer's assets.

- **Laws related to sovereign immunity.** See Question 2 above.

- **International Capital Market Association (ICMA) model sovereign bond provisions.** ICMA is an industry group focused on the international debt capital markets, whose membership includes issuers, intermediaries, investors, and capital market infrastructure providers in approximately 60 countries worldwide. ICMA has published model CACs, *pari passu* clauses. See Question 9.

Regulatory Trends

Question 9: What are the major regulatory trends affecting sovereign entities?

Key trends affecting sovereign issuers (which are not of a regulatory nature per se but are of a legal nature) include the recent market developments in CACs, *pari passu* clauses, and creditor engagement provisions.

In 2014, ICMA published model English law-governed CACs and *pari passu* and creditor engagement clauses after an extensive consultation process that involved a wide range of issuers, investors, and other market participants. The model CACs are aimed at preventing future disorderly and costly sovereign bond restructurings of the type that had been experienced in the sovereign bond restructurings of Argentina and Greece. ICMA has recommended the use of these standardized provisions to facilitate orderly and efficient future sovereign debt restructurings. The model provisions also include *pari passu* and creditor engagement clauses for sovereign bonds. The most novel feature introduced in the model CACs—which received the endorsement of the IMF—is the so-called single-limb aggregated voting mechanism. This mechanism enables aggregation of votes across multiple series of bonds when agreeing to changes in bond payment terms, such as maturity extensions or principal reductions, with bondholders in each affected series being bound by the outcome of a single cross-series vote. Following their publication, the ICMA model CACs were included in full in the English law-governed bond offering by Kazakhstan, and several other countries, including Vietnam and Mexico, subsequently included ICMA's model voting provisions in their New York law-governed bonds. However, the New York law-governed bonds contained a modified formulation of the clauses that was designed to conform to market practice for New York law-governed documentation.

In 2015, ICMA published a revised version of its model CACs for sovereign bonds governed by English law, together with new model CACs for sovereign bonds governed by New York law. The updated model clauses were aimed at achieving consistency between the English law and New York law provisions while at the same time taking into account market differences. One of the key changes in the revised model clauses was an amendment to the definition of the term "Uniformly Applicable," which is a key condition to the use of the single-limb aggregated voting mechanism. The amendment is intended to clarify when that voting mechanism can be used.

The ICMA model CACs have generally gained market acceptance, and should this continue they are expected to create greater consistency in the sovereign bond markets and to facilitate smoother and more efficient sovereign bond restructurings. In particular, the standardization of creditor engagement provisions included in the ICMA model CACs is important because, as demonstrated by practical experience over the last several decades, creditor committees are valuable for addressing identified risks and achieving prompt, fair, and sustainable restructuring of sovereign bonds.

Commercial Trends

Question 10: What are the major commercial trends affecting sovereign entities?

A recent commercial trend in the area of securities offerings by sovereign entities is a focus on the role of GDP-linked securities in the sovereign debt markets. GDP-linked securities can take many forms, but they have the common feature that payments on them are dependent on the level of GDP recorded in the issuer's country. In the past, GDP-linked warrants (and similar instruments) have been issued in certain sovereign restructurings, in order to give investors who restructured their bonds (and typically made sacrifices in doing so) the opportunity to share in the upside that may be achieved following that restructuring. Thus far, GDP-linked securities generally have only consisted of GDP-linked warrants (and similar instruments) issued in the context of restructurings of existing bonds rather than as new issuances in capital raisings. However, in March 2017, an ad hoc working group consisting of investment managers, lawyers and economists from the Bank of England, together with support from ICMA and other trade associations produced a model set of terms and conditions for English law governed GDP-linked bonds, which are debt securities in respect of which interest and principal payments are indexed to GDP so as to allow both the burden of servicing interest payments and repayment of principal to adjust with the sovereign's ability to pay. In 2016, the G20 forum called for further analysis of GDP-linked bonds, and the IMF is expected to produce a paper on GDP-linked bonds in advance of the G20's 2017 spring meeting. It is contemplated that GDP-linked bonds, if accepted by the market, could be issued both as part of restructurings or in capital raisings outside of the restructuring context.

There are a number of active initiatives involving the IMF, World Bank, and various financial markets industry groups that are aimed at making the sovereign bond markets more efficient, and a number of innovative ideas are being considered. These efforts have intensified in the wake of the Argentina and Greece sovereign debt crises. The IMF has been actively involved in a number of reforms (including the CAC and *pari passu* reforms discussed above) designed to reduce the costs of sovereign debt restructurings for the benefit of debtors, creditors, and the system more generally.

Practice Tips

Question 11: What practice points can you give to lawyers working with sovereign entities?

Lawyers working with sovereign entities should be mindful of the differences between the way governmental entities function as compared with corporations. For example, when working with a sovereign entity as issuer's counsel, it will be necessary to obtain, manage, and synthesize input from various ministries, departments, and other governmental bodies such as the central bank, both with regard to disclosure as well as legal issues in relation to the transaction.

With regard to the terms of sovereign bonds, it is particularly important to focus on how the provisions in the bonds will work in the event of a default and restructuring. This is the case because, unlike corporations, sovereign entities are not subject to insolvency regimes and accordingly the contractual terms in the bonds are the primary basis for resolving a default and effecting a restructuring. It is for this reason that CACs and creditor engagement provisions are particularly important.