Black Swan Laws: in Changing Times and Seasons

By Kingsley Ong

He changes times and seasons; he deposes kings and raises up others.

He gives wisdom to the wise and knowledge to the discerning.

Daniel 2:21

Introduction[1]

In most people's living memory, recent global events have probably been the most dramatic since post–World War II. Never in recent history has there been such a perfect convergence of various crises happening together.

In the last 4 years, the world witnessed global travel restrictions caused by the COVID-19 global pandemic, the introduction of compulsory vaccination laws around the world,[2] restriction on civil liberties for those refusing to take the vaccines,[3] the 2022 Russia-Ukraine war, hyper-inflation,[4] the pressure of rapidly rising interest rates,[5] a global energy and commodity crisis,[6] a looming global food shortage crisis,[7] and social unrest.[8] The combination of all these crises has the potential to create a perfect storm, which could dwarf the 2008 GFC or even the 1929 Great Depression.[9]

In further signs of the changing of seasons, it was recently reported that BRICS[10] has overtaken the G7[11] in global GDP.[12] For the first time in living memory, the USA is encountering a true rival power in China.[13] History has shown that the period leading up to a change of world order is usually prologued by the economic downturn, the printing of money and credit, revolutions and wars, and debt and political restructuring.[14]

In such times, it is important to be prepared for radical changes which can affect every aspect of life that is normally taken for granted (including civil liberties, contract enforcement, insolvency rules, peace and social order, etc). During times of major crisis, interventions by politicians become more pronounced, and politics will focus on political, social, and financial stability—traditional rule of law will be of lesser priority.

This article will look at Black Swan laws enacted in times of crisis, where the "unthinkable" became reality.

Black Swan Laws

1. Restrictions on Private Ownership of Gold

(a) USA

The stock market crash of 28 October 1929 resulted in multiple bank failures and led to the Great Depression—the "longest, deepest, and most widespread depression of the 20th century"[15]

Many people started holding physical gold as protection against inflation and deflation. This made it difficult for the US Federal Reserve to maintain the gold standard and stabilize the economy. The Fed was constrained from increasing the money supply as a result of gold "hoarding" by the public, and this was viewed as a threat to the stability of the US financial system.[16]

In 1933, the US Government suddenly decided to nationalize gold. On 5 April 1933, US President Franklin D. Roosevelt signed the US Presidential Executive Order 6102 to "prohibit the hoarding of gold coin, gold bullion, and gold certificates within the continental United States". The Executive Order further provides that:

> Section 2. All persons are hereby required to deliver on or before May 1, 1933, to a Federal Reserve

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> Bank… all gold coin, gold bullion and gold certificates now owned by them or coming into their ownership on or before April 28, 1933…
>
> Section 3. Until otherwise ordered, any person becoming the owner of any gold coin, gold bullion, or gold certificates after April 28, 1933, shall, within three days after receipt thereof, deliver the same in the manner prescribed in Section 2…[17]

Under the *US Trading With the Enemy Act 1917* (and later amended by the *Emergency Banking Relief Act* of March 9, 1933[18]), violation of the order was punishable by a fine up to US$10,000, up to 10 years in prison, or both.

To protect against inflation, during the Great Depression, many business contracts contained "gold clauses". Such clauses allowed creditors to have the option to receive payment in gold or gold equivalent. Gold clauses were made unenforceable by the *US Gold Reserve Act* of 1934.

It was only on 31 December 1974 that private ownership of physical gold coins and bars was legalized again in the USA.

(b) Australia

The nationalization of physical gold during the Great Depression is not unique. The Australian *Banking Act 1959*[19] creates a similar regime in Australia. Section 40(2) of the Australian *Banking Act 1959* provides:

> Where the Governor-General is satisfied that *it is expedient so to do, for the protection of the currency or of the public credit of the Commonwealth* the Governor-General may, by Proclamation, declare that this Part, or such of the provisions of this Part as are specified in the Proclamation, shall come into operation, and this Part, or the provisions so specified, shall thereupon come into operation.[20]

Section 42 of the Australian *Banking Act 1959* adds:

> Subject to this Part, a person who has any gold in the person's possession or under the person's control, not being:
>
> (a) gold coins the total value of the gold content of which does not exceed the prescribed amount; or
> (b) gold lawfully in the possession of that person for the purpose of being worked or used by that person in connexion with the person's profession or trade; shall deliver the gold to the Reserve Bank, or as prescribed, within one month after the gold comes into the person's possession or under the person's control or, if the gold is in the person's possession or under the person's control on any date on which this Part comes into operation, within one month after that date.

These provisions allow the Australian Government in times of crisis to seize physical gold from private citizens and to pay compensation in paper currency.[21]

(c) UK

State restrictions on physical gold ownership also occurred in the UK. Under the UK's *Exchange Control (Gold Coins Exemption) Order 1966*,[22] all UK residents were limited to four gold coins minted after 1837. Anything in excess of that had to be surrendered for sale to an authorized dealer at a price authorized by the Bank of England. This regulation was put forward at a time of economic crisis and soaring inflation.[23] The restriction on gold ownership was removed in April 1971, and the Exchange Control Act was repealed completely by Margaret Thatcher's government in 1979, allowing British citizens to freely trade and possess gold bullion again.[24]

2. 1997 Asian Financial Crisis

In 1995, the daily volume of derivatives-based foreign currency transactions reached US$1.3 trillion.[25] Leveraged currency trading[26] was particularly prevalent in Southeast Asia. On 2 July 1997, institutional derivatives players, notably George Soros, sold off their leveraged holdings of the Thailand currency, resulting in a 38% collapse of the Thai baht and an inflation rate of 65%. This started a run on Asia's financial institutions, leading to the collapse of over 150 Asian banks, securities firms, and insurance companies.

In response to the 1997 Asian Financial Crisis, on 1 September 1997, Malaysia suddenly imposed currency controls.[27] Malaysia's unexpected currency controls triggered frustration and force majeure, and caused the termination of many foreign currency contracts linked to the Malaysian ringgit.

3. 2008 Global Financial Crisis

The 2008 Global Financial Crisis led to the near-collapse and government rescues of powerful and highly-regarded financial institutions like Bear Stearns, Bradford & Bingley, Citigroup, Fannie Mae, Freddie Mac, HBOS/Lloyds Banking Group, IndyMac, Merrill Lynch/Bank of America, Northern Rock, The Royal Bank of Scotland, Wachovia and Washington Mutual. It culminated in the unprecedented collapse of the Lehman Brothers empire and the Icelandic banks (Kaupthing, Glitinir, and Landsbanki). The 2008 Global Financial Crisis is probably the worst financial crisis since the 1929 Great Depression.[28]

As a result of the 2008 Global Financial Crisis, governments around the world sought to mitigate any future systemic risks to the global financial markets caused by OTC derivatives. They started to regulate OTC derivatives, forcing such contracts to be centrally cleared and reported to regulators, and forcing non-centrally cleared OTC derivatives to be subject to additional margin requirements.[29] The EU adopted the *European Market Infrastructure Regulation 648/2012*[30] and the US introduced *Dodd-Frank Wall Street Reform and Consumer Protection Act* of 2010[31] respectively. Other jurisdictions implemented the IOSCO recommendations through their own local laws and regulations.[32]

4. COVID-19 Pandemic

Following the outbreak of COVID-19 in December 2019, the World Health Organisation (WHO) declared the coronavirus a "public health emergency of international concern" on 30 January 2020 and characterized the outbreak as a pandemic on 11 March 2020.

Vaccines, especially mRNA technology vaccines introduced to humans for the first time, were manufactured and approved at accelerated speeds. This was followed by the implementation of compulsory vaccination laws around the world.[33] Unvaccinated people who refused to get vaccinated were subject to unprecedented restrictions on their civil liberties.[34] Such curtailment of civil liberties for refusing to take vaccines was previously unheard of.

The COVID-19 pandemic also slowed down economic activities around the world. As a result, many debtors were unable to service their debts. Various governments and regulators urged creditors to give forbearance to debtors. For example, in China, the China Banking and Insurance Regulatory Commission asked lenders to allow payment extensions to borrowers.[35] In February 2020, it was reported that China issued a "record number of force majeure certificates" to exempt local exporters from fulfilling contracts with overseas buyers.[36] As of 3 March 2020, it was reported that China had issued 4,811 force majeure certificates covering contracts worth CNY373.7 billion due to the pandemic.[37]

On 16 April 2020, the PRC Supreme People's Court (SPC) issued the *Several Issues concerning the Proper Trial of Civil Cases Related to the Novel Coronavirus Pneumonia (COVID-19) Epidemic According to the Law*.[38] On 13 May 2020, the SPC issued the *Guiding Opinions on Several Issues Concerning the Proper Handling of Enforcement Cases Related to the Novel Coronavirus Pneumonia (COVID-19) Epidemic According to the Law*.[39] These SPC guiding opinions provided guidance to the People's Courts on handling COVID-19-related cases, including suspension of the enforcement application period.[40]

On 1 January 2021, the PRC Civil Code came into force. The PRC Civil Code provides that there shall be no civil liability in respect of civil obligations that fail to be performed due to force majeure.[41] Contract parties may terminate the contract if the purpose of the contract is rendered impossible to achieve due to force majeure.[42] If a contract cannot be performed due to force majeure, the liabilities shall be exempted.[43]

Other jurisdictions have taken more drastic measures and passed legislation to impose mandatory forbearance (standstill legislation).[44] For example, the UK *Coronavirus Act 2020*[45] introduced various new laws, including forcing landlords to wait at least three months before initiating eviction proceedings for non-payment of rent for private and social accommodation.[46]

Singapore introduced the *COVID-19 Measures (Temporary Measures) Act 2020*[47] (Singapore COVID-19 Act) on 7 April 2020. The Singapore COVID-19 Act allowed for a temporary suspension of obligations to perform "scheduled contracts"[48] that were "materially affected by COVID-19".[49] Certain mandatory forbearance requirements under the Singapore COVID-19 Act were extended to 30 September 2021,[50] and then further extended to 31 March 2022.[51]

In Hong Kong, the Hong Kong Monetary Authority encouraged Hong Kong banks to take a "sympathetic stance" when dealing with customers facing financial difficulty.[52] On 23 February 2022, to help businesses survive the fifth wave of Covid-19, the Hong Kong government announced that SMEs[53] in certain sectors will be allowed to defer their retail and office rental payments by up to six months.[54] It was also reported that the Hong Kong Monetary Authority (HKMA) may direct banks to give some flexibility to owners of premises facing mortgage repayment difficulties. It was originally expected that the relief measures will be valid for three months and may be extended by a further three months, giving a total of six months of relief. This is not without controversy,[55] and eventually, the Hong Kong government only approved rent deferral for three months with no extension option.[56]

5. 2022 Russia–Ukraine conflict

The Russia–Ukraine military conflict, which started on 24 February 2022,[57] has the potential to escalate into a wider military conflict.[58] The world may be on a verge of a nuclear war.[59]

It was reported that in 2021, Russia accounted for 9.2% of the world's total nickel mine production, and holds 7.5 million tonnes of nickel in reserves. Before the military conflict, in early January 2022, nickel prices were trading at US$20,700 per tonne. On 24 February 2022, in response to the Russian offensive, nickel price rose to above US$26,000 per tonne. On 8 March 2022, the nickel market price spiked to over US$100,000 per tonne before the London Metal Exchange (LME) was forced to step in and halt trading to avoid a systemic meltdown. This price spike was accelerated by market participants rushing to unwind their hedges to cut their losses. Commentators described the events as "unprecedented", "never happened before in the history of the nickel market", "the mother of all short squeezes".[60] Noting the cancellation of nickel trading contracts, Mark Thompson, executive vice chairman of the trading firm Tungsten West, tweeted that "*to cancel Nickel trades between willing buyers and sellers is unforgivable. UNFORGIVABLE.*".[61]

Separately, it was widely reported that the assets of Russian oligarchs (who are private citizens) were suddenly seized and converted[62] due to their perceived association with Russian President Vladimir Putin.[63] This controversial expropriation action could arguably be a breach of fundamental social contract theory,[64] *pacta sunt servanda,* and rule of law principles. Unsurprisingly, China was reported to be making contingency plans to "protect the country's overseas assets from US-led sanctions similar to those imposed on Russia for its invasion of Ukraine".[65]

6. 2023 Banking Crisis

In a mere 48 hours, Silicon Valley Bank became the largest bank failure since the 2008 global financial crisis.[66] Silicon Valley Bank's demise[67] led to a collapse of public confidence in banks, resulting in more bank runs. Public confidence remains fragile, and the banking crisis may not be over.[68] The resulting collateral damage so far is the collapse of Signature Bank on 12 March 2023, and the fire sale of Credit Suisse to UBS on 19 March 2023.[69]

In a shocking twist of trite law, as part of the Credit Suisse sale, the Swedish government and the Swiss Financial Market Supervisory Authority (FINMA) decided to wipe out Credit Suisse's AT1 bondholders, whereas Credit Suisse shareholders were still able to make recoveries. This effectively made AT1 debt subordinated to equity, which was previously inconceivable and went against the expectations of the market that debt always ranked ahead of equity in insolvency.[70] Given the importance of AT1 debt as a component of the capital structure of European and UK banks, the European Central Bank (ECB) and the Bank of England were quick to express their disagreement with the Swiss authorities' approach.[71] The Singapore regulator has also actively clarified that Singapore would not follow the Swedish approach.[72] Nonetheless, this gives little comfort to Credit Suisse's AT1 bondholders who have lost everything.[73]

Conclusion

At the time of writing this article, the Russia–Ukraine war remains serious, confidence in banks remains fragile, inflation remains high,[74] the high and rising interest rates environment looks set to become the new normal,[75] the global energy and commodity markets remain gloomy,[76] and a global food shortage crisis appears more and more likely.[77]

The combination of all these crises has the potential to create a perfect storm, which could dwarf the 2008 GFC or even the 1929 Great Depression.[78] We may still yet to see the "Mother of all Black Swans".

At times like these, it is ever more important to prepare well. A few observations can be made based on my previous experience in handling the 2008 crisis:

(a) Reduce Debt

Reduce debt and leverage. Having massive debt leverage in an adverse changing market environment can be very risky even for the mightiest corporations. The new normal of high and rising interest rates, rapid inflation, tightened liquidity and reduced available funding, and severe market volatility, is unlikely to change in the near future.

(b) Reduce Counterparty Risk

Acquiring gold has been a time-tested method of preserving wealth in times of crisis. It is interesting to observe some governments are significantly loading up their gold reserves.[79] However, beware of a possible repeat of Black Swan laws restricting private ownership of gold.

(c) Retain good lawyers

When markets become volatile, time is of the essence. Decisions must be made quickly, and delays can be costly. Establish good relationships with experienced and trusted lawyers so that legal support can be obtained quickly. In a crisis, it is very likely that legal advice will be needed. The best lawyers may be conflicted and could end up acting against you if you approach them too late.

In conclusion, discerning and navigating the changing of times and seasons requires wisdom.

Notes

1. The law is stated at 10 April 2023. All views expressed in this article are those of the author only. This article is adapted from an earlier article by the author, 'Contract enforcement during the Global Financial Crisis: Lessons for the coming tsunami', published in 'Contract Law in Changing Times: Asian Perspectives on Pacta Sunt Servanda' (2022, Routledge, edited by Normann Witzleb).
2. Factbox: Countries making COVID-19 vaccines mandatory (16 August 2021), *Reuters https://www.reuters.com/world/countries-make-covid-19-vaccines-mandatory-2021-07-13/*.
3. Novak Djokovic: Tennis star deported after losing Australia visa battle (16 January 2022) *BBC News* <*https://www.bbc.com/news/world-australia-60014059*>.
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9. Marco Quiroz-Gutierrez, 'Deutsche Bank just predicted "a major recession" weeks after forecasting a "mild" one' *Fortune* (27 April 2022) <*https://fortune-com.cdn.ampproject.org/c/s/fortune.com/2022/04/27/deutsche-bank-major-recession-2023-inflation-federal-reserve/amp/*>.
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13. Ray Dalio, 'The Changing World Order: Why Nations Succeed or Fail' (2021), p 13, *Avid Reader Press*. The Soviet Union was only a military rival to the USA – but China is a rival both militarily and economically.
14. Ray Dalio, 'The Changing World Order: Why Nations Succeed or Fail' (2021), *Avid Reader Press*.
15. Charles Duhigg, 'Depression, You Say? Check Those Safety Nets' *The New York Times* (23 March 2008) <*www.nytimes.com/2008/03/23/weekinreview/23duhigg.html*>.
16. Andrew Hecht, 'The Relationship between Gold and the US Dollar' *The Balance* (18 June 2021), <*www.thebalance.com/gold-prices-and-the-u-s-economy-3305656*>.
17. US Executive Order 6102, ss.2 and 3.
18. Text at <*https://catalog.archives.gov/id/299829*>.
19. Text at <*www.legislation.gov.au/Details/C2021C00574*>.
20. Emphasis added.
21. *Banking Act 1959* (Cth) ss.43–44.
22. S.I., 1966, No. 438; text at <*www.legislation.gov.uk/uksi/1975/609/contents/made*>.
23. *See* UK Parliament, House of Commons, Debate 13 June 1966, Hansard vol.729 col. 1173–95 <*https://api.parliament.uk/historic-hansard/commons/1966/jun/13/exchange-control-gold-coins*>.
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25. Norm Franz, *Money and Wealth in the New Millennium: A Prophetic Guide to the New Word Economic Order* (Loveland, Co/USA: Ascension Publishing, 2001) 99.
26. This involves the use of borrowed money to invest in Forex trading.
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30. [2012] EU OJ L201/1 <*https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32012R0648*>.
31. 124 Stat. 1376 <*www.govinfo.gov/app/details/STATUTE-124/STATUTE-124-Pg1376*>.
32. *See* n.2 above. *See also*: Hong Kong Monetary Authority, *Non-centrally Cleared OTC Derivatives Transactions – Margin and Other Risk Mitigation Standards*, CR-G-14, September 2020 <*https://www.hkma.gov.hk/media/eng/doc/key-functions/banking-stability/supervisory-policy-manual/CR-G-14.pdf*>.
33. Factbox: Countries making COVID-19 vaccines mandatory (16 August 2021), *Reuters https://www.reuters.com/world/countries-make-covid-19-vaccines-mandatory-2021-07-13/*.
34. Novak Djokovic: Tennis star deported after losing Australia visa battle (16 January 2022) *BBC News* <*https://www.bbc.com/news/world-australia-60014059*>.
35. On 26 January 2020, *see* Fitch Ratings, 'What Investors Want to Know: Coronavirus Impact on Structured Finance in Asia-Pacific' (13 March 2020), p 2 <*www.fitchratings.com/research/structured-finance/what-investors-want-to-know-coronavirus-impact-on-structured-finance-in-asia-pacific-12-03-2020*>.
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39. Supreme People's Court, *Notice by the Supreme People's Court of Issuing the Guiding Opinions (Part II) on Several Issues of Properly Hearing Civil Cases concerning the COVID-19 Pandemic* 《最高人民法院關於依法妥善辦理涉新冠肺炎疫情執行案件若干問題的指導意見》(《第二意見》.
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41. Article 180, PRC Civil Code.
42. Article 563, PRC Civil Code.
43. Article 590, PRC Civil Code.
44. Kingsley Ong and Stan Ho, 'The Impact of COVID-19 on Asset-Backed Securitisations in Asia' in *The Securitisation & Structured Finance Handbook 2021* (11th ed, Capital Markets Intelligence 2020), ch.7.
45. Text at <*www.legislation.gov.uk/ukpga/2020/7/contents/enacted*>.
46. This became effective on 26 March 2020. The latest UK Coronavirus Act March 2022 report is available here: <*https://www.gov.uk/government/publications/coronavirus-act-report-march-2022*>.
47. Text at <*https://sso.agc.gov.sg/Act/COVID19TMA2020*≥.
48. This term is defined in the Singapore COVID-19 Act, Schedule 1.
49. *ibid*, s.9(1). *See* further Wayne Courtney, 'Contracts in the time of COVID-19: common law and statutory solutions in Singapore', ch.6 (in this volume).
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53. Small- and medium-sized enterprises.
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