



Debt relief as if justice mattered

A framework for a comprehensive approach to debt relief that works

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This report is the last in a series from the Jubilee research programme – one of the official successors to the Jubilee 2000 debt campaign – at **nef** (the new economics foundation) designed to stimulate progress towards a comprehensive and fair treatment of the crisis of sovereign debt of some of the world’s poorest nations. With concern growing about the stability of the global financial system, and the end of an unprecedented period of low interest rates now in sight, this is needed more than ever. There is a clear need for a new approach to resolving sovereign debt problems which is comprehensive, systematic, fair and transparent and above all, just.

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A new, comprehensive approach to debt relief

This report is the last in a series from **nef** (the new economics foundation) on the subject of sovereign debt.

The first was *Chapter 9/11: resolving international debt crises*,ⁱ the second was *Debt relief as if people mattered*,ⁱⁱ and the third was *Odious lending: debt relief as if morals mattered*.ⁱⁱⁱ This final report aims to draw these threads together and provide details of administrative options for implementing a comprehensive approach to debt relief. It also updates the results from the previous studies, including taking into account the effect of debt relief granted under HIPC and MDRI.^{iv} It summarises the earlier reports which can be found on our website.^v Comments are more than welcome and should be sent to david.woodward@neweconomics.org

Executive summary

This report is the last in a series from the Jubilee research programme – one of the official successors to the Jubilee 2000 debt campaign – at **nef** (the new economics foundation) designed to stimulate progress towards a comprehensive and fair treatment of the crisis of sovereign debt of some of the world's poorest nations.

With concern growing about the stability of the global financial system, and the end of an unprecedented period of low interest rates now in sight, this is needed more than ever.

As this report shows:

- Some countries are spending more than twice their education and health budgets on debt service. For example, Lebanon spends 52 per cent of its government budget on debt service compared to 23 per cent on health and education combined.
- Six times the level of debt relief currently available under global initiatives to reduce the debt of the Heavily Indebted Poor Countries (HIPC) is needed if all countries are to achieve debt sustainability – a level of debt that protects government spending needed to meet basic human development needs as well as not taxing those people who already live below the poverty line.
- The level of debt relief required to achieve debt sustainability for all lower and middle income countries is estimated at \$501 billion.
- The total available debt relief envisaged under both HIPC and the Multilateral Debt Relief Initiative (MDRI) is \$95 billion, of which \$54 billion has been allocated to the 22 countries that have completed the HIPC process.

This is before 'Odious' lending - lending made to corrupt and dictatorial regimes – currently not considered in debt relief programmes is taken into account.

This report gathers together, and updates, research previously published by the Jubilee Research programme at **nef**, and makes the case for a comprehensive new approach for debt relief for the world's most indebted nations. There is a clear need for a new approach to resolving sovereign debt problems which is comprehensive, systematic, fair and transparent and above all, just. Responses so far to such criticisms from the creditors have been grossly inadequate.

Debt relief isn't working: Current approaches to debt relief (HIPC and MDRI for poor countries, and Paris and London Club renegotiations for middle income countries) are not solving the problems of Third World indebtedness. HIPC and MDRI are reducing debt burdens but only for a small range of countries and after long delays, and at a high cost in terms of loss of policy space. While non-HIPC poor countries continue to have major debt problems and middle-income country indebtedness continues to grow. The present approach is marred by the involvement of creditors as judge, prosecution and jury in direct conflict with natural justice and by the failure to take into account either the human rights of the people of debtor nations or the moral obscenity of odious debt. It is all too little and too late.

Human rights: This report updates the calculations of debt sustainability taking human rights into account for 136 countries, first carried out in our report *Debt relief as if people mattered*, using the latest figures available and taking MDRI into account. Even after the debt relief already granted under HIPC and MDRI, 47 countries need 100% debt cancellation on this basis and a further 34 to 58 need partial cancellation, amounting to \$334 to \$501 billion in net present value terms, if they are to get to a point where debt service does not seriously affect basic human rights. None of the countries needing debt relief can afford to take out any extra debt and so a marked increase in grant aid is also needed if poverty is to be reduced and the Millennium Development goals achieved.

This is before the problem of domestic debt is taken into account. With increasing relaxation of capital controls on foreign exchange transactions and growing involvement of financial corporations in Third World domestic debt, the boundary between domestic and foreign debt is becoming increasingly blurred. Data is scarce but we make a first attempt to quantify the problem.

Odious debt: It seems inherently unfair if a blatantly corrupt and dictatorial regime can take out loans in the name of its country, but without the consent of the people, steal the proceeds and then leave the unfortunate inhabitants and their children to pay back the creditors, without those creditors taking any responsibility for knowingly lending to these odious regime. Our report, *Debt relief as if morals mattered*, calculated the cost of odious lending to 13 case study countries and showed that 10 of them had odious debt greater than their current outstanding debt and that 5 of them have odious debt greater than their national income. Lenders must be held to account for irresponsible lending, including lending that sustains regimes that violate human rights.

Mechanisms needed: We conclude that there needs to be a quasi-judicial process whereby regimes can be declared odious and mechanisms put in place for an orderly work-out of both odious and unsustainable debt. As soon as there is such a working mechanism there is going to be a need for the inclusion of existing regimes if there is not to be the unintended consequence that finance becomes a lot more expensive or even impossible for any regime which might be considered odious in future.

We recommend the creation of a panel of adjudicators chosen on a regional basis by all legislatures. These adjudicators would sit in panels of three to assess the legitimacy of all regimes at the point of regime change. Present regimes could ask for a review of the legitimacy of past governments. Where a regime was declared odious, loan agreements would cease to be enforceable in court.

Whether on grounds of the odious nature of their debts or their unsustainability, governments should be able to call for a "Fair and Transparent Arbitration Procedure" (FTAP) in which equal nominees of creditor and debtor would sit with a mutually agreed chair to determine an orderly debt work-out. All creditors would be bound by such a work-out, thus outlawing the behaviour of vulture funds.

Loans declared odious should be cancelled and compensation payable by the creditor for any debt service paid. Odious loans "laundered" by being repaid (often by taking out new loans) should be compensated for by a rolling fund, which would itself seek recompense from the original odious lender and the direct beneficiaries of the loan (ie the corrupt rulers and their associates).

Only in this way can there be debt relief **as if justice mattered**.

1. Debt relief isn't working

Debt relief in 2007

Despite nearly three decades of measures billed as serious steps to end the debt crisis, the level of third world debt is higher than ever. Many countries are spending large proportions of their gross domestic product (GDP) and their government budget on debt service (Table 1). For example, in 2005, Lebanon spent 52 per cent of its budget on debt service, well over twice its spending on health and education, while the Philippines spent 32 per cent of its budget on debt service, compared with a total of 25 per cent on health and education. Uruguay also spent 32 per cent of its budget on debt service compared with 21 per cent on the same social services, while the figures for Peru were 31 per cent and 25 per cent respectively.

^{vi} All of these are counted as middle-income countries and so are not eligible for the much trumpeted Heavily Indebted Poor Countries (HIPC) programme, or the G8 Gleneagles initiative, otherwise known as the MDRI, which only applies to countries that complete HIPC.

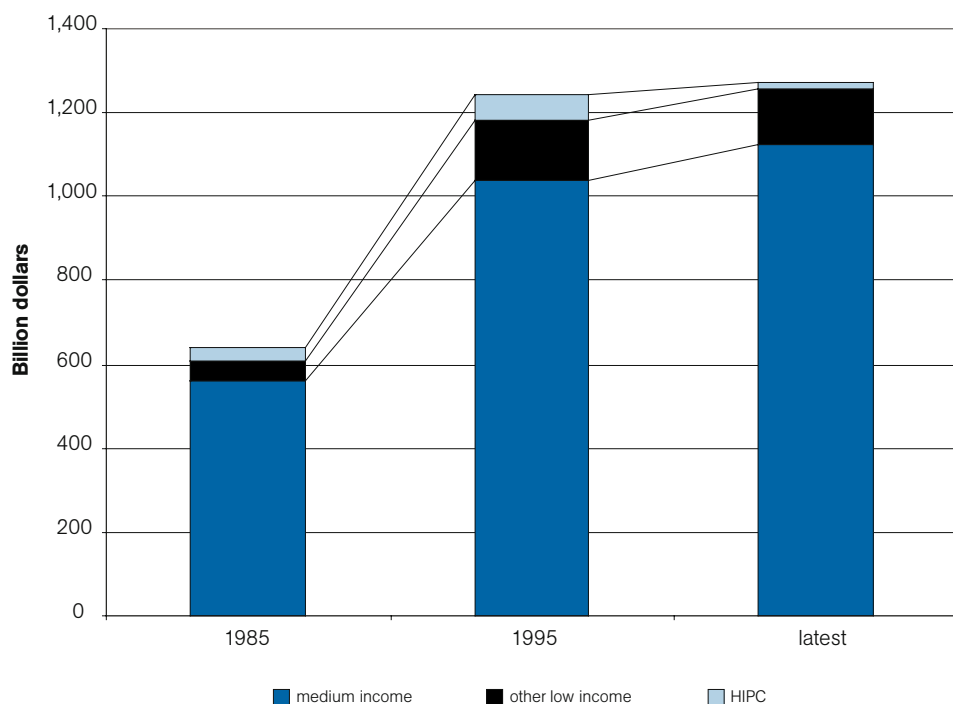
For the 22 countries that have so far (August 2007) jumped through the hoops set up by the IMF and managed to complete this programme, there has indeed been a substantial reduction in, but by no means an elimination of, debt. For the other 45 low-income countries there has not been any significant reduction, while the debt of middle-income countries has risen by a considerable margin. Figure 1 illustrates the evolution of total third world public and publicly guaranteed (PPG) debt over the last 20 years (in net present value (NPV) terms). The third column consists of data from 2005 (the latest year for which general data is available) except in the case of those countries that have completed HIPC, where post-MDRI data is used.

Table 1. Spending on debt service and on social services for selected countries 2005.

	Total debt service as a % of government expenditure	Health and education as a % of government expenditure
Lebanon	52.1	23.1
Uruguay	32.2	20.9
Philippines	31.9	24.7
Peru	30.8	24.8
Jamaica	27.9	16.1
Bulgaria	23.0	11.6
Tunisia	20.7	28.1

Debt relief at present comes in two forms: debt rescheduling and (to varying degrees) debt write-down after negotiations with the so-called Paris^{vii} and London Clubs for middle-income countries (and for low-income countries as a preamble to HIPC); and HIPC and MDRI^{viii} for low-income countries.

Figure 1. Third world debt 1985 to 2005.



All of these processes:

- reflect the imbalance in power in the present international order – they are entirely dominated by the creditors, who act collectively to deal with one debtor country at a time and who act as judge, prosecution and jury in a case where they have a major direct interest;
- only take repayability into account – both HIPC and the two ‘Clubs’ look at the ratio of debt to export earnings and (in some cases in HIPC) government revenue but fail to take any account of other demands on these resources;
- are used by creditors to further their own commercial advantage (or rather that of their multinational corporations) – International Monetary Fund (IMF) programmes are a requirement for both Paris Club and HIPC debt relief, which carry a heavy burden of economic conditionality, almost always involving privatisation, lowering of import tariffs, liberalisation of government regulation and rules of business ownership, together with a very tight fiscal stance;
- are seen by creditors as a way of exerting control over the actions of debtor governments; and
- encourage reckless lending by minimising the default risk – commercial creditors have often lent to countries that cannot realistically afford to borrow, secure in the knowledge that the IMF will back their claims for repayment regardless of how corrupt and unrepresentative the regime and (in practice and in many instances) that it will lend its own resources to governments to bail out these same commercial creditors.

They also suffer from a number of other shortcomings.

- None are comprehensive: Middle-income countries can apply for relief under the two Clubs but cannot address the question of their multilateral debt (nor do the two Clubs cover all non-multilateral creditors). Even within the low-income countries, of the 67 International Development Association (IDA)-only^x countries only 41 are considered eligible (the debt of the others is adjudged sustainable by the IMF) and MDRI covers only 4 of the 23 multilateral agencies that are taking part in HIPC. Of the four, IDA is cancelling loans drawn down before the end of

2003 and the rest (IMF, African Development Fund (AfDF), and Inter-American Development Bank (IDB)) those drawn down before the end of 2004. More recent loans remain on the books.

- Our own research shows that about 100 countries need some or all of their debts cancelled if they are to have a chance of providing the most basic services without over-taxing their economies. Under HIPC, debt repayability is calculated on the ratio of the NPV of debt to exports. No cognisance is taken of other factors, not even the level of re-exports,^x unless the economy is an unusually open one (i.e., exports are greater than 30 per cent of GDP) when the ratio to government revenue becomes a factor.
- Moreover, the results of HIPC and MDRI are patchy. (For example, the non-African HIPCs are receiving much less generous terms than the others because so much of their debt is to the Inter-American Bank,^{xi} which has not found any donor resources to fund cancellation.) HIPC has some criteria to determine how much debt is written off. MDRI starts from this and writes off more, but is arbitrary in the sense that only debts to selected international financing agencies are included.
- Nor do they deal with commercial creditor litigation, as illustrated starkly by the case of Zambia (Box 1).
- They do not take cognisance of creditor co-responsibility – as detailed in *Odious lending: debt relief as if people mattered*, creditors must take a share of the responsibility for knowingly lending to corrupt and unrepresentative regimes where the population obtained little or no benefit from the loans.
- They fail to take the millennium (or other) development goals (MDGs) into account – as spelled out in *Debt relief as if people mattered*, governments have an obligation to provide for the welfare of their citizens and, at the very least, creditors should not stand in their way by demanding that debt servicing come before basic welfare. Again, creditors should take co-responsibility for lending to countries that clearly cannot afford to repay, just as creditors to individuals have to accept that those individuals may go bankrupt and the debt will then be written off and in this manner the creditors take responsibility for irresponsible lending. With countries (that have to carry on providing essential services to their population just as local authorities do) some provision (such as those under Chapter 9 of the US bankruptcy laws for local authorities) must be made for this to take precedence over servicing debt.
- They ignore other fundamental problems – for example, the fact that poor countries are typically in a weak position regarding many policy decisions, such as the determination of tax rates when they are facing steep competition from others in trying to attract foreign investment, or the freedom to tax imports when IMF/World Bank (WB) conditions, World Trade Organization (WTO) rules and bilateral trade agreements are all pressuring them to reduce tariffs. They are also at a disadvantage when negotiating prices and tax regimes with transnational corporations (TNCs) that will often have a turnover many times the host country's GDP, and they are frequently unable to prevent transfer pricing by TNCs depriving them of their tax base.

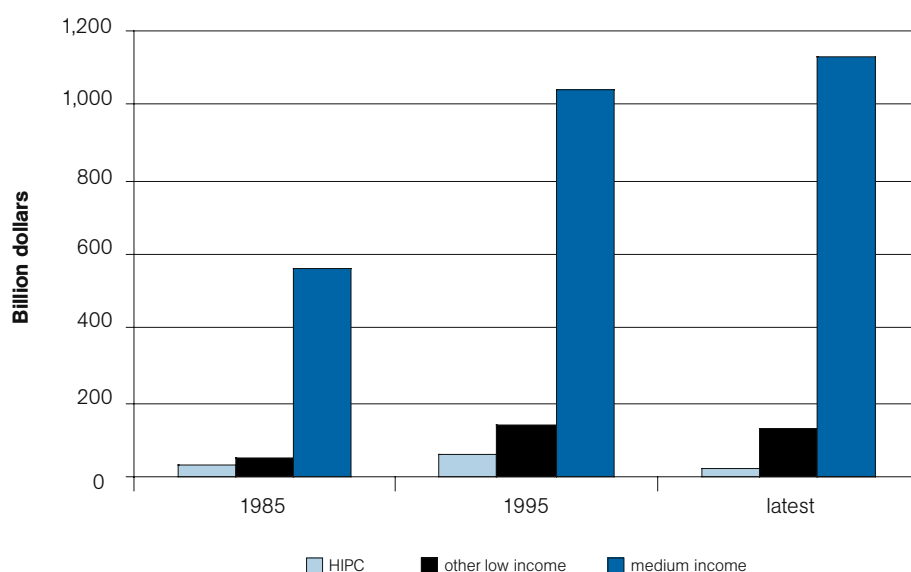
These flawed processes have had many adverse results:

- Many countries are stuck in a cycle of dependency and poverty.
- Debt relief is always too little, too late^{xii} – there have often been long delays before a country joins the HIPC process (i.e., reaches decision point^{xiii}) but even after this, the average length of time before full debt relief is available has been 37 months, during which time countries are required to keep up with their debt servicing, sums which are not recoverable. It is hard for observers of their behaviour on the ground to believe that a permanent end to the debt crisis is what the majority of creditors really want. Their actions belie this. It is clear that they do not really want to see a reduction in their control over the actions of debtor governments.

- The conditionality of IMF programmes condemn populations to severe hardship as a result of inadequate services, and to poverty from inadequate education, infrastructure etc. Resistance is growing (for example, in Kyrgyzstan, there have been many demonstrations against that country joining the HIPC process, resulting in the government deciding in March 2007 not to proceed with its application) but countries seldom have any choice under the present dispensation. Indeed, Kyrgyzstan may end up with the worst of both worlds, since it has decided to go ahead with a PRGF (Poverty Reduction and Growth Facility), which includes the conditions so many people object to, but not with HIPC, which at least brings debt relief in the end.
- Growing polarisation within and between countries – one of the results of IMF/WB conditionality has been the growing inequality within countries as a result of the poorly administered privatisation of state assets, the reduction in social services as countries have struggled to meet IMF requirements for reduction in budget deficits, the sacking of staff as the civil service and state-owned corporations are pruned, the increase in user fees for government services and utilities, the switch from import tariffs to value-added tax (which is generally a regressive move) and the elimination of government subsidies.^{xiv} There is also growing polarisation between countries as those who remain burdened by debt service fail to provide the infrastructure, education, health facilities etc., which might enable them to reduce poverty, while opening up their economies to transnational corporations in an attempt to pass through the hoops necessary to win IMF approval and some measure of debt relief. Instead, they fall further and further behind and become more subject to the nostrums of the IMF/WB whose model of development has so blatantly failed.

Figure 2 shows the net impact of debt relief and new lending on PPG debt stocks between 1985 and 2005, the latest figures available. We have inserted estimates of completion point HIPC debt after MDRI for this graph. It can be seen that for those HIPCs that have reached completion point, the process has had a significant effect on their overall indebtedness, reducing it from \$81 billion in 1995 to \$18 billion after MDRI. However, the impact of other measures has been negligible, and new lending, growth in penalties and arrears etc., have outweighed any debt cancelled to other countries, even though the period spans the Argentinian default and restructuring of 2002. The debt of other IDA-only countries went down a little between 1995 and 2005 (from \$142 to \$129 billion) while debt of the middle-income countries went up from \$1,038 to \$1,127 billion.

Figure 2. NPV of PPG debt 1985, 1995, and latest.



2. Towards a new approach

Overall rationale

The world needs an approach to debt management which:

- is comprehensive and fair (both to creditors and debtors);
- addresses the deficiencies summarised above;
- guards against unintended adverse consequences (for example, it helps to maintain the flow of new and rollover finance to those that can afford and need it);
- can take human development needs into account;
- examines the origin and circumstances of loans; and
- takes account of the need for creditors to exercise due diligence and to take their share of the responsibility for loans which go wrong for a variety of reasons.

Such a process needs to have the capacity to operate in the present international system, despite all the latter's imperfections.

In *Odious lending: debt as if morals mattered*^{xv} we discuss the typology of illegitimate debt. It is useful to distinguish between:

- illegal debt (where due process has not been followed in the contracting of the debt – such as when the signatory was not authorised to sign or the requisite procedures for approval of the loan were not followed);^{xvi}
- odious debt (where due process may have been followed but the regime contracting the debt had no right to impose the obligation of repayment on its successors because it itself lacked legitimacy and the creditors were in a position to know this); and
- onerous debt (where the terms of the loan were unfairly onerous) and other areas where the creditor was at least co-responsible for the failure of the loan to bring benefits to the people of the debtor country (for example, because of conditions attached to the loan, poor project design, or bad policy advice from the creditor).

All these can be considered illegitimate.

Creditor response to the criticisms

Some attempt has been made to propose alterations in the debt architecture to meet some of the criticisms mentioned above. This section summarises the current state of play.

CAC and SDRM

Collective Action Clause^{xvii} (CAC): One of the problems in the way of orderly debt work-out negotiations is often called the 'freerider' problem. If a country gets into difficulties and attempts to negotiate a settlement with its creditors, any one creditor may try to hold back from the settlement in an attempt to get better terms once the bulk of the debt has been rescheduled, thereby improving the country's financial viability. The Paris and London Clubs are pledged to negotiate together and to accept an equal 'haircut' but creditors who are not members of these Clubs and holders of bonds are not so obligated. One solution for the bond market has been the introduction of CACs. Bondholders generally opposed such clauses in the 1980s and 1990s, fearing that it gave debtors too much power. However, following Argentina's December 2001 default on its debts in which its bonds lost

70 per cent of their value (Box 2), CACs have become much more common, as they are now seen as potentially warding off more drastic action, but enabling easier coordination of bondholders. For those bonds which have them, CACs mitigate one of the flaws of the present system, whereby individual creditors can hold back from the settlement and take advantage of the relief to claim a better settlement for themselves, as is exemplified in extreme form by vulture funds (Box 1). Nevertheless, this feature does little to address the main concerns about the present system of debt management outlined above, notably the failure to take account of official and bank debt, of creditor co-responsibility and of the human-rights approach to debt sustainability.

Box 1: Zambia and the Vulture Fund

Zambia, which thought it would have at its disposal \$42 million in extra resources in 2007 as a result of the MDRI process, has since been sued in the London courts by a 'vulture' fund – Donegal International – for \$55 million in interest, penalties and the full principal. The fund bought some of Zambia's debt to Romania in 1999 (at the heavily discounted price of \$3.3 million), only shortly before it was due to be cancelled. Despite condemnation of the action by Gordon Brown and other key figures and civil society generally, a British judge has already found in favour of the fund in principle, though he criticised the firm and its witnesses. He has decreed that Zambia has to pay \$15.5 million, which is an outrageous return for 'investing' \$3.3 million eight years ago.

Box 2: Argentina: the one that got away

Argentina had pegged its currency to the dollar in 1991 in a (successful) attempt to combat hyperinflation but the corollary of this was an over-valued currency, currency flight and an ever-increasing debt so that by 1999 the country entered recession. The day of reckoning was postponed by a series of debt re-schedulings and IMF loans but the fundamentals remained unchanged. By 2001, this had developed into a full-blown crisis with a run on the banks as people sought to convert their savings into dollars and when investors lost confidence, the flight of money turned into a flood. Discontent flared and the President (de la Rúa) resigned. Within days the interim government defaulted on public debt (which at that point stood at about \$90 billion), and within a month the peso was allowed to float. Despite intense pressure from the IMF and others (and the dire predictions of most economists), the Argentine Government insisted on a restructuring of its debt which resulted eventually in 76 per cent of the defaulted bonds being exchanged for new ones at between 25 and 35 per cent of the original nominal value and at longer terms. 2002 was a difficult year for Argentina but since then things have been turned around. Helped by strong demand for soya beans, exports soared, the peso is back to about three to the dollar (having touched four at one point); foreign exchange reserves rebounded to the extent that in December 2005 the country was able to repay early all outstanding IMF debt (at par); growth averaged about 9 per cent a year from 2003 onwards; inflation, which had increased briefly with the devaluation to a peak of 10.4 per cent in the month of April 2002, fell rapidly thereafter and has been running at less than 1 per cent a month since; and by the end of 2005 the poverty rate had fallen to below its pre-crisis level. By 2006, Argentina was able to issue new bonds on the international market without difficulty. The IMF itself calls this a remarkable transformation, as indeed it is, achieved by rejecting most standard neo-liberal advice.

Sovereign debt reconstruction mechanism (SDRM): In 2003, after criticism concerning the lack of a comprehensive approach to debt problems, the IMF proposed to introduce the SDRM.^{xviii} It was designed primarily to cater for the large increase in bond issues relative to bank loans as a source of finance by some (mostly middle-income) countries. It would act rather as an imposition of a CAC for all commercial debtors, regardless of whether one existed for the particular bond issue or not. As proposed, SDRM has the merit of recognising the possible need for unilateral action initiating a freeze on debt service, the need for CACs and the probable need to impose controls on the movement of capital in the foreign exchange market to prevent capital flight, while negotiations are carried out. It has,

however, received very little support and is unlikely to progress. From the creditors' point of view it appears to threaten to put more power in the hands of the debtors, and they are worried it would make it too easy for debtors to default. Nor is it clear that it would be comprehensive, in so far as the IMF has not taken a clear stand as to whether it would replace the Paris Club. From the point of view of the debtors, it suffers primarily from the fact that the IMF put itself at the heart of the process, thus incorporating one of the flaws of the present system – that creditors have a conflict of interest by being both party to the dispute and arbiters of it. Another problem is the distrust of that institution generated by the effects of the last 25 years' disastrous advice and by the present governance of the IMF, which gives the creditor countries almost complete control.^{xix} Nor does it envisage an automatic stay on creditor litigation, though the IMF claims this would be 'discouraged'.^{xx}

There is also no evidence that it would take any wider view of debt sustainability than the narrow debt 'repayability' measures currently used by the Bretton Woods Institutions (BWI). The IMF's debt sustainability framework could be refocused from its present application to future lending for use in debt restructuring and now has greater sophistication in that it looks at a range of economic scenarios and looks at the probabilities of debt distress. Nevertheless it still has at its centre a concept of debt repayability that ignores human rights and the demands on the government budget other than for debt service. This also limits the value of any restructuring under IMF auspices.

Odious debt doctrine

Introduction

It seems inherently unfair if a blatantly corrupt and dictatorial regime (such as that of Mobutu Sese Seko in Zaire, Ferdinand Marcos in the Philippines, or General Galtieri in Argentina) can take out loans in the name of its country, but without the consent of the people, steal the proceeds and then leave the unfortunate inhabitants and their children to pay back the creditors, without those creditors taking any responsibility for knowingly lending to these odious regimes. Yet this is what is currently happening, not only in what is now the Democratic Republic of Congo, in the Philippines and in Argentina, but in Indonesia, Chile, South Africa and so on, often long after the perpetrators have left the scene.

The doctrine of odious debt has been rising up the international finance agenda in recent years. Not only are civil society organisations in both North and South giving it a high profile in their campaigns – it was given explicit mention in American efforts to get debt cancellation for Iraq after the 2003 war.^{xxi} In early 2007, there were no less than two conferences within a month at American universities on the topic.^{xxii} A major review of the doctrine was published by the Centre for International Sustainable Development Law of Canada in a working paper, *Advancing the odious debt doctrine*, for the Canadian Ecumenical Jubilee Initiative in March 2003 which examined in detail the status of the concept in international law.^{xxiii} Jeff King, one of its authors, concluded: *'The analysis ... indicates that the doctrine of odious debt can be clearly defined, has a fair bit of support under the traditional categories of international law, and can be modified to withstand prima facie theoretical objections ... after examining the state practice, general principles of law and writings and judicial decisions, it seems that there is much more material available to make such an argument than one would initially think. If nothing else, I hope that this paper has succeeded in establishing that there are legally persuasive arguments in favour of the morally compelling doctrine of odious debt.'*

Kremer and Jayachandran proposal

In a paper published in April 2005, *Odious debt*, by Seema Jayachandran and Michael Kremer^{xxiv} on the UCLA Department of Economics website, the two Harvard/UCLA economists update a paper they published on the IMF website^{xxv} (and elsewhere). This argues for the setting up of a sufficiently well-respected international body to adjudicate on the odiousness of *current* regimes and to declare that *future* loans to these regimes would be odious and unenforceable,

while leaving the question of past loans aside [author's emphasis]. They argue that this form of sanction would be more effective than trade sanctions, which countries have an incentive to evade. The appearance of this paper on the IMF's website suggests that the idea is gaining respectability, even in unlikely circles.

The conference at Duke University in January 2007 was wide-ranging but focused more on the question of whether it was possible to use the common law applied to domestic debt to deal with sovereign debt since about 90 per cent of all debt instruments are required to be interpreted under the law of either New York State or England. In a paper connected with this symposium, Bucheit, Gulati and Thompson argue that, since the 1970s, sovereign governments can be held to account in the courts of Britain and New York but can also call on defences recognised by those courts against the enforcement of loan contracts.^{xxvi} Such defences include situations where the claimants used bribery to suborn the agents of a principal (here the principal can be taken as the people of the country concerned, and the person signing the loan as the agent), or were otherwise engaged in illegal activity, or where the said agents were known by the creditor to be acting against the interests of the principal. In contrast to Jeff King, they further argue that the problems of definition for a general doctrine of odious debt are so great that the chance of there being sufficient international acceptance of such a doctrine is very remote. However, despite this, the idea of repudiating an odious debt and defending this in court has yet to be tried, though the lack of success attending Zambia in its attempt to fend off the vulture fund, Donegal International, is not encouraging. Admittedly, it seems that Zamiba has not suggested that the original loan was odious, though there are suspicions about the way in which Donegal International acquired the loan from Romania.

Jus Cogens^{xxvii}

There is a strand of legal opinion that argues that the concept of *jus cogens*, or peremptory law, can be used to deal with illegitimate debt. Where there is sufficient acceptance of such a concept at an international level (whether witnessed by convention or by the signing of United Nations (UN) conventions etc.), it can be enforced through national or international courts. For example, enforcement of the prohibition of genocide or slavery is compulsory for all nations, and individuals or governments who ignore these practices can be prosecuted even if they have not signed any particular treaty. Thus if a loan contract can be shown to violate a UN convention, for example, the Convention on the Rights of the Child, it could be challenged. Similarly, a debtor shown to have broken such prohibitions could be considered odious, and any loans extended to that debtor could be deemed odious loans.

Conclusion

There is as yet no consensus about the way forward. It is clear that the present system is not working – overall debt is rising, and the little debt relief that is being granted only reaches a small range of countries, typically after severe delays. There is also a high cost in terms of loss of policy space for debtor governments, and in terms of thwarted human development for the countries concerned. In short, the mechanisms that exist are so dominated by the creditors that basic norms of fairness between contending parties are violated and the welfare of the world's poorest is seriously damaged.

Our two recent studies attempted to assess the extent of the problem quantitatively. *Debt relief as if people mattered* estimated the level of debt that each country could sustain, and thus estimated the amount of debt relief required to bring debt down to a sustainable level. *Odious lending: debt relief as if morals mattered* estimated the extent of odious debt for a selection of 13 countries that had been ruled in the past by clearly odious regimes.

3. Debt sustainability

Introduction

Our approach to debt sustainability is founded on the belief that it is a fundamental human right to have basic needs met – food, clean water, shelter, education and health.^{xxviii} Yet 45 per cent of the world's population live on less than \$2 a day,^{xxix} at which level life expectancy is markedly reduced because the ability to meet these needs is restricted.

This restriction is partly the result of the high costs of debt service. Twenty countries spend more than 20 per cent of their budget servicing foreign debt,^{xxx} and in many of the world's poorest nations, debt-service payments have taken precedence over providing people with the most basic services. The BWI's concept of debt sustainability does not take a country's ability to provide such basic needs into account, and should rather be called a concept of debt *repayability*.

The UK and other Northern governments like to paint a picture of their generosity in giving debt relief to the poorer countries of the world. In fact, the net flow of resources from North to South (that is the flow taking both net capital flows and interest paid on loans into account) would be negative were it not for grant aid (which includes debt cancellation). Even allowing for this, the *total* net flow from North to South over the 34 years since 1970 amounts to a paltry \$92 per person living in the South. This is less than \$3 a year, little more than one-fifth of the average British child's **weekly** pocket money.^{xxxi} This is before we take account of the fact that the world's trade is largely in the hands of multinational corporations that can transfer prices to minimise the taxes they pay, and play one country off against another in a 'race to the bottom' to attract investment by offering ever more favourable tax and subsidy regimes. Nor does it acknowledge the wealth transferred by force during the colonial era, a transfer upon which the development of the North is largely founded. The picture is not one of any generosity on the part of the North.

Human rights and debt cancellation

National governments have an obligation to provide for the basic needs of their citizens. If a government can only meet its debt service payments by curtailing the provision of basic health and education services, or by taxing poorer citizens so heavily that they cannot pay for enough food or shelter, **this violates human rights**, and the creditors bear the responsibility for this violation. The amounts currently committed to relieve the debts of low-and middle-income countries fall far short of the levels needed to avoid this unacceptable situation.

In adopting the UN millennium development goals (MDGs), all the world's countries have made a commitment to reduce global poverty by 2015. The MDGs also reinforce earlier commitments to universal rights, including those pertaining to health and education. But the MDG targets will be impossible to meet as long as developing countries have to use such a large proportion of their resources to meet crippling debt-service payments.

Our approach to debt sustainability, therefore, takes as its starting point an assessment of the level of revenue that a government can realistically be expected to raise without increasing severe poverty or compromising future development. This means not taxing those people who already have less income than they need to fulfil their basic rights, and ring-fencing government spending needed to meet basic human development needs.

An ethical poverty line

Recent research shows that life expectancy falls off at an astonishing rate below a mean income of \$3 a day (taking into account relative prices), as illustrated in

Figure 3 below.^{xxxiii} At this level, life expectancy in a country is very roughly 70 years, while at \$1 a day it is in the region of 40 years. We therefore adopt an 'ethical poverty line' of \$3 per person per day – a level more compatible with the human rights to health (as represented by a reasonable life span) than the \$1- and \$2-a-day poverty lines used by the World Bank and others. Of course the relationship between a mean income of \$3 a day and the proportion of the population earning less than \$3 a day will vary depending on how skewed income distributions are. Further analysis involving the relationship between mean life expectancy and the proportion of the population living on different incomes is needed to refine this outcome. Nevertheless there is a strong argument for a higher figure than \$2 a day.

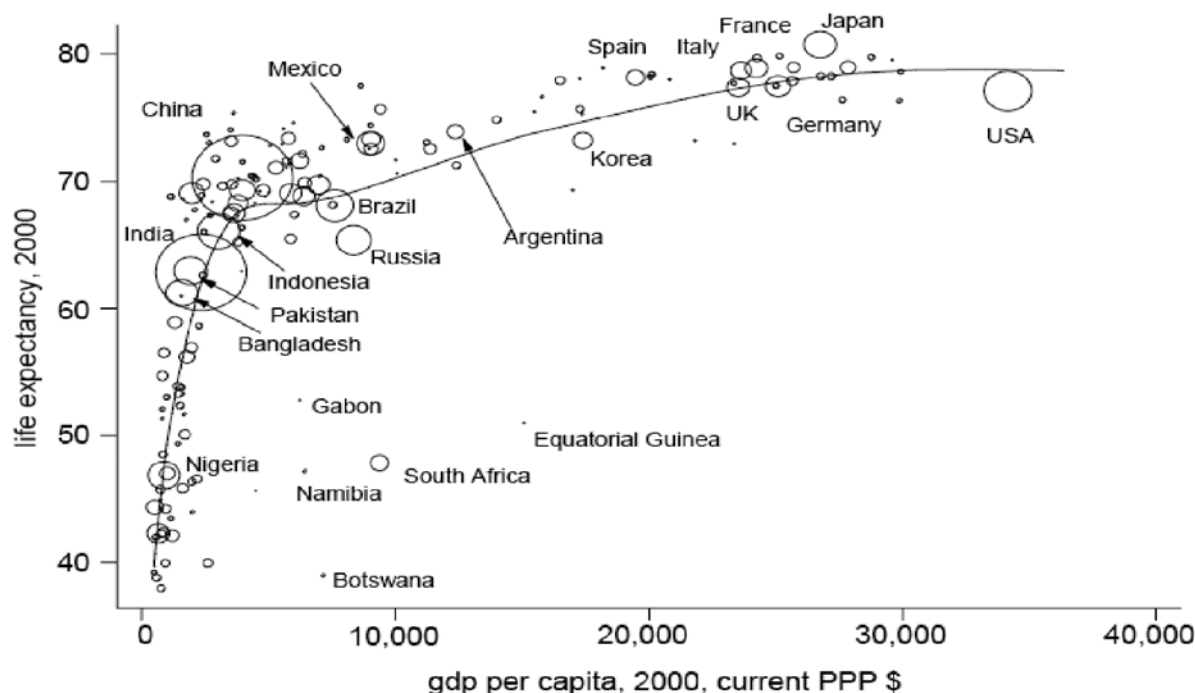
Calculating sustainable debt

We therefore calculate the taxable proportion of national income by deducting \$3 a day for each person living on more than this amount and actual income for those living on less. (We also carry out the same exercise using the World Bank's \$2-a-day poverty line.) We then estimate **maximum feasible gross revenue** as 25 per cent of this taxable national income, assuming that tax rates to generate revenue above this level would be too distorting to the economy.

From this maximum feasible revenue we deduct basic minimum expenditure on health, primary education and social expenditure to give **net feasible revenue**. Of this net feasible revenue, we then assume that between 20 per cent and 40 per cent could be set aside for paying interest on external debt. From these annual payments, we estimate the maximum NPV of debt which could be carried without violating human rights, and compare this with the current level of debt for each country.

Figure 3. Relationship between mean per capita income and average life expectancy

Source: Deaton (2003) quoted in Edward (2006).



Results

Based on these assumptions, and using data for 136 countries from 2005, we calculate how much debt cancellation each country would need to reduce its debt to a sustainable level.

- Of the 136 countries surveyed, between 43 and 47 need complete cancellation of their debts, and between 32 and 58 need partial cancellation on human rights grounds (depending on the poverty line and the proportion of net feasible revenue devoted to debt service).

- Based on the ethical poverty line of \$3 a day, the NPV of debt that should be cancelled is between \$334 and \$501 billion.^{xxxiii} This is far more than is envisaged under the current HIPC programme (under which the *maximum debt* which might be written off is \$44 billion for 30 countries post decision-point countries^{xxxiv,xxxv}) and MDRI which could at most amount to \$24 billion even if all countries qualified.^{xxxvi} These figures for debt relief available from existing programmes include \$41 billion and \$20 billion from HIPC and MDRI respectively that had been disbursed by December 2005, and so are not included in the totals for debt relief still required at that date by our study.
- Our recommended debt cancellation amounts to between 24 and 35 per cent of all outstanding developing-country debt and amounts to nearly ten times the amount currently envisaged. **This sounds a lot until it is compared with the shortfall of aid below the target of 0.7 per cent of rich countries' GDP, which was \$120 billion in 2005 alone. If the North had met the target each year between 2001 and 2005, it could have more than wiped out all this debt.**

Table 2. Summary of results, human-rights approach to debt cancellation.

Assumptions		Number of countries needing 100% debt cancellation	Number of countries needing partial debt cancellation	Total amount of debt cancellation (\$bn, present value)
Poverty line	Debt-service as %of nfr			
\$2 pd	20	43	54	425
	30	43	39	310
	40	43	32	241
\$3 pd	20	47	58	501
	30	47	39	398
	40	47	34	334

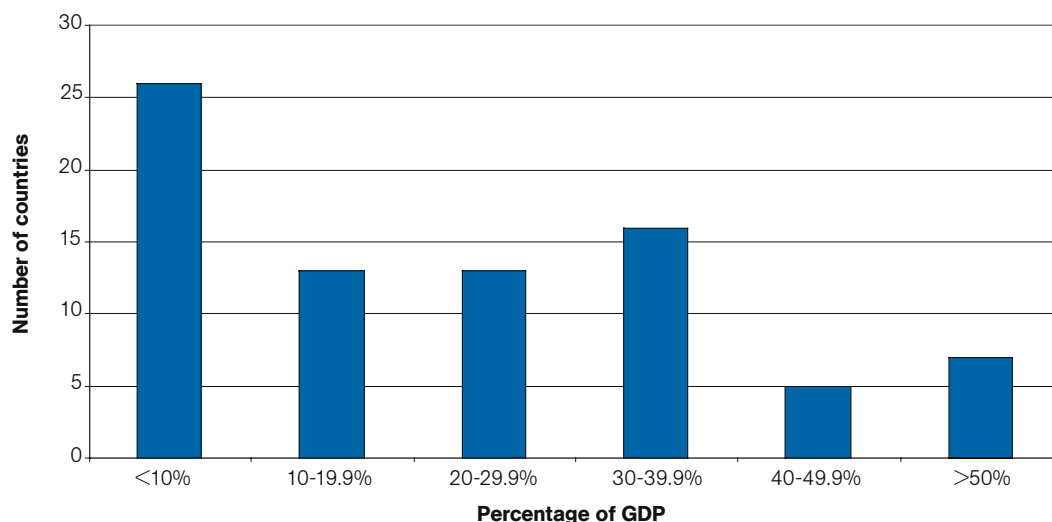
nfr = net feasible revenue pd = per day

Domestic debt

All major discussions to date have focused on foreign debt. However, with the increase of freely convertible currencies, and the ending of capital controls in many countries, the difference between foreign and domestic debt is becoming blurred. Particularly in middle-income countries, but even in some low-income countries, domestic debt is becoming a target of interest for international investors looking to increase returns on their investments, and the level of such debt can be high. Statistics are not yet being gathered consistently on foreign holdings of domestic debt, and remarkably little data is available from central databases such as the IMF's International Financial Statistics on domestic debt, regardless of the holder. Nevertheless, the demand on government resources resulting from domestic debt can be very great,^{xxxvii} and the vulnerability of the economy to shocks and speculative flows is high when a large proportion of domestic debt is held by foreign investors. Indeed the division between domestic and foreign debt becomes very blurred in the absence of capital controls and in the presence of funds that actively seek out high profits from the 'carry trade'.^{xxxviii} Actively managed funds are willing to take risks with the greater volatility of exchange rates in order to realise greater profits.^{xxxix} The fact that they are actively managed means that the risk of 'herd' behaviour resulting in surges of foreign exchange into and out of these countries is all the greater.

Figure 4 illustrates the distribution of the ratio of domestic public debt to Gross National Income (GNI) for the 75 countries for which data could be collected. Lebanon and the Seychelles top the list with domestic debt almost equivalent to their national incomes. Egypt and Jamaica come next with domestic debt amounting to about 75 per cent of national income. Three others have debt over half their national income, and over 40 per cent have debt over one-quarter of their national income. For details see Appendix 2. These levels are bound to restrict severely the funds available to governments to meet the basic needs of their populations.

Figure 4. Domestic debt (ratio to GNI or GDP).

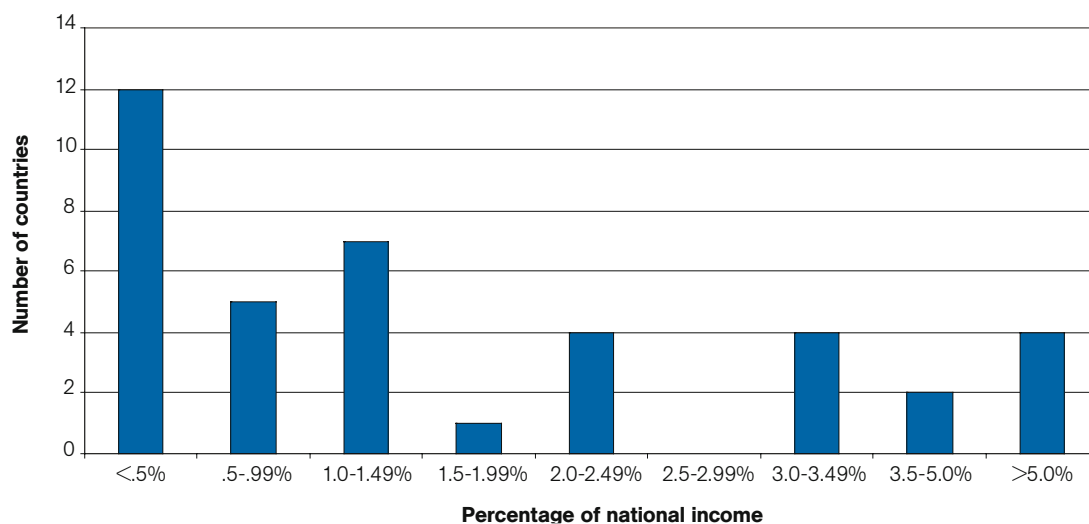


Interest rates vary widely between countries, however, and a total debt burden that is feasible in one country with low interest rates may be quite unsustainable in another, so the key question is not so much the size of the debt itself as the level of debt service. This data is even less easy to obtain. Figure 5 presents the data for 39 countries. More than a quarter (10) are paying out more than 3 per cent of national income on interest on domestic debt. Jamaica is paying out over 10 per cent, while Turkey and Brazil are paying over 8 per cent and 7 per cent respectively. Given that the maximum tax take that can be expected is of the order of 25 per cent of GNI, this means that a very high proportion of the national budget is preempted by interest payments for these countries. This is a serious situation.

Some countries are increasing their domestic debt in order to pay off international debt. In many instances this will mean swapping lower-interest international debt, which nevertheless carries a foreign exchange risk, for higher-interest domestic debt. Some countries may decide to do this in order to free themselves from the conditionality imposed by the IMF. On the other hand, an unsustainable level of foreign debt may force a country to rely on raising domestic loans merely to pay the interest on its foreign debt. This is completely unsustainable, for obvious reasons.

This problem will need to be taken into account in a comprehensive debt settlement, and the issue also raises other important questions. The treatment of purely domestic debt would seem to be a matter for domestic law, for instance – but the treatment of domestic debt held by foreign entities may need to be different.

Figure 5. Interest on domestic debt as share of GNI.



4. Odious debt

The concept of odious lending

Odious debt is a subset of illegitimate debt. Alexander Sack, who first codified the concept in 1927, defines a loan as odious if:

1. there is a lack of consent on the part of the people;
2. there is a lack of benefit; and
3. the creditor was in a position to know the above.

We argue that it is not necessary to prove the lack of benefit, as all loans to odious regimes (whether used for laudable or fraudulent purposes) ease the foreign exchange constraint and thus release domestic funds for other, possibly nefarious purposes. Given that any strengthening of an odious regime can be regarded as entrenching it (thus prolonging the period of oppression), no loan to an odious regime can be considered wholly innocent.

The effect of odious lending

The repercussions of odious debt reverberate for many decades after an oppressive and corrupt borrower regime may have left the scene. Not only are successor governments saddled with paying off the loans themselves, but because the loans were often not put to productive use, the funds needed to pay interest and repay capital were not generated. The result is that resources have to be diverted, or new loans have to be taken out, to service the odious ones, whatever the legitimacy and colour of the successor government, effectively 'laundering' the original loans. This defensive lending can give a legitimate cloak to odious debts.

The results of odious lending

Taking 13 case studies, we show that the impact of such odious debts is to absorb much (and often all) of the net benefit from international loans and so, long after odious debts are technically off the books, subsequent generations are still effectively paying for them. The net loss often exceeds the total outstanding debt. The people in these – often desperately poor – countries end up paying three times for the loans ostensibly taken out in their name: first they are oppressed by the regimes propped up and enriched by these loans; secondly they are impoverished by the cost of servicing the loans; and thirdly they are oppressed again by the penalties imposed if the odious regimes default. If debt cancellation only comes through Paris Club negotiations and the HIPC initiative, they pay a fourth time when IMF conditionality (without which a loan deal is currently not available) imposes the often disastrous policies of trade and capital account liberalisation, privatisation, and restriction of social expenditure.

We consider it a basic principle that a country should be no worse off as a result of odious lending than it would have been had the loan never been advanced. We therefore estimate how much debt cancellation and compensation would be needed to achieve this. This is done by disregarding the initial flow from the disbursement of the loan, capitalising all interest paid on odious loans and only allowing debt cancellation to reduce the total of odious debt once any legitimate debt had been cancelled.^{xi} We calculate total odious debt, repaid odious debt and outstanding odious debt.

The results are striking and are summarised in Table 3.

Table 3. Summary of results of analysis for the period 1970 to 2005.

Country	Total PPG Debt (US\$ billion)	Proportion of odious debt	Total Odious Debt (US\$ billion)	Cumulative Net Transfer (CNT) ^{xliii}	CNT taking Odious Debt into account	Repaid Odious Debt
Indonesia	72.3	100.0%	220.8	3.6	-140.9	148.5
Argentina	62.0	100.0%	175.8	36.2	-46.4	113.8
Nigeria	20.3	100.0%	96.6	3.3	-50.3	76.2
Philippines	35.2	100.0%	70.4	1.0	-33.8	35.2
Pakistan	29.5	100.0%	46.7	16.1	-19.8	17.2
Peru	22.2	100.0%	38.4	5.5	-15.5	16.2
Sudan	11.2	100.0%	17.3	10.2	-6.6	6.1
South Africa ^a	11.7	100.0%	17.7	5.0	-3.3	6.0
Congo, Dem. Rep.	9.4	100.0%	16.3	9.5	-6.7	6.9
Nicaragua	4.1	100.0%	10.6	10.0	2.5 ^b	6.5
Ghana	5.7	91.0%	5.2	5.6	-0.3	0.0
Malawi	3.0	87.2%	2.7	2.5	-0.2	0.0
Haiti	1.3	68.3%	0.9	1.2	0.2	0.0
Totals	288.0		719.4	109.7	-321.1	432.7

^a The total odious debt would be much higher if figures for debt service before the end of apartheid were available and so could be taken into account.

^b This is anomalous and relates to unexplained increases in debt recorded as positive transfers prior to 1989.

Ten of the thirteen countries are shown to have odious debt at least equal to all their current outstanding debts – the debt-service they have paid on the odious debts they inherited has been greater than their total new borrowing. The other three have between 68 per cent and 91 per cent – though it should be noted that all three of these require 100 per cent debt cancellation under the debt sustainability criteria outlined in *Debt relief as if people mattered*. The total of odious debt for these 13 countries amounts to US\$719 billion, compared with a total recorded outstanding debt of 'only' US\$288 billion.

For the ten countries with 100 per cent odious debt, all debt servicing is inappropriate. Accordingly, they have been 'overpaying' their debt service and are due not just the cancellation of all their debts but in addition are owed a substantial repayment by the creditors, currently US\$433 billion, which is considerably more than the nominal debt they still have outstanding on paper. The case of Indonesia is particularly striking – the country has already paid US\$148.5 billion relating to odious debt, which is more than twice as much as its remaining outstanding debt.

Table 4 compares the odious debt accumulated by each country with its average income. Five of the thirteen countries have odious debts exceeding their income. The worst cases are that of the Democratic Republic of Congo (formerly Zaire) and Nicaragua, where odious debt is well over twice the national income. Only three of these countries have odious debt of less than half of their national incomes, and one of these is South Africa, where we have not been able to take account of repaid odious debt.

Table 4. Odious debt and income per person.

Country	Odious debt per cap (US\$)	Per cap income (Atlas method) 2005 US\$	Ratio of odious debt to income
Congo, Dem. Rep.	283	120	236.2 per cent
Nicaragua	2,067	950	217.6 per cent
Nigeria	734	560	131.1 per cent
Malawi	206	160	128.6 per cent
Argentina	4,537	4,470	101.5 per cent
Indonesia	1,001	1,280	78.2 per cent
Sudan	477	640	74.5 per cent
Philippines	848	1,320	64.2 per cent
Ghana	236	450	52.4 per cent
Peru	1,373	2,650	51.8 per cent
Pakistan	300	690	43.4 per cent
Haiti	102	450	22.7 per cent
South Africa ^a	378	4,770	7.9 per cent

^a Odious debt for South Africa should be much higher but no figures are available in the WB database for debt service during the apartheid era.

Total odious debt will be very much higher than the total for the 13 case studies, since so many more countries have suffered odious regimes in the last 35 years. We can safely conclude that cancellation of odious debts will add considerably to the total debt cancellation required over and above the figure needed to wipe out unsustainable debt.

5. Mechanisms/procedures for a comprehensive debt work-out

Introduction

There are two main issues to be addressed in relation to sovereign debt: the extent to which it is legitimate and the extent to which it is sustainable. Logically the first should be examined before the latter – all illegitimate debt should be cancelled as soon as possible and compensation offered for debt servicing paid on such debt. Only then should the sustainability of the remaining debt be addressed. However, in practice the unsustainability of some of the debt has been universally accepted while the concept of the illegitimacy of any of the debt is still controversial. We would not wish to delay cancellation of unsustainable debt on the grounds that it might also be illegitimate – the question of compensation can always be addressed later, once the institutions necessary for dealing with illegitimate debt are in place. This is discussed later in the paper.

In practice, however, determining the odiousness of debts may take a long time – during which many people will die for lack of clean water and basic primary health care, and grow up without even a primary education. Unsustainable debt should therefore be cancelled first, and as soon as possible, as it is having a direct and continuing effect on people's lives. Debt sustainability is a concept that is generally accepted – the controversy surrounds the way of calculating it. It is, therefore, conceivable that an existing forum, such as the UN, could be used to agree the parameters. The input data required are objective and in the public domain. Provided the delays and conditions attending the current procedures were eliminated, this would 'only' require extending our proposed new methodology of assessing sustainability to the existing HIPC process. The implementation of the odious debt doctrine, on the other hand, will need new institutions, which would inevitably take a long time to put in place.

Principles for dealing with odious debts

We propose four basic principles for dealing with odious debt:

1. Unrepresentative and undemocratic governments do not have the right to impose external debts on subsequent representative and democratic governments.
2. Creditors act irresponsibly in lending to such governments, thereby promoting their continuation in office, and therefore forfeit the right either to profit from such loans or to recover the capital so provided, except from the persons directly profiting from the loan.
3. Legitimate governments should be no worse off, in terms of external indebtedness, as a result of odious debts having been incurred by previous governments than they would have been had these loans been refused.
4. Arbitration over the extent and treatment of odious debts should be in the hands of an independent international body, which is neither a creditor in its own right, nor controlled by creditors or debtors, and which conducts its activities in a transparent fashion.

Can existing institutions be used?

In practice, most loan agreements are enforceable by courts either in the state of New York or in England. Much recent discussion of the problems of debt crises has focused on the possibility of using principles well-established in domestic law on debt in these places to cope with such crises. In particular, the discussion at the symposium at Duke Law School^{xviii} focused on the possibility of using various

aspects of New York law to challenge individual loans. There are attractions to the proposal. No new institutions would be needed and no change in international law, only the preparedness of one or more countries to refuse to service a particular loan on the grounds that it is odious, and to wait for the creditor to take the matter through the courts. There is a possibility that Ecuador, for example, might do this.

However, the drawbacks are numerous. At present there is no general acceptance of the doctrine of odious debt. Financial markets will, naturally, react very adversely to any debt repudiation. The international financial institutions, led by the IMF, will make a tremendous fuss. Consequently, a country will be taking a huge risk if it repudiates a debt unilaterally on the grounds that it is odious. Argentina managed to force a radical restructuring of its debt (including a write-down to 30–35 per cent of face value), though, to the frustration of many campaigners, it did not attempt to use the undoubted illegitimacy of a large proportion of its debt in so doing (Box 2). It was, however, able to draw strength from the enormous size of its debt (about \$90 billion) and also benefited from the support of Venezuelan oil money, which meant it was not totally dependent on the open financial market. Few other countries would be in a similar position, and, even for Argentina, 2002 (the year after the default) was a very difficult year.

For any country trying this route, the supply of new finance is likely to dry up, or at least become very expensive, even if the (new) government concerned is both democratic and strictly honest. For another, there is no certainty as to the outcome of each case, at least until a good body of caselaw has been built up. Another drawback of this approach is the huge legal costs involved if a significant proportion of debt that campaigners regard as odious were to be challenged piecemeal in this way. (While not wishing to impune the undoubted high-minded principles of the lawyers at the symposia, it is clear that a substantial beneficiary of this approach would be those employed by the parties to the cases to argue the matter.) There are many who would therefore argue for a comprehensive and systematic approach which would deal with all of a country's debt at one time, and which would deal both with legitimacy and the question of sustainability. We now turn to an examination of what that might entail.

Possible administrative arrangements for debt workout

Introduction

In *Chapter 9/11 Resolving international debt crises* proposals for a fair and transparent arbitration procedure (FTAP) were outlined. This envisaged:

- an arbitration process started by the debtor government;
- a panel to arrive at a debt work-out with equal numbers of nominees from debtor and creditor;
- a mutually agreed chair;
- analysis of debts, loan by loan, to assess which were odious; and
- recognition that governments need to be able to continue to function for the good of their citizens regardless of their loan obligations, as recognised under Chapter 9 of US bankruptcy law with respect to local government, i.e., an approach to debt sustainability which recognises human needs.^{xliv}

In *Odious lending: debt relief as if morals mattered* the need for an international body that would assess the status of **current** governments was referred to. This would involve:

- a quasi-judicial procedure on a global scale;
- panels of adjudicators to assist impartiality and independence;

- provisions for judgments to be appealed; and
- an agreement that loan contracts to governments declared odious by the panel would be unenforceable.

It was further proposed that where odious loans were recognised, the accumulated debt servicing of those loans should be repayable first by the creditors responsible for odious loans, then by other creditors, who could pursue the former (odious) creditors and the members of odious regimes for recompense.

These concepts were only sketched out in the earlier papers. The process envisaged was that successor governments would be able to appeal to the international body for a declaration that some of its inherited loans were prima facie odious. If this were agreed, an FTAP would be set up for that country which would examine each loan and would agree which should be cancelled and whether further compensation were owed by the creditors. For this purpose, the FTAP was extended to include nominees of past as well as current creditors, who clearly have different interests. The FTAP would also be required to take into account the sustainability of the remaining debt (after cancellation of odious loans) on human rights grounds, along the lines proposed in *Debt relief as if people mattered*.

Problems and concerns

On closer examination, it is clear that there are a number of problems and concerns in connection with the following issues:^{xiv}

- the criteria for declaring lending odious, particularly whether all loans to an odious regime be considered odious;
- the repercussions on existing states of the acceptance of odious lending as a reason for debt cancellation;
- the difficulty of ensuring the independence of the body for determining the odiousness or otherwise of current regimes;
- the implications of such an international body for the workings of civil society in the countries concerned;
- the question of who should initiate action about existing regimes and on what grounds;
- the need for basic state functions to stay running during an odious regime and how to finance them; and
- the impossibility (in international or national law) of imposing the burden of compensation on innocent creditors.

Odious regimes or odious loans?

An important question is whether all loans to an odious regime should be considered odious. The bulk of the literature written from a legal standpoint has argued that all three of Alexander Sack's criteria are needed for a loan to be odious, to wit:

- absence of consent,
- absence of benefit, and
- awareness of the creditor of the above.

In *Odious lending: debt relief as if morals mattered*, looking at matters from an ethical standpoint, it was argued first that an odious government does not have the right to impose obligations on its legitimate successors, or on the population of the country and secondly that any loan to an odious regime strengthens it, and

furthermore it is difficult to be sure that the loan is funding expenditure which the regime would not have undertaken had the loan been absent. If the expenditure would have been made anyway, then the loan has simply freed up domestic funds for some other, quite possibly nefarious use. Economists refer to this as 'fungibility'. A classic example of fungibility was the use by the apartheid regime in South Africa of international loans to parastatal companies for projects with large domestic currency expenditure to free up foreign exchange for other purposes, including the purchase of arms. The fungibility problem led us to argue that all loans to an odious regime should be regarded as odious. This position is supported by some of the legal discussions, including the symposium at Duke University in January 2007.

Nevertheless it could be argued that certain projects undertaken by odious regimes did benefit the population and so could be regarded as legitimate. We propose that if a regime is judged odious, the burden of proof falls on the creditor to prove that it was of sufficient benefit to the country to be regarded as a legitimate loan. It will also be necessary to prove that the project would not have been undertaken without the loan. On the other hand, it should be open to successor regimes to make a case that a certain loan to a regime that was itself considered legitimate should be considered odious (for example, it was on excessively extortionate terms, or the project was badly designed at the creditor's instigation). Here the burden of proof falls on those wishing to repudiate the loan. In this way both process (the way in which the loan was contracted) and outcome are brought into account.

Arrangements for recognising odious regimes

As soon as a credible system for odious debt work-out for debt incurred under **former** regimes is accepted, there is likely to be a problem for **existing** governments. Creditors will be wary of lending to regimes they fear might be declared odious at some point in the future. Many existing governments will therefore have difficulties raising new and roll-over finance in case they are deemed to be odious once they have been replaced by a different regime. At the very least they will face greatly increased interest rates for commercial loans. This means that having an internationally accepted way to 'vet' regimes is an essential part of any system of debt work-out for odious debt, and it is important that this element provides positive vetting as well as negative. Creditors need to have assurance that loans to a non-odious regime will be collectible even if the regime in question is less than perfect; and it is in the interest of all governments that are **not** odious that this guarantee be given. The corollary of this is that existing governments that are pronounced odious will face financial sanctions. There is an immediate problem that there are, of course, degrees of odiousness. It is a contentious matter to declare a departed regime odious – how much more difficult will it be to agree on criteria by which to label current regimes?

The **objectives** of the process are:

- to provide a mechanism for declaring past and present regimes odious, legitimate, or under review;
- thereby, to provide a basis for ensuring that odious regimes do not impose financial burdens on the population of their countries or on legitimate successor governments; and
- to do so in such a way that maximises the chance of improvement in governance.

For it to achieve its objectives it needs to be truly independent and credible, with creditors, governments (both creditor and debtor) and civil society.

There is a serious tension between maintaining flexibility and the predictability necessary to avoid unnecessarily discouraging lending. Flexibility also greatly increases the risk of abuse and of inconsistent standards between cases. In addition, it could increase the scope for panel findings to be subject to legal challenge, which could make the process messy. Clearly, a minimum level of clear and specific criteria would have to be included in the process.

Indeed, the process of declaring current regimes odious is fraught with difficulties. For one thing, it raises very serious issues about the sovereignty of domestic political processes and the ability of the international community to involve itself in the workings of these processes. In particular, by declaring a regime odious, the international community is, in effect, saying that it should be changed. In certain circumstances this may not be realistic, or the alternative may be no better than the present regime. For example, many would call the Arroyo regime in the Philippines corrupt, but the main alternative, Joseph Estrada (and his stand-in at the last election Fernando Poe), sound no better. Estrada has been under house arrest for plunder for some time and Poe has since died.

One criterion by which a good procedure can be judged is the extent to which it promotes improvement from what may be very difficult circumstances. It is important to get the signals and incentives right. Are the pre-conditions for representative or effective government adequately in place? If they are not, what line should be taken? For example, what status should be accorded to the present Nigerian government? It is far from perfect but is better than its predecessors, and it appears to be making an effort both to be more democratic and less corrupt.^{xvii} The question of failed and fragile states is also a serious one. Liberia is just emerging from dreadful civil war – the new government needs support but cannot be expected to transform the situation overnight. Somalia cannot be said to have a functioning government at all at the time of writing. (Having said that, the problem for the institution being contemplated here may not be as great as all that – there is little chance that these really fragile states are in a position to take on any debt when the question of debt sustainability is considered.) Nevertheless, the body set up needs to bear in mind what the realistic alternative to the present regime actually is. It will therefore have to combine sufficient flexibility and realism with enough consistency to be credible.

One possible solution might be to rely on civil society in the country concerned to judge their own governments, but there are at least three problems with this option. The concern runs in both directions, i.e., both that odious regimes could be left unlabelled, and that regimes that are less than perfect but nevertheless not truly odious be condemned. On both counts there needs to be a system which has some chance of being accepted as reasonable by the creditors, while retaining the credibility of the population directly affected. The first problem relates to those countries where civil society is at a very rudimentary level of development and is too weak to stand up to the regime. In these circumstances, there needs to be provision for international intervention. The second scenario is where civil society is split – whether as a result of the regime setting up front organisations who support it while claiming to be independent, or, equally likely, as a result of different Civil Society Organizations (CSOs) representing different strands of society or opinion having different points of view. A third problem arises where there is a regime change (whether peaceful or otherwise), and it is in the new regime's interest to declare its predecessor corrupt or oppressive and claim odiousness (again perhaps backed by front organisations). Under these circumstances, the new regime could repudiate inherited debts, *provided it could do so without consequence to its own creditworthiness*. In all cases there needs to be a pronouncement of odiousness which can be supported with conviction; one that creditors will have to accept as valid, however reluctant they are to do so.

On the other hand there is a real and present danger that the body may be captured by the creditor countries. Ensuring independence from them is essential for the integrity of the system.

Moreover, a system which undermines local autonomy and institutions must be avoided, and this requirement needs to be taken into account as much as is feasible.

In *Odious lending: debt relief as if morals mattered* we argue that the roll-over loans used to service odious debts, even if taken out by perfectly legitimate successor governments, should be regarded as odious. In parallel with that, perhaps the loans taken out by odious regimes to service legitimate debt should also be treated as

legitimate. There is a certain logic to this, but in the case of many loans (with the notable exception of many in the social sectors), it could also be argued that if the legitimate loan had been used wisely it should subsequently be generating adequate returns to cover service costs. In these circumstances, any borrowing ostensibly aimed at servicing such debts is in practice freeing up resources for other purposes.

There is, however, still the difficult question of whether financial sanctions of this kind will cause unacceptable suffering for the population. This is, of course, on a par with the discussion over sanctions imposed on Iraq prior to the last war, which, coupled with Saddam Hussein's apparent indifference to the suffering of the Iraqi people, was associated with very considerable hardship. Donors of grants can be asked to find alternative means of delivering aid that by-passes the government, but credit can only be advanced through official channels.^{xlvii} It is always going to be hard to devise sanctions that hit a regime harder than the people if the regime is sufficiently indifferent to the hardships of the population. If it were really concerned, it would not be odious in character. There is no simple way out of this dilemma

Process

If it is accepted that there is a need for an international body, it is worth spending a little time envisaging how it might operate before looking at its constitution.

When the odious regime in question has been replaced by a legitimate successor, it is envisaged that this successor government would initiate the process by appealing for a debt work-out on the grounds of odious debt (or a combination of unsustainable and odious debt). The panel would then hear representations from interested parties (international observers, civil society, creditors, and the present government) before making a judgement on the nature of the regime in question. If the result were a decision that the regime had been odious, then FTAP would kick in.

With present regimes, a reference to the panel might be automatic (triggered by each election or other regime change), or based on representations from international or domestic civil society.^{xlviii} In any contentious case there would inevitably be some delay before the panel reached a decision, and yet something would need to be done to cater for the immediate financial needs of the country. When the panel meets, the procedure would presumably be similar to that described for former regimes.

The government of a country involved in the commercial loan market to any serious extent that is declared illegitimate will get into difficulty very quickly and that difficulty is unlikely to be confined to raising loans. The problem could spread to the foreign exchange and stock markets. If the regime cannot raise foreign loans the foreign exchange reserves will start to fall, domestic interest rates will rise as the government turns to the domestic market for funds and the threat to political stability will probably have an immediate effect on the stock market. While this means that the sanction is potentially very strong, it also means that great caution needs to be exercised in its use.

Constitution

Selection of panellists

Given the importance and delicacy of the work, it is vital that the selection of panellists is (and is seen to be) above board and that the members are independent. Appointing members to this body could be by any number of means, from selection by the UN Secretary-General, by some other body, either itself chosen by one of these methods, or an existing one, such as the International Court, through to direct election.

While there is an infinite variety of options, one possibility would be to establish a quasi-judicial international body, selected by some sort of voting system. It could, for instance, be voted on by *legislatures* (rather than by the governments or by direct election) in individual countries, which would automatically pronounce on the legitimacy of all new governments.

Modus operandi

We propose that there should be adjudicators from each region, who sit in panels of three (each from a different region). The panel would hear evidence from interested parties and then make a judgement. General principles should be determined by a plenary meeting of all (or a large proportion of) the panel members. This proposal is designed to ensure (as much as possible) that decisions are consistent and objective. The panels would assess each government whenever there was a change, whether by election or some other event.

There is also a need to decide on a system by which regimes could be called to account should the situation deteriorate significantly after an initial green light was awarded. This process could perhaps rely on civil society appeals, whether restricted to local civil society (an option which would not work in a country where civil society was too weak) or mediated by international CSOs. In this latter case, it might be difficult to determine which CSO was eligible to do the vetting, or how to avoid a Northern bias in making such a choice. It may be enough that the international body be empowered on its own initiative to reinvestigate existing regimes which it had initially ruled to be legitimate.

Details of these and other matters related to the operation of the adjudication panels are outlined in Appendix 1.

Fair and transparent arbitration process

Introduction

As described in *Odious lending: debt as if morals mattered*, it is envisaged that actual debt relief would result from an FTAP. The process would be initiated by a successor regime, whether as part of a bankruptcy process, when both the odiousness of the debt and the question of sustainability would be addressed, or simply because the successor regime wished to repudiate the debt on the grounds of its nature. In the latter case it would be necessary first to call in the services of the adjudication panel described above to pronounce on the odiousness of the [past] regime in question before starting the arbitration process.

The FTAP envisaged involves the setting up of an arbitration committee for each debtor country with people nominated equally by creditor and debtor, with a mutually chosen chair. It is important that these people are nominees, not representatives, or the panel may remain deadlocked as representatives refer back to their 'constituents' and issues become entrenched. It is proposed that there should be two nominees from the creditor side, chosen by current and former creditors.^{xix} There should also be two from the debtor side, one chosen by government and the other by civil society. The latter may be a difficult choice, for the question of who is entitled to choose on behalf of civil society may well itself be a contentious issue. It is possible that there is no 'one-size-fits-all' system possible for choosing the civil society nominee. If it goes to a vote it should be by all citizens of the country – it could hardly be restricted to self-selected civil society organisations, but this is not really a position suitable to fill by election. There is no easy answer to this problem.

If there were to be a single umbrella organisation for CSOs that was uncontroversial and universally accepted then this organisation could appoint a nominee. Unfortunately this happy situation is likely to be the rare exception, not the rule. The government nominee would no doubt be paid, but if the CSO nominee were also to be remunerated, then the post would become a desirable one in many debtor countries, and the selection process would become contentious. On the other hand, if the post were **not** paid, the nominee would be even more vulnerable to inducements that creditors might well offer in the hope of getting a more favourable outcome. There does not seem to be an easy solution to this dilemma either.

The chair (and the secretariat) of this panel would have to be paid. It is proposed that the funding for this would have to be under UN auspices, preferably paid for by international taxation or by donor funds if this does not compromise the neutrality of the chair too much.

Proposal for dealing with laundered odious debts

Background

A problem arises with odious loans which have been laundered by being rolled over or sold on, after a legitimate government has replaced an odious one. In *Odious lending: debt relief as if morals mattered*, an FTAP was proposed which would assign loans deemed odious first to creditors who had lent to the former (odious) regime but then to legitimate creditors, who would have the right to pursue the original creditors (and the members of the odious regime as individuals) for compensation.

In the case of official debt, the case should be relatively straightforward. However, in the case of commercial debt, matters are more difficult. It may well be that a past irresponsible creditor may not be involved in current lending, or if they are, that the outstanding debt is less than the accumulated odious debt. (Indeed in 10 of the countries in the 13 case studies odious debt amounted to more than all outstanding debt, so that this must be the case in aggregate.)

It is said that the demand that loans to legitimate creditors be cancelled to offset odious debt would be rejected as unjust and could have no standing in law. This argument is strong. Indeed if a legitimate regime approaches a creditor for a loan which it happens in practice to use for repaying a debt incurred under a predecessor regime, the new creditor cannot be deemed irresponsible. The purchaser of a debt sold on is less obviously innocent, if the loan in question is clearly an odious one. Nevertheless, it is a more complicated question than if the original creditor still holds the loan.

Objective

The objective is to devise a system which would not leave debtor countries to pursue creditors through the world's courts (and one can imagine all sorts of pressure that might be brought on a small third world country to drop its claims), and also to speed up the cancellation of debts, and disbursement of compensation for loans, deemed odious by the FTAP. Commercial creditors can be expected to fight hard to avoid cancellation of debt, but especially to avoid paying compensation for rolled-over odious debts and interest already paid.

Proposal

It is therefore proposed that a revolving fund be set up (with initial capital from the major donors, or possibly from bonds paid for out of international taxation, in the same manner as the International Finance Facility for Immunizations (IFFI) is paid for out of donor funds) to compensate the debtor country, and then to pursue the odious lenders and odious regime members itself to replenish the fund. This could be managed by the body set up to adjudicate on the odious or legitimate nature of current regimes or by some other international body with sufficient authority to ease the recovery of the funds.

Drawbacks

The drawbacks of this scheme are that:

- it would be in competition with other uses of donor funds if these are used;
- its cost will be high;
- there could be delays in recovering the vast sums involved from commercial creditors; and
- there is a danger that it will not be replenished from the creditors – if creditors have gone bankrupt or otherwise disappeared and odious regime members and their descendants have spent the proceeds or are untraceable.

Further discussion – recovering past service payments

The contention of *Odious lending: debt relief as if morals mattered* is that the debt service paid on odious loans should not have been paid. Interest paid is therefore capitalised in the calculations and added to the odious loan while capital repayments are ignored. For a loan on which any debt service has been paid, the related total will therefore exceed the outstanding principal. Once a loan has been declared odious, a country will be able to cease service payments (which, it is assumed, have been paid into an escrow account during the FTAP procedure) and recover the money in the escrow account. The past service payments should become repayable by the creditor. Where the original creditor has lent further funds to a legitimate successor regime it should be possible for the debtor to offset any liabilities for legitimate loans against amounts owed in compensation for payments made on odious loans. Problems arise whenever this is not the case. There will also be problems allocating responsibility for compensation where debts have been consolidated and documentation for old loans may well be lost or inadequate.

Managing the effects of compensation

In many cases, the funds involved in compensation will be large relative to the outstanding debt and to the economy of the debtor. (For an extreme example, in the case of Indonesia this would be twice the outstanding debt and equivalent to 90 per cent of GDP.) Paying this all at once would risk severe disruption to the economy in the form of Dutch disease (over-valuation of the exchange rate), inflation, over-liquidity of the banking system etc. While not wishing to encroach on Southern government autonomy, it is likely to be better for their economy that compensation be drawn down only gradually. It would be wise in many cases for the government to treat it as a 'Future Generations Fund' which would normally be used to generate revenue rather than draw down on the capital. This would also reduce disruption to the world financial system from the major transfers involved. It would, however, be a form of foreign exchange reserve that would itself do much to reduce the country's dependence on the IMF and insulate it to some degree from the vagaries of the international capital market.

Domestic debt

Odious regimes are no more eligible to take out domestic debt on behalf of their country's citizens than foreign debt. However, it is not possible for the international community to prevent their issuing such domestic debt. There is, therefore, no direct basis for the international community to take on an obligation to repay this debt, except in so far as foreign investors have bought local currency bond issues. It is best left to domestic courts to deal with disputes on such matters and to successor governments to decide whether to repudiate inherited national domestic debt.

Box 3. Implications of the Norwegian example

In 2005, a new government came into power in Norway. The declaration of the new coalition government – the Soria Moria declaration – marked a real change in attitude towards illegitimate debt, the result of a long campaign by civil society. This declaration states that:

'Norway must adopt an even more offensive position in the international work to reduce the debt burden of poor countries. The UN must establish criteria for what can be characterised as illegitimate debt, and such debt must be cancelled.'

Norway will lead the way in the work to ensure the debt cancellation of the poorest countries' outstanding debt in line with the international debt relief initiative. The costs of debt cancellation must not result in a reduction of Norwegian aid, cf. the adopted debt repayment plan. No requirements must be made for privatisation as a condition for the cancellation of debt. The Government will support the work to set up an international debt settlement court that will hear matters concerning illegitimate debt.'

This declaration made no specific reference to Norwegian debt but in practice the bulk of outstanding debt owed to Norway was the result of the Ship Export Campaign of the late 1970s, when export credits were used heavily to promote the export of ships from Norwegian shipyards that were suffering from a strong downturn in orders at the time.

In October 2006, Erik Solheim, Minister of International Development, said about the Ship Export Campaign, in announcing the cancellation of outstanding debts relating to the campaign: *'This campaign represented a development policy failure. As a creditor country Norway has a shared responsibility for the debts that followed.'*

(This cancellation has not been counted by Norway as part of its aid programme, unlike debt cancellations by many other OECD (Organisation for Economic Cooperation and Development) countries.)

The key phrase is 'shared responsibility', which represents a significant breaking of ranks amongst creditors. Shared responsibility can be taken to cover a much wider range of issues than odious debt, though naturally it should relate to loans to odious regimes as well. Lenders should share responsibility for lending (as opposed to giving) to countries that are too poor to be able to afford to repay; for lending for projects that are grossly misconceived but approved by the creditor; for lending in circumstances where funds are very likely to be misused; for lending at extortionate rates of interest, and for applying conditions to the loans which are primarily designed to assist the lender not the borrower.

Financing

The sums involved are substantial. By comparing Joe Hanlon's estimate of odious debt for 23 countries with our own estimate of the amount outstanding for our 13 case study countries, we estimate that total outstanding odious debt on our definition is likely to be of the order of \$700–800 billion (in nominal terms), without taking into account the need for compensation for over-payments. Unsustainable debt amounts to about \$500 billion (in NPV terms) or \$670 billion in nominal terms, in our estimation, although there is considerable overlap between the two categories. Where odious debts are identified and the creditor still has outstanding loans to the country, these can be cancelled.

With official creditors (multilateral and bilateral), it is to be expected that liability will already have been anticipated and (one hopes) accepted as part of the negotiations necessary for the setting in motion of this whole procedure. Nevertheless, there will be additional problems obtaining compensation for past payments, compared with the cancellation of outstanding debts. (It should be noted that Norway has not raised the question of compensation – merely cancelled remaining amounts outstanding.) Nevertheless, if past payments are not compensated for, there will be strong criticism of the system, which will penalise those countries who managed to pay for past loans compared with those who did not. While the first priority might be to get cancellation of any remaining debt, the need for compensation for past debt service should not be forgotten.

Commercial creditors can be expected to fight the measure tooth and nail, hence the need to find an intermediary between debtors – who successfully get a decision that a debt is odious – and their creditors. These countries cannot afford to wait while the issue is fought out in the courts or to pay for the legal battle.

There is a need for more funding. We suggest a revolving fund be set up which would reclaim the compensation from the odious lenders. Three possible sources of funding for such a revolving fund are suggested here: donor funds, international taxation and a global allocation of tradeable carbon credits.

The advantage of using donor funds is that this is an existing mechanism. The disadvantage is that it is extremely unlikely that sufficient funds can be made available from this source without severely restricting grant aid, which to the contrary

needs to be increased in tandem since loan funds will in future be restricted to those countries that can afford more debt. The advantage of international taxation is that it could be a new source of funds which does not compete with existing demands. The disadvantage is that the concept is in its infancy. The sums involved would require something in the nature of a Tobin tax as the airline ticket tax cannot be expected to raise a figure of this size. Tradeable carbon credits would provide a potentially major source of new funding for poorer countries, while helping to curb carbon emissions that are playing such a large part in global warming, a threat to well-being which dwarfs the effect of the debt overhang. However, such credits ought to be available as a matter of right, not as a source of compensation for past wrongs perpetrated by the North. It could be seen as an answer to the problem of unsustainable debt but not as a response to odious debt. We therefore propose that a Tobin tax be implemented to raise funds for the revolving fund. However, in order to raise a large pot of money quickly, we propose that the funds be raised from a bond issue, with the service costs of the issue to be funded by the tax, in a similar manner to the operation of the IFFI.

Conclusion

In order to stop the drain on Southern government budgets from debt servicing (which is one of the factors which prevent their meeting the basic needs of their populations), substantial debt cancellation is urgently needed beyond that provided under the HIPC initiative and the 2005 G8 deal.

A further implication is that none of the countries requiring debt cancellation on the grounds of debt sustainability can afford to take out more debt, though that is what has happened in the past. HIPC countries that reached completion point have already started building up new debts, and the longer ago that they reached it the higher their debt.¹¹ Yet they all need more resources, beyond the relief which could be provided by debt cancellation, if they are to meet the MDGs and reduce poverty to acceptable levels. There therefore needs to be a substantial increase in grant aid (at least up to the 0.7 per cent of GDP target) in addition to the debt cancellation we propose.

In addition, many developing countries have odious debts at least equal to their total outstanding debt burdens; while creditors persist in demanding the servicing of these debts, regardless of their responsibility for knowingly lending to corrupt and oppressive regimes. A fair, transparent and independent arbitration procedure is urgently required to deal with this, so that debt relief can be achieved **as if morality mattered**. Not only will this relieve millions of people from the burden of debts that were incurred without their consent and with little or no benefit to them, but the process should also hasten the end of a number of *current* odious regimes. The creditors who are currently propping them up will suddenly discover that they can no longer afford to ignore the crimes they are effectively bankrolling.

To achieve this outcome, a comprehensive approach to debt work-out is needed. We propose the setting up of a new institution to adjudicate on the odiousness or otherwise of regimes and the institutionalising of an arbitration procedure for each country affected.

This course is not without its problems:

- There is the danger that loan finance will dry up without a corresponding increase in other funding.
- An essential corollary for the recognition of a more comprehensive approach to debt sustainability is a significant increase in grant and other finance, such as international taxation and tradeable carbon credits.
- Finding adequate funds to compensate for past odious lending is not going to be easy and could compete with current grant aid.
- Deciding the allocation of responsibility for compensation for past odious lending when debts have been rolled over, consolidated and restructured is a complex task.

- Declaring a current regime odious, or even under warning, will have a major impact on the availability and cost of loan finance. Markets suffer where there is uncertainty.
- Doubts about the outcome of panel adjudication and FTAP procedures will increase this factor.

However, the benefits of at last having a comprehensive approach to debt work-out will also be great. In the short term, these would include:

- an increase in funds for essential services;
- improved policy space for governments due to the lifting of conditionality; and
- an increase in financial resources, coupled with lower demands on scarce administrative capacity as a result of reduced loan negotiation and management requirements.

In the longer term there would be improved incentives towards responsible and democratic government:

- This would be marked in particular by a greater accountability of governments to their own citizens when their unpopular decisions can no longer be laid at the door of the BWIs.
- Furthermore, governments could no longer undermine the authority of their parliaments by requesting that they rubber stamp agreements already agreed with the International institutions.
- Overall, freedom from the burden of debt service would afford increased autonomy, and encourage greater self-reliance in the countries of the South.

Ways forward

The ideas presented in this paper are an attempt to move forward measures to get a comprehensive and genuine solution to the third world debt crisis as if justice mattered. Clearly there is a long way to go before consensus is reached.

We are distributing this paper as widely as possible (and would welcome feedback), seeking ways to turn the ideas into reality. We would be grateful if readers could call attention to it in any suitable fora to which they have access. One of the next steps we should like to see would be a conference of debtor governments meeting together with creditors to seek agreement on a way forward, perhaps under UN auspices. Prior to that, it might be fruitful to get discussion of the ideas by Southern-based inter-governmental government organisations such as the G24 and the South Centre.

Another path to be pursued would be to identify a major debtor, perhaps one where a debt audit was already well advanced, who would be prepared to pioneer one of the approaches outlined here, whether by insisting on arbitration or pursuing the Engand/New York court route. In addition, smaller debtors could coordinate and agree on collective action in this arena. If a sufficiently large number of debtors could agree to apply jointly for debt cancellation on the grounds of its illegitimacy, there is some chance of forcing the creditors to move forward. In the meantime, progress is unlikely without great pressure being brought to bear on OECD governments by civil society to shame them into adequate action.

Appendix 1: Details of the adjudication panel concept

The following notes on the adjudication panel are intended to spell out some of the issues that need to be addressed in making the panel a reality and to illustrate possible solutions to these issues. These solutions are not meant to be definitive but to reassure the reader that workable solutions do indeed exist for the problems identified.

1. Note on criteria and standards

The panel plenary body would need to decide on the criteria it would use to define odiousness. These would presumably include:

- abuse of the democratic process;
- absence of the rule of law;
- gross corruption; and
- abuse of human rights.

The key point in this instance is to identify the criteria by which to judge that the regime has forfeited the right to bind the people of the country to commitments for the future. (This concept might have ramifications for other treaty obligations, such as WTO agreements.) It is likely that the standards by which these criteria are judged will start out at a relatively low level *for current regimes* at first – sufficient to pick up Uzbekistan and Myanmar, perhaps. This standard could be raised, with due notice, to encourage reform at a later stage.

It is also important that the standards take account of what is feasible, given the history of the country. Very difficult questions are involved. There are a number of circumstances which make the creation of a genuinely representative government extremely difficult: for example, if the country's borders are a historical (and perhaps colonial) accident with little coherence, bringing together peoples with no identity as a nation; or if politics are not values-based but based on ethnic or patronage ties. Transformation from a dire situation cannot be achieved overnight and it is difficult for outsiders to know what is feasible. Yet there are situations which the international community should not ignore. Events such as the genocide in Rwanda require international intervention and this should include withholding loans.

Is democracy feasible in Somalia? Are levels of corruption improving enough, albeit from a high level in, for example, Nigeria? What is possible in countries emerging from conflict, such as Liberia? Should bloodless coups, such as in Thailand in October 2006, be met by instant withdrawal of lending, plunging the country into chaos, or should they be given a short period to organise fresh elections? These are all difficult cases which will need to be dealt with by the proposed body.

2. A traffic-light system

The judgement might be in the form of recommendations by a panel to the plenary body, which would then endorse the findings or not, as the case may be, or they could be in the form of judgements, which would be subject to appeal by interested parties to the plenary panel. Judgements could be in the form of a 'green light'; an immediate declaration of odiousness ('red light'); or a warning ('amber light') with a six-month (or similar period) notice to organise fresh elections free from whatever abuses caused the problem, possibly with a ceiling on borrowing in the meantime. However, since the state needs to continue to function while fresh elections are organised – and this often means that some borrowing is required,

if only to roll over existing loans – instant condemnation would have to be rare to prevent serious damage to the economy and consequent hardship for the general population. It is not envisaged that the panel would question the result of elections that had been accepted by the UN Electoral Assistance Division (UNEAD), since an election, unless badly flawed, represents the best expression of civil society that can be achieved.^{lii,liii} Conversely, a military coup *against an elected government* would normally receive an immediate condemnation, on the grounds that a government which is not representative of the people has no right to take out loans which the latter will have to repay. In this context, was the government of Prime Minister Shinawatra sufficiently corrupt and manipulative of democratic processes to allow the coup leaders some time to prove their good intentions?

Of course, the effect of an amber light can be expected to be marked – creditors are likely to be very wary of lending to a regime under any sort of warning. The positive side of this is that this will be a strong disincentive to perpetrate abuses likely to lead to a negative verdict. The negative side is that great care would need to be taken by the panel not to make a bad situation worse.^{liv}

3. Selection of panellists by region

It is proposed that panellists be chosen by region to ensure a fair representation from around the world. These regions will need to be defined – the UN defines 18 regions, for example. The regions should normally be geographic (though there might be a case to be made for there to be a constituency of small island states). It might, however, be also desirable to divide constituencies into debtor and creditor countries, as the perspective of the latter is likely to be different to that of the former (both in terms of greater or lower realism and in terms of greater or lesser regard for creditor interests). Each region could have the same number of panellists, but the number could also be in some relationship to population or to numbers of countries. We propose that debtors and creditors be in separate regions, that the number of panellists from each region be determined in proportion to the square root of the population of the regions.

Panels could always consist of one panellist chosen by creditor countries and two by debtor ones or this could be random. We propose that the selection be random, but unanimity be required amongst the three panellists. If agreement cannot be reached on an issue, the question would go to the full assembly of panellists.

Should adjudicators be barred from dealing with their own region? Or should there be a requirement that one of the three be from the region but none from the country under review?^v The former rule might reduce the danger of bias, while the latter might promote the concept of peer review. We propose that the latter apply.

4. Selection of panellists

The current proposal is that there should be some weight given to a country's vote related to population but not fully proportionally; that is, related to either the square root or the cube root of the population. This would mean that Country A with 4 million people would have half the weight of Country B with 16 million (square root) or 64 million (cube root).^{vi} Having no weights would mean that the voters in, say, Vanuatu, would have the same weight as those in China, which seems extreme, while weighting by population would mean that China and India would be overdominant.

Election by legislatures of all the countries in the region should mean that there were too many voters to bribe, while reducing the cost and logistical difficulties of a direct popular vote for something that, it must be recognised, will not be of immediate interest to the population at large. The legislators would probably in any case have less interest in voting for corruptible people than their governments, although that is itself a contentious matter – some legislatures would be as bad as their governments, while others may not exist or be completely dominated by their governments. Moreover, should a country that has no elected legislature be disenfranchised? Should the international community try to organise a direct

election over the head of the unelected government? This would be unrealistic. In which case there may be no choice but to leave the country disenfranchised. It would hardly be acceptable to allow an unelected government to vote for panellists on a body like this. In addition, there remains the grey area of disputed elections, although it is proposed only to query elections where a UN body has denounced them. Despite this problem, election by legislators might give a better chance that the result would be free and fair than other methods.

5. How might voting for panellists be conducted?

Should this vote be a single transferable vote? Where there is more than one panellist per region, should each remain a single transferable vote (STV), or should multiple transferable votes be preferred? This might be judged unnecessarily complicated. There is a need to combine the STVs of one legislature with those of another. First a matrix of the votes for each country would be produced, then (if so decided) a weight assigned to that outcome. STV works by eliminating the candidate with the fewest first votes and assigning the second votes of those people who voted for the loser to the remaining candidates. This process is repeated until there are only two candidates, in the case of a one-member 'constituency'. A computer could work out the result of this, but the process would be opaque to observers.

It would be simpler, and perhaps sufficient, to take the proportionate share of first-past-the-post votes from each legislature and take this as the 'STV' of the country concerned. Where there are multiple seats for a region, the balance of the votes for the first candidate to achieve enough votes to be elected above that target level are then passed on to the second choices of all those who voted for the successful candidate but only in proportion to the extra votes above the target. In other words, if Candidate A gets twice as many votes as is needed to be elected, the second choices of **all** those who voted for Candidate A are given to the other candidates but halved in value. If Candidate A had only got 120 per cent of the votes needed, the proportion passed on would be one-sixth.

6. Note on workload and procedure

Under 'normal' circumstances, with about 200 countries in the world, one can expect 40 or so elections a year, assuming an average of 4- to 5-year terms of office, for the majority that have elections of some sort. Some of these may be uncontroversial – presumably the panel will not need to take very long to pronounce on elections in Sweden or Botswana (but how long would it have needed for the US Presidential election in 2000?). However, if hearings of several weeks are to be held for 75 per cent of countries (say 30–40 panel-months a year), with longer investigations for controversial or difficult cases (say 20 per cent, involving a further 20–30 months), the process would involve about 50–70 panel-months a year.

Of course to start with there will be a backlog both of current regimes and of past *prima facie* odious ones. In addition to the 13 cases in *Odious lending: debt as if morals mattered*, there can be few countries in the South which have no history of dubious regimes. If it is left to successor governments to take the initiative to appeal for an FTAP, however, the number coming forward may not be very large and will consist of overwhelmingly clear-cut cases. It might be realistic to expect only 20 cases in the first year, as states test the waters. This might add 40 panel-months. A triage system might be needed to deal with the start-up of the new dispensation. In other words, countries would be divided into three groups: those that could be pronounced acceptable after only the most cursory review; those so extreme that should be considered odious with only a brief analysis; and the rest – those that would need more careful review. Some temporary reassurance to creditors would be needed for the latter.

This effort will need to be headed by an exceptional person with vision and drive. Selection of the head of the organisation could perhaps be by direct election by legislatures worldwide, as envisaged in some quarters for heads of the UN and other international bodies, or by the panellists themselves. There would also be a

need for the panellists to sit in plenary session to decide on procedures, guidelines and standards.

If it is decided that judgements should be in the form of recommendations by the small panel to the plenary, there would be considerable extra work for panellists, who would have to make time to sit in plenary session.

This would mean a workload of 100 panel-months a year for the individual country work plus an allowance for plenary work of, say, 25 per cent, i.e., about 13 panels would be needed, allowing for vacant posts, leave and illness. There would be no necessity for the plenary sessions to involve all panellists. Rather, some flexibility would allow a different composition for members of the plenary sessions than for the population of panellists as a whole, should this be helpful. For example, it would allow the composition of the plenary to reflect the population of creditor and debtor countries globally, while the number of panellists from each region could retain their relationship to the number of countries in their group.

7. Term of office

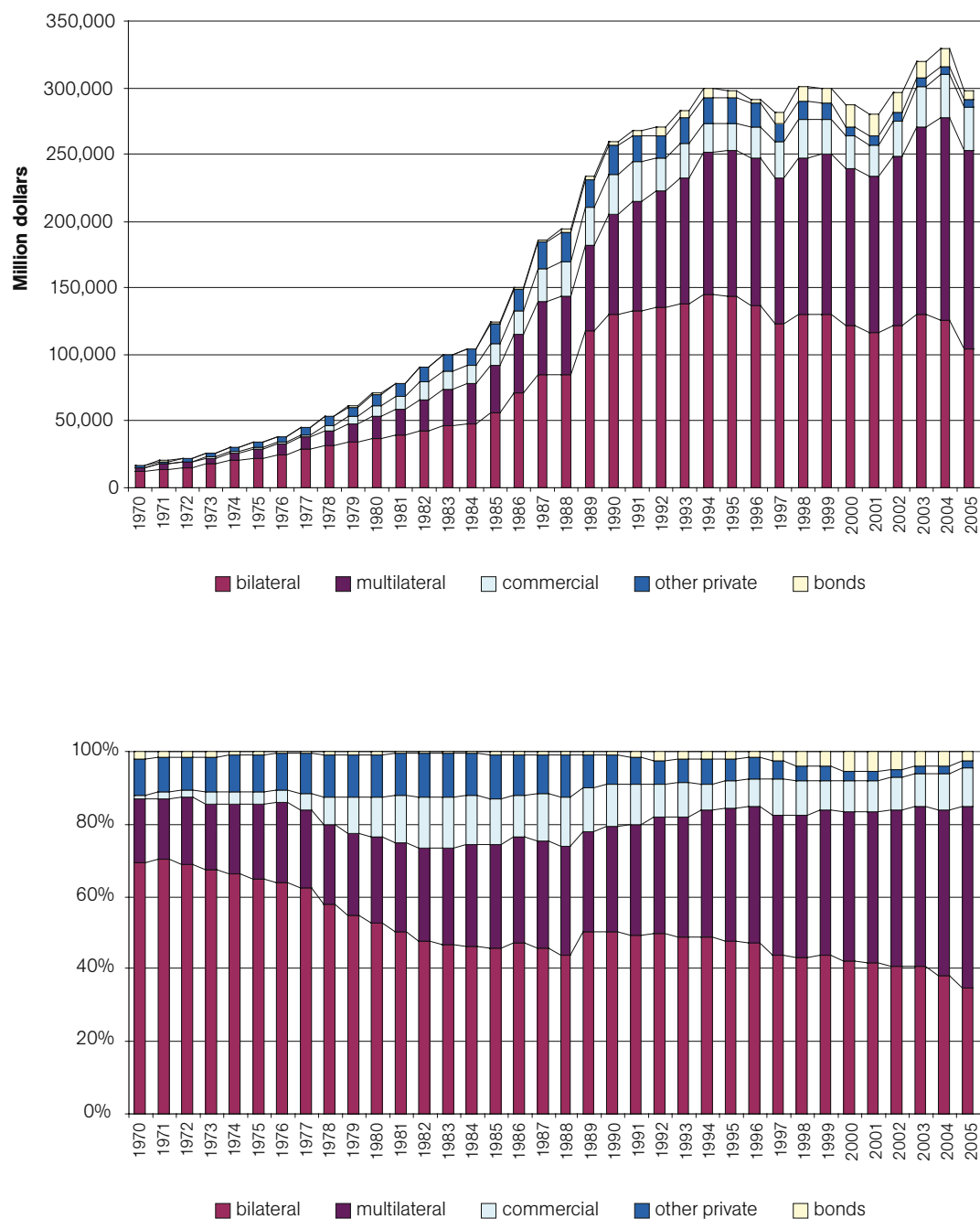
It is proposed that panellists be barred from sitting for more than one term (be it 5, 6 or 7 years) so that they are free from the desire to seek re-election, since this would potentially make them vulnerable to pressure to please those who could influence whether they got re-elected. The disadvantage of this would be that all panellists would be relatively inexperienced and would not be disciplined by the desire to seek re-election. Some of the problems of inexperience could be reduced by staggering the election of panellists from multi-member constituencies.^{lvii} This would allow some continuity and should improve effectiveness, although it would be at the cost of reducing the extent to which election reflected the current views of those voting. There would, of course, also need to be some form of secretariat for the organisation and a review body that could call panellists to account for failure to execute their duties properly (unless the plenary meeting of the panel be considered adequate for the latter purpose). This, in turn, raises issues of how it should be selected, how much discretion to allow the head of the body, and so on.

Appendix 2: Evolution of third world debt – which creditors when?

In this appendix we examine the evolution of third world debt by types of creditor. In order to improve understanding of the responsibility for the debt crisis it is instructive to look at who has been lending to whom and when.

Low-income countries^{viii}

Figure A1: Low-income debt evolution.



The first thing to note about low-income-country debt is that overall levels rose in every year up 1994, with significant declines only in 1996 and 1997, in 2000 and 2001 and again in 2005. The last two are partly the effect of HIPC, but the main influence in 2005 is the Nigerian debt buy-back and write-off. The combined effect of all the debt relief efforts has only been to bring the 2005 total back to the level of 1994, just before the HIPC initiative started – when, presumably, debt levels were considered to be so alarmingly great that the need for the initiative was finally being accepted in official circles.

Naturally, for this income group, debt is primarily official. From Figure A1 it is clear that bilateral creditors were responsible for about two-thirds of all lending to low-income countries in the 1970s and about half in the 1980s. Since 1990, however, the proportion has slowly dropped to below 40 per cent, while the absolute amount carried on growing to 1994 and has dropped a little since then. The drop in proportion is largely the result of an increase in multilateral lending. The first graph in Figure A1 illustrates that the massive increase in low-income-country debt arose between 1984 and 1990 as a result of big increases in both bilateral and multilateral lending. It is interesting that this period corresponds to the final years of the Cold War and comes after the first major debt crisis (the early 1980s). It shows that official creditors learnt nothing from that crisis. The multilateral creditors (IDA, AfDB, IADB etc.), having been responsible for less than 20 per cent of lending in 1970, have seen their share grow pretty steadily throughout the period to 50 per cent in 2005, overtaking bilateral creditors in share in 2001.

It comes as no surprise that private lending has been responsible for only a fairly small proportion of the total throughout the period. However, it is significant that the share of private lending grew during the late 1970s and early 1980s reaching a peak of 26.6 per cent in 1982, when banks were frantically trying to recycle petrodollars from proceeds of the second big oil-price hike. In this year commercial bank lending reached a peak of 14.3 per cent of the total. By 2005, however, all private lending was back to 15 per cent, not much above the 1970 level of 13 per cent. This irresponsible lending has thus been laundered into multilateral debt and the commercial banks have in this way been rescued from their over-exposed position by the multilaterals. It is also notable that export credit guarantees hovered between 10 and 12 per cent of the total for most years up to 1988, when a decline began which has brought the share down to less than 2 per cent.

Lower middle income^{lix}

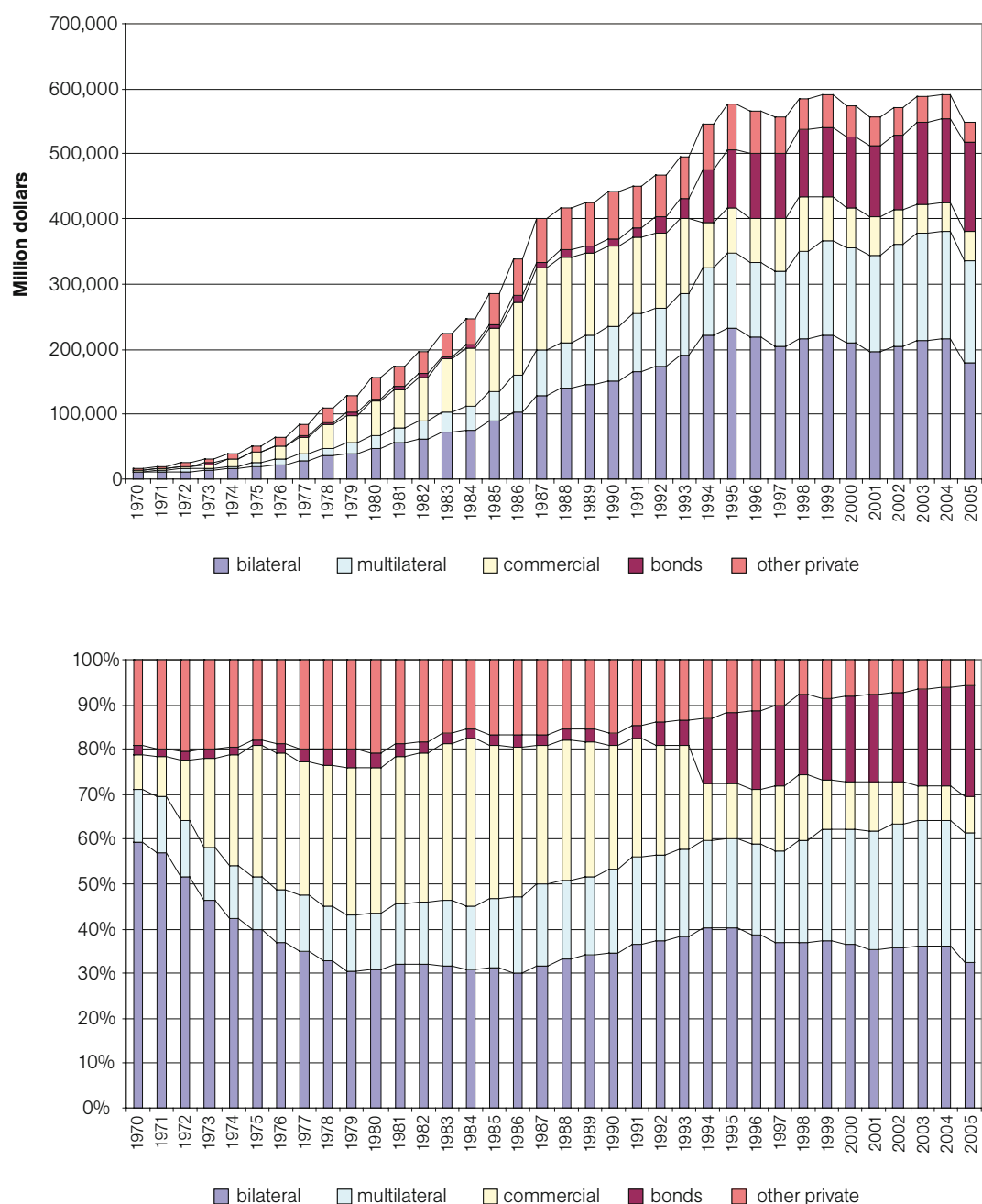
As can be seen from Figure A2 the composition of lower-middle-income debt is rather different. The overall levels follow a similar pattern, with rises in every year until 1995 and declines only in 1996 and 1997, 2000 and 2001, and 2005. Official debt accounted for a large proportion of the total for most of the period, though always a lower proportion than for the low-income countries, falling fast from over 71 per cent in 1970 to a low of 43 per cent in 1979, but followed by a steady rise back up to about 60 per cent since 1994. It has been over 50 per cent for all years except those between 1976 and 1986. Bilateral debt in 1970 was much greater than multilateral, itself accounting for 59 per cent of all debt. This has gradually shifted as multilateral debt has grown in almost every year throughout the period until the two are roughly equal – multilateral now accounts for 29 per cent of all debt compared with bilateral debt share of 32.5 per cent. Where the proportion of official debt has fallen, it has not been the result of any reduction in lending but because commercial bank lending rose by so much more than it. This is primarily explained by the drive by commercial banks to recycle petro-dollars after the big rise in oil prices, first in 1973 and again in 1979, which resulted in large surpluses for the OPEC (Organization of Petroleum Exporting Countries) oil exporters, which they then deposited in the commercial banks. In the mid-1970s, interest rates were often negative in real terms, which encouraged oil importers to borrow even for meeting consumption needs. After the second oil-price shock, however, the Reagan and Thatcher governments responded by raising interest rates, with the result that borrowing became much more expensive. The more recent growth in official debt can be seen as rescuing the commercial banks from their reckless lending before 1985.

Bonds formed an insignificant proportion of the total until the early 1990s. After two years of modest increase, the amount of debt accounted for by bonds shot up 9 percentage points (\$42 billion) in the one year 1994. It is remarkable and worthy of

more investigation than can be given in this study. This is likely to be related to the introduction of Brady bonds from 1990, which converted (often non-performing) loans into tradable assets, thus improving banks' balance sheets, but also reflects the entry of Poland into the market with an issue of \$7 billion. The share taken by bonds grew by a further 10 percentage points more gradually through the following decade and they now account for a quarter of all outstanding debt. By contrast, commercial lending, having grown rapidly in the late 1970s and early 1980s to peak at 37.5 per cent of all debt in 1984 and reaching an absolute peak in 1988 of \$130 billion, declined thereafter and in 2005 constituted only 8 per cent of the total and one-third of that sum.

Another notable feature illustrated by Figure A2 is the importance of 'other private' debt, primarily export credit guarantees. These grew from very small absolute amounts in the early 1970s to a peak of \$71 billion in 1990. However, in proportionate terms it was in the range of 19–20 per cent from 1970 to 1980 before starting a steady decline and now constitutes under 6 per cent of lower-middle-income-country debt.

Figure A2. Evolution of lower-middle-income debt 1970–2005.



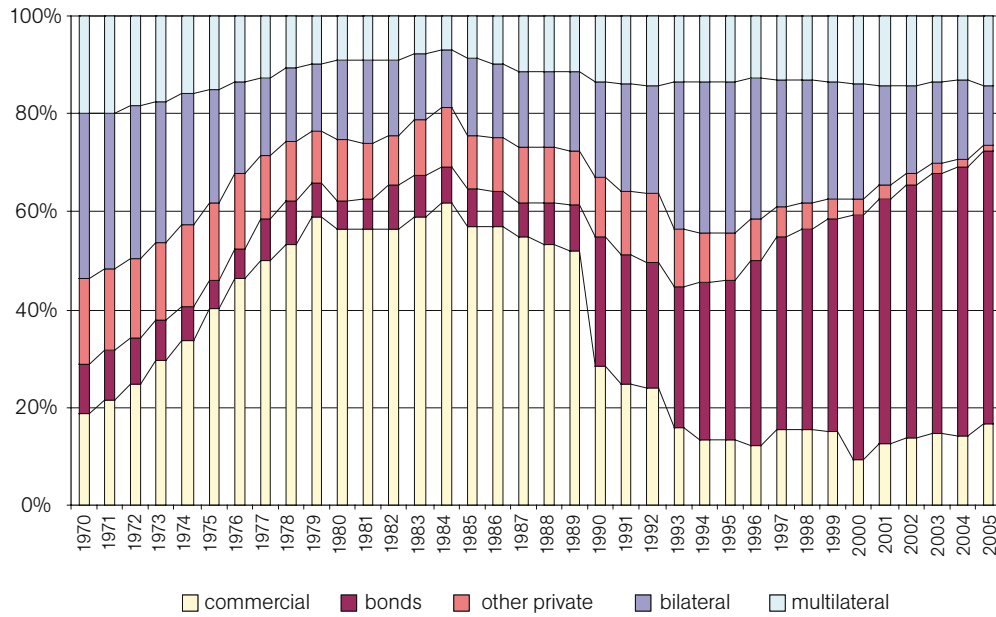
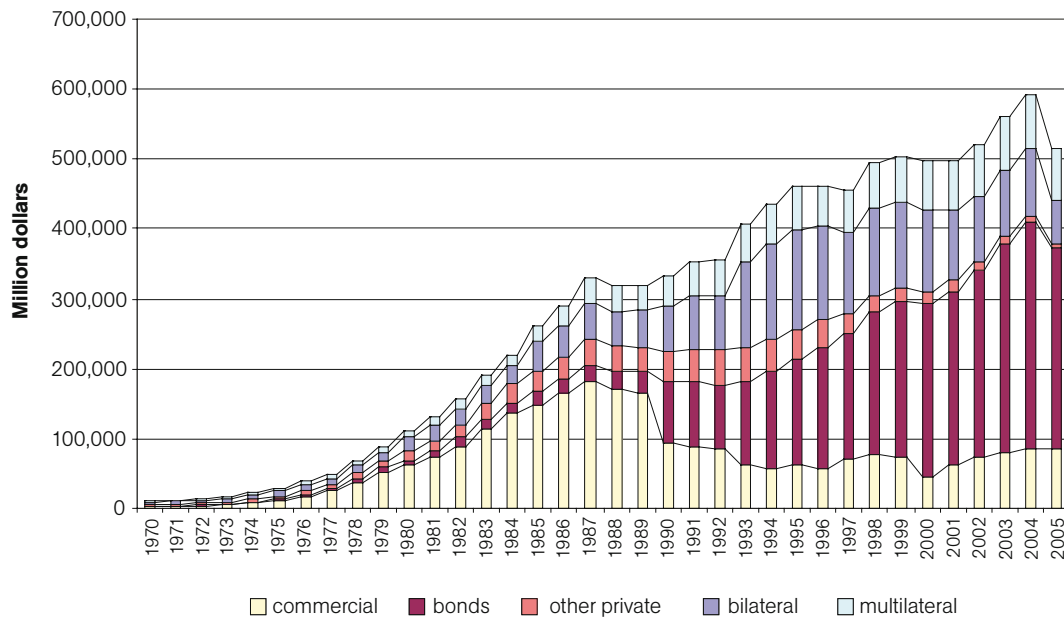
Upper middle income^{ix}

There are a number of interesting aspects about the evolution of upper-middle-income-country debt. Although private lending is a greater proportion of the total for this group than for the poorer countries, as could be expected, official debt accounted for a surprisingly large proportion of the total for a lot of the period, falling fast from 54 per cent in 1970 to a low of 19 per cent in 1984, but followed by a steady rise back up to about 45 per cent by 1994 (helped by a massive increase in bilateral loans to the Russian Federation (of \$43 billion) in 1993, two years after Yeltsin became president and while he was facing a constitutional crisis). This is primarily from bilateral creditors, who contributed 34 per cent of all credit in 1970; a proportion that fell quite rapidly to 12 per cent in 1984 before rising between then and 1994, when it reached a new peak of 31 per cent. This movement no doubt reflects the fact that commercial bank lending to these countries was great in the late 1970s/early 1980s (with the recycling of petro-dollars) and bilateral lenders were subsequently keen to rescue their banks from over-exposure, once the chickens had come home to roost with the debt crises. Multilateral credit contributed 20 per cent of the total in 1970, falling to a low of 7 per cent in 1984 but then rising back up to 14 per cent by 1991, at which proportion it has stayed more or less ever since. In absolute terms, multilateral debt has grown fairly steadily throughout the period, before a slight fall in 2005, presumably mainly reflecting the paying off of IMF credits by Brazil, Argentina and others.

Commercial bank lending rose rapidly from 1970 to 1987, when it reached a peak of \$182 billion, before falling to \$58 billion in 1994 and even \$46 billion in 2000. This latter was not, however, part of a trend and in 2005 it had climbed back up to \$87 billion. In proportionate terms it rose from 18.5 per cent to 62 per cent in 1984, before falling rapidly to 13 per cent in 1994. It has, however, contributed in the region of 15 per cent since then. Bonds formed an insignificant proportion of the total until 1990, when the total outstanding went up by \$58 billion. In that year, Mexico raised \$36 billion and Venezuela \$18 billion primarily as part of the Brady initiative, mentioned above. There was a further leap in 1994 when a further \$22 billion were added to the total. In fact, the increase is more than accounted for by three countries who entered the bond market for the first time in a big way in that year – Brazil raised an extra \$42 billion, and Bulgaria \$5 billion, and South Africa \$2 billion.

In a manner similar to the situation with lower-middle-income countries (but more pronounced) export credits accounted for 17 per cent of outstanding debt in 1970 but that proportion declined to 10 per cent by 1979 and, after a relatively stable share to 1995, has now dropped to only 1.4 per cent. In absolute terms it peaked at \$50 billion in 1992 and is now \$7 billion.

Figure A3. Evolution of upper-middle-income debt 1970–2005.



- i Pettifor A (2002) *Chapter 9/11? Resolving international iebt crises – the Jubilee framework for international insolvency*. (nef: London). http://www.jubileeresearch.org/analysis/reports/jubilee_framework.pdf
- ii Mandel S (June 2006) *Debt relief as if people mattered: a rights-based approach to debt sustainability* (nef: London) (DRAIPM). http://www.jubileeresearch.org/news/debt_relief_final.pdf
- iii Mandel S (September 2006) *Odious lending: debt relief as if morals mattered* (nef: London). <http://www.jubileeresearch.org/news/Odiouslendingfinal.pdf>
- iv In June 2005, the Group of 8 (G-8) major industrial countries proposed that three multilateral institutions—the IMF, the International Development Association (IDA) of the World Bank, and the African Development Fund (AfDF)—cancel 100 per cent of their debt claims on countries that have reached, or will eventually reach, the completion point under the joint IMF-World Bank enhanced Initiative for Heavily Indebted Poor Countries (HIPC Initiative). The HIPC Initiative entailed coordinated action by multilateral organizations and governments to reduce to sustainable levels the external debt burdens of the most heavily indebted poor countries. The MDRI goes further by providing full debt relief so as to free up additional resources to help these countries reach the MDGs. Unlike the HIPC Initiative, the MDRI does not propose any parallel debt relief on the part of official bilateral or private creditors, or of multilateral institutions beyond the IMF, IDA, and the AfDF. However, in early 2007, the Inter-American Development Bank also decided to provide similar debt relief to the five HIPCs in the Western Hemisphere. (Source: www.imf.org).
- v <http://www.jubileeresearch.org>
- vi World Bank's WDI and GDF data bases, UNESCO education statistics.
- vii The Paris Club consists of the main creditor countries with a secretariat in the French Foreign Ministry. The London Club is the equivalent of major commercial creditors.
- viii Multilateral debt relief initiative, often known as the Gleneagles G8 deal.
- ix Only those countries with a per capita income that is low enough to qualify for only IDA (the World Bank's soft loan 'window') can be considered for HIPC.
- x Re-exports can have a very high import content so the net increase in foreign exchange available will be small.
- xi In March 2007, the Inter-American Development Bank (IADB) finalised its part of the MDRI initiative but this is far less generous than AfDB since there is no additionality. All debt cancellation is being funded by the account which offers grants and subsidised loans – in fact four of the five countries involved will have a net cut in resources as a result of this so-called debt relief (see <http://www.jubileeresearch.org/news/IDB's%20approach%20to%20MDRI.pdf>).
- xii Callaghy T (2002) 'Innovations in the Sovereign Debt Regime: from the Paris Club to enhanced HIPC and beyond' (World Bank: Washington DC).
- xiii For an explanation of this and other terms see Mandel S (September 2006) *op. cit.*
- xiv Some of these measures are, no doubt, necessary but the purported benefits (greater competitiveness in exports, lower costs to consumers) are often slow to be realised and the viability of the whole development model (export-focused growth) is open to question, when applied to all countries at the same time.
- xv Mandel S (June 2006) *op. cit.*
- xvi Creditors have a duty to reassure themselves that due process has been followed and so should bear the risk if this is not the case.
- xvii A **collective action clause** (CAC) allows a supermajority (usually 80 or 90 per cent) of bondholders to agree a debt restructuring that is legally binding on all holders of the bond, including those who vote against the restructuring.

- xviii For details of the proposed SDRM, see <http://www.imf.org/external/np/exr/facts/sdrm.htm>
- xix The USA has enough votes on its own to veto all major decisions; creditor countries collectively, which account for 20 per cent of Fund members and 15 per cent of the world's population, have a substantial majority (60.4 per cent) of the votes.
- xx For a detailed analysis of the SDRM see Akyuz Y (2005) *Reforming the IMF: back to the drawing board* (Third World Network: Penang, Malaysia).
- xxi Mandel S (September 2006) *op. cit.*
- xxii Duke University January 2007 and North Carolina February 2007.
- xxiii Khalfan A, King J, Thomas B (2002) *Advancing the odious debt doctrine* (Magill University, Canada).
- xxiv Kramer M, Jayachandran S (2002) 'Odious debt' National Bureau of Economic Research, Working paper No. 8953. Most recently the pair published a further paper on the subject at <http://www.aeaweb.org/aer/contents/mar2006.html>
- xxv <http://www.imf.org/external/np/res/seminars/2002/poverty/mksj.pdf>
- xxvi Bucheit LC, Mitu Gulati G, Thompon RB (2006) 'The dilemma of odious debts' *Duke Law Journal* (forthcoming). http://eprints.law.duke.edu/archive/00001567/01/Dilemma_of_Odious_Debts_9-20-06.pdf
- xxvii A **peremptory norm** (also called **jus cogens**, Latin for 'compelling law') is a fundamental principle of international law considered to have acceptance among the international community of states as a whole.
- xxviii As indeed does the UK Government, according to its recent White Paper on International Development (July 2006) p73.
- xxix At purchasing power parity. For a definition of this see Mandel (June 2006) *op. cit.*
- xxx World Bank's WDI and GDF data bases. Data for 2004.
- xxxi *The Guardian*, 15 April 2006.
- xxxii Edward P (2006) 'The ethical poverty line: a moral quantification of absolute poverty', *Third World Quarterly*, **27**(2).
- xxxiii We also carried out the same calculations using the more common \$2-a-day poverty line. Even at this lower level, our results show that between \$241 and \$425 billion of debt cancellation is needed for a wide range of countries if their debt is to be brought down to sustainable levels.
- xxxiv IMF (2007) Initiative for Heavily Indebted Poor Countries (HIPC) and Multilateral Debt Relief Initiative (MDRI) – Status of Implementation (IMF: Washington DC). <http://siteresources.worldbank.org/INTDEBTDEPT/ProgressReports/21050877/HIPCProgressReport20060821.pdf> .
- xxxv World Bank (2007) *HIPC at a glance* (World Bank: Washington DC).
- xxxvi The larger numbers quoted freely elsewhere relate to nominal values, not net present values, and are therefore not comparable with our figures.
- xxxvii Domestic interest rates can be much higher than international ones.
- xxxviii The carry trade is where investment funds borrow in markets where interest rates are low (quintessentially Japan in recent years) to invest in markets where interest rates are higher.
- xxxix The origin of the Asian crisis was not public but private commercial debt. Banks in Thailand borrowed short to lend long, and so were extremely vulnerable when panic set in and foreign banks refused to roll over the short-term loans they had offered. However, the same vulnerability exists when domestic bearer bond debt is held by foreigners who can sell and take their money elsewhere at will.
- xl The foreign exchange risk for the borrower is that the value of their currency may decline, increasing both the amount of interest to be paid in terms of local currency and the size of their outstanding loans. When domestic debt is held by foreigners, this risk is transferred to the holder, who would therefore only hold the debt if compensated by a higher interest rate. This is the theory at any rate. The opposite applies in countries where an appreciation of the currency is more likely than depreciation.
- xli For a discussion about this, see Mandel S (September 2006) *op cit.*
- xlii This is the transfer from North to South, taking account of the initial loan, interest payments, repayments and any cancellation. A negative figure is a net transfer from South to North.
- xliii For a copy of papers presented to the symposium see <http://www.blackwell-synergy.com/toc/eia/21/1>
- xliv Mandel (June 2006) *op. cit.*
- xlv Some of these were pointed out by readers of the earlier papers, for which contributions we are very grateful.
- xlvi The elections which have just been held have been widely criticised. It is too early to judge the tenor of the new president but the process, however flawed, has resulted in the first relatively peaceful transition from one elected government to another in Nigeria.
- xlvii It could, however, be argued that those countries that are prosperous enough to be able to take out extra credit after taking into account human rights needs (DRAIPM calculated that about 100 could not) will be sufficiently sophisticated that financial sanctions should hit the rich more than the poor and could generate high pressure for regime change within a short period.
- xlviii In this latter case, there is a problem of how to determine who had the standing to make a case. In a democratic system there are often losers that are prepared to cry foul, and the issue is seldom absolutely clear cut.
- xlix Attempts by current creditors to hold up the process by refusing to appoint nominees would be mitigated by the fact that debt service would

no longer be being paid to them. However, it is anticipated there may be problems getting official and commercial creditors to agree on a nominee. Former debtors would not have this incentive, which may mean they forfeit the right to nominate, to be replaced by one official and one commercial nominee.

- i Payment into the escrow account could be encouraged by a penalty rate of interest for unpaid amounts if the judgement went against the debtor country. On the other hand, where there was in any event a clear case for a reduction in debt service on debt sustainability grounds an early adjudication reducing the amount to be paid into the escrow account could be made.
- ii World Bank (2006) Debt relief for the poorest: an evaluation update of the HIPC Initiative <http://www.worldbank.org/ieg/hipc/> [13 October 2007].
- iii One corollary of this greater importance of acceptable levels of democracy should be that more resources be allocated by donors and international bodies to the support of the electoral process. Perhaps a global fund to support the democratic process would help to end the problems of funding of campaigning and of political parties (and the undue influence of the rich and corporate world) both in the North and the South? This would elevate due democratic process to the status of a world public good. Given the importance globally of the governance of the North this is not an idle point.
- iiii Involvement of UNEAD in the organisation of elections would create a conflict of interest between this and proper election monitoring. Ideally the body monitoring elections should not be involved in their organisation.
- iv Funds will also need to be made available to assist in the organisation of elections where the resources to run free and fair polling do not exist. This should be by a body such as the UNEAD.
- v This would be a problem if there is only one panellist from a region.
- vi By the way, this ties in with proposals being developed within **nef** around global governance. We want to propose that heads of major international bodies (UN, WB, IMF, WHO etc.) are elected by legislatures with this sort of weighting.
- vii If a constituency has, say, three panellists to choose, one should be selected every two years. In this way (after the system is up and running) one member will have had two and one four years' experience whenever a new member is chosen. .
- viii Those with per capita national income under \$875 in 2005.
- ix Those with per capita income of between \$876 and \$3,465 in 2005.
- x Those with per capita income above \$3,465 and below \$10,725 in 2005.

One of the other things we do

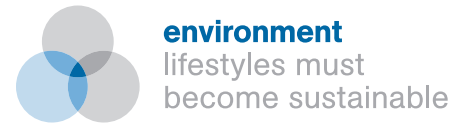


Photo: Marcelo Alves

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For more information please call
020 7820 6300

Written by: Stephen Mandel, Senior economist, new global economy programme, **nef**

Edited by: Mary Murphy

Design by: Rapsiderweb

new economics foundation

3 Jonathan Street
London SE11 5NH
United Kingdom

Telephone: +44 (0)20 7820 6300
Facsimile: +44 (0)20 7820 6301
E-mail: info@neweconomics.org
Website: www.neweconomics.org

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