



Opinion of the Advisory Council on Policy Coherence for Development “Managing the external debt of developing countries”

1. Introduction

01. This opinion is concerned with the management of the external debt of developing countries. It makes a series of recommendations aimed at aligning debt management with the principles of international law and the Sustainable Development Goals. In particular it analyses the role of “vulture funds” in a context of the annulment appeal submitted by the fund NML Capital to the Constitutional Court against the Belgian law of July 2015. This opinion was approved by the Advisory Council on Policy Coherence for Development at the Council meeting of 12th December 2016.

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2. Overview of the problems

02. According to the Declaration on the Sustainable Development Goals adopted by the United Nations General Assembly in September 2015¹, the “debt burden” of developing countries is an obstacle to the achievement of these goals. As part of Sustainable Development Goal 17, on the subject of stronger global partnerships for sustainable development, the Heads of State and Government committed to “assist developing countries in attaining long-term debt sustainability through co-ordinated policies aimed at fostering debt financing, debt relief and debt restructuring, as appropriate, and address the external debt of highly indebted poor countries to reduce debt distress” (para. 17.4).

03. As of 31st December 2014, Belgium held over 305 million euros in credits with regard to forty-three countries, including over 72 million euros towards eight debtor countries considered “low income countries” and over 22 million euros towards nine debtors classified as “less developed countries”. The credit contracts of DuCroire (Belgium’s public credit insurer) amounted to some 647.68 million euros towards seventeen debtor countries as of the same date.

04. The “HIPC initiative”, designed to provide relief for approximately thirty highly indebted poor countries and improve the international outlook, following the increase in raw material prices and the decrease in interest rates, contributed towards making the debt of developing countries more sustainable during the 2000s. This encouraged several poor countries to turn to the international financial markets for borrowing. Since 2010, however, the decrease in raw material prices and a worsening international outlook has made indebted countries more vulnerable to external shocks².

05. In the case of a payment default, in the absence of a multilateral debt restructuring mechanism that would allow indebted countries to negotiate a restructuring of their debt according to terms that apply to all creditors, “free rider” practices among creditors are common. This term is used to denote the behaviour of creditors refusing to participate in restructuring and asking for their credits to be reimbursed in full, to the detriment of indebted countries and other creditors.

06. Among the factors that particularly serve to weaken developing countries is the emergence of what are known as “vulture funds”, specialising in buying up public debt at a low cost with a view to eventually undertaking a judicial procedure to obtain the full nominal value of these credits in addition

¹ A/70/L.1.

² IMF, “Global Financial Security Report”, October 2015; United Nations Conference on Trade and Development (UNCTAD), *Economic Development in Africa. 2016 Report. Debt dynamics and development finance in Africa*, New York and Geneva, 2016.



to interest incurred and any potential penalties³.

07. The Law of 12th July 2015 on combating the activities of vulture funds⁴ allows, under certain conditions, a Belgian judge to limit the rights of “vulture funds” to be reimbursed to the value paid when buying back the debts in question⁵. In other words, Belgian law prevents vulture funds from asking for a higher amount than they paid for the debt on a secondary market. In March 2016 *NML Capital*, subsidiary of the group *Elliott Management Corporation*, submitted an annulment appeal against this law before the Constitutional Court.

08. According to international law, some of the debts of developing countries are illegal, odious or illegitimate debts. Illegal debts are debts that were contracted in violation of legal procedures in place (for example by circumventing parliamentary procedures), those shaped by serious misconduct of the creditor (for example by resorting to corruption, threats or coercion) or resulting from loans associated with conditions that violate national law (in the country of the debtor or creditor) and/or international law, including the general principles of law. According to the guiding principles on foreign debt and human rights, odious and illegitimate debt meet three criteria: “i) The absence of consent by the debtor State’s population; ii) The absence of benefit to the debtor State’s population; and iii) The creditor’s awareness of the above facts.”⁶

09. Managing sovereign debt is not a problem that is specific to developing countries. Several Member States of the European Union have unsustainable levels of public debt and are vulnerable to speculation on debt instruments which is likely to lead to a downgrading of their financial rating, an increased risk premium and difficulties paying back the debt. An international framework promoting consistency between debt management and achieving the Sustainable Development Goals would therefore be equally beneficial for developed countries.

3. Recommendations

10. The advisory council on policy coherence for development recommends that Belgium undertake the following activities:

- Set up an audit of Belgian credits to identify the possible share of illegal, odious and illegitimate debts held by Belgium, by applying the resolutions adopted by all Belgian parliamentary assemblies⁷ and international law⁸.
- Cancel Belgian credits in developing countries which constitute illegal, odious or illegitimate debts.

³ A. Zacharie and A. Gambini (coord.), *Fonds vautours : rationalité, éthique et solutions*, Dounia - Revue d’intelligence stratégique et des relations internationales, n°5, L’Harmattan/CISRI, June 2012

⁴ Mon. b., 11 September 2015.

⁵ This law follows on from a first law from 2008 preventing vulture funds from seizing financial resources relating to Belgian public development aid.

⁶ The guiding principles on foreign debt and human rights appear as an annex to the report of the independent expert in charge of examining the effects of foreign debt and other related international financial obligations of States on the full enjoyment of all human rights, particularly economic, social and cultural rights, Cephias Lumina, presented at the 20th session of the Human Rights Council on 10 April 2012 (A/HCR/20/23). The guiding principles have been approved by the Human Rights Council.

⁷ Especially the Resolution of the Belgian Senate from 27 March 2007 on cancelling the debt of less developed countries.

⁸ Especially the guiding principles on foreign debt and human rights, Annex to the report of the independent expert in charge of examining the effects of foreign debt and other related international financial obligations of States on the full enjoyment of all human rights, particularly economic, social and cultural rights, Cephias Lumi, of 10 April 2012 (A/HCR/20/23).



- Sign a framework agreement with the relevant developing countries to define an investment plan financed through the sums released by cancelling illegal, odious or illegitimate debts and aimed at sectors ranked as priorities for attaining the Sustainable Development Goals.
- Encourage the other European Union Member States and the Paris Club to implement equivalent measures.

11. Contribute towards putting an end to the practices of “vulture funds”:

- Confirm Belgium’s policy for combating the practices of vulture funds, including as part of the appeal before the Constitutional Court to maintain the Law of 12th July 2015 relating to efforts to tackle the activities of vulture funds prohibiting a speculative fund from benefiting from a clear disproportion between the price of buying the credit and the amount requested before the courts.
- Encourage the other European Union Member States and the OECD to adopt equivalent legislation.

12. Promote the introduction of a multilateral mechanism for restructuring sovereign debt:

- Support the introduction of a multilateral mechanism for restructuring sovereign debt, which is independent, transparent and fair, in order to allow States that have defaulted on payment to negotiate agreements to restructure their debt which applies to all creditors and prevent “free riding” practices.
- Apply the nine principles on restructuring sovereign debt defined in the resolution adopted by the United Nations General Assembly on 10th September 2015⁹.
- Promote the systematic integration of “collective action clauses” in new bond loans, guaranteeing a special majority of 65% of creditors in the event of restructuring of debt, with this agreement applying to all creditors.

4. Justification of the recommendations

13. Various bodies of the United Nations that are competent in the domain of human rights have been underlining for several years that States’ payment of debt servicing could impede development and the full enjoyment of human rights¹⁰. Two concerns in particular have been expressed in recent years. They concern the obstacle of paying back debt to achieving economic, social and cultural rights, as well as the Sustainable Development Goals; and the actions of “vulture funds” which buy up credit at low prices in order to claim back the face value of the loan before national courts.

External debt as an obstacle to achieving economic, social and cultural rights and the Sustainable Development Goals

14. In its resolution of 23rd March 2016, the UN’s Human Rights Council highlights that the “world financial and economic crisis is still threatening debt sustainability in some developing countries through, inter alia, its impact on the real economy and the increase in borrowing undertaken in order to mitigate the negative impacts of the crisis and that the austerity measures adopted in response to that crisis have had a robust social impact that has perpetuated or exacerbated inequality”. A worsening of the international outlook has caused debt viability problems in several developing

⁹ Resolution A/69/L.84 of the UN General Assembly adopted on 10 September 2015.

¹⁰ See the resolutions and decisions adopted by the Commission on Human rights on the effects of the foreign debt on the full enjoyment of human rights and, in particular the economic, social and cultural rights, particularly resolutions 1998/24, 1999/22, 2000/82, 2004/18 and 2005/19 of the Commission, dated 17 April 1998, 23 April 1999, 26 April 2000, 16 April 2004 and 14 April 2005, as well as resolutions 7/4, 11/5, 14/4, 17/7, 19/38, 20/10 of the Human Rights Council, dated 27 March 2008, 17 June 2009, 17 June 2010, 16 June 2011, 23 March 2012 and 18 July 2012 and the decision 12/119 of the Council dated 2 October 2009.



countries: according to a study by the NGO *Jubilee UK*¹¹, twelve developing countries have difficulties making payments¹², twenty-two countries run the risk of eventually facing similar difficulties (including three countries that are partners to Belgium: Burkina Faso, Mali, Niger)¹³ and fourteen other countries have a “very high” risk of excessive external debt (including four partner countries to Belgium: Mozambique, Uganda, Senegal and Tanzania)¹⁴.

15. Debt audits are one of the recommendations included in the UN’s Guiding Principles on Foreign Debt and Human Rights. The audit should “assess the loan contraction process, use of loan funds and the impact of debt on development and the realization of human rights” (paragraph 68). Furthermore it should be based on “participation” and “transparency”. These terms are specified in paragraphs 29, 30, 31 and 32 and are developed in the following section.

16. The Resolution from the Senate from 27th March 2007 asks the government to introduce a moratorium with a freeze on interest on the servicing of the bilateral debts of less developed countries (LDC)s and heavily indebted poor countries (HIPC)s; and to “sign as quickly as possible a framework contract to define the terms and conditions of completely cancelling the debt of these countries and [...] determine the sectors of human development linked to the Millennium Development Goals which should be financed as a priority by the funds freed up by this cancellation”.

Steps to tackle “vulture funds”

17. The activities of “vulture funds” represent an obstacle to the attainment of human rights and the Sustainable Development Goals. As the UN Human Rights Council affirmed in its resolution of 23rd September 2014: “the activities of vulture funds highlight some of the problems in the global financial system and are indicative of the unjust nature of the current system, which directly affects the enjoyment of human rights in debtor States”. African countries are the main targets of vulture funds, with an average of eight new procedures per year¹⁵.

18. In its Resolution of the 27th July 2015 (paragraph 100), the United Nations General Assembly recommends that States legislate against “vulture funds” which, on the one hand, deprive States in a financially difficult position of the sums needed for their development and the welfare of their people and, on the other hand, disrupt the collective debt restructuring activities of highly indebted countries.

19. The Law of 12th July 2015 relating to efforts to tackle the activities of vulture funds aims to ban the practices of “vulture funds”. According to this law, a creditor cannot obtain the reimbursement of credits that have been acquired in the presence of “the clear disproportion between the value of buying back the loan or the credit by the creditor and the face value of the loan or the credit or even between the value of buying back the loan or the credit by the creditor and the sums demanded as payment” before a court of law in Belgium, provided that at least one of the other elements mentioned

¹¹ Jubilee UK (2015), “The new debt trap”, London, p. 13.

¹² These twelve countries have a debt that is higher than 30% of their GDP and spend more than 15% of their income on debt repayment: Belize, Costa Rica, Gambia, Grenada, Marshall Islands, Jamaica, Lebanon, Dominican Republic, Salvador, Sri Lanka, Saint Vincent and the Grenadines and Tunisia.

¹³ These twenty-two countries have a debt that is higher than 30% of their GDP and will in the coming years, according to estimates, spend more than 15% of their income on repayment or will have a budgetary deficit of more than 5% of their GDP: Burkina Faso, Cambodia, Cameroon, Ivory Coast, Djibouti, Guyana, Haiti, Kyrgyzstan, Lesotho, Liberia, Madagascar, Maldives, Mali, Niger, Central African Republic, Rwanda, Sierra Leone, Saint Lucia, Chad, Togo, Tonga, Zambia

¹⁴ The fourteen countries are the following: Bhutan, Cape Verde, Dominica, Ethiopia, Ghana, Laos, Mauretania, Mongolia, Mozambique, Uganda, Samoa, São Tomé and Príncipe, Senegal, Tanzania.

¹⁵ United Nations Human Rights Council, “Effects of foreign debt and other related international financial obligations of States on the full enjoyment of all human rights, particularly economic, social and cultural rights: the activities of vulture funds”, resolution A/HRC/27/L.26, Geneva, 23 September 2014.



by the law is present, among which: a situation of financial distress of the State at the time of buying the credit; the creditor being domiciled in a tax haven; refusal to take part in debt restructuring; or even the harmful effect of action on the living conditions of the population of the State under attack. If this condition is met, the advantage sought by the creditor is qualified as “illegitimate”. Consequently, the creditor may only receive the amount paid for the credit, including when a favourable decision has been made to the foreigner. In March 2016, the fund *NML Capital* submitted an appeal before the Constitutional Court to cancel the Law of 12th July 2015 relating to efforts to tackle the activities of vulture funds. At the time of adopting this opinion, this appeal was still pending.

20. The Addis Ababa Action Agenda on development financing (July 2015) recommends that governments adopt legal measures akin to those undertaken in Belgium: “We are concerned by the ability of non-cooperative minority bondholders to disrupt the will of the large majority of bondholders who accept a restructuring of a debt-crisis country’s obligations, given the potential broader implications in other countries. We note legislative steps taken by certain countries to prevent these activities and encourage all Governments to take action, as appropriate”¹⁶.

21. The Resolution of the European Parliament of 19th May 2015 on Financing for Development “insists that sustainable debt solutions, including standards for responsible lending and borrowing, must be facilitated through a multilateral legal framework for sovereign debt restructuring processes, with a view to alleviating the debt burden and avoiding unsustainable debt; asks the EU to engage constructively in the UN negotiations on this framework;” (point 46).

22. The resolution adopted on 10th September 2015 by the United Nations General Assembly defines nine principles on sovereign debt restructuring, in order to put an end to the “free riding” practices of “vulture funds”¹⁷.

¹⁶ Addis Ababa Action Agenda resulting from the third international conference on financing for development (Addis Ababa Action Agenda), approved by the UN GA, resolution 69/313 of 27 July 2015, paragraph 100, http://www.un.org/ga/search/view_doc.asp?symbol=A/69/L.82&Lang=E

¹⁷ <http://www.rightingfinance.org/wp-content/uploads/2015/09/resolution.pdf>;
<http://eurodad.org/UNdebtprinciples>.