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Report of the independent expert on 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, Cephas Lumina*

Summary

Despite their limitations, international debt relief efforts have helped reduce the external debt burden of heavily indebted poor countries (HIPCs) and contributed to the creation of fiscal space for resources to be channelled to poverty-reducing expenditures and economic development in these countries. Evidence also suggests that the additional fiscal space has allowed some HIPCs to increase their public spending on essential, human rights-related social services, such as health care and education, thereby contributing to the realization of human rights, particularly economic, social and cultural rights, in these countries.

Nevertheless, the voluntary nature of these debt relief measures has created opportunities for some commercial creditors to eschew such efforts and then attempt to recover the full value of their debt through litigation. These creditors — termed "vulture funds" — purchase the defaulted debt at significant discounts, hold out for other creditors to cancel their debts and then aggressively pursue repayments that are vastly in excess of the amount that they paid for the debt. These activities not only dilute the impact of debt relief by reducing the resources available to the targeted debtor countries to finance development and reduce poverty, they also diminish the capacity of indebted poor countries to create the conditions necessary for the realization of human rights, particularly economic, social and cultural rights.

The present report, which is submitted in accordance with Human Rights Council resolution 11/5, is intended to draw global attention to the adverse impacts of vulture fund activities on debt relief and on the capacity of poor countries to fulfil their human rights

* Late submission.

obligations and attain their development goals. It also includes a call for definitive international and national action to combat vulture fund activity.

The report has five sections. In section I, the independent expert introduces the report. In section II, the activities that the independent expert has undertaken since his last report to the Council (A/HRC/11/10) are outlined. In section III, the independent expert briefly discusses what vulture funds are and provides some illustrations of vulture fund litigation against HIPCs. He also outlines the impact of vulture fund activities on debt relief and their implications for the realization of human rights in the countries targeted by these predatory creditors. In section IV, the independent expert sketches official initiatives that have been undertaken or are being considered to combat vulture funds. In section V, he offers some recommendations on measures to address the negative effects of vulture fund activities.

Contents

I. Introduction

1. The present report is submitted in accordance with Human Rights Council resolution 11/5, in which the Council requested the independent expert on 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, to submit analytical reports to the Council and the General Assembly on the implementation of that resolution.

2. In his report to the Council at its eleventh session (A/HRC/11/10), the independent expert outlined a preliminary conceptual framework for understanding the link between foreign debt and human rights, based on international legal standards. In his report to the General Assembly (A/64/289), he highlighted the relevance of the concept of illegitimate debt to international efforts to find a fair and sustainable solution to the debt crisis, and argued that human rights considerations must inform the formulation of the concept in precise terms. The present report is intended to achieve three objectives: (a) to draw global attention to the negative impacts of "vulture fund" activities on international debt relief efforts and on the capacity of indebted poor countries that have benefitted from debt relief to create the necessary conditions for the realization of human rights and attainment of their development goals; (b) to examine the measures and proposals designed to combat these speculative investors; and (c) to make recommendations concerning these initiatives.

II. Activities undertaken

3. Since he submitted his first report to the Council (A/HRC/11/10) in June 2009, the independent expert has engaged in a broad range of activities. The activities that he undertook during the period March to July 2009 are outlined in his report to the General Assembly (A/64/289).

4. From 31 August to 2 September 2009, the independent expert participated in the Social Forum of the Council in Geneva, at which he spoke on the impact of the global economic and financial crises on efforts to combat poverty. On 12 November, he participated in the inaugural meeting of the expert working group established by the United Nations Conference on Trade and Development (UNCTAD), under its project on promoting responsible sovereign lending and borrowing, to provide technical and policy analysis to inform the discussions concerning principles that could promote responsible sovereign lending and borrowing. On 17 December, he issued a press statement in which he expressed regret at the decision of the British High Court that Liberia must pay a debt dating to 1978 to two vulture funds. This event and other initiatives detailed in this report informed the decision of the independent expert to focus the present report on vulture funds.

5. From 11 to 13 January 2010, the independent expert participated in a colloquium in Geneva on human rights in the global economy, which was organized by the International Council on Human Rights Policy in collaboration with Realizing Rights: The Ethical Globalization Initiative. On 21 January, he participated in a panel discussion on Millennium Development Goal 8, Targets B and D on debt relief, held by the High-Level Task Force on the Implementation of the Right to Development during its sixth session (14–22 January) in Geneva. During this event, the independent expert delivered a statement in which he critically assessed the achievements and limitations of the multilateral debt relief initiatives in response to statements by representatives of the World Bank and the International Monetary Fund (IMF).

6. In addition, the independent expert undertook his first country missions to Norway (28–30 April 2009) and Ecuador (2–8 May 2009) at the invitation of the Governments of these countries. The main objective of the missions was to examine the unique roles of the two countries in the debate concerning illegitimate debt and to consider the effect, on the enjoyment of human rights, of the decisions by both countries concerning public debt, from the creditor and debtor perspectives. The official report on these missions is contained in the addendum to this report (A/HRC/14/21/Add.1).

7. For ease of reference, all United Nations documents related to the work of the independent expert, including reports to the General Assembly and the Council, interventions on foreign debt and human rights, and press statements, are available on the website of the Office of the High Commissioner for Human Rights at www2.ohchr.org/english/issues/development/debt/index.htm.

III. Vulture funds

A. What are "vulture funds"?

8. The term "vulture funds" is used to describe private commercial entities that acquire, either by purchase, assignment or some other form of transaction, defaulted or distressed debts, and sometimes actual court judgements, with the aim of achieving a high return. In the sovereign debt context, vulture funds (or "distressed debt funds", as they often describe themselves) usually acquire the defaulted sovereign debt of poor countries (many of which are heavily indebted poor countries (HIPCs)) on the secondary market at a price far less than its face value and then attempt, through litigation, seizure of assets or political pressure, to seek repayment of the full face value of the debt together with interest, penalties and legal fees.[1] According to the African Development Bank (AfDB), vulture funds have averaged recovery rates of approximately 3 to 20 times their investment, equivalent to returns of 300 to 2,000 per cent.[2] AfDB describes these recovery rates as "probably the highest in the distressed debt market".[3] At present, there are neither laws that limit the amount of interest or profit such funds can collect through litigation, nor regulatory frameworks that require disclosure of the amount such funds paid to purchase the debt.

9. It is difficult to state with precision how many lawsuits have been instituted by vulture funds. However, it is estimated that there have been over 50 lawsuits by commercial creditors against HIPCs and many of these are still outstanding.[4] According to the World Bank and IMF, 54 court cases were instituted against 12 HIPCs between 1998 and 2008.[5]

[1] See African Development Bank (AfDB), "Vulture funds in the sovereign debt context". Available from www.afdb.org/en/topics-sectors/initiatives-partnerships/african-legal-support-facility/vulture-funds-in-the-sovereign-debt-context/.

[2] Ibid.

[3] Ibid.

[4] Examples include Greylock Global Opportunity registered in the British Virgin Islands and owned by Greylock Capital Management, which sued Nicaragua and was awarded US$ 50.9 million; FG Hemisphere registered in the United States, which sued the Congo and the Democratic Republic of the Congo and was awarded US$ 151.9 million and $81.7 million, respectively; Kensington International, registered in the Cayman Islands and owned by Elliott Management, which sued the Congo and was awarded US$ 118.6 million; and Donegal International registered in the British Virgin Islands (ownership unclear), which sued Zambia and was awarded US$ 15.4 million.

[5] International Development Association (IDA) and IMF, "Heavily Indebted Poor Countries (HIPC) Initiative and Multilateral Debt Relief Initiative (MDRI) – status of implementation" (2008), para. 38.

Of those, 33 had not been settled as of September 2008. In the majority of cases a court judgement had been granted, for an estimated total of $1.2 billion (excluding awards extinguished through Debt Reduction Facility buy-backs). The potential impact of court awards varied from less than 0.5 per cent of the debtor country's gross domestic product (GDP) to 49 per cent in the case of Liberia.[6]

10. The 2009 report on the status of implementation of the HIPC Initiative and Multilateral Debt Relief Initiative indicates that litigation by commercial creditors appeared to be "less of a problem" in 2009 as compared to the previous year and that the number of cases still pending declined from 33 in 2008 to 14 in 2009.[7] However, the same report warns that "the threat of new litigation remains" and states that new lawsuits were initiated in 2008 against the Democratic Republic of the Congo, Sierra Leone, the Sudan and Zambia.[8]

11. Commercial creditor litigation is not confined to HIPCs. According to a study by the Trade Association for the Emerging Markets (EMTA), at least nine non-HIPC countries have been the subject of such litigation.[9] In a number of these cases, the litigating creditor was awarded what EMTA has described as "a substantial amount" relative to what was paid for the debt obligation in the secondary market, or to what other creditors who voluntarily exchanged their debt in the restructuring received.[10]

12. Vulture fund lawsuits tend to be instituted in the courts of the developed countries. This may be where the vulture fund is registered or it may be the jurisdiction specified in the loan agreement. Most lawsuits are filed in courts in the United States of America, the United Kingdom of Great Britain and Northern Ireland and France, which are perceived as "creditor-friendly" jurisdictions. A small number of lawsuits have been filed in the courts of HIPCs.

13. It is notable that vulture funds are often secretive, both in terms of their ownership and operations, and many of them are incorporated in offshore financial centres and banking secrecy jurisdictions, commonly referred to as tax havens.[11] Some are owned by large financial institutions such as hedge funds (often based in the United States) and in other cases their ownership is obscure. Often, companies are established to pursue a single debt. For example, Donegal International Limited, which sued Zambia in 2006 (see below), was incorporated in the British Virgin Islands on 18 December 1997 by Debt Advisory International LLC, a company based in the United States and owned by Michael Sheehan,

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It should be noted, however, that IMF only tracks private creditor lawsuits for HIPC Initiative eligible countries that have reached the decision or completion point.

[6] Ibid., para. 38.

[7] IDA and IMF, "Heavily Indebted Poor Countries (HIPC) Initiative and Multilateral Debt Relief Initiative (MDRI) – status of implementation" (2009), para. 24. According to IDA and IMF, the drop in the number of active cases is attributable to Debt Reduction Facility operations in Nicaragua and Liberia, out-of-court settlements by Cameroon, the Republic of the Congo, Sierra Leone and Zambia, and the discontinuation, by five creditors, of lawsuits against Nicaragua (para. 24).

[8] Ibid., para. 25.

[9] These are Argentina, Brazil, Bulgaria, Costa Rica, Ecuador, Panama, Paraguay, Peru and Poland. However, EMTA states that it is "unable to confirm that this is a complete list of cases brought against non-HIPC sovereigns in the restructuring context". (EMTA, "Creditor litigation in the non-HIPC sovereign debt restructuring context: EMTA case summaries", discussion draft (2009), p. 1).

[10] EMTA, "Preliminary analysis of creditor litigation in the non-HIPC sovereign debt restructuring context", discussion draft (2009), p. 3.

[11] Many tax havens are located in Europe, or are dependencies or overseas territories of European countries. See European Network on Debt and Development (Eurodad) and others, "Addressing development's black hole: regulating capital flight" (May 2008), p. 9.

with the sole aim of pursuing a debt owed by Zambia to Romania. As at the time of its litigation against Zambia, Donegal was owned by Select Capital Limited, a company registered in the British Virgin Islands on 27 June 1997. In the *Donegal International* case, the court found that the "ultimate ownership of Select Capital (was) rather obscure" and in his testimony before the court, Mr. Sheehan said that Select Capital had been set up offshore because "many of the investors were European and did not want to be subject to US tax".[12]

14. The independent expert supports the view that tax havens facilitate the secretive manner in which vulture funds operate as well as the flight of much-needed capital from developing countries.[13] Consequently, he considers that a key priority for the international community should be to end this secrecy and lack of transparency. In his estimation, tackling tax havens would also help address money laundering, tax evasion and capital flight.

B. Case studies

Liberia

15. In 1978 Liberia borrowed US$ 6.5 million from Chemical Bank, a company based in the United States.[14] The bank sold the debt to FH International Financial Services Inc. and Sifida Investment Company S.A., which later brought an action for its recovery before a court in New York. On 19 June 2002, the court entered a default judgement against Liberia for approximately US$ 18.4 million. Following the judgement, the debt was assigned several times by FH International Financial Services and Sifida to third parties and back to the two judgement creditors. The debt was subsequently assigned to Hamsah Investments Ltd. (registered in the British Virgin Islands) and Wall Capital Ltd. (registered in the Cayman Islands).

16. In June 2008, Hamsah Investments and Wall Capital commenced proceedings in the High Court in London to register, as an English judgement, the judgement of the New York court.[15] On 26 November 2009, the High Court ordered Liberia to pay the claimants more than US$ 20 million including interest. While it accepted that Liberia was "short of money" and that the judgement debt was "a substantial sum", the court stated that Liberia "must do the best they can".[16] The court rejected the submission of Liberia that it had been unable to respond to the claim before the New York court because of the financial difficulties which it faced, particularly during the period of the country's civil war.[17] The court also held that

[12] *Donegal International Ltd. v. Republic of Zambia & Another* [2007] EWHC 197 (Comm.), para. 27.

[13] See Jubilee Debt Campaign, "Time to stop the debt vultures" (June 2009). The flow of financial resources from developing to developed countries is estimated at US$ 500 billion – US$ 800 billion each year (Eurodad, "Addressing development's black hole", p. 4). See also L. Ndikumana and J.K. Boyce, "New estimates of capital flight from sub-Saharan Africa: linkages with external borrowing and policy options", Working Paper No. 166 (Political Economy Research Institute, University of Massachusetts, April 2008).

[14] See H. Stewart, "Vulture funds sue Liberia for £12m in high court", 25 November 2009. Available from www.guardian.co.uk/business/2009/nov/25/vulture-funds-sue-liberia.

[15] See *Hamsah Investments Ltd. & Anor v. The Republic of Liberia*, Case No. 2008/587 (High Court of Justice, London), judgement of 26 November 2009.

[16] Ibid., para. 29.

[17] Ibid., paras. 4 and 17.

the debt rescheduling agreements Liberia had reached with its Paris Club creditors did not affect the obligations of the State to the private companies.[18]

17. Liberia, an HIPC with a GDP of US$ 870 million, ranks 169th out of 182 countries in the Human Development Index.[19] Over 94 per cent of the country's population of more than 4 million lives on less than US$ 2 per day, while the unemployment rate is as high as 85 per cent. Life expectancy is less than 50 years and only slightly more than a third of the population is literate. The estimated adult HIV prevalence rate is 1.7 per cent.[20] The country is attempting to recover from the effects of a devastating civil war that include badly damaged infrastructure as well as limited or no access to safe water and sanitation or electricity for the majority of the population. The judgement debt of US$ 20 million payable by Liberia is equivalent to about 5 per cent of the budget of the Government of Liberia this year, the country's entire education budget and 150 per cent of its health budget in 2008.[21] Plainly, Liberia cannot service its debt without jeopardizing its poverty-reduction and economic development prospects, let alone pay an amount that the British High Court accepted was "a substantial sum".

Democratic Republic of the Congo

18. In 1980 and 1986 the Democratic Republic of the Congo (formerly Zaire) and its national electricity company (Société Nationale d'Électricité) entered into credit agreements with Energoinvest, a Yugoslav company, to provide electrical infrastructure. The Government guaranteed the amount but by the late 1980s both the electricity company and the Government had defaulted on the debts. In 2003, the International Chamber of Commerce made two arbitral awards in favour of Energoinvest for US$ 18.43 million and US$ 11.725 million plus 9 per cent interest and the cost of arbitration. In 2004 the United States District Court for the District of Columbia confirmed the US$ 11.725 million arbitral award and in 2005 confirmed the US$ 18.43 million arbitral award.

19. Energoinvest then sold its interests in the arbitral awards and judgements to a company called FG Hemisphere (now FG Capital Management) which specializes in uncovering, investigating and managing alternative investment opportunities and special situations within the emerging markets.[22] Subsequently, FG Hemisphere attempted to seize assets of the Democratic Republic of the Congo in the Bahamas, Europe, South Africa, the United States and in Hong Kong, Special Administrative Region of China. In 2005, the company obtained a court order compelling the State to furnish detailed information about all its assets throughout the world. The State failed to comply with the order, arguing that it imposed a virtually impossible burden. In May 2008, FG Hemisphere filed a motion in the United States District Court for the District of Columbia to hold the Democratic Republic of the Congo in contempt.[23] In March 2009, the court fined the State the sum of US$ 5,000

[18] Ibid.

[19] United Nations Development Programme (UNDP), *Human Development Report 2009* (New York, 2009), p. 145; World Bank, *World Development Indicators* (October 2009), available from http://data.worldbank.org/indicator/NY.GDP.MKTP.CD.

[20] Joint United Nations Programme on HIV/AIDS (UNAIDS), *2008 Report on the Global AIDS Epidemic* (2008), p. 215.

[21] Jubilee USA Network, "UK judge awards funds $20 million, more than Liberia's total spending on education last year". Available from www.jubileeusa.org/press/press-item/article/advocacy-groups-decry-profiteering-by-vulture-funds-in-liberia.html?tx_ttnews%5BbackPid%5D=170&cHash=924f4678be.

[22] H. Stewart and A. Seager, "Vulture fund swoops on Congo over $100m debt", *Observer*, 9 August 2009. Available from www.guardian.co.uk/world/2009/aug/09/congo.

[23] See M. Stulman, "Indebted nations fight off vulture funds", *Asia Times* Online, 8 July 2009.

per week and rising every four weeks to a maximum of US$ 80,000 per week, for failing to comply with the order.[24]

20. The Democratic Republic of the Congo, which has a GDP of US$ 11.6 billion and a Human Development Index ranking of 176, remains embroiled in a civil war.[25] Approximately 79.5 per cent of its nearly 66 million population lives on less than US$ 2 per day. Government expenditure on health is estimated at 7.2 per cent of GDP.[26] With a debt burden deemed unsustainable by the World Bank and IMF, the Democratic Republic of the Congo cannot service its external debt obligations without harming its poverty-reduction and economic development prospects. It is currently going through the HIPC process; the court awards mentioned above threaten the country's potential gains from international debt relief efforts and its capacity to create the conditions for fulfilling its human rights obligations.

Zambia[27]

21. In 1979 Romania lent Zambia US$ 15 million, which the latter used to purchase tractors and other agricultural machinery from the former. It appears that some of this equipment arrived in an unusable condition. This situation was compounded by the fact that European subsidies rendered it difficult for Zambia to compete in the global marketplace. Unable to raise enough revenue from its exports to service the loan, Zambia defaulted.

22. In early 1997 Debt Advisory International (which later incorporated Donegal International to pursue the debt Zambia owed to Romania) started putting forward proposals to acquire the Zambian debt from Romania. In an obvious attempt to persuade Romania to accept its proposal to acquire the debt, Debt Advisory International sent a memorandum to Romania in May in which it stated:

> We understand that Zambia is currently not servicing its debt to Romania and has not made any serious attempts to reschedule these claims in many years. Furthermore, Zambia is not likely to resume servicing its obligations to Romania in the near term. Zambia's economic situation remains dire, and the country's unsustainable external debt burden makes it one of the countries likely to benefit from the Heavily Indebted Poor Countries (HIPC) Initiative … Under the HIPC initiative, Zambia will receive additional debt reduction from its bilateral creditors … In particular, bilateral creditors may need to write off up to 90 per cent of their Zambian claims and reschedule the remaining 10 per cent over 23 years or more. It is the practice of the Paris Club to require African Governments to agree a minute to the effect that they will not afford any other sovereign creditor better rescheduling terms than they have afforded the Paris Club. Consequently, we believe that there is very little chance that Romania can expect to obtain more in net present value terms that we are presently offering.[28]

23. In 1998, Romania agreed to sell the debt to Donegal International for US$ 3.2 million subject to the fulfilment of certain conditions by Donegal. The company failed to meet one of these conditions, namely, meeting a deadline of 31 December 1998 for the completion of the assignment. In December 1998, the two countries commenced negotiations to liquidate the debt for US$ 3,281,780 and subsequently signed a

Available from www.atimes.com/atimes/Global_Economy/KG08Dj02.html.

[24] Ibid.

[25] UNDP, *Human Development Report 2009*, p. 145 and World Bank, *World Development Indicators*.

[26] UNDP, *Human Development Report 2009*, pp. 178 and 201.

[27] See *Donegal International v. Zambia* (see footnote 12).

[28] Ibid., para. 75.

memorandum of understanding to the effect that Zambia would have until 31 January 1999 to confirm its offer to purchase the debt at its slightly higher offer of US$ 3.5 million. Just 12 days before this deadline and, without prior notice to Zambia, Romania sold the debt to Donegal International for US$ 3.2 million. At the time, the debt had a face value of approximately US$ 30 million.

24. In September 2002, after unsuccessfully attempting to swap the debt for investments in Zambia, Donegal International commenced litigation in the British Virgin Islands for approximately US$ 43 million. In April 2003, in controversial circumstances involving allegations of corruption and bribing of public officials, Zambia signed a settlement agreement with Donegal International in which it agreed to waive sovereign immunity from litigation and pay around US$ 15 million of the then US$ 44 million face value. It also agreed to penal rates of interest in the event of default and to have any disputes determined under English law. Zambia paid a total of US$ 3.4 million in three instalments and thereafter stopped paying, arguing that the agreement was tainted with corruption and had been signed without the requisite authority.

25. In 2006, months before Zambia was due to receive debt cancellation under the HIPC Initiative, Donegal International instituted legal action against the country for US$ 55 million – an amount that was nearly 17 times the amount the company paid for the debt. In February 2007, the British High Court ruled in favour of Donegal International. Despite having found that the owner of the company, Mr. Sheehan, was "deliberately evasive and even dishonest", that he had "deliberately" given "false evidence", that the company had "deliberately" withheld documents "because they contradicted the case that they were seeking to advance" and that "the evidence from the witnesses called by Donegal (was) vague and inconsistent",[29] the court held that Donegal International had a case in law. However, it subsequently ruled that Zambia had a real prospect of establishing that certain provisions of the settlement agreement were penal and therefore unlawful. It ordered Zambia to pay US$ 15.4 million (an amount equivalent to 65 per cent of the country's savings in debt relief in 2006)[30] to Donegal International. Under HIPC Initiative terms, Zambia could have expected 88 per cent cancellation of its debt.

26. This case underscores the need for debtor countries to fully comprehend the implications of formally recognizing claims arising out of sovereign debts sold on the secondary market.

C. Vulture funds, debt relief and human rights

27. There are two main international debt relief schemes: the Heavily Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative (MDRI). The HIPC Initiative was created in 1996 with the aim of reducing the debt burden of the world's poorest countries to "sustainable levels".[31] A comprehensive review in 1999 resulted in the

[29] Ibid., paras. 51 (iii), 64, 90 and 127. See also paras. 132, 136, 150, 151, 156 (ii), 159, 167, 181, 188, 273, 344, 544.

[30] See Jubilee USA Network, "Vulture funds and poor country debt: recent developments and policy responses", Briefing Note 4, April 2008, citing IDA and IMF, "Heavily Indebted Poor Countries (HIPC) Initiative and Multilateral Debt Relief Initiative (MDRI) – status of implementation" (2006), p. 65.

[31] In order to qualify for debt relief under the HIPC Initiative, a country must: (a) have an unsustainable debt burden (i.e. a net present value of debt-to-exports ratio, after traditional debt relief, of more than 150 per cent); (b) establish a track record of policies and reforms through IMF- and IDA-supported programmes; and (c) have prepared a poverty reduction strategy paper through "a broad-based participatory process".

Enhanced HIPC Initiative to ensure faster, deeper and broader debt relief with the core objective of poverty reduction. In 2005, the HIPC Initiative was supplemented by MDRI to help accelerate countries' progress towards the Millennium Development Goals. MDRI ostensibly provides countries that complete the HIPC Initiative with full debt cancellation from four main multilateral institutions: IMF, the International Development Association (IDA), African Development Fund (administered by AfDB) and the Inter-American Development Bank.[32]

28. As of end-July 2009, 26 of the 40 eligible countries had completed the HIPC Initiative and qualified for irrevocable debt relief, while a further 9 had reached the decision point and qualified for interim debt relief. In September 2009, the World Bank and IMF reported that the total debt relief committed to the 35 post-decision-point HIPCs under the initiatives was US$ 124 billion (in nominal terms), representing on average about 40 per cent of the 2008 GDP of these countries.[33] Commercial creditors account for 6 per cent of the total cost of debt relief to be provided to the 35 post-decision-point HIPCs, but only around a third of this has been provided.

29. According to the World Bank and IMF, the two international debt relief initiatives have helped significantly reduce the external debt burden of HIPCs and contributed to creating the fiscal space necessary for poverty-reducing expenditure and economic development in these countries. Countries that have benefitted from debt relief have increased average spending on health and education and now spend on average six times more on these basic services than they do on debt service. The 2009 HIPC and MDRI status of implementation report indicates that between 2001 and 2008, poverty-reducing spending in the 35 post-decision-point HIPCs increased by 2 percentage points of GDP on average, while debt service obligations declined concomitantly.

30. There is a dearth of empirical studies on the impact of HIPC and MDRI debt relief on economic and human development. Nevertheless, a few studies show a positive correlation between the reduction in debt service and the increase in poverty-reducing expenditure. For example, a study by Crespo Cuaresma and Vincellette shows that average educational expenditures are about 18.5 per cent of total government expenditures in post-completion-point HIPCs, which is 2 to 3 percentage points higher than in pre-decision-point countries.[34]

31. From a human rights perspective, reduced debt burdens and increased fiscal capacity have contributed to the creation of the conditions necessary for the realization of human rights, particularly economic, social and cultural rights, in HIPCs. Some of the human rights impacts of debt cancellation include the abolition of primary school fees in Ghana, Malawi, Uganda, the United Republic of Tanzania and Zambia, resulting in increased school enrolments in these countries; abolition of user fees for health care in Zambia, thereby making basic health care available to millions of Zambians living in rural areas; and improvement of health care in Mauritania and the Plurinational State of Bolivia.[35]

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[32] The initiative covers all post-completion point HIPCs. Debt relief covers all debt due to IMF, the African Development Fund, and Inter-American Development Bank (IDB) by end-December 2004 and all debt due to IDA by end-December 2003 and still outstanding at the time of qualifying (i.e. after HIPC Initiative debt relief). See www.imf.org/external/np/exr/facts/mdri.htm.

[33] IDA and IMF, "HIPC Initiative" (2009) (see footnote 7), para. 4.

[34] J. Crespo Cuaresma and G.A. Vincelette, "Debt relief and education in heavily indebted poor countries" in C.A. Primo Braga and D. Domeland (eds.), *Debt Relief and Beyond: Lessons Learned and Challenges Ahead* (Washington DC, World Bank, 2009), pp. 40–41.

[35] See Jubilee Debt Campaign, *Unfinished Business: Ten Years of Dropping the Debt* (London, Jubilee Debt Campaign, 2008), pp. 25–26.

32. Nevertheless, the voluntary nature of the two international debt relief schemes discussed above creates opportunities for individual creditors to refuse to participate and then attempt to recover — through litigation, seizure of assets or political pressure — the full value of their debt.[36] In particular, this has enabled vulture funds to purchase defaulted debts and to litigate for the full face value at the expense of the debtor country and of other creditors.

33. Vulture fund litigation prevents heavily indebted poor countries from using resources freed up by debt relief for their development and poverty reduction programmes, and therefore diminishes the capacity of these countries to create the conditions necessary for the realization of human rights for their people. Money that is earmarked for poverty reduction and basic social services, such as health and education, is diverted to settling the substantial claims of vulture funds. In short, vulture funds erode the gains from debt relief for poor countries and jeopardize the fulfilment of these countries' human rights obligations.

34. It has been estimated that the average potential impact of vulture fund litigation against HIPCs amounts to 18 per cent of spending on health care and education, 59 per cent of debt repayments, and 5 per cent of budget revenue. A 2007 study by Debt Relief International found that lawsuit costs amount to 52 per cent of health and education in the Niger and 98 per cent of revenue in Cameroon. In 2008, the World Bank and IMF estimated that the potential impact of court awards varied from less than 0.5 per cent of the debtor country's GDP to 49 per cent in the case of Liberia.[37]

35. Vulture fund litigation can also be lengthy and costly for HIPC countries, thereby diverting much needed resources and attention from pressing development, social and human rights issues. According to AfDB, vulture funds "grind down poor countries in cycles of litigation" and many lawsuits typically take 3 to 10 years to settle.[38]

36. It is noteworthy that the World Bank and IMF have recognized that litigation by commercial creditors has been "an impediment to the delivery of full debt relief to HIPCs".[39] Similarly, the European Commission has acknowledged that cases of aggressive litigation by commercial creditors have diluted some of the benefits of debt relief initiatives. In 2007, the Paris Club acknowledged that litigation against HIPCs "is a cause of concern for the international community".[40]

IV. Official initiatives to tackle vulture funds

37. A number of initiatives have been adopted or are being considered at the international and national levels to tackle vulture funds. In this section, the independent expert sketches these initiatives and briefly addresses some of the key concerns raised in relation to the potential adverse consequences of proposed national legislative measures on the development prospects of the intended beneficiaries – HIPCs.

[36] Thus, even when a country reaches the completion point, creditors retain their legal rights to enforce claims against the country concerned.

[37] IDA and IMF, "HIPC Initiative" (2008) (see footnote 5), para. 38.

[38] AfDB, "Vulture funds" (see footnote 1).

[39] IDA and IMF, "HIPC Initiative" (2009) (see sect. III, footnote 7), para. 24.

[40] See www.clubdeparis.org/sections/types-traitement/reechelonnement/initiative-ppte/sujets-relatifs-aux/sujets-relatifs-aux.

A. Multilateral initiatives

38. The IDA Debt Reduction Facility, established in 1989, provides grants to heavily indebted IDA-only countries to enable them buy back, at a significant discount, commercially held external sovereign debt.[41] The facility provides grants for both the preparation and the implementation of commercial debt-reduction operations. In order to be eligible for support from the Debt Reduction Facility, countries must meet certain conditions, including the demonstration of "satisfactory performance under a medium term adjustment program" and implementation of a "satisfactory strategy for debt management that seeks comprehensively to address commercial debt, provides substantial relief from official bilateral creditors, and enhances the country's growth and development prospects".[42] Since its inception, the facility has helped extinguish approximately US$ 10 billion of external commercial debt.

39. In April 2008, changes were made to the policies and procedures of the Debt Reduction Facility to improve its effectiveness at assisting eligible countries to reduce their burden of sovereign commercial external debt and reducing the opportunities for commercial creditors to profit from litigation against HIPC countries. In terms of the modifications, formerly bilateral debts sold to commercial creditors and domestic debts sold to external creditors after the HIPC decision-point reference date are no longer considered eligible for buy-back. These changes aim to prevent distressed debt funds (i.e., vulture funds) from making a profit by buying claims at a deep discount and tendering them for a buy-back under the facility and to discourage the sale of debt from official to commercial creditors.[43]

40 Despite these successes and enhancements, the Debt Reduction Facility has a major limitation: participation by commercial creditors is entirely voluntary. In other words, the facility does not prevent a creditor from holding out and then suing to recover the full face value of its debt instrument. The case of Liberia illustrates this problem. In April 2009, commercial creditors provided debt relief to Liberia under a debt buy-back operation under the facility and contributions from bilateral donors, which extinguished US$ 1.2 billion of commercial debt at a deep discount of 97 per cent of face value. Despite this buy-back, the non-participating creditors continued to hold claims against Liberia worth 85 per cent of the cost of the facility buy-backs. In November, the British High Court ordered Liberia to pay more than US$ 20 million to two vulture funds (see para. 16 above). Thus, as the Government of the United Kingdom has acknowledged, the Debt Reduction Facility "cannot address the problem posed by creditors determined to pursue a higher payout than that given by HIPC Initiative terms".[44]

41. In September 2006, the Commonwealth Secretariat established a Legal Debt Clinic to provide legal advice to both Commonwealth and non-Commonwealth HIPCs facing or likely to face litigation by commercial creditors. The clinic also aims to hold regional seminars to raise awareness about the legal aspects of debt management, legal soundness of loan agreements, debt restructuring and how to deal with litigation threats.[45]

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[41] See http://go.worldbank.org/DB88PB5XA0. See also B. Gamarra, M. Pollock and C.A. Primo Braga, "Debt relief to low-income countries: a retrospective", in C.A. Primo Braga and D. Domeland (eds.), *Debt Relief and Beyond* (see footnote 13), pp. 24–25.

[42] See http://go.worldbank.org/2W4HSIN5I0.

[43] IDA and IMF, "HIPC Initiative" (2008) (see sect. III, footnote 5), p. 32, box 3.

[44] United Kingdom, *Ensuring Effective Debt Relief for Poor Countries: A Consultation on Legislation* (HM Treasury, 2009), p. 22.

[45] See www.thecommonwealth.org/Internal/39284/157583/legal_debt_clinic/.

42. The Paris Club creditors have collectively committed not to sell claims on HIPC countries to creditors who do not intend to provide debt relief, and called upon other creditors to make the same commitment.[46]

43. In 2008, Commonwealth Finance Ministers issued a communiqué in which they "recognized the importance of Commonwealth creditors leading by example by providing full HIPC relief and not selling claims on to other creditors".[47]

44. In May 2008, European Union countries pledged to take action to "deter aggressive litigation by distressed-debt funds" and agreed not to sell claims on HIPCs to creditors who are not willing to provide debt relief.[48] They further agreed to support: (a) dialogue with other creditors (bilateral, multilateral and commercial) and with borrowing countries; and (b) technical assistance to strengthen the debt management capacities of low-income countries and assist efficient debt negotiations; and (c) commercial debt buy-backs complementary to HIPC debt relief operations.[49]

45. In June 2009, AfDB launched the African Legal Support Facility with the goal of maximizing resources available for economic development and social progress for its member countries by enhancing their access to technical legal advice in dealing with lawsuits and other claims brought by vulture funds, in addition to other ancillary areas.[50] The facility is designed to, among other things: (a) provide members of the facility involved in creditor litigation with legal advice and services; and (b) provide members of the facility with technical legal assistance to enhance their legal expertise and negotiating capacity in matters related to debt management; natural resources and extractive industries management and contracting; investment agreements; and related commercial and business transactions.

46. The independent expert welcomes the foregoing multilateral initiatives against vulture funds. However, he is of the view that they are insufficient to prevent vulture fund activity. All of these initiatives depend on voluntary commitments not to sell debt obligations on to speculative investors or they provide funds or technical legal support to heavily indebted poor countries. Further, as the European Network on Debt and Development has argued, multilateral initiatives to discourage vulture fund activity appear to have ignored the fact that "it is entirely legal for vulture funds to pursue their claims in court".[51] Significantly, these measures do not prevent speculative commercial creditor litigation against poor countries. Indeed, the potential for profit remains a strong incentive for vulture funds to continue their activities.[52] The problem is aptly summed up in the

[46] Paris Club, press release on the threats posed by some litigating creditors to heavily indebted poor countries, 22 May 2007. Available from www.clubdeparis.org/sections/communication/archives-2007/communique-presse-du/switchLanguage/en.

[47] See www.thecommonwealth.org/document/184212/commonwealth_finance_ministers_meeting_communiqu.htm.

[48] Council of Europe, "Council conclusions: speeding up progress towards the Millennium Development Goals (MDGs)", 2870th External Relations Council Meeting, Brussels, 26 and 27 May 2008, para. 41. Available from www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/gena/100688.pdf.

[49] Ibid.

[50] See www.afdb.org/en/topics-sectors/initiatives-partnerships/african-legal-support-facility/goals-and-objectives/. See also IDA and IMF, "HIPC Initiative" (2009) (see sect. III, footnote 7), para. 25.

[51] Eurodad, "Taming the vultures: are new measures enough to protect debt relief gains?" (Brussels, 2008), p. 11.

[52] The Government of the United Kingdom acknowledges the problem as follows: "These methods cannot prevent creditors intent on pursuing their claims through the courts from doing so. So long as it remains possible and potentially profitable (depending on the price paid for the debt) to litigate for

words of Michael Sheehan of Donegal International: "Our experience and that of others in this business is that you always eventually recover. You have a legal claim. Eventually if you litigate and work hard enough, you will always recover a sufficient amount to cover your costs."[53] The independent expert therefore calls upon all countries — creditor and debtor alike — to urgently consider enacting legislation that would make vulture fund profiteering illegal within their respective jurisdictions.

47. The following section briefly reviews the legislative measures that have been taken or are being considered by individual countries to tackle the vulture fund problem.

B. Initiatives at the national level

48. At the national level, legislative proposals are being considered or have been adopted in the United States and the United Kingdom to limit vulture fund litigation against HIPCs. In Belgium, the Senate approved a Law in May 2008 which prohibited vulture fund litigation in that country.[54] The law stresses that official development assistance funds are "untouchable and non-transferable". The Senate also adopted a non-binding resolution which, inter alia, called upon the Government of Belgium to urge the World Bank and IMF to develop the necessary legal instruments to ensure that debt relief initiatives are binding on all creditors.[55]

49. In July 2009, Representative Maxine Waters introduced the Stop Very Unscrupulous Loan Transfers from Underprivileged Countries to Rich, Exploitive Funds Act, or the Stop VULTURE Funds Act (H.R.2932), in the United States House of Representatives. This legislation is designed to protect low-income developing countries from the predatory practices of vulture funds by preventing "speculation and profiteering in the defaulted debt of certain poor countries". The proposed legislation (which is limited to countries that are eligible to borrow from IDA, the concessional loan facility of the World Bank) would make it illegal for any private creditor holding defaulted sovereign debt to use litigation in a United States court, or the threat of such litigation, to secure payment of more than the total amount they paid for the debt obligation plus 6 per cent simple interest from the date the debt was acquired from an eligible poor country. Companies or individuals that act in contravention of this law would be subject to fines in amounts equal to the sum they sought to claim through litigation. The legislation also seeks to promote transparency by requiring full disclosure from any private creditor seeking to litigate against poor countries in United States courts.

50. It is notable that the United States draft legislation recognizes that profiteering in defaulted sovereign debt is facilitated by the lack of insolvency protections for sovereign debtors that are available to private debtors. Insolvency laws generally protect private debtors by, among other things, stays of execution pending restructuring of debt, suspension of accrual of interest and the ability to discharge debts and obligations as part of a debt restructuring process.

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payment of the full value once other creditors have provided relief, some creditors are likely to take this route." United Kingdom, "*Ensuring Effective Debt Relief*" (see footnote 23), p. 19.

[53] *Donegal International v. Zambia* (see sect. III, footnote 12), para. 76.

[54] See http://reflex.raadvst-consetat.be/reflex/pdf/Mbbs/2008/05/16/109374.pdf.

[55] P. Vandevoort (11.11.11 Belgium), "Belgian Senate unanimously approves 'vulture fund' legislation", 1 February 2008. Available from http://jubileeusa.typepad.com/blog_the_debt/2008/02/belgian-senate.html. See also IDA and IMF, "HIPC Initiative" (2009) (see sect. III, footnote 7), para. 26.

51. In July 2009, the Government of the United Kingdom launched a public consultation on possible legislation that would limit the extent to which vulture funds could recover debt already contracted by a HIPC under British law.[56] In February 2010, the Government published a response to the consultation as well as an impact assessment in support of the Debt Relief (Developing Countries) Bill, a Private Member's Bill introduced in the House of Commons in December 2009 by Andrew Gwynne MP.[57] On 8 April, the Bill was passed into law as the Debt Relief (Developing Countries) Act (c. 22) and it received the Royal Assent on the same date. The Act, which has a duration of one year from the date of commencement (although it may be extended for a further period or made permanent), is designed to limit the ability of vulture funds to use courts in the United Kingdom to recover debts owed by HIPCs.

52. The initiatives that have been undertaken or are being undertaken in Belgium, the United States and the United Kingdom to curb vulture fund activity are commendable. The independent expert urges all countries, particularly those that are preferred jurisdictions for vulture funds, to urgently consider enacting legislation to curtail vulture fund activity. Such a course of action would be consonant with the commitment, made in the Monterrey Consensus of the International Conference on Financing for Development, by all countries to share responsibility for preventing and resolving unsustainable debt situations as well as with the recognition in the Monterrey Consensus of the role of comprehensive strategies in reducing the vulnerability of debtor countries.[58]

53. The independent expert believes that such legislative frameworks should include measures to promote transparency in the secondary debt market and to tackle tax havens. In addition, as the Jubilee Debt Campaign has suggested in relation to the legislative proposals in the United Kingdom, the legislation should not be limited to HIPCs but should extend to all developing countries, with HIPC terms applied to HIPCs and a profiteering cap applied to all other developing countries.[59]

C. Concerns over proposed legislative controls on vulture funds

54. There has been some opposition to legislative proposals to curb vulture fund activity based on the concerns that, among other things, the proposed legislative controls offer minimal benefits to the beneficiary countries, they have adverse consequences for the secondary debt market and may limit access to credit for the intended beneficiary countries.[60] Due to space limitations, these concerns are addressed briefly.

55. In its submission in response to the consultation of the Government of the United Kingdom on proposed vulture fund legislation, EMTA — an organization which describes

[56] United Kingdom, *Ensuring Effective Debt Relief* (see footnote 44).

[57] United Kingdom, "Impact assessment of measures to address non-participation in debt relief", (HM Treasury, 2010), available from www.hm-treasury.gov.uk/consult_debt_relief.htm.

[58] *Report of the International Conference on Financing for Development, Monterrey, Mexico, 18–22 March 2002* (United Nations publication, Sales No. E.02.II.A.7), chap. I, resolution 1, annex, para. 47.

[59] See Jubilee Debt Campaign, "The business case for prohibiting 'vulture' actions in UK courts". Available from www.jubileedebtcampaign.org.uk/download.php?id=859.

[60] See, for instance, the submissions of (a) EMTA and (b) Africa Fighting Malaria, International Policy Network, Free Market Foundation of Southern Africa and Imani Ghana, in United Kingdom, *Ensuring Effective Debt Relief for Poor Countries: Consultation Responses Received* (2010). See also Free Market Foundation of Southern Africa, *The UK Debt Relief (Developing Countries) Bill: A Threat to Growth and Prosperity in Africa*. Available from www.freemarketfoundation.com/DynamicData/Event_18.pdf.

itself as "the principal industry trade association for the financial institutions worldwide that buy, sell and hold debt instruments issued by Emerging Markets countries and obligors located therein" and claims that it is "dedicated to promoting the orderly development of fair, efficient and transparent trading markets for Emerging Market instruments … and to helping to integrate the Emerging Markets more fully" into the international financial system[61] — contends that the proposed legislation "while intended to provide a very limited 'benefit' to certain highly indebted poor countries (HIPCs), would in fact negatively affect market access of all HIPCs, and therefore, limit their long-term prospects for development and economic growth, and jeopardize their further integration into the international financial system".[62] It further claims that the implications of the proposed legislation to the broader market include: "(i) a dramatic reduction of liquidity and price in the secondary market for defaulted claims, (ii) a corresponding reduction in the supply of credit and/or increased cost of financing for HIPC borrowers …, and (iii) potential increased cost of financing across the wider Emerging Markets, as creditors interpret this Legislative Proposal as hostile to creditor rights".[63] However, the submission fails to offer any cogent evidence to support the EMTA claims.

56. Contrary to the claims of the EMTA, legislation designed to protect debt relief gains from the predatory activities of vulture funds would not curtail the secondary debt market. Rather, it would enable the secondary debt market to function in a more transparent and efficient manner. The British legislation does not preclude creditors from obtaining recompense through the legal system for debts owing to them. It only prevents them from obtaining extortionate payments on sovereign debt at the expense of other creditors in much the same way that insolvency law does in relation to private debtors.

57. Vulture fund activity not only dilutes the gains from debt relief, it also complicates the debt relief process and undermines other creditors by forcing debtor countries to grant vulture funds preferential treatment at the expense of responsible creditors who may be involved in debt restructuring with the debtor countries. Unlike vulture funds, responsible secondary debt participants do not acquire sovereign debt for the sole purpose of enforcing payment of usurious interest rates from impoverished countries. Responsible and ethical creditors therefore have nothing to fear from the proposed legislation.

58. Further, vulture fund litigation and freezing of the assets of debtor countries in the course of such litigation jeopardizes the servicing of debt obligations by the affected countries. It also inhibits trade and investment relations with developing countries.[64] Illustratively, in 2001, the vulture funds FG Hemisphere Associates LLC and Af-Cap sued CMS Nomeco, an oil and gas company in Texas, in a bid to garnish payments that CMS Nomeco owed to the Republic of the Congo.[65] In 2008, FG Hemisphere Associates approached the High Court of Hong Kong, Special Administrative Region of China to try to force the China Railway Group to hand over part of its infrastructure investment in the Democratic Republic of the Congo. Such actions provide a disincentive for companies to trade with or invest in countries targeted by vulture funds and therefore harm the development prospects of these countries.[66]

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[61] Letter from Michael Chamberlin, Executive Director of EMTA to the Judicial Appeal Committee, House of Lords, 23 June 2007. See also EMTA, "Submission" (see footnote 60 above), p. 1.

[62] EMTA, "Submission", p. 1.

[63] Ibid., p. 13.

[64] Jubilee Debt Campaign, "The business case".

[65] See *FG Hemisphere Associates v. République du Congo*, 455 F.3d 575 (5th Circ. 2006) and *Af-Cap Inc v. The Republic of Congo*, 462 F.3d 417 (5th Cir. 2006).

[66] For a discussion of the difficulties faced by companies doing business with poor countries being targeted by vulture funds, see A.B. Derman and A. Melsheimer, "Recent developments in foreign

59. According to a joint World Bank and IMF report, pending litigation and outstanding court awards may also prevent HIPCs from regularizing financial relationships with the international banking community.[67]

60. EMTA also claims that "the process of commercial creditor debt renegotiation and debt relief within the HIPC Initiative framework is already functioning effectively without legislative intervention".[68] To buttress its claims, it relies on the example of the Liberia Debt Reduction Facility buy-back operation in April 2009 which saw US$ 1.2 billion of commercial debt extinguished at 97 per cent of face value. However, EMTA expediently omits to mention that participation in Debt Reduction Facility buy-back operations is voluntary and the facility does not prevent hold-outs by creditors, as the case of *Hamsah Investments Ltd v. Liberia*,[69] discussed in section III above, clearly demonstrates.

61. In its consultation paper on vulture fund legislation, the Government of the United Kingdom acknowledges the successful Liberian buy-back operation but cautions that "the non-participating creditors continue to hold claims against Liberia worth 85% of the cost of the Debt Reduction Facility buybacks".[70] Further, the World Bank and IMF have repeatedly emphasized that while the HIPC Initiative has helped reduce the external debt burdens of HIPCs, a number of challenges remain, including ensuring that HIPCs get full debt relief from all creditors, including private creditors.[71] This underscores the pressing need for legislative measures to combat predatory creditor activity.

62. In the estimation of the independent expert, the EMTA submission and similar concerns by other proponents of vulture funds appear to be based on the erroneous assumption that markets have efficient, self-correcting mechanisms. As the recent financial crisis has amply demonstrated, this assumption is fundamentally mistaken. It is precisely the lack of State regulation that facilitated the abuses that manifested themselves in the financial crisis.[72] In the Outcome of the Conference on the World Financial and Economic Crisis and Its Impact on Development, Governments recognized that the crisis was caused by "regulatory failures, compounded by over-reliance on market self-regulation, overall lack of transparency, financial integrity and irresponsible behaviour …".[73] Vulture funds are part of this flawed international financial system. Consequently, measures to reform the global financial system must include measures to curb profiteering by unethical commercial creditors. In this regard, it is worth recalling that the Monterrey Consensus recognizes that the orderly development of capital markets aimed at addressing development financing needs and nurturing productive investments requires "a sound system of financial intermediation, transparent regulatory frameworks and effective supervisory mechanisms" (para. 17).

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sovereign immunity and Texas garnishment law: a new threat facing U.S. oil and gas companies", *Houston Journal of International Law*, vol. 29 (winter, 2007), p. 277.

67 IMF and IDA, "Heavily Indebted Poor Countries (HIPC) Initiative – status of implementation" (2003), para. 54.

68 EMTA, "Submission" (see footnote 60), p. 4.

69 High Court of Justice, Case No. 2008/587, 26 November 2009.

70 United Kingdom, *Ensuring Effective Debt Relief* (see footnote 44), p. 17.

71 IDA and IMF, "HIPC Initiative" (2009), p. 5 (see sect. III, footnote 7).

72 The financial crisis started as the "sub-prime mortgage crisis" in the United States in August 2007 and then erupted into a global credit crisis in September 2008. It was caused by a combination of factors, including loose monetary policy, deregulation, excessive risk taking by banks and the explosion of credit/debt between 2002 and 2007. See UNCTAD, *The Global Economic Crisis: Systemic Failures and Multilateral Remedies* (United Nations publication, Sales No. E.09.II.D.4).

73 General Assembly resolution 63/303, annex, para. 9.

63. A further claim in the EMTA submission is that the British legislative proposal would appear to put the United Kingdom in contravention of international treaties that guarantee actionable property rights, such as the European Convention on Human Rights.[74] This submission appears to be based on the misguided notion that the right to property is an absolute right. Human rights supervisory bodies have made clear that a State is entitled to limit or control the use of property (including contractual rights with an economic value) in accordance with the general interest by enforcing such laws as it deems necessary for the aim pursued.[75] The limitation imposed by the Debt Relief (Developing Countries) Act is a "control of use" rather than a deprivation since there is no practical or legal extinction of the rights of ownership. Significantly, the Act does not preclude creditors from seeking reasonable recompense but merely seeks to prevent them from profiteering at the expense of indebted poor countries as well as the taxpayers who have contributed to international debt relief efforts. There are also compelling public interest grounds for reducing the recoverability of debts and judgements by vulture funds, namely, that the Act promotes fairness among creditors and that it promotes the development of HIPCs.

64. It is noteworthy that EMTA includes among its members a number of vulture funds (such as Elliott Associates, Debt Advisory International and Greylock Capital), as well as law firms such as Allen & Overy (which represented Donegal International in its lawsuit against Zambia) and Dechert LLP (which represented the two vulture funds, Hamsah Investments and Wall Capital, in their lawsuit against Liberia). It may therefore be asserted that the EMTA opposition to legislative measures to curtail vulture fund activity is actuated more by self-interest than a real concern for the development prospects of poor countries.

65. Governments have a responsibility to intervene "when markets fail to create the conditions in which all people, including the poorest and most marginalized, can exercise the full range of their human rights".[76] Although the consultation paper does not explicitly state so, it can be argued that the British legislation is ultimately intended to help HIPCs create the necessary conditions for the realization of the basic rights of their citizens and the right to development. This would be in keeping with the spirit of international assistance and cooperation recognized in the Charter of the United Nations and binding international human rights instruments such as the International Covenant on Economic, Social and Cultural Rights which the United Kingdom has ratified.[77]

66. It is clear that existing laws in the "creditor-friendly" jurisdictions cannot effectively protect poor countries from predatory creditor activity. The case of *Donegal International Ltd v. Republic of Zambia & Another*[78]provides a good illustration of the problem. In that case, the British High Court, while accepting that Zambia "is a poor country", stressed that it was concerned with the "legal questions" raised by the applications before it and "not with questions of morality or humanity".[79] This underlines the need for Governments to

[74] EMTA, "Submission" (see footnote 60), p. 16. See also submission of Dechert LLP, in United Kingdom, *Ensuring Effective Debt Relief for Poor Countries: Consultation responses received* (2010).

[75] Case of *Sporrong and Lonnroth*, judgement of 23 September 1982, Publications of the European Court of Human Rights, Series A, No. 52, para. 61.

[76] Centre for Economic and Social Rights, "Human rights and the global economic crisis: consequences, causes and responses" (2009), p. 5.

[77] "The Government believes it is in the interests of the UK and the world to tackle the many challenges of world poverty. In an increasingly interdependent world, international development is vital to global common interests that will profoundly affect the quality of life for all …." (United Kingdom, *Ensuring Effective Debt Relief* (see footnote 44), p. 11).

[78] See sect. III, footnote 12.

[79] Ibid., para. 2.

implement legislative measures (which the courts would be bound to apply) to protect vulnerable countries from vulture fund activity.

V. Conclusions and recommendations

67. **Despite their limitations, international debt relief initiatives have helped reduce the debt burdens of heavily indebted poor countries (HIPCs) and create fiscal space for poverty-reducing expenditures in these countries. There is some evidence that reduced debt burdens and improved fiscal space has led to increased investment in essential social services related to human rights, such as health and education, in these countries.**

68. **Nevertheless, the voluntary nature of international debt relief schemes has created opportunities for vulture funds to acquire defaulted sovereign debt at vastly reduced prices and then seek repayment of the full value of the debt through litigation, seizure of assets or political pressure. While the debts held by vulture funds do not represent the bulk of poor countries' debt, awards in vulture fund lawsuits represent a considerable burden on the budgets of these countries. Further, vulture fund activities complicate sovereign debt restructuring by causing inequitable burden sharing among creditors, and undermine trade and investment relations of the countries that they target. They may also hamper efforts by HIPCs to normalize their financial relationships with the international banking community.**

69. **By forcing HIPCs, through litigation and other means, to divert financial resources saved from debt cancellation, vulture funds diminish the impact of, or dilute the potential gains from, debt relief for these countries, thereby undermining the core objectives of internationally agreed debt relief measures. Vulture funds profiteer at the expense of both the citizens of HIPCs and the taxpayers of countries that have supported international debt relief efforts.**

70. **From a human rights perspective, the settlement of excessive vulture fund claims by poor countries with unsustainable debt levels has a direct negative effect on the capacity of the Governments of these countries to fulfil their human rights obligations, especially with regard to economic, social and cultural rights, such as the rights to water and sanitation, food, health, adequate housing and education.**

71. **The various initiatives (including the creation of legal support funds, voluntary codes and provision of legal advice) that have been undertaken at the international level to address vulture fund activity have all contributed towards addressing the negative effects of vulture fund activity on debt relief. However, these initiatives are insufficient. Given that the success rate of past litigation may generate more lawsuits against HIPCs, more concrete, legally enforceable measures are urgently required to curb predatory creditor activity and preserve the gains from international debt relief efforts.**

72. **Consideration should be given to making international debt relief schemes legally binding on all creditors (including commercial creditors). This would help prevent the exploitation of the proceeds of debt cancellation by unscrupulous creditors.**

73. **The absence of an international insolvency procedure concerning defaulted sovereign debt creates opportunities for vulture funds to profiteer at the expense of HIPCs and other creditors. Consequently, urgent consideration should be given to the establishment of a fair and transparent debt resolution mechanism at the international level. As the independent expert intimated in his report to the General**

Assembly (A/64/289, para. 52), an independent and impartial international debt resolution mechanism based on the principles of equity, transparency, inclusion and participation would help resolve sovereign debt repayment difficulties and disputes fairly and efficiently.[80]

74. **The international community should adopt legally binding standards on responsible sovereign lending and borrowing which should contain provisions restricting the right of creditors to unilaterally assign debt obligations to third parties without the prior informed consent of the debtor. In this regard, the independent expert calls upon all countries to support the United Nations Conference on Trade and Development project on promoting responsible sovereign lending and borrowing. In addition, it may be necessary to consider whether a secondary market for sovereign debt is appropriate, while remaining aware of the importance of the secondary market for other types of debt.**

75. **The independent expert welcomes the initiatives undertaken or under consideration in Belgium, the United Kingdom and the United States to combat vulture fund activity. In particular, he commends the United Kingdom for passing legislation to protect poor countries against vulture fund lawsuits and to safeguard the gains from international debt relief efforts. He urges the United Kingdom to make the Debt Relief (Developing Countries) Act permanent upon expiry of its initial period of validity with such enhancements as may be appropriate. He also urges all other countries, particularly the major creditor countries, to urgently consider implementing legal frameworks to curtail predatory vulture fund activities within their jurisdictions. These measures would be consistent with the principle of the shared responsibility of creditors and debtors for resolving unsustainable debt situations which is enshrined in the Monterrey Consensus.**[81]

76. **Such legislation should not be limited to HIPCs but should cover a wider group of poor countries (particularly those eligible for International Development Association lending) and should, in view of the negative effects of the global recession on the budgets of many developing countries, cover post-HIPC debts, original debts (some of which may be of questionable legitimacy) and court judgements which have already been obtained.**[82] **Additionally, the legislation should promote transparency in the secondary debt market by compelling full disclosure (to the courts and other appropriate national authorities), by creditors seeking to sue developing countries for recovery of debt, of information concerning loan amounts, procurement documentation and details of the creditors.**

77. **The independent expert calls upon creditor countries to support the African Legal Support Facility and the Legal Debt Clinic of the Commonwealth Secretariat both politically and financially. He also urges debtor countries to avail themselves of the assistance proffered under these initiatives and, in particular, to enhance their own national legal expertise over time.**

78. **Borrower countries should also consider implementing legislative measures to assure transparency, participation and accountability in the negotiation, contraction, restructuring and settlement of public loans, and to provide for oversight of loan**

[80] See also Eurodad, "Taming the vultures" (see sect. IV, footnote 51), p. 16.

[81] *Report of the International Conference on Financing* (see sect. IV, footnote 58).

[82] This is a call that has also been made by debt relief campaigners. See for example the submission of the Catholic Agency for Overseas Development (CAFOD) in United Kingdom, *Ensuring Effective Debt Relief* (see sect. IV, footnote 44).

contraction, loan use and debt management by parliaments and civil society organizations.

79. **Tax havens aid vulture fund activity by assuring secrecy and lack of transparency in the operation of these funds. Consequently, there is a pressing need for international action to address tax havens. In this regard, the independent expert supports the Eurodad proposals concerning the imposition of financial levies on transactions with tax havens and sanctions on tax havens that do not cooperate as regards disclosure of information.**[83]

80. **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. Measures to combat vulture funds should therefore be part and parcel of reforms of the international financial system.**

[83] Eurodad, "Taming the vultures" (see sect. IV, footnote 51), p. 4.