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Compiled by
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End the Debt Trap

Options for national legislative action.
Background papers dossier

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Contents

Introduction

With developing country debt reaching unprecedented levels—trapping nations in cycles that undermine economic sovereignty and social development—the *End the Debt Trap* project seeks to promote policy solutions that can break these destructive patterns. Its goals include fostering collaboration at both national and international levels, sharing experiences to develop sustainable strategies across regions, engaging policymakers in debt-distressed countries, and contributing to the global conversation on debt management policies.

Debt, while an essential instrument for financing national development, has become a double-edged sword for many, especially in the Global South. The lack of robust legislative frameworks to manage public borrowing has driven nations into cycles of unsustainable debt, undermining their economic sovereignty and social development.

At present, the complexities of a diverse creditor landscape, compounded by fiscal pressures stemming from the COVID-19 pandemic and geopolitical tensions, have significantly increased the challenges of public debt management in many developing countries. This heightened complexity underscores the urgent need for capacity building and knowledge enhancement among lawmakers and other stakeholders responsible for oversight in public debt management (UNGA & UN ECOSOC, 2022), as they play a pivotal role in ensuring the establishment of robust debt management practices, transparent reporting, and effective oversight policies to manage both domestic and foreign debt efficiently.

Moreover, the escalation of public debt levels has brought debt transparency into sharp focus. Factors such as the growing presence of non-traditional lenders, increased borrowing by non-central government entities, and the use of complex financial instruments have limited public access to information about loan agreements. This lack of transparency also hinders legislative oversight and public scrutiny, impeding accountability. Ensuring debt transparency is essential for enabling policymakers to make informed decisions, allowing creditors to assess borrowers' debt sustainability, and empowering citizens to hold governments accountable (Rivetti, 2022).

Consequently, enhancing national legislation for sovereign debt becomes crucial, particularly for developing countries, for a range of interconnected economic, legal, and developmental reasons. It forms the foundation of effective fiscal management and sustainable development, especially for nations with limited resources. Currently, many developing countries lack robust legal frameworks to govern their borrowing and debt management practices, leaving them vulnerable to financial shocks, political instability, and governance challenges. Effective parliamentary oversight plays a key role in mitigating these risks.

This Dossier explores several examples of how improved legislation in diverse countries can make a difference. Robust national legislation for sovereign debt should aim to reduce vulnerability to economic and financial shocks, build trust among stakeholders, and ensure that debt contributes to, rather than undermines, the country's long-term growth and stability.

What is more, designing and implementing a sustainable debt legislation can enhance debt transparency, fiscal responsibility, democratic oversight and social participation in the management of public debt. A poor legal framework design is one in which debt policies are too dependent on the political cycle or the preferences of a specific party. This kind of framework is vulnerable to changes and reversals which can undermine the credibility and effectiveness of public policies over time. International action and cooperation are essential in addressing this issue, particularly the role of International Financial Institutions (IFIs).

The Addis Ababa Agenda of the UN encourages countries to consider strengthening domestic legislation to align with guiding principles for the effective, timely, orderly, and equitable resolution of sovereign debt crises. Experiences included in the Dossier from debt-distressed nations emphasize the importance of legislative measures to curb executive overreach. The findings in this Dossier reveal that external shocks and weak revenue systems significantly heighten a country's debt vulnerabilities. As a result, the prioritization of domestic revenue mobilization emerges as a critical policy focus. Furthermore, a key consensus among all contributors is the crucial need to strengthen the role of Parliaments in overseeing debt management.

The *End the Debt Trap: Options for National Legislative Action Dossier* examines case studies from Sub-Saharan Africa, South Asia, Latin America, and the Middle East to highlight systemic weaknesses in debt governance. Through comparative analysis and experiences of concrete countries, the Dossier advocates for legislative reforms that emphasize transparency, accountability, oversight, and sustainability in public finance management. By connecting these reforms to human rights, economic equity, and environmental sustainability, the Dossier contributes to the international debate by providing a practical roadmap for nations to escape the debt trap and protect their developmental goals. The chapters, authored by experts and civil society representatives, offer lessons learned, actionable recommendations, and insights into the unintended consequences of selected cases. Finally, the contributions were prepared in 2024 and reflect the political situation at that time.

1. Initiatives from Argentina - Lessons learned

Initiatives from Argentina - Lessons learned

by Juan Pablo Bohoslavsky & Francisco Cantamutto

The background

Argentina has exhibited an erratic record on recent sovereign debt management. It defaulted on half of its total debt in 2001, then restructured most of it in 2005 (and again in 2010). A few holdout creditors did not accept the proposal to restructure their debt and litigated against Argentina in the New York courts, obtaining judicial victories, especially after 2012. This default effectively limited Argentina's participation in international financial markets until a new government took office and passed a law to pay the claims of these creditors. This opened a new phase of over-indebtedness, which was short (two years). In 2018, after 15 years, Argentina signed a Stand-By Agreement (SBA) with the International Monetary Fund (IMF) in the middle of a balance of payment crisis. Despite the SBA, the country had to reintroduce foreign-exchange controls, and finally a new government restructured its debt once again in 2020, during the pandemic crisis. In 2022, Argentina signed an Extended Facility Facility (EFF) with the IMF to pay off the SBA. In 2025, a new EFF was signed, making Argentina the single greatest IMF's debtor, accounting for two-fifths of its total credit. The country remains in a delicate situation in terms of its debt.

The country has faced various situations with regard to its debt burden during the 21st century, including improvements in its sustainability and resilience to withstand crises. This is mainly explained by the diverse political forces within government: while some members of the government have declared an intention to pay off debt in line with economic growth, other have used indebtedness as a lever to achieve fiscal consolidation and structural reforms. The efforts of the former have undermined the ability of the latter to reinitiate new debt cycles. With the aim of contributing to global debates around possible legislative/domestic initiatives to help prevent/mitigate the accumulation of unsustainable debt for developing countries, we provide examples of laws, bills and other proposals related to transparency, parliamentary approval and citizenship participation regarding debt contracts that have been either discussed or passed in Argentina. We understand that strengthening these could work as a way to both cope with the current debt crisis and as a firewall against new over-indebtedness cycles.

General and persistent (wrongful) legal practice.

The Argentine national constitution is crystal clear in terms of which branch is in charge of borrowing decisions: the Congress (Articles 4 and 75.4). Yet the Congress can delegate these decisions to the executive branch, for example, by passing an annual budget which contains new borrowing. In turn, law 24.156 (article 56) provides that the State can take on new debt to finance productive investments, to address cases of evident "national needs", to restructure its own organization, or to re-finance its liabilities (including interest). Borrowing to finance current spending is not allowed.

Subnational indebtedness is less regulated, despite the fact that it has reached almost seven per cent of total sovereign debt in recent times. Subnational (State) governments have, to some extent, autonomy, given that Argentina is a federal state. These State administrations have some liberty regarding the management of fiscal resources, but Article 75 of the Constitution nevertheless applies to those jurisdictions, as does Article 124, which allows subnational units to make international arrangements that do not affect national credit (Manzo 2023). During the 1990s, the national government approved some further regulations on this matter, compelling subnational administrations to require authorisation to take on further debt in foreign currency, to regularly provide information about their credit situation and to meet some minimum fiscal requirements (Ministry of Economy resolution N° 1,075/93, N° 277/95 and 731/95). Subnational debt may not be used for current spending and must not exceed 15 per cent of the fiscal resources allocated by the national government.

This basic legal framework has been blatantly ignored in governmental debt practices, as debt has usually been taken on by the executive branch without the required delegation from the Congress and it has regularly been used to finance expenditures for purposes not allowed by law (Erbin 2022). In regard to subnational debt, during the 1990s and again in 2016-17, national government allowed over-indebtedness insofar as it aligned with its own interests with regard to access to international markets. Checks and balances have proved to be weak, in both cases resulting in debt crisis and massive restructuring.

The multi-billion 2018 IMF SBA is an example of non-compliance with fundamental constitutional provisions (Justo 2021), which poses serious questions regarding the SBA's legality in light of the Vienna Convention on the Law of Treaties. The government negotiated an agreement without Congress authorisation or budget and legal evaluations by appropriate offices, and this loan was used to finance capital outflows, a usage which is explicitly prohibited in the IMF's own Articles of Agreement (Article VI).

In principle, a national government may not invoke the provisions of its internal law as justification for its failure to perform a treaty (for example, a debt contract) (Article 27, of the Vienna Convention). However, a State may not invoke the fact that its consent to be bound by a treaty has been expressed in violation of a provision of its internal law regarding competence to conclude treaties as invalidating its consent unless that violation *was manifest and concerned a rule of its internal law of fundamental importance*. A violation *is manifest if it would be objectively evident* to any State conducting itself in the matter in accordance with normal practice and in good faith (Article 46 of the Vienna Convention).

Despite these gross flaws in the legal conformation of the national act, the effects of this agreement persisted long afterwards. The following government launched two independent investigations on this matter. First, an official report on debt and capital flight that had occurred during the term of office of the preceding administration, which was conducted by the Central Bank (BCRA 2020), showed how debt was not effectively used for the legally authorised goals but to finance capital outflows. Second, the National General Audit Office (AGN 2023) focused on the IMF agreement and its impacts on debt sustainability, showing a straightforward deterioration of Argentina's financial position due to this operation. This was partially recognized by the IMF's Independent Office in 2021 (IMF 2021). These

1 Causa N° 3561/2019 "Macri Mauricio y otros s/ defraudación por administración fraudulenta y defraudación contra la administración pública" https://www.boletinoficial.gob.ar/pdf/aviso/primera/242791/20220905

findings were used to file a legal demand against the former president, Mauricio Macri, and some other members of his cabinet, based on alleged fraud[1] Even when these official findings proved that there had been serious legal flaws, this was not translated into accountability for the creditors or for the sovereign's official who had taken out the loan on behalf of the State. In fact, 2018 SBA was repaid with a 2022 EFF, meanwhile it accrued interest and surcharges.

These two investigations were not the first to be carried out by Argentina into its debt. In 2000, federal judge Ballesteros ruled that the debt contracted by the dictatorship in office during 1976-1983 was illegal and illegitimate. The ruling was then sent to the Congress for further constitutional action, but there was no follow-up whatsoever. Nevertheless, by the time the ruling got to Congress, the debt contracted by the dictatorship had already been restructured many times. There were no consequences for creditors nor for the officers who originally issued the debt that was eventually declared illegal by the court.

Argentina crashed into a debt crisis the following year, in 2001. A special parliamentary committee on capital outflows was constituted in the Chamber of Representatives of the Congress. Its conclusions were made public in 2005[2], during the restructuring of the 2001 defaulted debt. At least four bill projects were submitted during 2006-2010 to constitute investigation committees on debt, supported by 19 deputies[3]. None of those initiatives succeeded; after the debt was restructured in 2005, the government did not engage with the idea of further investigating. Instead, as explained below, the government reopened the debt swap twice. In the Senators Chamber, seven projects aimed at achieving this same objective were proposed by 21 Senators between 2004 and 2016[4]. All these efforts were aimed at investigating the legitimacy and legality of the restructured debt. Senator and former president for a week, Adolfo Rodríguez Saá, who declared the 2001 default, co-authored four of these projects.

In 2014, by law N° 26,984, another parliamentary committee was set up, this time in a permanent fashion within both chambers of Congress, centred on the investigation of the origins of external debt as well as on its management and repayments. Strikingly, the same law that created this committee also ruled that repaying the debt was of national interest. If there was any doubt regarding the legal basis of this debt, this possibility was dispelled by a simultaneous acknowledgment of the paramount importance of fully repaying the debt. The committee worked until December 2015, when its report was presented. By that time, a new government had taken office, and the Congress did not take any action based on the report. In fact, a 2016 law (N° 27,249) dismantled the committee. In 2021, there was another unsuccessful attempt to create a new investigative parliamentary committee.

As we have seen, the Argentinean State has on several occasions accumulated official evidence of sovereign debt mismanagement from a number of independent offices. Every time, this valuable information arrived late (in terms of the restructuring purposes) and was not used to legally question the debt in either national or regional/international courts). No politician or officer had to respond regarding their behaviour in the matter. The main focus was to gain political leverage in the context of negotiations on restructuring, but the effectiveness of this strategy is hard to assess given both the lack of accountability of those officials that participated in the borrowings and the persistently stringent conditions negotiated with creditors, especially with the IMF.

2 Final report of the Committee on "Capital flights in Argentina, 2001," Chamber of Deputies, National Congress, 2005.
3 Files 3850-D-2006, 0607-D-2008, 1666-D-2009 and 0418-D-2010.
4 Bill projects S-56/04, S-454/07, S-291/09, S-2068/12, S-1962/14, S-2654/14 and S-406/16.

Three cases of good legislative initiatives

At least three recently enacted laws on debt in recent times are worthy of being highlighted for the purposes of comparison and learning lessons.

Law 26,017

The defaulted bonds in 2001 had no Collective Action Clauses, which were not internationally implemented in bond issuances before 2003. During the negotiation with private creditors, the Argentine State enacted in 2005 law N° 26,017. In order to put pressure on the bondholders to accept the official proposal, the so-called "Lock Law" (1) prohibited the government from reopening the restructuring offer after the expiration of the first attempt, (2) prohibited the government from conducting any type of in-court, out-of-court or private settlement, and (3) required the government to remove all defaulted bonds from listings on all domestic and foreign markets and exchanges. This was a national legal effort to somehow fill the well-known fundamental gaps in international bankruptcy law for sovereign debt. This national legal effort was successful, given that 76 per cent of bondholders accepted the deal.

Yet the lock did not last long. In 2010, through presidential decree 563/10, and later again in 2013, through law N° 26,886, the government reopened the offer and made it again possible for those bondholders that had not accepted the deal the first time to do it several years afterwards. Strikingly, both the first law and the later practice contradicting the former were approved by the same political force in office. Finally, during a different government administration, in 2016 the Congress enacted law 27,249, which repealed the Lock Law and ratified the agreements in principle and terms and conditions of the settlement offer, allowing the new government to pay in full under all settlement agreements reached with the litigant bondholders in the New York courts.

Law 27,544

In February 2020 the Congress enacted Law 27,544 for the "Restoration of the Sustainability of the Public Debt issued under Foreign Law," authorising the executive branch to carry out a series of operations to achieve that objective. The Ministry of Finance was authorised by law to agree to provisions that would submit the government to foreign courts and to renounce the sovereign immunity defence, exclusively as regards the transactions involved in the debt-restructuring process and with the exceptions regarding those assets which are usually protected from these claims.

The law also grants wide powers to the Ministry of Finance to carry out any necessary act to complete the restructuring process and to issue new securities in order to modify the existing interest and principal maturity terms and to determine the terms, methods and procedures for the issuance of new securities. The government did not act completely on its own, but had specific guidance on how to restructure debt.

Law 27,612

In March 2021 the Congress enacted law N° 27,612 on "Strengthening the Sustainability of the Public Debt" that establishes that new requirements for issuing sovereign bonds denominated in foreign currency and governed by foreign law, as well as all programmes agreed with the IMF, shall require a law of the Congress expressly approving it. Indeed, this law reinforced the Constitution and law N° 24,156 to engage Congress in any deal on foreign debt, including IMF agreements. Yet the law does not indicate the contents or details of the agreement that have to be submitted to and approved by the Congress. Indeed, the specificities of the IMF agreements can vary widely, often including commitments to fiscal consolidation and structural reforms, all of which are relevant in terms of building political consensus in the Congress.

In any case, in practice, new bonds denominated in foreign currency and governed by other countries' laws are not regularly passed by the national Congress. Current Argentine President, Milei's government has tried to override this law, so far without success. (This law is studied in detail in another working paper commissioned for the *End the Debt Trap* workshop). Government obtained in 2025 the Congress approval to negotiate with IMF, but without any indication of the parameters of such negotiation, and no control over the final content of the agreement. The 2025 EFF agreement included several structural benchmarks that were included in the following parliamentary work despite the legislative branch had no voice in its negotiation.

There was at least one precedent for the bill presented by 18 senators in 2019 (file S-3516/19), limiting government discretion on the subject. This bill did not refer explicitly to IMF agreements, but included the prohibition of extension of jurisdiction – a measure not applicable to other projects.

Multilateral soft law initiatives

In 2010 UNCTAD released the "Principles on Sovereign Responsible Lending and borrowing[5]." In 2011 Argentina supported these Principles[6], while in 2012 the National Auditor General's office started to use them[7]. Despite this background, these principles were not formally incorporated into the national legal order, which would have enhanced their usefulness in the field of debt management.

Argentina had a leading role in the drafting and negotiating process of the "Basic Principles on Sovereign Debt Restructuring" adopted in 2015 by the United Nations General Assembly (UN Doc. A/69/L.84), with the support of the Group of 77 plus China. This resolution enacts nine principles, providing that sovereign debt restructuring processes should be guided by customary law and by basic international principles of law, such as sovereignty, good faith, transparency, legitimacy, equitable treatment and sustainability. Law 27.207 (2015) formally incorporated the UN Basic Principles into the Argentine domestic legal system.

In 2019 the United Nations Human Rights Council enacted resolution 40/8, passing the "Guiding Principles on Human Rights Impact Assessment of Economic Reforms," which contain rules on debt sustainability and debtors' and creditors' human rights obligations on debt policies (Principle 12). The Argentine representative in the Human Rights Council did not vote this time in alignment with the Group of 77 plus China but with the EU and the US, rejecting the initiative. The following government administration (2019-2023) did not make concrete efforts to endorse and incorporate this resolution into the national legal framework. Argentina's government has not been active in UN Framework Convention on Sovereign Debt negotiations.

One common absence: citizens' direct participation

A common feature arises in all the preceding initiatives. There has been no direct participation of citizens and/or civil society organisations at all in any stage of the debt cycle (i.e. from when credit is taken until the debt becomes unsustainable and has to be renegotiated). The debt has been originally created and renegotiated without the participation of the people. Presidential or legislative elections do not usually define the specific orientation of policy on particular matters such as debt management. There is a need to design and implement adequate consultation mechanisms for this purpose. Far from such a

5 https://unctad.org/system/files/official-document/osgdp20102_en.pdf
6 https://unctad.org/news/second-draft-unctad-principles-responsible-sovereign-lending-and-borrowing
7 https://www.agn.gob.ar/sites/default/files/files/Normas%20NCEG/Normas%20de%20Aplicables%20a%20la%20realización%20de%20Auditor%C3%ADas%20Especializadas%20-%20Deuda%20Pública.pdf

proposal being utopian, Argentina's society has proven to be deeply interested and involved in debt matters, as it proved by a number of initiatives from civil society (Keene, 2023).

In November 2000, the Ethical Tribunal on Foreign Debt and Neoliberal Adjustment Policies composed by a number of social organisations, including Mothers and Grandmothers of Plaza de Mayo and the Nobel Peace Prize winner, Adolfo Pérez Esquivel, ruled on the illegal nature of sovereign debt[8]. In November 2003, a social front of multiple social organisations launched a popular consultation initiative, a mechanism regulated by law N° 25,432, against the Free Trade Area of the Americas, the militarisation of Latin America, and the debt. A total of 2,252,358 people voted, of whom 88 per cent indicated that debt payments should be stopped. This information was formally submitted to President Nestor Kirchner in 2004, when the first debt restructuring offer was presented (Echaide, 2005). In July 2004, three deputies presented the "Zero Foreign Debt" popular consultation bill (file 3711-D-2004), which was not approved by the respective commissions. In October of that year, 15 deputies presented another bill (file 6943-D-2004) to declare the illegitimacy of the foreign public debt contracted by the military dictatorship during the years 1976-1983 in line with Ballesteros' ruling referred above. During this period, at least three projects were presented in the Senators Chamber to constitute committees to assess and engage with debt restructuring negotiation, but they were not passed (files 1641/02, 289/04 and 1430/04). The government negotiated on its own, without Congress or citizen participation. It must be stressed that no evaluation of economic and social impact of the proposals was carried out public before the swap.

Between 2014 and 2016, in the midst of the conflict between Argentina and the vulture funds, another civil society initiative arose. The so-called Assembly for the Suspension of Payment and Investigation of the Debt and for the Defense of the National Patrimony and the Common Goods of Argentina argued for a comprehensive and participatory audit[9]. Several organisations participated in that process, but their position and claims were not considered in formulating the official debt strategy. In fact, this initiative escalated during the next debt crisis. In January 2020, several social organisations organised a "Self-Call" for the Suspension of Payment and Investigation of the Debt, which launched a "Popular Trial of the Debt and the IMF". In December of the same year, after months of sessions with presentations on the impacts of the debt, the People's Tribunal, composed of Pérez Esquivel, the Mother of Plaza de Mayo Nora Cortiñas, feminist lawyer Nina Brugo Marcó, journalist Alejandro Bercovich and former federal judge Miguel Rodríguez Villafañe, presented its conclusions[10]. Considering the illegal origin of sovereign debt, which had not been solved by the many swaps completed through the years, it alleged that the debt was null and announced the need for an immediate suspension of payments while a deeper participative audit was addressed. It also required open access to official information on debt operations, including a complete creditors list, as well as a veto power on the legal and accountancy firms which had participated in those operations.

In 2022, organisations of the popular economy set up the "Committee of Creditors of the Internal Debt" to claim for social debts in line with the previous experiences referred above, together with a quarterly review of the social situation. They proposed to establish a tax on the capital that had fled, financed by sovereign debt. For this to happen, they demanded an end to banking secrecy[11].

8 https://www.agn.gob.ar/sites/default/files/files/Normas%20NCEG/Normas%20de%20Aplicables%20a%20la%20realización%20de%20Auditor%C3%ADas%20Especializadas%20-%20Deuda%20Pública.pdf
9 https://asambleadeudaybienescomunes.wordpress.com/
10 https://autoconvocatoriadeuda.blogspot.com/2020/12/fallo-del-tribunal-del-juicio-popular.html
11 https://www.pagina12.com.ar/414950-se-conformo-el-comite-de-acreedores-de-la-deuda-interna

As all these experiences show, Argentinian social organisations and unions have a strong interest in participating in discussions around debt sustainability and management. In different occasions, they have organised and presented evidence on debt impacts, demanding to be a part of the decisions in this field. Many of their findings were also verified or confirmed by Congress' special committees and official investigations. The opportunity to gain social engagement on debt matters was missed, as well as the possibility of adding new ideas on how to cope with the crisis in a participatory, rights-based and sustainable manner. This kind of mechanism could be upgraded if proper evaluations of the social impact of economic reforms were carried out.

Lessons learned

The lack of a robust national political consensus around debt policies explains to a great extent the radical changes in terms of debt policy approaches from one government to another.

Passing laws has not succeeded in ensuring fair, effective and rights-based debt policies or debt-restructuring strategies. This is not only because laws can change over time (as has been the case even under the same political force in office). Governmental practice often blatantly ignores basic constitutional provisions with no ultimate accountability, even when official evidence has demonstrated the legal responsibility of both the State's officials and creditors for their — to say the least — conscious negligence. Many times, both Congress and government have engaged in investigations of the legal aspects of debt, but this fact has not been translated into any kind of accountability mechanism.

The lack of an effective and fair mechanism for debt dispute resolution in the international arena has led to the disproportionate exposure of Argentina in foreign courts. This has even enabled an odd legal interpretation of typical clauses such as *pari passu* on debt bonds, to detriment of the country. The persistent extension of jurisdiction in new issuances of debt has enabled this kind of conflict. It is unclear if this weakening of the sovereign position has worked to gain access to new credit, given the persistent conflicts it has meant.

Multilateral soft law initiatives in which Argentina has actively participated have not modelled debt policies over time. Argentina led and supported important initiatives at the UN, crystallising principles to tackle collective action problems and ensure the realisation of the population's human rights, but these advances were somehow reversed by more creditor-oriented governments in the country.

All these developments have something in common: direct citizens' participation was not invited or allowed when deciding on debt issuance. The Inter-American human rights system, to which Argentina is bound, clearly states that citizens' direct participation in deciding fundamental debt (and other economy-related) policies is mandatory (Sagel 2024). Citizens' voices on debt issues should be considered binding for governments. Hence, innovative channels should be designed and/or implemented (some of them are already enacted in the national constitution, such as referendums) in order to promote and ensure citizens' participation.

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2.Background Paper on Ecuador

Background Paper on Ecuador

by Andrés Chiriboga

Introduction

Ecuador's contemporary indebtedness began in the late 1970s.[1] For more than two decades, the debt burden increased significantly, privileging the interests and conditions of private, bilateral and multilateral creditors to the detriment of the country's sovereignty and development. The country's vulnerable position[2] reached a turning point in 2007 with the arrival of a new government. Criticism of indebtedness was central to the government's programme of "Citizens' Revolution", which was materialised in the 2008 Constitution and in the economic laws that completed the new constitutional framework. During this period (2007-2017), Ecuador's government also launched a comprehensive citizen audit of external and internal debt, broke off relations with the IMF, and audited and denounced its investment treaties, which have historically generated contingent liabilities resulting from arbitration awards unfavorable to the Ecuadorian state.

In this text, I will refer to the main legal transformations in the area of debt and the influence of the emblematic audit of 2007-2008 that left important lessons for other countries and for Ecuador itself.[3] These decisions were, importantly, contingent upon politics, so were subject to setbacks and unexpected consequences, which will also be briefly discussed throughout this text.

The CAIC integral debt audit and its normative impact

The most important milestone in Ecuador in sovereign and transparent debt management has been the establishment of an integral audit of the country's external and internal debt. This process was carried out between July 2007 and July 2008 by a commission including government representatives and, mostly, civil society and independent Ecuadorian and foreign experts. The creation of this commission *(Comisión*

1 The previous process of great indebtedness of the country goes back to the distribution of the independence obligations (the "English debt"). Ecuador assumed its part in 1834, after the division of "Gran Colombia", and finished paying it off in 1974, just when the new cycle of indebtedness began (Paz y Miño 2006).

2 The only peculiar exception to this position regarding external debt was the convening, by President Osvaldo Hurtado, of the Latin American Economic Conference in January 1984. This summit followed the regional debt crisis of the early 1980s and aimed to establish a common position vis-à-vis private creditors (several US banks). This meeting started the so-called "Cartagena Initiative", which intended to form a sovereign debtors' club. This initiative was not successful for a number of reasons, among them, the bilateral negotiations that creditors rushed into with Mexico, Brazil, Venezuela, the Dominican Republic and Chile that undermined the possibility of a joint strategy.

3 After 2017, Ecuador made a 180-degree turn and resumed a debt policy mostly favourable to creditors and largely supervised by the IMF. The last three governments (Moreno, Lasso and Noboa) have kept this position. With the exception of the constitutional framework, a large part of these norms and policies have been dismantled or reformed. There is no current debate in the National Assembly on legal reforms intended to address sovereign debt management. There is only one draft bill "under consideration" that was presented in 2018 by former member of parliament, Gabriela Rivadeneira (Alianza PAIS). This draft bill, entitled the "Integral Law on Sovereign Debt Processes", proposes the incorporation of the Basic Principles for Sovereign Debt Restructuring Processes defined by the UN General Assembly in September 2015. The project was referred to the economic commission, where it has not been addressed.

de Auditoría Integral del Crédito Público, CAIC) was a key campaign offer and an important part of the government programme[4] proposed by former President Rafael Correa, who governed Ecuador between 2007 and 2017. This audit investigated private, multilateral, bilateral and domestic loans contracted by the Ecuadorian government since the 1970s. The final public report and its extended version, delivered to the Ecuadorian authorities in November 2008, revealed a series of damages and irregularities in all the debt tranches analysed. On the basis of the report, Correa decided to default on payments on two of Ecuador's bonds issuances (Global Bonds due in 2021 and 2030) with outstanding payments scheduled for late 2008. Leveraging this threat, and in the context of the global financial crisis of 2007-2008 and increased flexibility from oil revenue reforms[5], Correa's government successfully executed a repurchase through a reverse auction with a floor of 30 cents on the US dollar. The repurchase had a participation rate of 91 per cent at a buyback price of 35 cents on the US dollar (Gulati and Buchheit 2009, Feibelman 2017). Through this repurchase, the country avoided paying 7.5 billion US dollars of its debt service that had been due by 2030. Although the buyout was well received by the market, Ecuador was nonetheless shut out of private international financial markets until 2014 and the government privileged borrowing from regional Development Banks and bilateral creditors, including China and Russia (Lienau 2014).

CAIC's final report

The CAIC commission was created by Executive Decree No. 472 of 9 July 2007 prior to the start of a Constituent Assembly that convened between 30 November 2007 and 25 October 2008. Although the creation of the commission did not require a new constitutional framework, its mission was strengthened with the approval by the Constituent Assembly of an Organic Law on the use of oil revenues and the optimisation of debt management (*Ley Orgánica para la Recuperación del Uso de los Recursos Petroleros del Estado y Racionalización Administrativa de los Procesos de Endeudamiento*), which was enacted on April 3rd, 2008.[6]

4 The criticism of foreign debt, its conditions and limits to development was an integral part of Alianza PAIS's government plan for the 2006 elections. The proposal for an integral audit can be found on page 22 of the plan (free translation by the author): "**Integral audit of the external debt and of the state resources**: The use of external debt will be audited and it will be paid to the extent that it does not affect national development priorities. This proposal justifies the need to consolidate the existing National Commission for the Audit of the External Debt. The Alianza PAIS government will provide the Commission with a solid legal framework, independence from political and economic powers, as well as the necessary material support and political recognition"

5 In 2007, Correa issued an executive decree stipulating that 99 per cent of the extraordinary profits generated by the high price of crude oil would go 99 per cent to the state and 1 per cent to private oil companies. Those companies had participation contracts that provided for higher per centages in the event of price increases in international markets.

6 This bill created a government committee in charge of decisions on external debt. In addition to the Minister of Economy, the President of the Republic or her/his delegate participates in and chairs the committee. It also includes the National Planning Secretariat which has the goal of ensuring that debt is used for the country's development objectives. This collegial body, with the same structure, is maintained in current legislation. The bill also included the so-called fiscal *Golden Rule* (Pigou 1928, Musgrave 1939, Blanchard and Giavazzi 2004, Mintz, and Smart 2006) whereby current government spending - including debt service- cannot be paid with revenues from oil exports or new debt. One of the main findings that the CAIC audit exposed was that several loans granted to Ecuador by MDBs had been used to pay arrears or debt guarantees. This implied a violation of the articles of agreement of these entities and, in some cases, the deviation of funds originally intended for other purposes in the debt contracts (CAIC 2008).

The Constituent Assembly completed its work in July 2008. The draft Constitution was approved by a National Referendum held on 28 September 2008 with 63.93 per cent of valid votes. The new Constitution, still in force today, is very advanced in terms of sovereign debt management[7] and states an obligation to link borrowing to national development objectives within the guidelines of an economic model focused on *Good Living (Buen Vivir)*.[8] The Constitution establishes that the government must elaborate a development plan that shall respect the principle of economic sovereignty. This principle includes, among other things, transparent and sustainable borrowing. Likewise, the Constitution stipulates that foreign borrowing should be done when it is absolutely necessary and when it does not affect the rights to *Buen Vivir,* the country's sovereignty or the rights of nature (Pazmiño 2015).

The political support given by the government,[9] which had an absolute majority in the Assembly (80 of the 130 members belonged to President Correa's Alianza PAIS party), explains the important influence that the audit and other criticisms of foreign debt dependence have in the current *Magna Carta*. The Constitution adopted several recommendations of the CAIC and formalised the existence of citizen audits of public indebtedness. The articles that notably include these recommendations are 289 and 290 (the underlining is the author's own)[10]:

Article 289: *At all levels of the State, incurring public debt shall be governed by the guidelines of the respective planning and budget, and shall be authorised by a debt and financing committee pursuant to the law, which shall also define its establishment and operation. The State shall promote bodies enabling the citizenry to oversee and audit public borrowing.*

Article 290: *Public borrowing shall be subject to the following regulations:*

1. Public borrowing shall be resorted to only when fiscal revenues and resources from international cooperation are insufficient.
2. Public borrowing shall be monitored to ensure that it does not affect sovereignty, rights, good living and nature conservation.
3. Public borrowing shall be used exclusively to finance programmes and projects investing in infrastructure, or those with the financial capacity for repayment. Financing the foreign public debt may be restructured only if new conditions are more beneficial to Ecuador.
4. Renegotiation agreements shall not contain, either tacitly or expressly, any form of compound interest or usury.
5. Debts declared unlawful by the competent authority shall be challenged. In the case of declared illegality, the right to recovery shall be exercised.
6. Any legal action for administrative or civil liabilities arising from the acquisition or man-

7 The previous constitution, in force since 1998, included general procedural and competence references to debt management. Nonetheless, it has been severely criticised, as it included a temporary provision that allowed the Central Bank of Ecuador to grant stability and solvency loans to banking institutions that were already bankrupt or in financial trouble at the end of the decade due to irresponsible and corrupt management facilitated by financial de-regulation. This bank bailout exacerbated the crisis and fuelled a further devaluation of the national currency, which was finally abandoned in favour of a formal dollarisation of the economy in 2000 (Paéz 2004).

8 The Constitution adopted this political concept as a paragon to largely define a political and economic transition for the country. The broad definition given to *Buen Vivir* speaks of a harmonious life among human beings and between human beings and nature. However, it has never ceased to be a concept in tension wherever the confluence of three currents is identified (Le Quang 2017): the "culturalist and indigenist", the "environmentalist and post-developmentalist" and the "ecomarxist and statist". The discussion of external debt and ecological debt is addressed in the environmentalist and post-developmentalist reflections of Buen Vivir (i.e. Acosta 2003).

9 Previously, during the administration of President Alfredo Palacio, a Commission for the Investigation of External Debts (CEIDEX, for its Spanish accronym) was created. However, it did not have the political support or access to information that CAIC did.

10 The CAIC report ultimately did not include normative or other type of recommendations. However, in the course of their work period and together with other organisations gathered in the so-called "National Debt Group", its members met with the President of the Constituent Assembly, Alberto Acosta, on 21 March 2008, to present a list of proposals. These proposals can be found in the following repository: https://www.cadtm.org/IMG/pdf/Propuesta_GND.pdf Subsequently, the CAIC also met with the "Development Model" Commission to discuss those proposals, some of which were included into the constitutional text. For the preparation of this document, the author also interviewed Piedad Mancero, member of the CAIC, on 4 July 2024.

agement of the public debt shall not be subject to a statute of limitations.

7. The State is forbidden to take up any private debt.

8. The granting of debt securities by the State shall be regulated by law.

9. The Executive Branch may decide whether or not to take up debts of decentralised autonomous governments.

Article 291: *The competent bodies specified by the Constitution and the law shall conduct prior financial, social and environmental analyses on the impact of projects that entail public borrowing, to determine their potential financing. Said bodies shall perform the control and financial, social and environmental auditing at all stages of domestic and foreign public borrowing, in contracting as well as in management and renegotiation.*

Although it does not appear as an explicit recommendation of the CAIC for the Constitution, the audit criticised the structural adjustment conditionalities of the IMF credit agreements with Ecuador and their economic and social effects. The Constitution includes an article that requires the National Assembly to analyse international treaties and instruments that impose obligations on the government's economic policy:

Article 419.5: *The ratification or denunciation of international treaties shall require prior approval by the National Assembly in the following cases: (...) 5. When they bind the State's economic policy in its National Development Plan to conditions of international financial institutions or transnational companies.*

In recent years, Ecuador has signed three credit facilities with the IMF: in 2019, 2020 and, most recently, in 2024. All of them include economic policy conditionalities and they have been launched without the parliamentary approval required by the Constitution.[11] With the support of 86 out of 137 members of Parliament, the current IMF programme is currently being audited by the Assembly's Citizen Participation Commission and unconstitutionality filings are being prepared.

The Organic Code for Planning and Public Finance: the Golden Rule nuanced

The Constituent Assembly drafted and adopted several economic bills during its establishment.[12] On debt, the most important norm is the Organic Code for Planning and Public Finance that was sanctioned in October 2010[13] One of the main objectives of creating this new macro law was to make public finances subject to planning, in accordance with the new Constitution. As mentioned above, the Constitution provides that external debt must be used for infrastructure or other projects capable of generating sufficient revenue for repayment (Art. 290.3). The responsibility of preparing the bill fell largely on two technical entities of the executive branch: the National Secretariat of Planning and the Ministry of Finance. The former was mainly led by progressive intellectuals, and the latter was still dominated by a highly skilled and conservative technocracy subject to the main politi-

11 The disputed argument for bypassing the Parliament is that a credit facility cannot be considered a treaty. This claim illegally disregards the fact that these are instruments between two actors under international law, which is the treaty definition by the Vienna Convention and is clarified in several resolutions of the International Court of Justice (Cabral and Pino 2019).

12 Prior to the approval of the Constitution, the Constitutional Assembly drafted and approved six economic laws: the Tax Equity Reform Law, the Organic Law for the Recovery of the State's Oil Revenues and the Administrative Rationalisation of Debt Management, and the Organic Law for the Reform and Interpretation of the Internal Tax System, the Tax Code and the Tax Equity Reform Law.

13 In the newly elected Parliament (July 2009-May 2013), after the new Constitution came into force, the ruling Alianza PAIS party no longer had an absolute majority as it had had in the Constituent Assembly (it held only 59 seats out of 124). The government had to engage in important negotiations with some political blocs, and in particular with a group of seven independent legislators, who gained considerable relevance and power during this legislative period. As part of its institutional reform process, the government created a Ministry of Political Coordination, which, among other things, was in charge of leading "political operations" in the National Assembly. The significant intervention of the government's political and technical teams in the Assembly was a constant feature of the 10 years of President Correa's regime.

cal directives of the incumbent President. The authorship of the bill is not a minor issue and largely explains how the constitutional mandates on debt management were translated into law.

The Code for Planning and Public Finance and its secondary regulations have been important tools in detailing the functioning of the national planning system and its interaction with the processes overseen by the Ministry of Finance. Among other things, the Code includes the Debt Committee and establishes the guidelines for its operation and sets a limit on public indebtedness (at 40 per cent of GDP). However, the Code is less strict than the Constitution itself regarding the safeguards for avoiding discretion in the use of debt. For example, the Code provides a broad definition of what constitutes an investment (Art. 55): "expenditures and/or transactions carried out with public funds in order to maintain or increase the wealth and social capacity of the State". It also stipulates that the Ministry of Finance will distribute the funds coming from borrowing and that it will define the programmes and projects that meet the requirements as part of its general budgeting process (Art. 124). This loosening of constitutional safeguards was not free of criticism, for example from the "National Debt Group", a group of renown academics and activists dedicated to research and advocacy on debt. The need for the Golden Rule to have an exceptional "escape valve" comes with the risk of it becoming common practice. Since the Code came into force, it has become common to support investment projects to hire personnel in public institutions and, although it is clearly unconstitutional, the Code does not prohibit contracting credits with conditions tied to the payment of arrears, as seen in the 2019, 2020, and 2024 IMF programs.

Financial and Monetary Code: emergence and disappearance of (self) financing mechanisms from the Central Bank

Ecuador's historic weak negotiating position in international capital markets is accompanied by a lack of local alternatives. On the one hand, Ecuador does not have a properly organised local debt market. After the 1999 crisis, government debt issuances became largely dependent on demand from the National Pension Fund (IESS) and, to a lesser extent, the Armed Forces Pension Fund (ISSFA) and the Police Pension Fund (ISSPOL). To date, there is not a fully developed market for public debt, which has also hindered the development of the local securities market as a whole (Chiriboga 2023).

On the other hand, the laws that regulated dollarisation — enacted in the early 2000s — reduced the role of the Central Bank and, among other things, limited its monetary or quasi-monetary operations under the argument that it had stopped issuing currency. This changed with the 2008 Constitution, when an Organic Monetary and Financial Code was enacted in order to have a macro-law on monetary, financial, securities and insurance matters.[14] One of the main directives of the Constitution for the government's economic programme is the channelling of liquidity for development (Art. 302.3). The Constitution also gave the Central Bank a fundamental role in operationalising the economic policy of the Executive (Art. 303). In this sense, the new Code provided the Central Bank with liquidity management tools. In particular, it gave it the possibility of investing its liquidity surpluses (art. 124 of the Code) through a domestic investment program (art. 125 of the Code), which could be used to purchase public and private securities.

14 The bill was proposed by the government's economic team, which again included officials from the Ministry of Finance and authorities from the government's planning team. This time the Assembly was completely favourable to the government. Alianza PAIS held 130 of the 137 seats.

Once the Code was enacted, this tool was used significantly[15] to purchase short-term Treasury bills (CETES, for their Spanish acronym) from the Ministry of Finance to meet its liquidity needs, which began to increase at the end of 2014 after the fall in oil prices and the appreciation of the US dollar. To a lesser extent, the programme allocated resources to public development banks. A more diversified portfolio, for example, to channel more resources through the financial entities of the popular and solidarity economy, is a critique that can be sustained of the way the tool was managed. In any case, the availability of these self-financing mechanisms reduces the need for external borrowing and puts the country in a better negotiating position in international capital markets and vis-à-vis different types of creditors.

In the context of rebuilding relations with the IMF and in direct coordination with the representatives of the economic elites16[16], the government of former President Lenín Moreno (2017-2021), through a legal reform adopted in August 2018, limited the programme and impeded any investments in government securities. The main argument of the economic elites and the IMF for "killing" the programme is that it endangers dollarisation because it has a negative impact on the level of international reserves.[17] This is a fallacious argument, since only movements that imply an outflow of dollars from the economy (capital flight, debt payments and/or import payments) have a negative impact on the level of international reserves. For example, if the Ministry of Finance gets more funds through the issuance of CETES to pay salaries, this movement per se does not imply an outflow of dollars from the economy. The real concern of the IMF is that there should be immediate resources in the government accounts to guarantee the payment of arrears.[18] Contrary to its argument, it is arrears payments that imply dollar outflows and do not contribute to strengthening dollarisation.

The current Ecuador-IMF programme insists that this type of quantitative easing should not be used. However, the IMF recognises that a temporary reform of the Financial and Monetary Code approved in December 2023 to allow for a one-off reprofiling of these operations was beneficial to smooth the debt service profile, reducing interest and amortisation payments in the near term (IMF 2024, p. 9).

Recommendations for parliamentary advocacy

Ecuador has a significant debt problem with important repayments coming due in the next few years (Figure 1).[19] Room for advocacy must consider the current and rapidly changing political context. The position of the incumbent government (reelected for the period May 2025 – May 2029) is unfavourable to debt policies that do not involve structural adjustment. Following the preceding administration, President Noboa's regime is also fond of the implementation of debt-for-nature swaps that have already been already criticised as false solutions that provide very limited debt relief.[20] Despite an unfavourable context in the Executive, room for advocacy can be explored with some legislators and members

15 As of March 2019, before Ecuador entered into a new credit facility with the IMF, the Central Bank reported that 3.5 billion US dollars were invested in CETES. One of the conditions imposed by the IMF in the 2019, 2020, and 2024 programmes was to stop these operations between the Central Bank and any public entity.

16 Moreno appointed Richard Martínez as his Minister of the Economy. Before his appointment, Mr. Martínez was the President of the Ecuadorian Business Chamber (CEE is its acronym in Spanish).

17 For a detailed explanation of the way International Reserves work under dollarisation in Ecuador, the reader can refer to the text by Carvajal (2021).

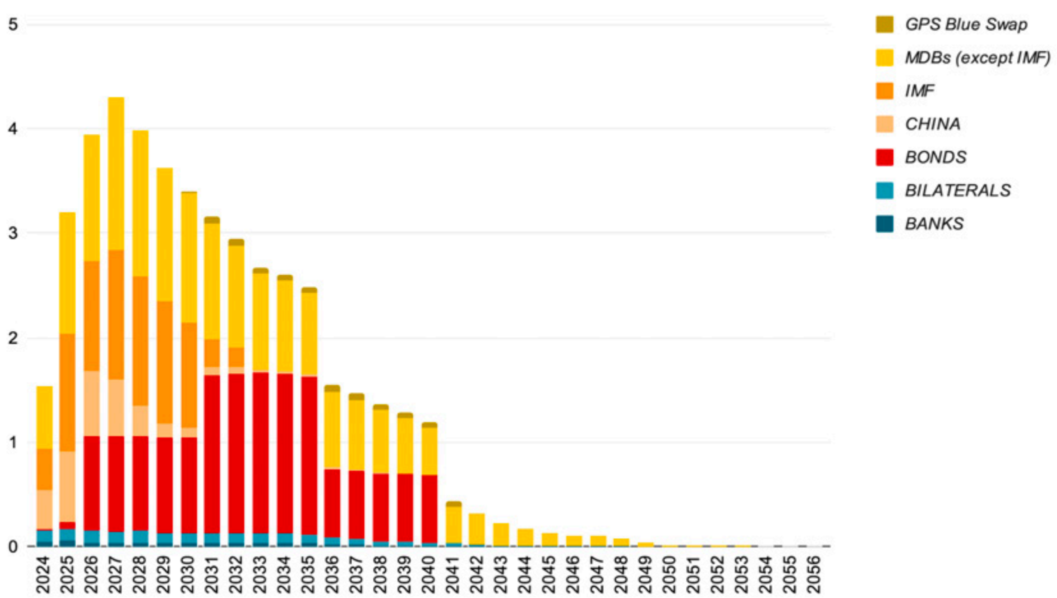
18 The Debt Sustainability Analysis (DSA) of the last credit agreement signed between Ecuador and the IMF states that "Ecuador is at moderate overall risk of sovereign distress and debt sustainability, but not with high probability in the baseline program forecast" and recommends that the "steadfast implementation of fiscal reforms would strengthen Ecuador's public debt sustainability" (IMF 2024, p. 46). The fiscal reforms referred to in the agreement are an increase in the VAT, the elimination of fuel subsidies, and further debt contracting so that the central government accounts comply with Quantitative Performance Criteria (QPC) No. 4: "Non-accumulation of external payment arrears by the NFPS in 2024 and 2025" (Ibid, pg 48).

of other state institutions such as the Participation Council (CPCCS is its Spanish acronym).[21]

President Daniel Noboa was initially elected for a short term after winning the 2023 snap election. He was reelected in April 2025 and will be in power until 2029. Despite initial successes in appointing authorities to parliament, the ruling party will continue to face opposition and will need support from other parties to secure majority votes. Noboa's party, National Democratic Action (ADN), together with its allies, holds 66 out of 151 seats. The largest the opposition bloc, the Citizens' Revolution-RC (66 seats), has sharpened its criticism of Noboa's economic policy. This bloc has previously led actions to scrutinise the agreement with the IMF and condemns the fact that it was implemented without the approval of the Assembly. The 9-seat group of the indigenous movement (Pachakutik-PK) is di-

Figure 1

Ecuador's External Debt Service 2024 - 2056
(Principal amortizations per creditor in USD billions)



Source: Ministry of Economy and Finance

Note: Latest official data dates from April 2024. It does not include the 4 billion credit facility with the IMF signed in May 2024.

19 This official data does not take into account the new 4 billion US dollars programme with the IMF, which is primarily linked to arrears payment conditionality and will add to future amortisations.
20 An example is the Galápagos Debt-for-Nature Swap. A critical analysis explaining that the instrument delivers no major debt reduction while it implies important sacrifices in terms of environmental governance and sovereignty can be found here: https://latindadd.org/arquitectura-financiera/galapagos-deal-an-ignominious-legacy/
21 This council, which is considered the fifth power of the State in Ecuador, is responsible for organising the processes for the selection of control authorities (the Attorney General, Superintendents, etc.) and for promoting citizen participation. The latter has been very little exercised, to the detriment of the coveted and controversial selection of control authorities.

vided. There are also some critical voices standing from a programmatic left-wing position. Other members of this bloc, however, have negotiated and aligned themselves with the government. The minoritarian right-wing parties Construye (1 seat) and the Social Christian Party (4 seats), initially allies of Noboa, could swing between opposing and supporting the incumbent government according to their convenience.

An economic legislative agenda is a pending task for parliamentary groups such as RC and some legislators from PK, where there is appetite for proposals and advice. A relevant input would be a package of reforms to the two codes, monetary and planning, that could recover and improve past experiences and propose new elements on debt and liquidity management. For example, the dematerialisation of debt securities and tax credit notes so that they can be quasi-monetary electronic means of payment. Similarly, reforms are needed to organise and promote the development of a domestic debt market and the securities market in general. However, beyond the capacity of legislators to propose laws, the executive has always set the pace of economic reform (now constrained by IMF conditionalities). The impact of such proposals will largely depend on the space that can be created in upcoming legislative and executive bills and on the (re)configuration of the political panorama after the presidential and legislative elections of 2025.

Beyond working on a mid-term legislative agenda, there are two other areas where members of parliament can play an important role. The first one is the ongoing investigations and actions regarding the IMF programme.

There is an appetite for analysis and technical support for the ongoing processes and, subsequently, of the programme revisions that are linked to upcoming disbursements. A second important area is citizen auditing which now has constitutional status. In addition, there are mechanisms and provisions regarding access to information established in the Participation Law that should support the role of such audits. Although the context of the CAIC was very particular, members of the parliament and the CPCCS could promote and give political backing to a new process of citizen audit of external indebtedness.

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Constitución de la República del Ecuador

Código Orgánico de Planificación y Finanzas Públicas (COPLAFIP)

Código Orgánico Monetario y Financiero (COMYF)

Ley Órgánica de Participación Ciudadana

3. Legislative Reform for IFI Borrowing in South Africa

Legislative Reform for IFI Borrowing in South Africa

A Background Paper for the End the Debt Trap Project

by Liso Mdutyana & Kamal Ramburuth

Introduction

South Africa is in urgent need of parliamentary oversight on foreign loans. The volume at which the state has taken up foreign currency debt from International Financial Institutions (IFIs) since 2019 should alarm policymakers and the public. This is because the unsupervised uptake of foreign debt can threaten debt sustainability, sovereignty, democracy and the realisation of human rights, environmental sustainability and gender equity. In this background paper, the first section describes the legislative proposals for South Africa. The second section details the experiences of the campaign to increase parliamentary oversight of public debt management in South Africa and the lessons from debt-distressed countries. The third section looks at the unintended negative consequences of the campaign so far. The fourth and last section features our recommendations for effective advocacy and legislation in order to protect countries from debt distress.

The legislation which currently governs how sovereign borrowing is carried out gives inordinate power to the Finance Minister in the executive. Management of South Africa's public finances is set out in the Public Finance Management Act (PFMA) of 1999. Within this act, sections 66, 70 and 71 to 74 outline the executive's power to enter into debt arrangements such as loan agreements or guarantees. Notably, section 72 stipulates that "The Minister, *on conditions determined by the Minister*" may authorise someone to enter into loan agreements on behalf of the state (Public Finance Management Act no. 1 of 1999). In essence, the Minister is allowed to set the parameters of their own actions. This level of discretion is arguably too great, given that taking loans has at times threatened the realisation of basic human rights such as healthcare and education, when attached to austerity conditionality. The public should have a say in the acquisition of any public debt, and there should be specific approval and oversight of debt from IFIs. As such, it is imperative that Parliament qualifies the powers that are given to the executive by providing majority approval on foreign IFI loans, such that Parliament fulfils its constitutional duties.

"In the South African context, oversight is a constitutionally mandated function of legislative organs of state to scrutinise and oversee executive action and any organ of state." (Parliament of the Republic of South Africa 2011). The potential risks that are associated with borrowing from IFIs, which includes the undermining of sovereignty and human rights (both of which are Constitutionally protected) (Chapter 1 of the Constitution of the Republic of South 1996) warrants that policymakers consider the extension of Parliament's oversight mandate regarding IFI borrowing.

Parliament's mandate also prescribes the process under which oversight and accountability should be done. In conducting oversight and accountability, South Africa's Parliament must detect and prevent, among other things, unconstitutional behaviour; and secondly, in terms of section 55(2), must "provide mechanisms to ensure that all executive organs of state in the national sphere of government are accountable to it" (Parliament of the Republic of South Africa 2011).

An example of such a mechanism is budget votes. The Minister of Finance tables a budget – which contains planned spending for the coming fiscal year – that has to be approved by Parliament. Parliamentarians' budget votes are then debated in Parliament. In this manner, Parliament is able to evaluate whether National Treasury and government departments "kept the promises of the previous year and spent taxpayers' money properly" (Parliament of the Republic of South Africa 2011). Importantly, the process of evaluating planned spending happens before the National Treasury distributes the money to departments. This allows the National Assembly time to evaluate, through looking at the previous year's performance, whether giving a certain amount of money to a department or programme is justified. By contrast, with International Financial Institutions (IFIs) loan agreements, Parliament is not given the opportunity to consider and potentially reject a loan which they might deem to be unjustifiable. The process of approval is especially important for IFI loans and should have an independent approval process separate from the budget vote because of their particular implications for legally binding policy conditionalities and exchange-rate risk. If parliamentary oversight on sovereign borrowing from IFIs is to be effective, Parliament must be given the legal power, framework, time and resources necessary to make a thorough evaluation.

Principles for Parliamentary assessment

Our proposal is that the discretionary powers accorded to the Minister of Finance must be qualified using a set of well-grounded principles. These are: debt sustainability, human rights, development, national sovereignty and economic democracy.

1. **Debt Sustainability - Debt Sustainability Analysis (DSA)**

The National Treasury, the IFI and the Parliamentary Budget Office, must conduct a comprehensive debt sustainability analysis (DSA), which considers not only the state's ability to repay but also the implication of additional debt on the government's ability to provide a sufficient amount of public goods. This DSA must be presented to the National Parliament's Portfolio Committee on Finance. From this analysis, the Portfolio Committee on Finance will have an opportunity to mitigate against the likelihood of debt distress.

2. **Human Rights - Human Rights, Gender and Environmental Impact Assessment**

The National Treasury, alongside the Department of Women, Youth, and Persons with Disabilities and relevant government departments, must conduct and submit a participatory assessment of the potential impact of the loan and related servicing costs on the realisation of human rights, availability of resources to realise human rights, gender equity and the disproportionate impact of IFI lending and debt-servicing costs on women, children and the environment. These assessments must be submitted to the Portfolio Committee on Finance.

3. **Development**

The National Treasury must demonstrate that taking on the loan will advance and will not be detrimental to South Africa's long-term development agenda. This means that the loan must not contain conditionalities which if followed would lead to socially, economically or environmentally regressive outcomes either in the short- or long-term.

4. **National Sovereignty (Conditionalities)**

If the loan contains policy recommendations/ commitments or conditionalities, the National Treasury must write a report where it demonstrates that: (1) These do not go against the Constitution and other existing laws; (2) These do not go against current national policy; (3) That the impact of departing from these commitments or conditionalities would be negligible on the country's standing in financial markets; and (4) They will not unfairly bind the policy space of future democratically elected governments. Loans with policy conditionality must be submitted to the National Assembly.

If the Portfolio Committee on Finance finds that taking on the loan would be detrimental to debt sustainability, human rights, gender equity, or environmental sustainability, economic development, and/or national sovereignty, then they have an opportunity to recommend that the National Assembly reject the loan.

It would be prudent for Parliament to consider amendments to both the PFMA and possibly the Municipal Finance Management Act (Act 56 of 2023) in order to qualify the powers of the relevant authorities to enter into debt arrangements which contain policy conditionalities. An example of this lies in the powers contained in sections 66, 70 and 71 of the PFMA, which affords the executive the power to enter into debt arrangements that are binding on the state and grant the creditor a direct charge against the Revenue Fund.

The potential for non-financial conditions (policy conditionality) to be attached to IFI debt instruments is not adequately addressed by the PFMA. We argue that the discretionary power afforded to the executive in terms of these provisions is too broad and warrants legislative intervention to set parameters within which such power is to be exercised (i.e. in accordance with the principles articulated in this paper) and to include specific reporting mechanisms for Parliament (i.e. that IFI agreement with conditions must be tabled in Parliament).

5. **Economic Democracy - Majority vote and public consultation**

First, the terms and conditions of the loan, namely: maturity, interest rate, principal amount, interest payments and their timing, currency, any policy recommendations/commitments or conditionalities, transactional costs (such as the commitment and appraisal fees), and its purpose should be made publicly available on the National Treasury website and should be included in National Treasury's annual Debt Management Reports. Second, the Portfolio Committee on Finance should, for a period of three weeks, allow for public input through online submissions and public hall meetings. Third, the Portfolio Committee on Finance should summon National Treasury and use these public comments to scrutinise the loan.

Practically, this means that prior to signing a loan agreement or guaranteeing debt, the Minister would have to demonstrate, to the satisfaction of Parliament, that the debt arrangement would not violate these principles. Finally, the Portfolio Committee on Finance must compile this scrutiny and the National Treasury's response and submit it to the National Assembly. The National Assembly must be given adequate time to evaluate the report (consisting of the DSA; Human Rights, Gender and Environmental Impact Assessment; and National Sovereignty and Development assessments). Following which, the approval or rejection of the loan must be done through a majority vote.

Criteria for Parliamentary Evaluation

Official Financing comprises concessional and non-concessional flows from a governmental (bilateral) or intergovernmental (multilateral) institution. Private flows are defined as flows at market terms and financed out of private-sector resources and private grants, referring to loan financing that is acquired through bond auctions, switch auctions, borrowing from retail investors or from the Corporation for Public Deposits. This therefore includes loans or credit facilities from both IFIs and sovereign states. A loan originating from an official source should be a necessary but not sufficient condition for tabling in Parliament. In order to qualify for special parliamentary scrutiny and approval, a non-market loan must also be characterised by any of the following:

- → Denominated in foreign currency.
- → Accompanied by policy conditionalities / recommendations / commitments
- → With a variable interest rate or with a fixed interest rate that is greater than the three-year average (conservative) expected GDP growth rate.
- → Part of an ongoing programme (for example, a credit facility or a tranche loan).

Domestic Campaign

The four pillars which have underpinned the progress of the advocacy driven by civil society and labour so far have been: 1. Robust background research, 2. Mass mobilisation and collective education, 3. Use of available channels for engaging government and 4. Construction of a diverse, progressive and democratically-run working group.

Background research was essential as it allows for a thorough understanding of the issues, and lends credibility to the project. The evidence compiled in the report ('International Financial Institutions' Covid Lending in South Africa: Context, Contentions, and Policy Implications) followed from interviews and discussions held with individuals from the government, multilateral banks and lawyers (Ramburuth et al. 2023). Moreover, the report was publicly launched and was subjected to scrutiny (leading to revisions) by representatives from the IMF (Institute for Economic Justice 2023). This added legitimacy to the project, as it was based on research which could be considered credible.

Research allowed for an uncovering of relevant groups and allowed for targeted mobilisation and collective education. Once the background research was completed, it became clear which groups would be in support of or would benefit from the policy recommendations contained in the report. Among the key insights from the research was that IFI loans, through policy conditionality, can entrench regressive socioeconomic policy such as austerity. Since austerity has had a direct impact on the public service, the provision of social service, and the government's capacity to respond to crises, it has become imperative to recruit groups which are focused on these issues. Thus, marginalised communities, labour unions, healthcare and education, and climate justice organisations were brought together in a workshop. In this workshop, the interest groups shared knowledge and experiences, allowing for collective learning, and collectively devised the strategies and tactics that would be essential in enabling legislative reform.

The use of existing channels of parliamentary participation around the Medium-Term Budget process allowed our recommendations to be heard by and find support from Parliament. The workshop was structured around making a submission to Parliament, to raise awareness of the issue and to try and rouse the support of allies in Civil Society Organisations (CSOs) and labour. The Joint Parliamentary Submission (Institute for Economic Justice 2023b) was developed collectively by groups which participated in the workshop. All participants were given time to read a basic proposed submission, and then breakout groups allowed everyone in the room to have a say and summarise their inputs. Given the large and diverse participating organisations, there was strong legitimacy behind the proposal. Following this, the Coalition on Debt Justice, representing the participant organisations, presented the recommendations to parliament during the public hearings that followed the Medium-Term Budget Policy Statement in 2023 (Coalition for Debt Justice 2023), with the Finance Standing Committee in Parliament endorsed the key resolutions (Finance Standing Committee 2023).

The fourth measure that has been crucial in driving the campaign is the formation of a working group. A campaign to push for legislative reform requires a multitude of skill sets, like research, legal expertise, capacity building, media and communications and mass mobilisation. The working group, composed of key CSO and trade union partners, allowed the campaign to be backed by credible legal and economic advice and political support by key social forces. Regular online meetings and a collaborative approach to decision-making ensure that the individuals within the group feel ownership of the project and have their contributions considered.

Lessons from Best Practices in Advocacy and Implementation of Reform

Three main lessons can be drawn from countries that have experienced debt distress and could be used to strengthen domestic legislation:

First, the procedure for parliamentary oversight (ratification and monitoring) must be captured in legislation. In the case of Argentina and Zambia, prior to their episodes of debt distress, the Constitution already provided for parliamentary oversight on sovereign borrowing. However, in both cases, the executive took on foreign debt without any process of parliamentary ratification/approval. This is probably because no additional legislation outlined the steps, they must undertake to realise the constitutional provisions. Had a statute explicitly stated that the oversight process must involve parliamentary approval, then prosecutors may have been able to make a case to convince courts to declare the debt acquired without supervision to be illegitimate. This would have allowed countries to dismiss, rather than default on, the debt. That writing off of debt may in turn have reduced the severity of the economic crises they ended up suffering.

Second, legislation must compel the executive to report extensively and regularly to Parliament. In the case of Zimbabwe and Zambia, there were no standards for reporting on public debt to Parliament. Had this been in place before the countries' debt crises, it is likely that Parliament would have preemptively sounded the alarm on the high levels of foreign-currency-denominated debt. This may have persuaded the states to pursue debt restructuring much faster. On the other hand, the case of Mozambique showed that the presence of regular reporting standards can be insufficient when some debt is taken off the country's balance sheet. Hence, reports by the executive must be buttressed with competent and independent auditing institutions to make Parliament confident that the executive's reports are a true reflection of public debt. In addition to auditing institutions, there must be clear and predictable punishment of individuals who are found to be in contravention of the law so as to discourage a repetition of such behaviour in the future. For instance, Zambia remains vulnerable to the debt crisis partly because, even with laws requiring regular and extensive reporting, the Ministry of Finance does not conduct regular, publicly available updates on the execution of the Annual Borrowing Plan. Additionally, the executive also sometimes bypasses the parliamentary oversight process with little punishment, with the Minister sometimes concluding loan deals personally on behalf of the state during international travels (AFRODAD 2024).

Third, legislation must outline principles that guide the approval and monitoring of loans. The case of Argentina is instructive here. Even as the legislative reform of 2020 required that all programmes conducted by the IMF be approved by Parliament, Argentina has continued to accumulate foreign-currency debt, which has been criticised as being no different from past programmes which contributed to debt distress (Lacour 2022). A set of principles would operate as a helpful guide for Members of Parliament. One principle, prescribed by AFRODAD, is that debt must be evaluated from a value-for-money perspective (AFRODAD 2024). This is especially pertinent for foreign debt, wherein a foreign currency debt-financed project should be partly judged for its ability to generate foreign currency, so as not to burden the foreign currency reserves of the state. It should be noted however, that this still would not stop the contracting of clearly problematic debt — as appeals to these principles could be disregarded by party-line voting, especially where the governing party is dominant in Parliament.

Our campaign's challenge to the power concentrated in the National Treasury over signing loan agreements may be detrimental to future collaboration with the department. The essence of our campaign is that decision-making over taking on foreign loans should be democratised. This would disperse power, allowing the public – through Parliament – to have a greater say. This could be problematic for the National Treasury, as using International Financial Institutions has been an increasingly relied-upon financing strategy employed since 2020. The call to qualify their powers may thus undermine their financing strategy, and potentially harm their relationship with us. This poses challenges for some of the work done by the Institute as a whole. A lot of the advocacy work done by the Institute, such as Feminist Economics, Budget Advocacy and International Debt, depends crucially on engaging with government officials. A soured relationship, as a result of the pressure we have applied so far, undermines our ability to work cooperatively in other streams of work. One lesson here is that advocacy of this kind – which directly challenges the power of government departments – could be done in a more subtle manner, so as not to close off the channel for future engagement. Moreover, deference to "best practice" and evidence-based policy reform is useful to rely upon to avoid having to make purely political arguments for reform.

However, this is not a lost cause. An ongoing leg of our campaign is to continue bilateral meetings with National Treasury officials to maintain a cordial relationship with departments and to work cooperatively so that they can be assured that the process of parliamentary approval is understood as a necessary check against executive powers and helps the public gain confidence that their government is doing things that are in their best interest.

The large and diverse Steering Committee driving the advocacy has made decision-making more strenuous, leading to a slower than desired pace of the campaign. This is the trade-off between speed and consensus with participation. Steering Committee organisations have different internal decision-making processes that often delay the undertaking of activities necessary to achieve the objectives of the Steering Committee. Moreover, these organisations have their own – sometimes complicated – relationships with some of the targets of our advocacy, namely, political parties. In addition, our recommendations for reform in public debt management are politically sensitive. For example, parliamentary approval could lead to there being a need for cooperation between parties or could potentially trigger further conflict between parties that have irreconcilable stances on the taking on of foreign debt. Overall, these factors make it necessary that the Steering Committee receives explicit approval from the constituent organisations. In reality, this has not been easy to come by, as these organisations (especially at leadership position level) are preoccupied with multiple competing demands and do not have sufficient time to deliberate on the merits of our advocacy and the strategy around it.

A positive unintended consequence, however, has been the coordination of progressive movements in South Africa which has laid the groundwork for further collaborative efforts. Participation in roundtable discussions, working groups, and coalitions with the intention of gathering support for our project has revealed alliances with different organisations on other economic issues. This has led us to support and partake in other progressive causes such as the campaign to increase access to information relating to the Just Energy Transition in the Country.

Legislation must be comprehensive. This is an important step for the content, wording and processes that the bill engenders. Internationally, on the African continent, a big weakness uncovered in the court cases brought against the executive in Zimbabwe and Zambia was that while legislation did provide for parliamentary approval, it did not set out the procedures that must be followed to realise that approval. A comprehensive statute – which includes not only that approval must be received, but the exact process through which it must be received – would be deemed advantageous. Where the executive fails to follow the steps in the law, it will be easy to demonstrate that a loan was acquired illegally, and thus the state should not be liable to repay it. Further, legislation must also include commonly-agreed principles that must guide members of the Parliament when assessing whether a loan should be ratified. An appeal to principles can mean that parliamentarians are guided more by objective, well-grounded factors in their choice to vote for or against the acquisition of a loan.

Activists must study and learn from past international experience. First, the push to increase parliamentary oversight of public debt is one which has happened in many countries across the world, especially in the Global South. As such, activists can research and learn from the tactics that have been deployed in other countries, rather than attempting to devise tactics from scratch. Second, we often find that the political economy of different countries is similar. In that case, it may be very fruitful to learn from the successes and failures of the tactics and strategies used in those countries, so that they can be more easily applied in one's own country. Third, researching international cases, especially through interviews with the activists and individuals that were involved in campaigns, can lead one to uncover other vital but overlooked individuals or data.

The issue of legislative reform in public debt must be linked to related struggles. There are a few advantages with this. Firstly, linking the debt issue to other struggles allows for the construction of a wider base for support. A wide support base is important when a campaign resolves to take on-the-ground action such as protests or the occupation of strategic locations. Second, linking different struggles allows advocacy campaigns to draw lessons from each other, especially if the individuals in these campaigns work closely together. Third, the issue of parliamentary approval of loans can sometimes seem foreign compared to more tangible struggles around the provision of public services or the climate transition. Linking these different struggles makes explicit the importance that loans, especially from IFIs, can have on the lived reality of the general public.

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4. Background Paper on Kenya's Debt Situation

Background Paper on Kenya's Debt Situation 2014-2024

by Kwame Owino & Betty Wainaina

Legislative initiatives

Public Debt in Kenya is managed under the guidance of several legislative and legal instruments. These include the Constitution of Kenya 2010; the Public Financial Management Act (PFMA) 2012, with the most recent amendment of 2023; the PFM National Government Regulations (PFM NGR) 2015 amended in 2018; the Public Debt and Borrowing Policy (PDBP) 2020; the annual Medium-Term Debt Management Strategy (MTDMS); and the annual Budget Policy Statement (BPS). Public debt constitutes debt incurred by national and county governments and their respective entities.

The Constitution of Kenya 2010[1] provides the overarching framework for public debt in Kenya. This is further expounded in the PFMA 2012. Article 201 states that there shall be openness and accountability, including public participation in financial matters. Article 211 gives Parliament the powers through legislation to prescribe the terms on which the national government may borrow and impose reporting requirements. Parliament by resolution can request the Cabinet Secretary responsible for the National Treasury (CSNT) to present information on any loan or guarantee, and this information should be submitted within seven days. This information should be able to explain the level of indebtedness, the use the loan has been put to, the plan for repayment and the progress made towards repayment[2]. Article 212 allows county governments to also borrow if the national government guarantees the loan and there is approval by the County Government Assembly (CGA). The CGA is responsible every year for setting the level of debt as a per centage of the county revenue.

According to the PFMA (Kenya Law Reports 2012)[3] the National Treasury is responsible for managing the level and composition of the national public debt and national public guarantees and is responsible for enforcing the principle of managing debt and financial obligations at sustainable levels, with the approval of Parliament. The act stipulates that borrowing in the medium term shall be used only for financing development expenditures and not for financing recurrent expenditures, and that the National Treasury shall ensure that public debt does not exceed the amount specified in the annual MTDMS.

The National Treasury prepares through a consultative process the BPS which is submitted to Parliament by February 15th each year. The lim-

1 https://kenyalaw.org/kl/fileadmin/pdfdownloads/TheConstitutionOfKenya.pdf
2 https://repository.kippra.or.ke/bitstream/handle/123456789/1857/2019%20Debt%20Policy%20and%20Borrowing%20Framework.pdf?sequence=1&isAllowed=y
3 https://www.worldbank.org/content/dam/Worldbank/document/Africa/Kenya/Kenay%20Devolution/Public%20Finance%20Management%20Act%20%282012%29.pdf

its on total annual debt are also included in the BPS. This is tabled and discussed in Parliament and within 14 days Parliament passes a report that adopts the BPS with or without amendments. Treasury, in preparing the annual budget, gives due consideration to the recommendations of this report and is required to submit a memorandum explaining how the resolution was considered. The MTDS is also submitted to Parliament at this time. This submission includes information on: the total stock of debt at the time of the BPS; the sources of loans and the nature of guarantees given by the national government; the principal risks; the assumptions of the strategy; and an analysis of the sustainability of the amount of debt, both actual and potential. Within 14 days of submitting the strategy it is submitted to the Commission on Revenue Allocation and the Intergovernmental Budget and Economic Council, and is made public. The act also provides that at the end of every four months the CSNT is required to submit to Parliament a report of all loans made to the national government, national government entities and county governments. Treasury submits the budget estimates to the National Assembly (KNA) by 30th April, when these are also made public. In addition, they also submit a budget summary, which contains a summary of budget policies including policies on revenue, expenditure, debt and deficit financing, including information on all loans and guarantees. The KNA considers the estimates with a view to approving them with or without amendments and is guided by the BPS in this process.

Treasury can also guarantee loans by public entities, county governments or even private individuals. The draft loan guarantee documents are first approved by Parliament before the guarantee can be affected.

Section 66 of PFMA establishes the Public Debt Management Office (PDMO). The objective of this office is to minimise the cost of public debt management and borrowing over the long term, taking account of risk; to promote the development of market institutions for Government debt securities; and to ensure the sharing of the benefits and costs of public debt between current and future generations. The head of PDMO makes operational decisions on borrowing and debt management by delegation from the CSNT. The CSNT is accountable to Parliament for the work of the PDMO.

In accordance with section 80 of PFMA, the NT prepares comprehensive annual financial statements at the end of the financial year. These include a statement of the total amount of national public debt that is outstanding. These statements are submitted to the auditor general no later than four months after the end of the financial year. According to the PFM NGR 2015 (Government of Kenya 2015)[4], a public debt incurred by the national government shall be a first charge on the Consolidated Fund and the County Revenue Fund. This is done to ensure that the government does not default on its debt obligations.

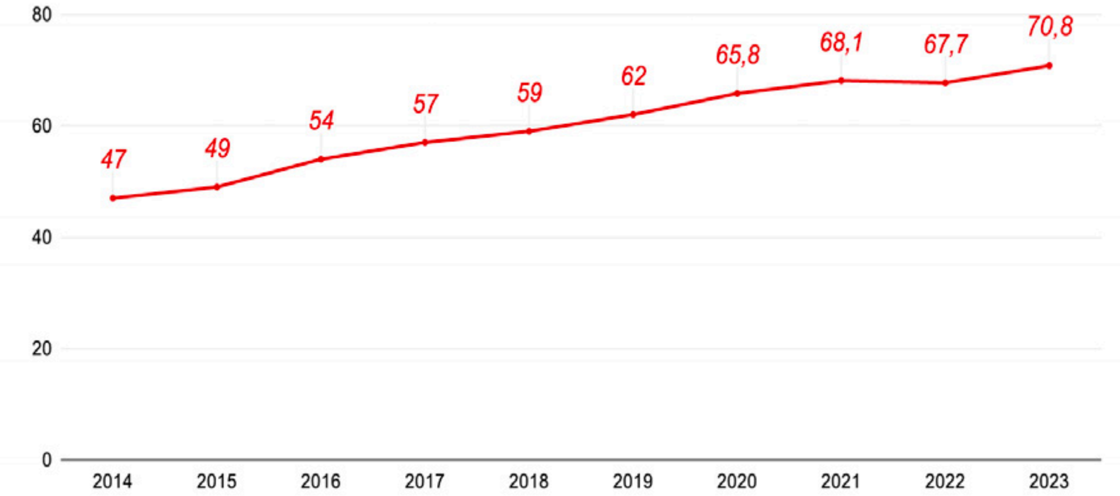
In accordance with section 64 of the PFMA, and further elaborated in the PFM NGR 2015, the National Treasury publishes and submits to Parliament an annual Public Debt Management Report (PDMR)[5] no later than three months after the end of the financial year. The Report covers the legal framework underpinning public debt management; the level of public and publicly guaranteed debt; the borrowing and debt service obligations; the outlook for the medium term; implementation of the MTDS; the Debt Sustainability Analysis (DSA); and public debt management reforms. This report is also made publicly available.

In summary, the Constitution and the relevant legislation and policies have made substantive provision for the role of Parliament in public debt management, including: enacting the laws

4 https://s3-eu-west-1.amazonaws.com/s3.sourceafrica.net/documents/119214/Public-Finance-Management-Act.pdf
5 https://www.treasury.go.ke/wp-content/uploads/2024/01/Annual-Public-Debt-Report-2022-2023-Sept-2023.pdf

Figure 1

Debt % of GDP



Source GOK Economic Survey GOK

governing public debt management; approving annual Government borrowing; approving the annual debt ceiling; approving guarantees to county governments and other public investments; and authorising payment of debt out of the Consolidated Fund (CF) or any other public fund. Further, these instruments provide for a framework for public participation in financial matters in which debt management is concerned. However, despite this institutional arrangement, the oversight on debt management is not as effective as is envisioned on paper. This is evidenced by the rate at which the national public debt has been growing and by the disgruntled public discourse that has surrounded it.

According to the annual PDMR 2023 and the MTDS 2024, at end-June 2023 the public debt stock had increased to 10.3 trillion Kenyan Shillings (70.8 per cent of GDP and equivalent to 71.8 billion US dollars) from 8.6 trillion Kenyan Shillings in June 2022. Figure 1 below shows this growth since 2014. This comprised 52 per cent external debt and 48 per cent domestic debt. External debt constitutes multilateral debt at 48.6 per cent, commercial debt including international sovereign bonds at 26.4 per cent and bilateral debt at 26.4 per cent. The largest of that debt is from the World Bank IDA and IBRD at 1.7 trillion Kenyan Shillings (12.3 billion US dollars). The main multilateral lenders comprise the International Development Association (IDA), the International Bank for Reconstruction and Development (IBRD), the African Development Bank (ADB), the African Development Fund (ADF) and the International Monetary Fund (IMF), while dominant bilateral lenders include China, France and Japan as at end-June 2023. With regard to domestic debt, Treasury bonds constituted 83.1 per cent and Treasury bills 12.7 per cent of the total domestic debt.

One of the issues that has contributed to this exponential increase has been the process of setting debt limits. According to the PFM NGR 2015, one of the fiscal responsibility principles is that the national public debt shall not exceed 50 per cent of GDP in net present value (NPV) terms. In addition to this debt limit, Parliament sets the annual thresholds for the annual borrowing by the national and county governments and their entities. This debt ceiling has been raised six times since 2013. In 2019, because the government had broken the ceiling limit, parliament amended the PFMA to change the debt limit to numerical figure of 9 trillion Kenyan Shillings[6] (Muiruri 2019). This was to allow the government room for additional borrowing. The government has continued to exceed these limits again and again in subsequent years. As recently as 2023, the stock of debt as we have shown in this paper was above the debt ceiling of 10 trillion Kenyan Shillings. Parliament in 2023 approved an amendment to the PFMA 2012 converting the standard used from a nominal number to a debt anchor as a per centage of GDP. The new threshold is now 55 per cent of GDP with a 5 per cent window for expansion[7] (The African Sovereign Debt Justice Network 2023). They also deleted the clause in the act that required the CSNT to report to Parliament if the NT breached the debt anchor through excessive borrowing. The amendment[8] (Republic of Kenya 2022) now allows the government to exceed the limit under certain circumstances. These circumstances include depreciation of the Kenyan Shilling, material balance of payments imbalances, or fiscal disruptions caused by wars, health pandemics or national disasters (Mutai 2023)[9]. These amendments to strict procedure raise fundamental questions relating to how committed the organs of government, both the executive and the legislature, are to the principles of public financial management, in particular regarding questions of debt sustainability.

Kenya is assessed as a medium performer in terms of Debt Carrying Capacity (DCC), with an estimated Composite Indicator (CI)[10] of 2.98. The downgrade from Strong to Medium performer means it will be assessed based on lower debt sustainability thresholds for external debt and benchmarks for total public debt. The table below shows the proposed threshold versus the ac-

Table 1

Measure	Threshold	2023 Actual	2024 Projected
External debt as % of exports	180	256	
External Debt as % of GDP	40	31.7	
External Debt service as % of exports	15	24.9	36
External Debt service as % of revenue	18	17.3	28.5
Total public debt as a % of GDP	55	70.8	
Total public debt as % of grants and revenue		380	
Total public debt servicing as % of revenue and grants		55.2	68.9

6 https://www.citizen.digital/business/senate-votes-to-raise-kenyas-borrowing-ceiling-to-ksh-9-trillion-292552/
7 https://www.afronomicslaw.org/index.php/category/african-sovereign-debt-justice-network-afsdjn/ninety-fourth-sovereign-debt-news-update
8 http://www.parliament.go.ke/sites/default/files/2022-04/The%20Public%20Finance%20Management%20%28Amendment%29%20Bill%2C%202022.pdf

tual values. The government finds itself in a very difficult situation, with total debt service as a per centage of ordinary revenue being 58.8 per cent. This situation is worsening in the short term.

Successful Experiences and Practices

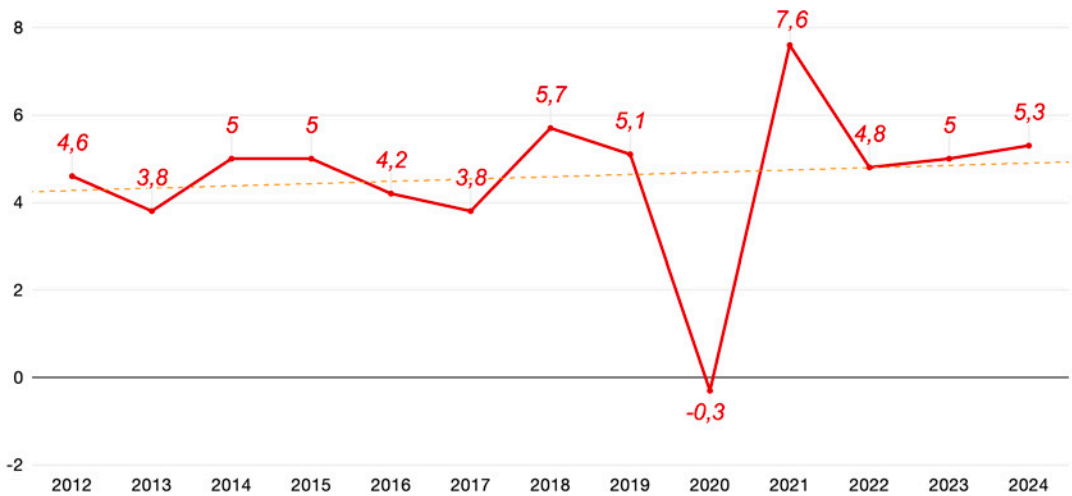
Economic growth in Kenya was severely depressed by the emergence of the Covid-19 pandemic in early 2020. The result of this was that Kenya's GDP fell by 0.3%, meaning that the economy shrunk by a small amount. The effect of this was that the government of Kenya could not secure or generate revenues to support a large fiscal stimulus, as happened in other parts of the world. Chart 1 shows the trend line in the growth of annual output in Kenya in the decade in which growth of public debt as a share of GDP grew the fastest. The shock in output growth that resulted from the Covid-19 pandemic did not last, as shown by the large recovery that followed it.

In the quest to ensure that there was relief to firms and households, the government of Kenya initiated a fiscal stimulus in the form of tax cuts. Specifically, the government passed laws to reduce the marginal tax rate for personal income tax to 25 per cent from 30 per cent. Regarding corporations, the law allowed for the reduction of the corporate tax to 25 per cent. This provided relief to Kenyan households and firms while the pandemic was still raging and as Kenya tried to secure access to vaccines. This reduction in tax rates prevented the devastation of the economy and caused a modest reduction in tax revenue collections.

In spite of the large output growth that occurred

Figure 2

Kenya's Economic Growth



Source: KNBS, 2024; IMF forecast

9 https://nation.africa/kenya/business/kenya-s-debt-ceiling-now-anchored-to-gdp-as-sh10trn-cap-scrapped-4280480
10 The CI captures the impact of various factors through a weighted average of an institutional indicator (measured by the World Bank's Cou

in 2021, the public-sector finances in Kenya were already showing considerable strain. This strain was shown by the fact that employment rates had fallen and not recovered and the drought continued to afflict most Kenyan households for whom agriculture provides the main form of sustenance. The obligations for debt repayment as a proportion of the revenues were growing.

IMF programme

Faced with the fact that the maturity of debts could not be shifted at the time, while revenue growth did not match it, Kenya's government formally entered a programme with the International Monetary Fund in April 2021. The commencement of this support enabled Kenya to have access to Extended Credit Facility (ECF) and Extended Economic Facility (EEF) for an initial period of 38 months. According to the report, the programme was made necessary by the fact that Kenya faced risk of debt distress on account of the Covid-19 and that this "exacerbated existing debt vulnerabilities". To the extent that the assessment of Kenya's authorities was that this shock was real but temporary, the entry into a formal IMF programme to access credit facilities that would support macroeconomic stability was the correct decision.

Ring-fencing Social Spending

While the government of Kenya was implementing the programme, Kenya's debt distress position did not get better. The commitments under the agreed programme required policy commitments to undertake a set of changes to restore growth and stability for the Kenyan economy. Underlying the changes in the patterns and quantum of expenditures were requirements to protect spending in key sectors and social services. The government committed itself to reduce expenditure but to preserve spending on health services, education and social protection.

Monetary Policy Adjustments

It became increasingly clear that as bullet payments for commercial creditors would come due mainly in 2024 and 2025, the real opportunity for access to financial markets would be critical for debt default to be avoided. At the same time, Kenya faced pressures from external shocks in the form of rising inflation from the adjustments in economies that had undertaken huge fiscal stimulus. In addition, the government of Russia started a war by invading Ukraine and the war reduced exports of cereals from the two countries. This raised the price of food in Kenya, which is an importer of cereals and food products from Ukraine and Russia. With limited scope for expanding Kenya's deficit, the government used monetary policy instruments to manage inflation arising from price rises of non-food items and to restore balance.

Debt Refinancing

Towards the end of 2023, the Kenyan Shilling started to face pressure for depreciation owing to the decision by the US Federal Reserve Bank to raise interest rates to unprecedented heights. This created pressure on the Kenyan Shilling at an inopportune time because global financial markets were frozen due to the pressures facing developed countries. The consequence of this depreciation is that Kenya's public debt that is denominated in foreign currency would rise in comparison to its amount denominated in Kenyan Shillings. This timing of rapid depreciation of the Kenyan Shilling was disadvantageously timed, as a bullet payment of 2 billion US dollars was due in June 2024. The government of Kenya resorted to a refinancing of the debt in February 2024 and received 1.5 billion US dollars for this, thereby ensuring that no default would happen in 2024.

Freeze on Hiring Staff

Kenya's season of debt distress has not abated by June 2024, in spite of the fact that a default has been avoided in the medium term. The government of Kenya is undertaking a fiscal consolidation plan which requires raising more revenue while also prioritising spending on care services. In 2023, the cost of staff expenditure in Kenya is equivalent to 45 per cent of all public spending. Thus, the cost of labour is the largest single largest cost centre. While public labour services are critical for service delivery, the need to balance budgets requires a freeze or reduction in the pace of new employment until the fiscal position improves. The Cabinet Secretary for Finance stated in the budget statement to Parliament that the public service will freeze any new hires except for teachers and medical interns for the whole of the financial year starting in July 2024.

Unintended consequences

In response to the fact that debt repayments have been equivalent to a large and growing share of government revenue during the past decade, Kenya has instituted measures of fiscal consolidation and other reforms. Many of these reforms were stated as targets in the programme with the IMF that has been referred to above. The Kenya Economic Update June 2024 states that the Government of Kenya has kept to a fiscal consolidation path by raising revenues and tightening non-priority expenditures. While this fiscal consolidation programme was agreed upon, it required steep rises in tax rates together with reductions in other spending. The combined effect of these measures generated unintended consequences of varying degrees of severity.

(a) Reduction in Social Spending

The first unintended consequence was that the government of Kenya maintained nominal spending for the basic education sector, but real investment in education has been lower because inflation for the calendar year 2023 has been at 7.7 per cent (Republic of Kenya 2024). Government spending on basic education in 2024 was lower in real terms in spite of the fact that the nominal spending did not change. The implication of this is that the share of public spending dedicated to core public services has been reduced.

(b) Refinancing at Steep Rates

The pressure to defer or avoid any default on the national debt at a time when revenue collections were near their peak while currency depreciation was unfolding was unbearable. It is evident that international markets could not reopen soon enough for the government of Kenya. As a consequence of the fall in the Sovereign Credit rating for Kenya in October 2024, the probability of Kenya's default was elevated and the pressure on the Kenyan Shilling intensified. The evidence for this pressure was displayed by the deep discounting of Kenya's Eurobonds, revealing the fact that investors understood the difficulty. As a result, Kenya successfully negotiated and completed a refinancing transaction for 1.5 billion US dollars in February 2024. Announcement of this transaction gave confidence that the default would not happen in 2024 but came a steep coupon rate of 10 per cent.

(c) Instability and Social Unrest

When the Finance Bill for 2024 was issued, it was debated in the public through public participation events that were hosted by the Finance Committee of Kenya's Parliament. These routine processes of public participation led to the presentation of up to 900 petitions addressing various facets of the law. Although the Finance Committee made small but insignificant concessions, the public clamour for the rejection of the entire law rose. On 25 June 2024, Kenya's protesting youth marched throughout many urban areas towards government offices to protest the final debate on the Finance Bill 2024.

As live transmission of the passage of the law was proceeding, a small number of protesters entered the parliamentary grounds in Nairobi and disrupted the proceedings of Parliament. The extreme reaction of the National Police Service (NPS) led to shootings in Nairobi that led to the reported deaths of 26 protesters and injuries to more than 100 citizens. This led to a chaotic period of a fortnight during which the follow-up demonstrations, which were intended to be peaceful, were infiltrated by criminals and gangs and this led to further injuries, death and damage of business premises in the main urban centres in Kenya. Later, on 26 June, the President of Kenya announced that he would not provide assent to the Finance Bill 2024 in spite of Parliament's passage of the bill and advised that the National Assembly's Committee on Finance should delete it in its entirety.

Recommendations

Kenya's debt management process is enshrined in a fairly robust legislative and institutional framework. Parliamentary oversight and public participation are key features of the instruments that govern the process. What has become very evident, however, is that in a presidential system such as Kenya's, parliamentary oversight is compromised when the ruling government has a majority in Parliament. Legislators see their role as that of facilitating the implementation of the government agenda, and use their role to support the government rather than to keep it in check. A second issue is that the KNA has a big conflict of interest in budgetary matters. Members of Parliament (MPs) are allocated 2.5 per cent of the total budget in what is known as the National Government Constituency Development Fund (NGCDF). The MP is the patron of the respective constituency development committee that oversees the use of these resources. MPs, irrespective of party, have an adverse incentive to approve a high budget, as this will increase their allocations. Having approved a budget they can then not contest the means of financing that budget. In such a situation therefore, public participation needs to be enhanced. Whilst public participation is embedded in the PFM process, matters relating to debt only come to the fore when there is a crisis. Requiring public engagement on the medium-term debt management strategy could ensure these issues get public attention before the fact.

Secondly, the Parliamentary Budget Office plays a critical role in advising the legislature on PFM matters, including debt. Strengthening the PBO and requiring the PBO to also undertake public engagement on PFM matters would enable public participation to take place in a more robust fashion.

It has been argued in this paper that the procurement of expensive debt and its deterioration into debt distress is not the result of absence of institutions, processes or laws. It attributes the present condition of Kenya to a dysfunctional political economy.

(I). Therefore, the fixes to this issue cannot be confined to technical solutions alone. Instead, the effect of the solutions must be to nudge the legislature towards greater vigilance and independent action to restore balance to the dysfunctional oversight of public debt.

In Kenya it is necessary to conduct a more objective review of the effects of proposed borrowing choices, duration and terms. The historical review of the decade from 2014 shows that the existing mechanism within Parliament for examination of the debt portfolio and approvals of debt instruments and their deployment are suboptimal. The express requirement is for Parliament to form a standing and joint committee of both the National Assembly and the Senate. The specific obligation of this committee is to exercise constant and independent oversight of the proposals for borrowing and to have regular interface with the National Treasury in monitoring net instruments throughout the cycle from procurement to ultimate repayment.

(ii) Kenya's debt management strategy is in the custody of the National Treasury and this means that the debt management office is situated within the same organisation. With the clear objective of separating out the tight control of debt information by the National Treasury, Kenya's

Parliament should amend the Public Finance Management law to provide complete operational and financial autonomy to the Debt Management Office. The direct implication of this is that the Directorate of Debt Management will cease to be an office under the Cabinet Secretary for the Treasury and become instead a custodian and reference point for debt records, contract documents and payment schedules. By separating out the custody of the records and management of payments from the National Treasury, the accountability cycle would be improved because the Treasury would be unable to obfuscate the records in terms of the terms of debt and the profile of the creditors.

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5. Background Paper on Ghana

Background Paper on Ghana

by Kwabena Nyarko Otoo

Introduction

In 2022, Ghana officially defaulted on its debts and the country embarked on a debt exchange programme. Excessive expenditures, excessive borrowing and the failure of revenue policies have all contributed to this situation. Given the low revenue base, national investments in health, education and infrastructure in the last four decades have been accomplished through massive borrowing. At the end of 2022, total public debt (broadly defined) was more than 100 per cent of GDP. Ghana is now devoting more than half of its tax revenues in servicing debts, leaving practically nothing for investments in the sectors that can spur growth and development[1].

The country lost access to the international bond market towards the end of 2021 after series of downgrades by the ratings agencies. With no access to the external bond market and facing large fiscal deficits, the Bank of Ghana picked up the bill leading to rising inflation[2] and large currency depreciation. In the last two years, the national currency, the cedi (Ghanaian Cedi) has lost more than half of its value.

In July 2022, the Government of Ghana asked the International Monetary Fund (IMF) for a bailout, marking the 17th time Ghana has had to seek refuge in the IMF. The country was compelled to undertake extensive debt restructuring including, for the first time, restructuring of domestic debts. The domestic debts exchange was largely successful imposing a hefty 61 billion Ghanaian Cedi (5.1 billion US dollar) losses on bondholders. And in June 2024, external bondholders and bilateral creditors have agreed to sizable haircut of 8 billion US dollars and 2.5 billion US dollars respectively. The combined effect of the domestic and external restructurings is that Ghana now has significant fiscal breathing space to pursue economic growth and poverty reduction.

But the country has been here before. In 2006, in the framework of the Heavily Indebted Poor Country (HIPC), the Multilateral Debt Relief Initiative (MDRI) delivered substantial cancellation of Ghana's debt. In fact, the external debt stock of the Ghanaian government fell from 6.6 billion US dollars in 2003 to 2.3 billion US dollars by 2006. The ratio of total debt to Gross Domestic Product (GDP) fell sharply from 182 per cent in 2000 to 32 per cent in 2006.

The country exited the IMF programme having achieved significant fiscal space for investment in poverty reduction and economic growth. But

1 Debt servicing is now the number one expenditure item for the government, surpassing the combined expenditure on education and health.
2 Inflation closed at more than 54 per cent in 2023.

large-scale lending and borrowings resumed following the discovery of oil and high commodity prices. By 2013, the country was borrowing to pay interest on previous debts, leading to increases in the overall size of its debts. The practice of borrowing to pay interests on previous debts continued up to December 2021, when the country could no longer borrow on the international bond market sparking off official default and its 17th trip to the IMF for a bailout.

The underlying causes of the perennial debt build-up have not been addressed. This short report seeks to address the root causes of the debt build up in Ghana. It does so from a legislative perspective, looking at how law can be used to curb the build-up foreign-currency-denominated debts in Ghana.

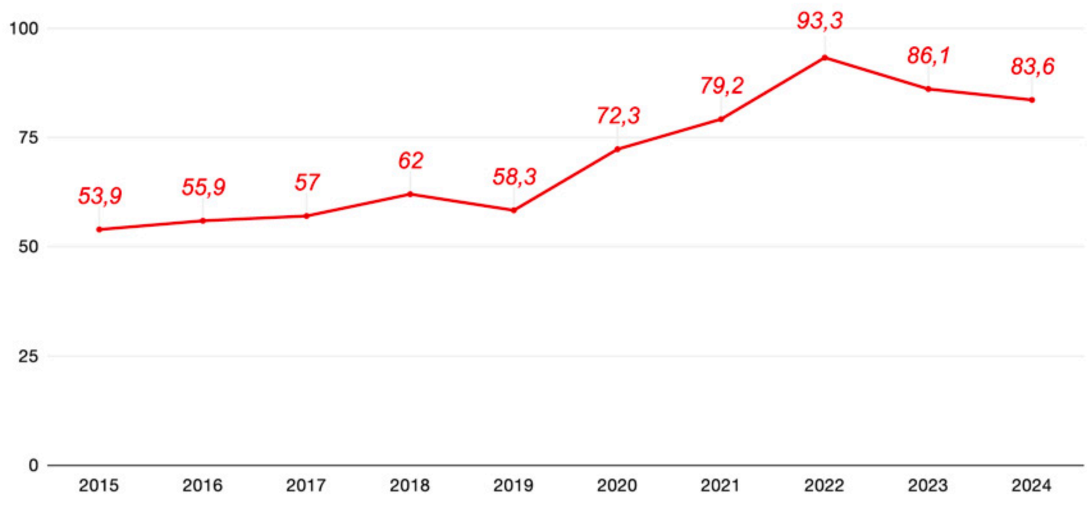
Background

By current standards, Ghana at independence was a middle-income country. Macroeconomic indicators showed a very stable economy with hardly any inflationary pressures (Frimpong-Ansah 1991). Gross international reserves were impressive. The country had no public debt record at independence. With a relatively high per capita GDP, well-functioning public administration, sound budgetary situation and virtually no balance of payment constraints, the country hit the path to 'modernisation' with a clean bill of health (Killick 2010).

With a desire for rapid modernisation, the country moved away from surplus budgets to debt financing and gradual accumulation of debts. By 1965, Ghana's public debt stood at 25 per cent of GDP (Musah 2023). Since then, the country has run a budget deficit right to the present day. In 2001, Ghana was classified as a "Heavily Indebted Poor Country" (HIPC) as a result of the high debt levels. The International Monetary Fund (IMF) and World Bank wrote off large portions of the country's debts (ibid). The country's public debt then fell from 182 per cent of GDP in 2000 to 32 per cent of GDP in 2008 (Hilton 2021).

Figure 1

General government gross debt (Per cent of GDP)



Source: Adapted from IMF

Figure 1 shows that public debt in Ghana has been above 53.9 per cent of GDP since 2015, peaking at 93.3 per cent in 2022. The sharp rise

In the public debt stock has been linked to COVID-induced spending and the disruptions to global trade from the Russia–Ukraine war (Akolgo 2023). Undoubtedly, the COVID-19 pandemic.

It is equally true that before the pandemic and the advent of the Russia–Ukraine war, the signs of a country heading into a debt crisis were visible in Ghana. As illustrated by Figure 1, public debt-to-GDP was 62 per cent in 2018 a year prior to the outbreaks of the COVID 19 pan demic and the Russia-Ukraine war. The acute debt crisis the country experienced in 2022 was the result of COVID-induced external shocks intensifying pre-existing debt vulnerabilities.

The Government of Ghana has been complicit in the creation of the debt burden and debt sustainability crisis in the country (Saani et. al. 2024; Akolgo 2023; Amankwah et. al. 2018). Spending and borrowings have been excessive as the country struggles to fix its infrastructure and extend public service in the areas of education and health. But revenue policies have not been as effective as to enable domestic revenue mobilisation to match national expenditures. The recourse to borrowings has fueled a debt binge over many years that ultimately resulted in the debt crisis.

A United Nations Development Programme (UNDP) paper argues that Ghana's fiscal and debt sustainability has been eroded by rising government spending in the context of continuously low domestic resource mobilisation (UNDP 2023).

Many reasons account for the large-scale borrowings and the resulting debt build-up. Ghana, like many other countries in Africa, is faced with monumental deficits in infrastructure. For example, there is great need to expand education and healthcare facilities. Road infrastructure is bad and deteriorating. The desire to fix these challenges and expand public services has been growing[3]. There is an equally strong desire by government to respond to the clamour to uplift national infrastructure. After all, investments in roads, railways, healthcare and education are necessary for broad-based growth.

However, domestic resource mobilisation has been weak, lagging behind the desire to expand infrastructure and the cost associated with it. The country collects just about 15 per cent of GDP in taxes, significantly underperforming its peers in Sub-Saharan Africa region. The tax-GDP ratio in Ghana is among the lowest in West Africa despite having the second-largest economy in the sub-region. Therefore, the moderate expansion in infrastructure, education and health that the country has achieved has only been made possible by borrowing. The country has always borrowed externally to fund the growing revenue-expenditure gap.

High national expenditures and low revenues also reflect inefficiencies in public finance management. Corruption plays a key role. It embellishes national expenditures and diminishes national revenues. Government continues to procure at far higher costs than the private sector. The tax system is plagued by loopholes and exemptions. Non-transparent granting of tax exemptions decreases revenues. The IMF estimates that VAT and customs exemptions are at 4 per cent of GDP. The result is a perpetual budget deficit and recourse to borrowings to finance embellished expenditures.

Legislative Initiatives on National Debts

The National Constitution and debt management

Ghana has substantial laws and regulations for public debt management. At the apex of this

3 The young population is demanding good roads, quality education and healthcare, internet connectivity and a general expansion of public services.

framework is the 1992 Constitution, which gives general guidelines for loan procurement and management. Article 181(3) specifies that "no loan shall be raised by the Government on behalf of itself or any other public institution or authority otherwise than by or under the authority of an Act of Parliament". The 1992 Constitution further clarifies that a "loan" includes any moneys lent or given to or by the Government on condition of return or repayment, and any other form of borrowing or lending in respect of which:

> *(a) moneys from the Consolidated Fund or any other public fund may be used for payment or repayment; or*
> *(b) moneys from any fund by whatever name called, established for the purposes of payment or repayment whether directly or indirectly, may be used for payment or repayment.*

The Constitution, however, places no limit on government's ability to contract loans. Parliamentary approval for external loans is required but Parliament rarely withholds such approvals. The approval process fails to account for the growth of public debt. The focus has tended to be on the economic and social benefits of the project the loan is intended to finance. But in the background lurk political gains by the ruling party. In recent years, the Ministries Departments and Agencies (MDAs) were allowed the fiscal room to undertake large extra-budgetary spending that commit government with no oversight by central government and Parliament. This has made it difficult to correctly estimate the size of the public debts.

During the life of the Constitution, the debt-to-GDP ratio increased to 182 per cent in 2000 before coming down to 32 per cent in 2006 following the MDRI mentioned earlier. Therefore, the Constitution on its own has very few safeguards for limiting borrowing and the accumulation of national debts.

In 2016, government adopted the Public Financial Management Act, 2016 (Act 921). The Act seeks to among others, ensure that "public funds are sustainable and consistent with the level of public debt". Act 921 establishes the Public Debt Management Office, stipulates rules for government borrowing and debt management, borrowing purposes, debt management objectives and debt management strategy. It also covers issuance of government debt securities in the domestic debt market, issuance of government debt securities abroad, and borrowing from banks and other financial institutions.

However, the Public Financial Management Law also fails to place any quantitative limit on the government borrowings and debt accumulation. The debt management objective of the law is focused primarily on meeting "the financing needs of government.... on a timely basis (see Section 58). This stands in sharp contrast to the PFM Act of the Kingdom of Tonga, which places a quantitative limit on government's borrowing in any financial year. In the year that Ghana adopted its PFM law, the debt-GDP ratio increased by nearly three per centage points.

In 2018, the country adopted the Financial Responsibility Act (FRA), 2018 (Act 982), a new law that was intended to curb budget deficits, borrowings and the accumulation of debts. The law aims to promote fiscal discipline and ensure debt sustainability by legislating it. It establishes rules and limitations, encourages efficient spending and resource allocation with a focus on responsible budgeting that prioritises essential services and infrastructure development, and sustainable economic growth.

Key provisions of the law include a ceiling on the fiscal deficit, a cap on debt accumulation, transparency and accountability rules, flexibility rules and the establishment of Fiscal Responsibility Advisory Council (FRAC). The law requires that overall fiscal balance on cash basis for a particular year shall not exceed a deficit of 5 per cent of the Gross Domestic Product (GDP) for that year. For transparency and accountability, the law mandates regular reporting on fiscal performance and requires the government to publish detailed information on public finances. The law further established the Fiscal Responsibility Advisory Council to monitor adherence to the fiscal rules.

An independent body, the Fiscal Responsibility Advisory Council, was established to monitor the government's adherence to the fiscal rules. The council was expected to provide regular reports and recommendations to facilitate compliance and transparency.

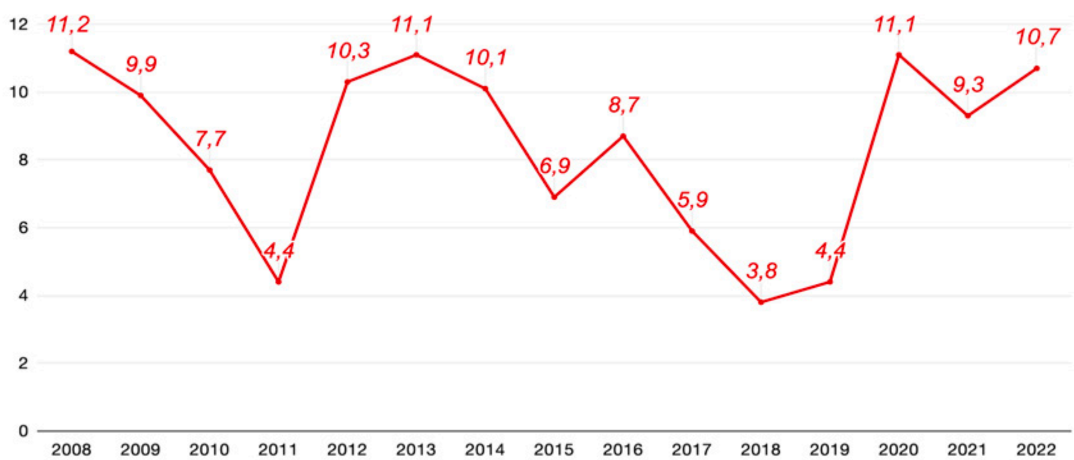
Despite setting limits on the deficits and debts, the law also made room for a level of flexibility that allows government to temporarily breach the limits in exceptional circumstances such as extraordinary economic crisis or natural disasters[4]. And this is what happened in 2020 following the outbreak of the COVID-19 pandemic and the difficult economic challenge it presented to the country.

Following the passage of the Fiscal Responsibility law, Ghana's fiscal deficit dropped from 5.9 per cent of GDP in 2017 to 3.8 per cent in 2018. In 2019, the deficit was 4.4 per cent. In the 10 years before the law (2008-2017), the fiscal deficit averaged 8.6 per cent. In 2020, the law was suspended allowing government to take extraordinary fiscal measures to combat the pandemic. The deficit ballooned to 11.1 per cent in 2020.

The adherence to the fiscal deficit ceiling did not prevent the accumulation of debts. In 2017, gross public debt had more than doubled to 57 per cent of GDP. And in 2018, the year the FRA was adopted, public debt went up to 62 per cent of GDP. By 2022, public debt was more than 93 per cent of GDP. The suspension of the FRA partly explains the steep jump in public debts. But even before the suspension of the FRA, the momentum for debt accumulation was evident. A joint World Bank-IMF Debt Sustainability Analysis in December 2019 revealed that the risk of external debt distress and overall risk of debt distress were high (World Bank and IMF 2019).

Figure 2

Fiscal Deficits (% of GDP) (2008 – 2022)



Source: Ministry of Finance, 2024

4 This is subject to parliamentary approval and a clear plan for returning to compliance.

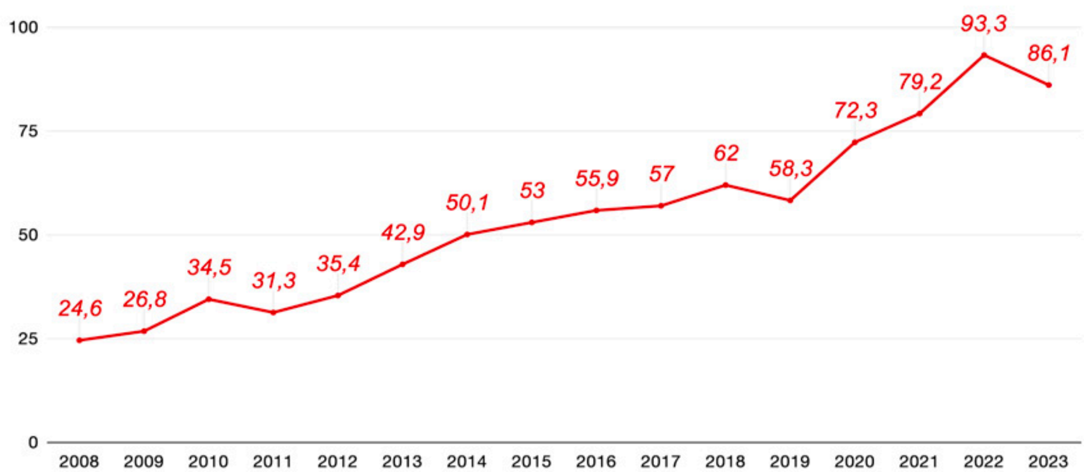
In fact, the fiscal responsibility law sets only one quantitative target that limits the fiscal deficit to no more than 5 per cent of GDP. The fiscal rule also incorporates the attainment of a positive primary balance. It then assumes that a limit on deficit will translate into a limit on debt procurement. This did not happen. Therefore, the implementation of the FRA went along with increases in the public debts.

The FRA failed to curb government's appetite and ability to contract loans for investments in infrastructure, social programs, and recurrent expenditures. A significant part of these expenditures was undertaken by MDAs as extra-budgetary expenditures and commitments. Interestingly, the suspension of the FRA in 2020 coincided with the Presidential and Parliamentary elections of that year. And as we have come know it, a remarkable feature of Ghana's fiscal trajectory is the tendency for deficits and debts to spike in election years. It is difficult to distinguish between COVID-related expenditures and elections-related ones following the suspension of the FRA.

An important measure to curb the deficits and limit debt levels occurred on the revenue side of government budget. And that involved the adoption of the Tax Exemptions Act. The IMF estimates that tax exemptions cost Ghana 4 per cent of GDP in tax revenues. These revenue giveaways have implications for fiscal deficits and debts accumulation. In 2022, government passed the Exemption Act to (a) rationalise the current exemptions regime by varying, where necessary, and consolidating existing statutory provisions on exemptions; and (b) provide for the administration of exemptions. Government also adopted Administrative Guidelines for the implementation of the Tax Exemptions Act.

Figure 3

Gross Government Debt (% of GDP) (2008-2023)



Source: IMF, 2024

However, the Exemption Act faces several constraints. First, it is not clear as to the real object of the Act. Rationalising the current exemptions regime is too generic. The wording of the Act gives no comfort that the beneficiaries of the existing exemptions will forfeit those exemptions, allowing government to acquire revenues. Second, the Act appears silent on the natural resource sector, where exemptions are prevalent, thus depriving the state of significant revenues. While that Act makes the bold claim that "it applies to all exemptions", it does not say how the Act will address the "fiscal stability rules" enshrined in Ghana's mining leases. Finally, and flowing from the above, since its passage not much has been heard about the Act in terms of actual implementation.

Dealing with the current Debt Crisis

It is evident that the various pieces of legislation adopted in the past have failed to stop the accumulation of debts and the current bouts of crisis. These laws failed to set a debt target. In the past two years, the focus has been on getting the country out of the debt crisis through debt restructuring. Last year the domestic debt component was successfully restructured saving the country up 5 billion US dollars. This year, the external debt component has also been successfully restructured adding another 10.5 billion US dollars of debt forgiveness.

In the past these reliefs afforded the country fiscal space to invest in economic and social infrastructure and growth. But a borrowing spree began a year or two thereafter. Ghana issued its first Eurobond in 2007, one year after the MDRI, which cancelled more than half of its external debts. History can repeat itself. The country continues to face a significant resource gap as it seeks to improve infrastructure and extend public services. Revenues continue to underperform. And demands for government provisioning remain high. In an electoral democracy, the pressure on the political leadership is immense. Undoubtedly, Ghana will continue to borrow. What is needed are tighter rules to ensure responsible borrowing, including more efficient use of borrowed money.

The current phase of the IMF programme incorporates changes to the Bank of Ghana (BoG) Act to limit monetary financing of the budget and to clearly define emergency situations that could trigger suspension of the limit. In the interim before changes are made to the law, the BoG and Ministry of Finance are compelled to sign a Memorandum of Understanding to purge BoG financing of the budget.

The IMF programme further seeks to amend the FRA as part of measures to enshrine fiscal discipline. The proposed amendment will add a debt target to the fiscal rule as well as expanding coverage of the rule to control extra budgetary spending. A reform of the Fiscal Advisory Council is also envisaged under the programme. The idea is to reinforce credibility of the Council and ensure effective implementation and enforcement of the fiscal rule.

There is also a proposal to add another fiscal rule to the FRA, which will that in any fiscal year budgeted expenditure does not exceed 105 per cent of the previous year's tax revenue. *The idea is to avoid a situation where budgetary expenditures are derived from overly optimistic revenue projections* (Bawumia 2024)[5]. This remains a promise by the presidential candidate of the ruling party.

Recommendations

What is to be done to free Ghana from its development financing quagmire? The popular sug-

5 https://www.graphic.com.gh/news/politics/dr-bawumia-advocates-for-fiscal-discipline-proposes-stricter-amendments-to-fiscal-responsibility-act.html

gestion is that Ghana must limit debt accumulation, particularly accumulation of foreign-currency denominated debts. The current IMF programme is conditioned on limiting the overall debt-to-GDP ratio to 55 per cent by 2028 (IMF, 2023). To achieve this without limiting Ghana's ability to invest towards achieving the SDGs, the following are recommended.

First, there is an obvious need for significant revamping of domestic revenue mobilisation. Tax-to-GDP ratio must increase from the current 16 per cent to at least 20 per cent over this period. This is the only means by which,Ghana other African countries can achieve significant debt reduction without compromising their ability to invest in education and healthcare. But increasing domestic revenues is difficult and deeply political. Broadening the tax base and making it efficient involves confronting vested interests and it must be done in tandem with revamping state capacity. Tax exemptions that deprive the state of revenues must be removed. The fiscal stability clauses enshrined in mining agreements must also be removed. Mining is an important economic activity that ought to contribute a little more to government revenue than is currently the case[6]

Second is the need for strict expenditure controls and rationalisation. The need for Ghana to invest in Sustainable Development Goals (SDGs), for example, is not in doubt. But a significant portion of national expenditures in the last few years have been frivolously and unproductively spent. Much of the spending can easily be avoided. A shining example is the building of a national cathedral estimated to cost 400 million US dollars (Jeffrey Haynes 2024). National expenditures can be curtailed without compromising investments in the SDGs. National expenditures will also need to be rationalised for optimal benefits. Building expensive roads and flyovers in Accra will surely ease traffic and make the city elegant. But the same resources could be invested in expanding food production, thus reducing imports of food and food price inflation.

Third is the need to enshrine a debt target in national laws. A broad debt target as suggested by the IMF is important. We can go beyond that. A cap on foreign currency denominated loans must be pursued. The risk associated with holding a debt in a currency a country does not control is just too high. The proposed amendment of the FRA must specifically place a limit on foreign currency loans. Within that, preference must made for concessionary loans as opposed to commercial loans. The Fiscal Responsibility Council must be broadened to include institutional representation and representation by trade unions and civil society organisations. Ghana needs an independent multi-stakeholder Debt Sustainability Commission to monitor adherence to fiscal responsibility rules.

Finally, parliamentary oversight must be enhanced to ensure that the laws on debts acquisition are adhered to. Capacities are low in parliament. A Parliamentary Research Unit (PRU) must be established along the lines of the Congressional Research Service of the United States to support the legislative and oversight functions of Ghana's parliament.

Conclusion

Ghana will surely continue to borrow to fund its development. The country requires extensive investments in education and health, roads, housing, transportation, and agriculture among others to achieve the SDGs. At about 16 per cent of GDP, domestic tax revenue is insufficient to fund government expenditures. At the same time, the domestic debt market is shallow and illiquid, with a limited funding pool that restricts the government to obtaining short-term loans at

6 In 2018, Ghana produced 5 million ounces of gold, representing 2.5 per cent of global output. This gave gross export revenue of roughly 5.7 billion US dollars. Out of this figure, the country earned 475 million US dollars (1.9 billion Ghanaian Ceti) in taxes and royalties, representing eight per cent of export earnings.

high interest rates (Sarkodie, 2022). To meet the scale of the development needs, external borrowing becomes almost inevitable. But as recent experiences have shown external borrowing exposes the country to much greater exchange rate risks and bigger and recurring debt crisis.

Debt crisis has persisted even with the passage of debt management laws and the creation of institutions for debt management, including Parliament and the Debt Management Division of the Ghana's Ministry of Finance. Political interest in accumulating debts is high in an electoral democracy with weak institutions. Public interest in the discourse around public debt is equally high especially following the Domestic Debt Exchange. This needs to be sustained to put pressure on the political leadership to enact and implement appropriation legislations to rein in Ghana's debts.

A debt target, limiting the amount of loans the government could take in any particular year through legislations is warranted. But its political feasibility depends on other measures to raise sufficient domestic revenues for investment in the SDGs and other growth-enhancing investments.

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6. Background Paper on Zambia

Background Paper on Zambia

by Dr. Charity Musamba

With The Assistance Of Mz. Kumbutso Phiri And Garth Phiri

Introduction

The aim of this paper is to contribute to the ongoing discussion on how to end the debt trap for developing countries, including Zambia. In order to achieve this, the paper will focus on examining the development challenges of the country regarding the current debt situation and the key causes of these challenges. The paper will conclude by making suggestions on how to overcome this debt trap. Specific attention will be given to explaining the legal measures that have been put in place to manage Zambia's loan and debt situation.

Qualifying the Debt Trap in Zambia

In this paper, a "debt trap" is understood to be a situation where a state "continually and perpetually accumulates debts to a level beyond its capacity to both repay and/or able to generate adequate resources and therefore begins to compromise its national development needs in order to meet its debt repayment requirements". For sure, Zambia presents an apt case of a debt trap. Paradoxically, Zambia is among the countries endowed with vast natural resources, but which have failed to embark on a sustainable path of development based on largely domestic resources, mainly because of an incapability to generate adequate resources to finance its development needs and/or as a result of the obligation to repay debts owed domestically or externally.

The total national debt of Zambia stood at 23.7 billion US dollars at the end of 2023, when the country had already embarked upon a debt restructuring programme under the IMF in which it borrowed 1.3 billion US dollars in 2022, and which required it to restructure its debt with other creditors. Zambia allocates more resources to servicing debts than to financing healthcare and education. The country has been battling debt crises from the early 1980s until now (GRZ 2010, GRZ 2022). In all cases of domestic financial deficits, Zambia has opted to secure loans, largely externally, during this period.

Domestically, the government has used Treasury Bills (TBs) and Promissory Notes (PNs) while it has secured external financing in the form of commercial and concessional loans. Here, it is also important to acknowledge the connection between domestic and external debt in the case of Zambia. Specifically, the country has opted to solicit the support of the Bretton Woods Institutions, namely the International Monetary Fund (IMF) and World Bank, in undertaking economic recovery processes aimed at resolving the country's financial problems. For example, Zambia has implemented Structural Adjustment Programmes (SAPs) in the late 1980s and 1990s (GRZ 2005). The country recently underwent a debt restructuring exercise that was concluded in 2024 (GRZ 2024).

All these instances have involved the implementation of economic, monetary and fiscal reforms tors such as agriculture, tourism and manufacly by removing state subsidies, commercialising services and expanding the tax collection base. Zambia is one of the countries that received a huge amount of debt relief under the Highly Indebted Poor Countries (HIPC) Initiatives and the Multilateral Debt Relief Initiative (MDRI) in 2003 and 2008 respectively (IMF 2003, IMF/WB 2008). The total debt stock has been reduced from 7.2 billion US dollars to 2.5 billion US dollars. However, the country already began to show signs of falling into a debt crisis by 2012, to the extent that its debts were classified as unsustainable by 2015 and it was advised to solicit international assistance by the international financial institutions (IFIs) by 2017 (IMF 2017). The key question is: Have these interventions ultimately helped to the country to resolve its financing problem? As shown below, Zambia remains trapped in debt.

Table 1

National Development - Trapped in debt

Budget Allocations	**2021**	**2021 %**	**2022**	**2022 %**	**2023**	**2023 %**	**2024**	**2024 %**
MoH	9,653,313,513	8.10%	13,911,599,575	8.00%	17,394,799,887	10.40%	20,906,443,693	11.80%
MoE	13,772,752,981	11.50%	18,073,367,991	10.40%	23,188,742,594	13.90%	27,354,806,191	15.40%
MoWD&S	2,172,274,286	1.82%	2,352,235,641	1.36%	2,269,481,977	1.36%	1,948,869,116	1.10%
Domestics Debt Interest	18,338,481,000	15.33%	27,364,645,716	15.82%	30,530,000,000	18.25%	32,905,550,262	18.50%
External Debt (Interest & Principal)	27,745,178,541	23.20%	51,315,495,958	29.66%	18,234,338,486	10.90%	6,011,715,419	3.38%
Total Domestic and External Debt	46,083,659,541	38.53%	78,680,141,674	45.48%	48,764,338,486	29.14%	38,917,265,681	21.88%
Total Budget	119,616,011,615		172,987,077,535		167,321,733,563		177,891,868,893	

Sources: National Budget Speeches 2021-2024

Unpacking the Key Causes and Drivers of The Debt Trap in Zambia

These economic, social and political conditions have implications for Zambia's debt situation and the ability of the country to manage it. Zambia rose to the status of a Middle-Income Country at the medium level in 2011 and was then reclassified to the lower status in the same category in 2015. As with other developing countries, Zambia's economic growth has stagnated consistently in the past decade at about three to four per cent compared with the projected eight to 10 per cent expected moving towards the year 2030 (GRZ 2022). The country has remained largely dependent on copper for its national revenues and has failed to diversify its economy into other potentially productive sec turing (GRZ 2022). There are two key challenges focused on curtailing public expenditures, main-resulting from this economic arrangement.

First, Zambia exports raw copper, a primary commodity whose price has been fluctuating, mainly on a downward trend, and, secondly, the mining sector has been privately owned by foreign investors, with investment agreements largely benefiting foreign investors rather than the host country. The country has also been losing colossal amounts of resources in the form of illicit flows since the introduction of a liberalised economic policy. Also glaringly evident is the increasingly declining capacity of the state to deliver quality developmental goods and services, as well as high levels of corruption (TIZ 2023). Consequently, the country has relied mostly on external financing, mainly in the form of loans and aid, to finance its development programmes (GRZ 2022, GRZ 2023).

The country is also considered to be one of the poorest, with almost half of its total population living in poverty (GRZ 2021). Recently, Zambia was classified as one of the most in the world. Social conditions are mainly characterised by mass unemployment, high cost of living and poor living standards, exclusion, and high levels of gender-based violence (GBV) (World Bank 2023). These are particularly prevalent among women, the youth, elderly persons and persons with disabilities (DWF 2021).

Politically, Zambia is lauded as being one of the most stable and promising growing democracies in Southern Africa. Generally, political pluralism and competition exist, civil societies are allowed to perform their functions, and democratic freedoms are guaranteed. However, progress towards the consolidation of these gains seems to be stuck in the tracks (Afrobarometer 2023). There is a perception that the democratic space, civic in particular, is shrinking, political parties are weakly institutionalised, checks and balances have remained weak, while systems of accountability and transparency seem to be failing (GRZ 2022, GRZ 2023). Overall, the lack of separation of powers between the three arms of government and the persistence of pervasive politics of patronage remain the key hindrances to the deepening of democracy in Zambia.

The Legal Context of Debt Management in Zambia

Zambia recently enacted a law to regulate the management of public debt for the country, the Public Debt Management Act (PDMA) of 2022. Currently, the most serious concerns are associated with the clauses that circumvent oversight by the National Assembly under a wide array of emergencies and discretionary measures as well as vagueness on disclosures and the publishing of information. A detailed analysis of the value of this legal provision shows the following as benefits and challenges associated with this Act.

Preliminary

1. Short title

    PROS: By employing the words “public”, “debt” and “management”, the drafters have clearly understood the enormity of matters relating to Zambia’s indebtedness. Secondly, the Act is forward-looking in that it uses the designation of management rather than regulation. The act concerns debt incurred by the state in all its manifestations: government, quasi-government, local government and state-owned-enterprises. It is therefore not limited to central government.

2. Interpretation

    CONS: A few critical words need clarity: The Minister, Bi-annual, Publish. These are key words in the overall framework of the Bill.

3. Government debt management objectives

    PROS: This is a positive inclusion into the Bill.

4. Medium Term Debt Strategy

PROS: It is a proactive approach to debt management.

CONS: There is no linkage between the ABP and the government debt management strategy. This linkage should be explicitly mentioned.

Debt Management Office

5. Establishment of Debt Management Office

PROS: This is a very positive creation of the Bill as it enables a focused and specialised team of technocrats to study all matters pertaining to debts, contracts, interests, repayment periods and the relevance/efficacy of particular debts.

CONS: The major weakness of this lies in its lack of autonomy or independence. As long as this office is controlled by the minister mentioned in this Bill, there is over-reliance on the minister's goodwill to ensure that it functions properly.

6. Functions of Debt Management Office:

CONS: The IMF and World Bank repeatedly state that the preparation of a Debt Sustainability Analysis (DSA) is a macroeconomic/fiscal management function best undertaken by fiscal managers in the Ministry of Finance.

Annual Borrowing Plan

8. Annual borrowing plan (ABP)

PROS: This is a very important aspect of debt management. The Act stipulates a 65 per cent debt-to-GDP ratio, thereby ensuring that the country only borrows within its means and according to its capacity to pay back.

CONS: However, this only works for debts that have a repayment period of only one year. Most debts span several years.

CONS: Debt transparency requirements stipulate that the public debt management framework (PDMF) "adopts reporting standards in support of debt transparency". This includes publishing the medium-term debt management strategy and the ABP and making it widely publicly available. This PDMA only provides for the ABP to be approved by the National Assembly.

9. Review of annual borrowing plan

PROS: This is as important as review of the annual budget. Estimates may change during the course of the year, as may the needs of the country.

CONS: There is no reference to National Assembly oversight. It is important, however, that such a review undergo serious parliamentary interrogation and approval, as is already stated within the Bill.

10. Update on implementation of annual borrowing plan

PROS: This is part of the ongoing disclosure requirements, and they are well captured under the Act.

CONS: This update must, however, be intended for the wider public, rather than just the National Assembly, as the general public are the true stakeholders and interested parties in all debt.

2. General Borrowing Powers

11. Power to raise loans

CONS: All powers to raise loans are vested in the Minister rather than in Cabinet, contrary to Article 114 of the Constitution.

CONS: Secondly, the minister is given unlimited discretionary powers.

PROS: The exceptions in clauses 3(a) and 3(b) are well thought out.

CONS: Of utmost concern are the exceptions or the derogations envisaged in subsection (4): they basically give the minister powers to circumvent the Constitution.

CONS: Further, subsection (5) completely breaks the mold by assigning powers to the President to obtain loans when parliament is dissolved. The Constitution, Article 81(10), already provides for the recall of a dissolved parliament in the event of an emergency

14. Suspension of approval by National Assembly in state of emergency

CONS: This draconian measure is similar to section 11. The only difference here is that the approval to suspend National Assembly approval is now being given by Cabinet.

CONS: The declaration of a threatened State of Emergency requires less stringent procedures, and it gives the President very wide discretionary powers to do so. This has the effect of lowering even further the threshold required to derogate from constitutional requirements and hand too much power to the President to dip into the coffers.

17. Supplier's credit, export credit and finance lease agreement

PROS: To meet the highest standard of transparency, the definition of public debt should be comprehensive and should be consistent with international debt reporting standards. The IMF defines total gross public debt as all financial claims that require payment of interest and/or principal by the debtor to the creditor at a date or dates in the future. The IMF public debt definition therefore applies to and includes suppliers, credits, export credits and finance lease agreements.

20. Agents to issue or raise bonds, stock or treasury bills

CONS: The PDMA does not provide a formalised agency agreement between the central bank and the ministry to clarify the roles and responsibilities of each party to support debt transparency and accountability.

Borrowing by Public Bodies

23. Loans by public body requiring National Assembly approval

PROS: This is a very good measure to ensure that no public body creates debt without the approval of the National Assembly.

24. Reporting requirements for public body

PROS: As above, the requirement to report on the performance of debts incurred by public bodies is a transparent measure, and it is commendable.

Sinking Funds

25. Establishment of sinking funds for redemption of bonds or stock

PROS: This is important to track down domestic and international borrowing, and to prepare for its redemption through a readily available acount.

Guarantees and Indemnities

PROS:

31. Power to give guarantees

32. Approval of guarantee by National Assembly

33. Payment of guarantee fee

34. Maximum amount of guarantees

35. Beneficiary to reimburse all costs

36. Indemnities

37. Guarantees and indemnities to be paid out of the Consolidated Fund

Power to Raise Grants

PROS:

38. Power to raise grants

39. Purpose of grants

Reports

40. DSA

PROS: This is a good provision

41. Debt statistical bulletin

CONS: This provision is vague on the timing of the publication. It does not state how soon after the end of the quarter the bulletin will be published. This does not meet the standard reporting requirement for a debt statistical bulletin.

42. Annual public debt, guarantees and grants execution report

PROS: The language of this provision does not clearly specify that this report will be made publicly available.

General observations

CONS: There is no provision for the equal treatment of creditors in this public debt management act. There are no provisions that mandate transaction level disclosure.

→ Action: Include provisions to disclose information on public debt at the transaction level including the general terms and conditions of all loans contracted;

→ Use of proceeds require enhanced scrutiny and approval for all debt that entails collateral or collateral-like features, novel features or unusual features.

CONS: There is no provision in the PDMA for an oversight committee such as the Debt Management Committee.

→ Action: Include a provision to establish a Debt Management Committee (DMC). Define it in the Interpretation and add a section that explicitly recognises, establishes and gives powers to the DMC.

General Provisions

50. Repeal of Cap. 366 and Cap. 350

CONS: The second schedule, section 50(2).3 states that the provisions for debt ceilings (65 per cent of GDP and 20 per cent of GDP) will only apply after five years. This renders these provisions academic.

Additional supportive legal provisions to this Act are include the National Planning and Budget Act No. 1 of 2020, the CDF Act 2022 and the National Decentralisation Policy 2023.

Recommendations

Policy-Oriented

→ Formulation of comprehensive national policies on loan and debt management – related to the national development priorities.

- Development of Debt Exit Strategies – illustrating short-medium and long term interventions.

- Promoting national and regional strategies on income generation – economic diversification, domestic investment, manufacturing and industrialisation.

- Supporting initiatives on fair and just trade both at regional and international level.

Legally Oriented

- Strengthening the role of parliamentary oversight throughout the loan contraction process.

- Strengthening the existing laws to enhance citizen participation – timely access to information, monitoring and tracking of debt contracting and repayment.

- Supporting the promotion and safeguarding of democratic freedoms and human rights – speech and assembly.

- Stiffening and fully implementing the laws on corruption and abuse of office.

- Ensuring effective implementation of the Access to Information Law.

Institutionally Oriented

- Strengthening parliamentary oversight in the loan contraction and repayment processes – especially during the negotiation stage.

- Strengthening networks and solidarity initiatives on debt among different actors – CSOs, Parliaments.

- Re-institution of National Donor-Government-CSO Consultative Group Meetings (CMGs).

- Building the capacities of Members of Parliament on debt and other closely related subjects.

- Lobby for IMF/WB reforms especially with regard to IFIs/State Agreements (Transparency and Accountability.

- Support activities focused on organising CSOs to undertake citizen sensitisation activities on debt and other closely related concerns.

Conclusion

If a "debt trap" refers to a situation where a State "continually and perpetually accumulates debts to a level beyond its capacity to both repay and/or able to generate adequate resources and therefore begins to compromise its national development needs in order to meet its debt repayment requirements", then an inquiry into possible suggestions for overcoming this challenge should also be fashioned in a multifaceted manner. The specific case of Zambia shows that countries can also be trapped in perpetual indebtedness as a result of myriad economic legal, policy, political, social and financial factors.

Zambia remains engulfed in a perennial debt problem, largely as a result of poor economic and financial performance and, perhaps more worryingly, declining democratic political and accountable fiscal conduct among the policy and political élites both at national and international level.

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With The Assistance Of **Mz. Kumbutso Phiri And Garth Phiri**

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7. Background Paper on Pakistan

Background Paper on Pakistan

by Sajid Amin Javed

Introduction

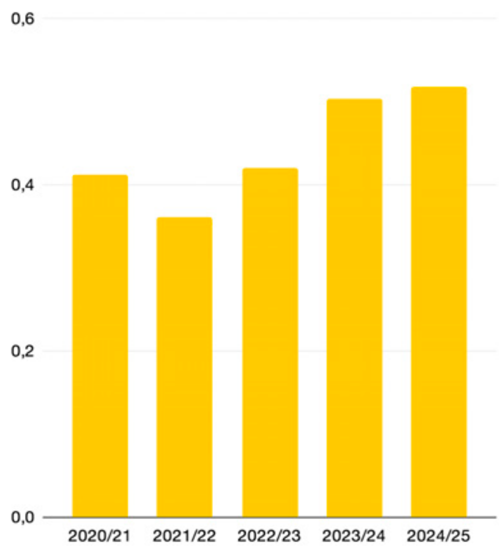
Global sovereign debt has skyrocketed to a near all-time high of 97 trillion US dollars in recent years (UNCTAD 2024). While most of the current debt stock belongs to developed countries (70 per cent), developing countries are increasing their debt at a much faster rate (UNCTAD 2024). This is a cause for concern as the growth in public borrowing of developing and low- and middle-income countries (LMICs) has surpassed the growth of their gross national incomes (GNI) and trade, resulting in debt becoming growingly unsustainable. Combined with various other challenges that developing countries are facing[1]. These factors have led to increased risks of debt distress or default (Adrian et al. 2023).

Pakistan, struggling on both the political and economic fronts, finds itself in a similar position. With a debt to GDP ratio of 71.8 per cent (IMF 2024) that has been rising over the last decade (Figure 1), Pakistan's debt level currently exceeds the estimated threshold of 60 per cent — the maximum upper limit as per the country's own debt laws — at which the risk of default rises substantially (Wahid 2023).

Most of the federal budget is allocated to interest payments. When coupled with low revenue due to limited tax collection and a narrow tax base, these factors lead to recurring fiscal deficits (Figure 2). In order to finance this gap and also the previously incurred debt, each year Pakistan is forced to acquire new debt, leading to a debt trap. As of the recent federal budget (2024), out of 18 trillion Pakistani rupees net federal revenue, 9.7 trillion Pakistani rupees (approximately 34 billion US dollars[2]) is allocated to interest payments on existing debt (Ministry of Finance 2024).

Figure 1

Interest Payments as % of Total Revenue



Source: Ministry of Finance Annual Budget Report

1 Hindered economic recovery in the post-pandemic era, low revenue growth, rising long-term borrowing costs, payment of interest expenses at the cost of reduced educational and health budgets, foreign currency exposure and vulnerability to external shocks (UNCTAD, 2023).
2 Based on 2024 6-month average exchange rate.

Box 1

Fiscal Deficit to Remain Up Till 2027

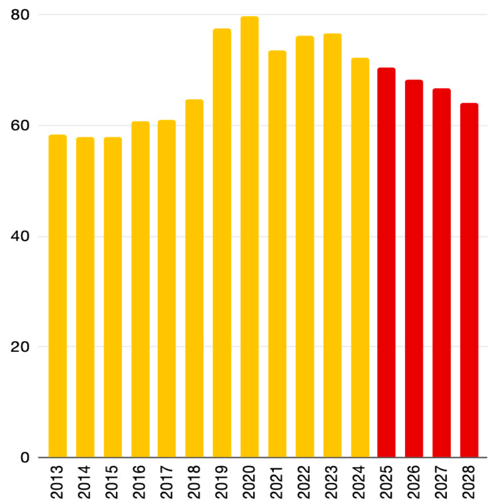
Fiscal deficits are projected to remain between 4 per cent to 7 per cent of GDP from 2024 to 2027.

For more information view "Pakistan - First Review Under the Stand-By Arrangement..." IMF Country Report No. 24/17

As shown in **Figure 2**, interest payments have taken more than 40 per cent of total revenue from fiscal years (FY)[3] 2020/21 to 2024/25 (with the exception of FY 2022/23). Moreover, Pakistan is expected to pay more than 18 trillion Pakistani rupees (approximately 64 billion US dollars[4]) in principal repayments during the same year (Public Debt Bulletin 2023).

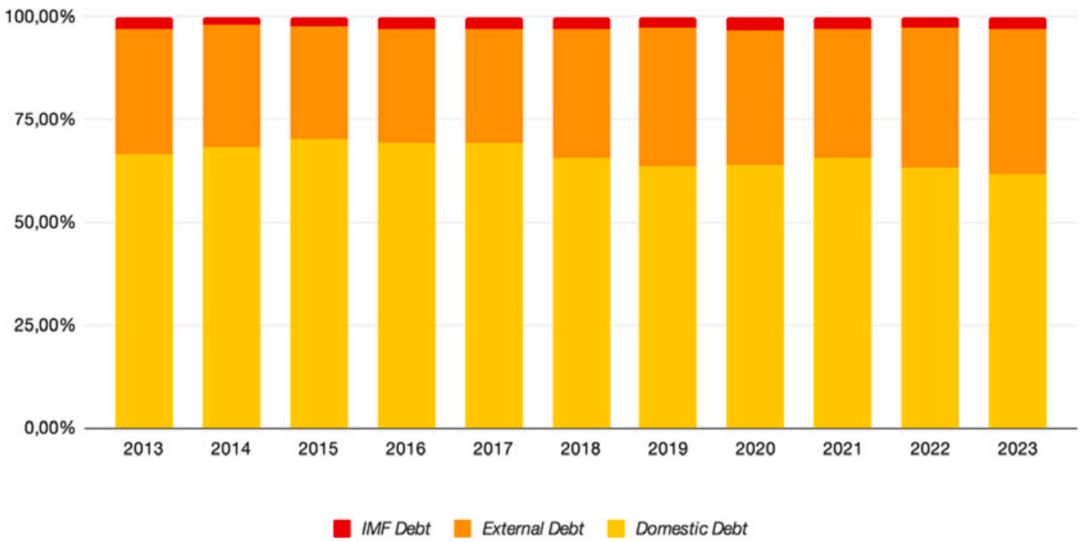
Figure 2

Interest Payments as % of Total Revenue



Source: Public Debt to GDP Ratio

Figure 3



3 Pakistan's fiscal year runs from 1 July to 30 June.

4 Based on 2024 6-month average exchange rate.

Box 2

Article 166 of the Constitution, 1973

Federation extends to borrowing upon the security of the Federal Consolidated Fund within such limits, if any, as may from time to time be fixed by Act of Majlis-e-Shoora (Parliament), and to the giving of guarantees within such limits, if any, as may be so fixed.

Note: For more information visit https://na.gov.pk/uploads/documents/1333523681_951.pdf

5 For more information visit: https://www.brecorder.com/news/40300932

Box 3

FRDL Act, 2005 – 2022 Amendment

(1) Limit the stock of government guarantees at 10pc of GDP

(2) Publish a Medium-Term National Macro-Fiscal Framework (MTMFF)

(3) Institutionalize debt management functions in a single office reporting to the finance secretary instead of the finance minister

Note: For more information visit https://www.finance.gov.pk/publications/frdla2005_amended_2022.pdf

Box 4

Public Finance Management Act, 2019(1) Limit the stock of government guarantees at 10pc of GDP

Budget Strategy Paper

(1) The Federal Government shall approve the budget strategy paper containing quantified macroeconomic and fiscal projections each year. The paper shall indicate strategic priorities of the Government revenue and spending policies and specify indicative levels of spending in various Ministries and Divisions. Upon approval of the paper, the Finance Division shall issue indicative budget ceilings to Ministries and Divisions.

(2) The Minister for Finance shall discuss the budget strategy paper with Standing Committees responsible for Finance and Revenue in the Senate and the National Assembly

Note: For more information visit https://www.sbp.org.pk/l_frame/PublicFinanceManagementAct_2019.pdf

Box 5

Special Parliamentary Committee on Foreign and Domestic Loans (2012)

12-member committee to probe 1) amount of loans obtained under different governments, 2) donors, 3) borrowing reasons and 4) where borrowed money was spent

Note: For more information visit: https://www.cadtm.org/Pakistan-Parliamentary-Body-starts

6 This probe, however, was mainly a political move to build corruption cases against the then outgoing government, instead of promoting debt transparency or responsible borrowing

Box 6

Public Finance Management Act 2019

Chapter II (3.2): Budget strategy paper — The Minister for Finance shall [also present and discuss the budget strategy paper with the Standing Committees] for Finance and Revenue in the Senate and the National Assembly.

Chapter II (5): Plan based Government's expenditure — All government expenditures, whether from a recurrent or development demand for grant, shall be based on well-defined plans and the strategic priorities approved in the budget strategy paper as per section 3.

Chapter II (10): Changes in schedule of authorised expenditure - If in respect of any financial year it is found ... the Federal Government shall have power, as prescribed, to authorise expenditure from the Federal Consolidated Fund, whether the expenditure is charged by the Constitution upon that Fund or not, and shall cause to be laid before the National Assembly Supplementary Budget Statement or, as the case may be, an Excess Budget Statement, setting out the amount of that expenditure, and the provisions of Articles 80 to 83 shall apply to those statements as they apply to the Annual Budget Statement.

Chapter III (20): Utilisation of public assets. — (1) Principal accounting officers shall ensure that the maximum possible returns are achieved on each and every asset falling under the oversight of the Ministry and Division. (3) With a view to achieving the maximization of returns on public assets, government may establish sovereign wealth funds through an Act of Parliament.

Chapter IV (23): Expenditure from Federal Consolidated Fund [and Public Account] — (1) No authority shall incur or commit any expenditure or enter into any liability involving expenditure from the Federal Consolidated Fund and Public Account of the Federation until the same has been sanctioned by a competent authority duly empowered and the expenditure has been provided for the financial yea... (3) Every grant approved by the National Assembly for a financial year and every other authority or sanction issued under this Act in respect of a financial year, shall lapse and cease to have any effect at the close of that financial year

Note: For more information visit https://finance.gov.pk/budget/PFM_Act_2019.pdf

7 The author of this paper, Sajid Amin Javed, was invited by the debt inquiry commission of 2019 to assist the commission and provide an expert opinion.

State Bank Amendment Act 2021

An important piece of legislation passed by the parliament in recent times is the State Bank Amendment Act of 2021. While the act largely deals with defining the functionalities, objectives and autonomy of the State Bank of Pakistan (SBP), it also introduces a key restriction on government borrowing. More specifically, the act prohibits new government borrowing for the SBP on account of the inflationary nature of this debt along with restrictions on quasi-fiscal operations undertaken by the SBP.

Box 7

The State Bank of Pakistan Act, 1956

The State Bank of Pakistan is empowered to manage public debt on behalf of the Government of Pakistan.

Note: For more information visit https://www.sbp.org.pk/about/act/SBP-Act.pdf

Box 8

State Bank Amendment Act, 2021

9C. Prohibition on the Government borrowing — *(1) The Bank shall not extend any direct credits to or guarantee any obligations of the Government, or any government-owned entity or any other public entity. (2) The prohibition laid down in sub-section (1) shall not apply to government owned or publicly-owned banks and other regulated entities, which shall be given the same treatment as privately-owned banks. (3) The Bank shall not purchase securities issued by the Government or, any government-owned entity or any other public entity on the primary market. Nonetheless the Bank may purchase such securities in the secondary market. (4) The Bank shall not guarantee any loan, advance or investment entered into by the Government, any government-owned entity or any other public entity: Provided that the existing outstanding debt owed to the Bank in the form of loans, advances or Government securities purchased on the primary market, at the time of the commencement of the State Bank of Pakistan (Amendment) Act, 2021 shall be retired in accordance with the terms and conditions under which such outstanding debts were extended. In compliance with the prohibition of monetary financing under this section no roll-over or re-profiling of such existing outstanding debt of the Government owed to the Bank shall be permitted. (5) The guarantees issued by the Bank to secure the obligations of the Government outstanding on the commencement of the State Bank of Pakistan (Amendment) Act, 2021, shall not be increased, but can be rolled-over in accordance with the terms and conditions under which such outstanding guarantees were issued.*

22. Amendment of section 20, Act XXXIII of 1956 - *In the said Act, in section 20, after clause (5), the following new clause shall be inserted, namely: "(5A) undertake any quasi-fiscal operations or development finance activities."*

Note: https://www.finance.gov.pk/SBP_Act_2021.pdf

2. Provincial Level

Article 167 on the other hand deals with debt at the provincial level, giving provinces the authority to raise and guarantee debt within limits outlined by their respective provincial assemblies[8]. Furthermore, under this article provinces are allowed to obtain debt from the federal government so long as the debt ceiling imposed by the parliament under article 166 is not exceeded.

Box 9

NFC Award

The NFC award is the framework under which funds are collected and disseminated between the federal government and provinces.

Note: For more information visit: https://finance.gos.pk/ResourceDistribution/NFC

Box 10

Article 167 of the Constitution, 1973

(1) *Subject to the provisions of this Article, the executive authority of a Province extends to borrowing upon the security of the Provincial Consolidated Fund within such limits, if any, as may from time to time be fixed by Act of the Provincial Assembly, and to the giving of guarantees within such limits, if any, as may be so fixed.*

(2) *The Federal Government may, subject to such conditions, if any, as it may think fit to impose, make loans to, or, so long as any limits fixed under Article 166 are not exceeded give guarantees in respect of loans raised by, any Province, and any sums required for the purpose of making loans to a Province shall be charged upon the Federal Consolidated Fund.*

(3) *A Province may not, without the consent of the Federal Government, raise any loan if there is still outstanding any part of a loan made to the Province by the Federal Government, or in respect of which guarantee has been given by the Federal Government; and consent under this clause may be granted subject to such conditions, if any, as the Federal Government may think fit to impose.*

(4) *A Province may raise domestic or international loan, or give guarantees on the security of the Provincial Consolidated Fund within such limits and subject to such conditions as may be specified by the National Economic Council.*

Note: For more information visit https://na.gov.pk/uploads/documents/1333523681_951.pdf

8 For more information visit: http://www.commonlii.org/pk/legis/const/1973/7.html

On the other hand, where federal funds are involved, the federal government is tasked with an oversight role over provincial borrowing. Additionally, amendment 167(4) allows provinces to secure debt from domestic sources up to a total of 0.85 per cent of GDP, with individual caps on provinces depending on their share in the National Finance Commission (NFC) Award[9]

Furthermore, each provincial assembly in Pakistan has also issued its own legislation concerning responsible fiscal and debt management.

The Punjab Public Financial Management Act 2022 (Chapter III & IV)

Chapter III and IV of this Act contain framework for public expenditures and debt in the province of Punjab including[10]:

- Debt Ceilings:
- Public Debt & Guarantees must not exceed 200 per cent of the average revenue of the previous three financial years.
- Government Debt & Guarantees must not exceed 160 per cent of the average revenue of the previous three financial years.
- Public corporations Debt and Guarantees must not exceed 40 per cent of the average revenue of the previous three financial years
- Interest expense on government Debt must not exceed 12 per cent of the average revenue of the previous three financial years.
- Issue annual medium term debt management strategy encompassing a three-year horizon.

Establish a Debt Management Unit in the Finance Department.

The Sindh Fiscal Responsibility and Debt Management Act, 2022

Like Punjab, the province of Sindh also recently issued legislature concerning fiscal responsibility and debt management. Important benchmarks of this legislation that are related to debt include[11]:

- Provincial fiscal deficits to be kept under 20 per cent of total revenue of the previous financial year
- Debt servicing of total public debt must not exceed 10 per cent of total revenue of the preceding Financial Year.

1. Publish a three-year debt management strategy.
2. Establish a Debt Management Unit in the Finance Department.
3. Government to maintain current revenue expenditure within prudent limits.
4. Government to minimise annual budget deficits over the long run.

Box 11

Sindh Public Finance Administration Act, 2020
(1) *Subject to the Article 167 of the Constitution and section 24, the Minister for Finance may enter into contractual borrowing arrangements that he deems to be expedient, including issuing Government Bills or Bonds or stock.*

(2) *The Minister for Finance shall ensure that any borrowing minimises the debt-related risks to the Government.*

Note: For more information visit http://www.pas.gov.pk/uploads/acts/Sindh%20Act%20No.X%20of%202021.pdf.X%20of%202021.pdf

9 The NFC award is the framework under which funds are disseminated from the federal government to the provinces. For more information visit: https://finance.gos.pk/ResourceDistribution/NFC
10 For more information refer to: http://punjablaws.gov.pk/laws/2861.html
11 For more information refer to: http://www.pas.gov.pk/uploads/acts/Sindh%20Act%20No.XXXIII%20of%202023.pdf

Khyber Pakhtunkhwa Fiscal Responsibility and Debt Management Act, 2022

For the province of Khyber Pakhtunkhwa, the Fiscal Responsibility and Debt Management Act entails the following[12] :

- *Debt Limitations:*

- Debt servicing must not exceed 10 per cent of the average provincial revenue.
- Combined stock of total public debt and guarantees to not exceed 150 per cent of the average provincial revenue.
- Combined total public debt, guarantees and pension liabilities to not exceed 400 per cent of the average provincial revenue.
- Public Corporations debt and guarantees to not exceed 30 per cent of the average provincial revenue.

- *Fiscal Limitations:*

- The annual fiscal deficit to be curtailed at a maximum of 10 per cent of average revenue in a given fiscal year.
- Net investment in non-financial assets to be greater than 15 per cent of average revenue of the province.

- *A three-year debt management strategy to be published every two years.*
- *Establish a Debt Management Unit in the Finance Department.*

1. Government must maintain high international standards of transparency in the reporting of finance and public-sector debt statistics.

Balochistan Finance Bill, 2020

Lastly, in the Balochistan province the "Balochistan Finance Bil[13]" that was presented to the provincial assembly in 2022, broadly covers debt and fiscal targets, such as:

- Eradicate budget deficit through gradual annual reductions in deficit by 10 billion Pakistani rupees.
- Restrict its total outstanding debt up to a threshold prescribed by the government.
- Target an annual gradual decrease in the percentage of nondevelopment expenditure.

Successful experiences and practices[14]

The Fiscal Responsibility and Debt Limitation (FRDL) Act of 2005 is the key piece of legislation in Pakistan that provides a legal framework for reducing Pakistan's public debt and ensuring fiscal responsibility and transparency in fiscal operations. Although this act has led to more scrutiny of government borrowing and debt levels, the success of the FRDL Act has been limited.

Firstly, while the requirement for annual statements under this act has provided some basis for assessing fiscal policy, much more key information and analysis are required to make the statements more effective. Secondly, the focus of this act was to limit total public debt to 60 per cent of GDP, with any borrowing beyond this limit mandating parliamentary approval, but this has not been the case.

Successive governments have been unable to meet the stipulation in the FRDL Act with little to no challenge against this observed on part of

12 For more information visit: https://kpcode.kp.gov.pk/uploads/THE_KHYBER_PAKHTUNKHWA_FISCAL_RESPONSIBILITY_AND_DEBT_MANAGEMENT_ACT_2022.pdf
13 For more information visit: https://www.finance.gob.pk/wp-content/uploads/2021/06/PFM-ACT-2020-OFFICIAL.pdf
14 The content in this section benefits from discussion with Dr. Vaqar Ahmed, Joint Executive Director SDPI, Mr. Zafar Almas, Deputy Economic Advisor, Ministry of Finance, GOP, Dr. Safdar Sohail, Ex- Secretary to cabinet and member of the debt inquiry commission of 2019.

the parliament. This is largely due to the parliament considering this limit as a flexible target rather than a concrete one. This is due to two factors: firstly, no concrete rationale has been offered to support the setting of a debt to GDP target of 60 per cent. While some empirical evidence suggests that beyond a debt to GDP ratio of 60 per cent economic growth is negatively affected (Reinhart and Rogoff 2010), the FRDL Act offers no such justification.

Moreover, these targets only serve as an anchor for debt planning and decisions, leaving the government free to acquire any level of debt it deems fit, thereby reducing parliament oversight. Secondly, parliamentary effectiveness is further diminished by the non-existence of penalties for the government if it misses the FRDL Act debt targets.

In comparison, take the example of Brazil where missing public debt targets leads to major repercussions, which range from fiscal penalties to criminal penalties, as outlined in their legislation (World Bank 2010). These enhance the effectiveness of parliament and ensure that the government meets its debt targets. Such penalties, however, are missing in the case of Pakistan, not only limiting the Pakistani parliament's effectiveness but also enabling the government to easily exceed the debt threshold and hence making the debt targets flexible in nature.

Box 12

Federal law no 10,028 of 2000 (Brazil)

The offence is considered a crime when the member has not ordered the excess debt to be reduced within the time set by the Federal Senate. The penalty is detention of three months to three years (for mayors) and/or loss of public office for up to five years (for mayors, governors and the President). These penalties do not exclude the possibility of trial and conviction for common crime.

The offense is considered an infringement when the member does not meet the prima 30% of the annual income for the agent responsible. The infringement is determined by the Court of Accounts responsible for enforcement.

Source: Public Debt: The Brazilian experience (World Bank).

Note: For more information visit https://documents1.worldbank.org/curated/en/967171469672182286/pdf/700810ESW0P1160Brazilian0Experience.pdf

Box 13

LRF and Senate Resolution 40 of 2001 (Brazil)

If the consolidated debt exceeds the limit at the end of a 4-month period, it must comply by the end of the next three periods, with a minimum of 25% reduction in the first period. Once the excess is verified, the member that violates the limit is:

a) prohibited from contracting internal or external credit operations, including ARO, except to refinance the debt principal and

b) required to obtain the balance needed to reduce the debt to the limit, restricting funding commitments, among other measures.

These restrictions apply immediately if the amount of debt exceeds the limit during the first fourmonth period of the President's last year. Once the period for reducing the debt has ended, and if the excess persists, the member will also be prohibited from receiving voluntary transfers from the federal government or the states.

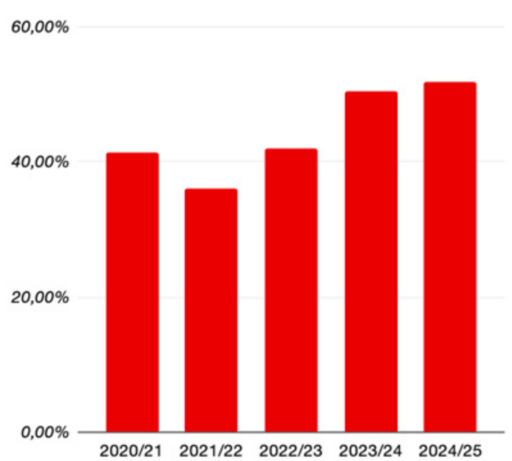
Source: Public Debt: The Brazilian experience (World Bank).

Note: For more information visit https://documents1.worldbank.org/curated/en/967171469672182286/pdf/700810ESW0P1160Brazilian0Experience.pdf

On the other hand, another major limitation in parliamentary effectiveness arises from the large budget deficits incurred each year. These deficits force the government to turn towards additional debt to finance the annual budget, which is then formally approved by the parliament. Under the current system, the parliament indirectly greenlights the acquiring of additional debt when it approves the budget, leading to a cycle of persistent debt.

At the start of this cycle lies the low rate of tax collection (12 per cent of GDP, according to the Ministry of Finance), which results in limited government revenue. A majority of the collected revenue is spent on interest payments on existing debt (Figure 4), with the remainder then being transferred to provinces under the NFC award. Consequently, little to no revenue is left for the development budget, which then entirely relies on debt financing. Therefore, from the moment it is presented in the parliament, the budget requires and causes additional borrowing. When the parliament approves this budget, it is giving de-facto approval to the government for obtaining debt beyond the 60 per cent threshold.

Figure 4



Source: Ministry of Finance (2024)

In the most recent budget, FY 2024/25[15], revenues stood at 18.87 trillion Pakistani rupees, while interest payments alone amounted to 9.77 trillion Pakistani rupees, followed by 7.438 trillion Pakistani rupees being transferred to the provinces as their combined share of revenues in the NFC award (Ministry of Finance 2024). The development budget, which amounted to 1.4 trillion Pakistani rupees, was left to be funded solely through additional borrowing. When the coalition government that occupies the majority of seats in the parliament, consisting of the Pakistan Muslim League-N (PMLN) and the Pakistan's Peoples' Party (PPP), approved this budget, the parliament gave its de facto approval for increasing public borrowing. Therefore, the current structure of fiscal expenditure operates and depends upon debt financing, which is then given parliamentary approval year after year, limiting the parliament's effectiveness in debt management.

Lastly, the FRDL Act, 2005 and PFM Act, 2009 clearly establish requirements for debt and budgetary reporting to the parliament in order to ensure transparency and accountability. However, as stated earlier, if the government fails to meet these requirements there exist no penalties. Consequently, Pakistan's global debt management rankings have declined between 2005 to 2019, leaving Pakistan just slightly above the average of the Asia-Pacific region (Singh, Charan, and Vatcharin Sirimaneetham 2021).

Moreover, as per the World Bank Debt Reporting Heat Map (2021), Pakistan also lags behind in debt reporting, specifically in information availability regarding previously acquired debt, annual borrowing plans and other debt statistics and contingent liabilities. Ultimately, Pakistan's dilemma is that, despite all the necessary legislatures being present, the country falls behind in enforcement of these laws and in the role of parliament in scrutinising the government's fiscal and debt management.

15 For details visit: https://www.finance.gov.pk/budget/Budget_2024_25/Budget_in_Brief.pdf

Unintended consequences

Despite legislation existing in Pakistan to ensure debt sustainability and effective management, along with preventing debt from going beyond a certain limit (60 per cent of GDP), Pakistan has far exceeded this level and has missed its annual debt reduction targets. In reality, as indicated by Figure 1, Pakistan's debt to GDP ratio has not only remained above 70 per cent of GDP since 2018 but has actually risen from 2018 until 2020 and from 2021 to 2023 (SBP, 2023). Although forecasts show the debt to GDP ratio gradually declining from 2024 to 2028, the overall ratio still remains above 60 per cent (SBP 2023). Additionally, for the year 2023, Pakistan's debt to GDP stood at 76.6 per cent, far above the target of 57.5 per cent set for this year.

The primary reason for this significant deviation from targets stems from the fact that there are no concrete repercussions in the FRDL Act, 2005 if the government fails to meet its targets or does not fulfil its responsibilities. As a consequence, this act has never been completely followed, with the government becoming negligent in fulfilling its specified duties. Hence the act has failed in creating a deterrence and safeguarding the country from irresponsible debt practices. Additionally, due to a lack of consequences, both the government and parliament have become lax in fulfilling their constitutional responsibilities. The government has given little to no briefings to the parliament on its debt decisions, while the parliament has not imposed any debt ceilings or restrictions on the government.

Additionally, due to the use of broad terminology for transparency and a lack of detailed transparency measures stated in the FRDL Act 2005, the government can get around the transparency requirements for public debt. Moreover, due to there being no mechanisms in place to ensure the government meets the outlined debt targets, consequences also arise for the general public.

Box 14

FRDL Act, 2005 (11)

Measures for fiscal transparency: (1) The Federal Government shall take appropriate measures to ensure greater transparency in its fiscal operations in public interest and minimise, as far as practicable, secrecy in the preparation of the annual budget. (2) In particular and without prejudice to the generality of the provisions of sub-section (1), the Federal Government shall, at the time of presentation of annual budget, disclose in a statement as may be prescribed,-(a) the significant changes in the accounting standards, definitions, policies and practices affecting, or likely to affect, the computation of prescribed fiscal indicators; and (b) as far as practicable and consistent with protection of public interest. all guarantees including those for rupee lending, bonds, rates of return, output purchase agreement, exchange risk, claims, and commitments made by the Federal Government having potential budgetary implications, including revenue demands raised but not realised and liability in respect of major works and contracts.

Note: For more information visit https://www.finance.gov.pk/frdla2005_amended_2016.pdf

As fiscal deficits and debt rise beyond their mandated threshold, the government tends to raise taxes and utility prices to finance these gaps, often at the expense of an already burdened and narrow tax base. These in turn can have further negative repercussions for economic growth and contribute towards increasing poverty.

16 The author is thankful to Dr. Ahamed Jalam Pirzada, Senior Lecturer in Economics at the University of Bristol, UK.

Conversely, The SBP Amendment Act, 2021 also yields two potential unintended consequences[16].

As the Act prohibits government borrowing from the SBP, the public sector is left no choice but to obtain debt from the remaining two sources: I) the domestic market, consisting of commercial banks and the private sector, and II) external sources. On the domestic front, extensive borrowing from commercial banks firstly leads to the crowding out of private sector, through higher costs of borrowing and the limited availability of loanable funds.

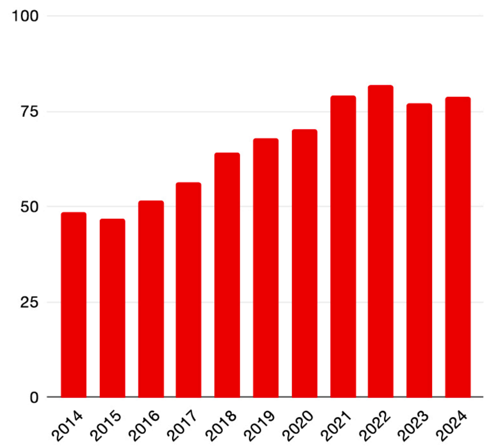
Subsequently, private investments are greatly reduced, which has negative implications for economic growth, as firms limit their expansion and have lower demand for labour, leading to higher unemployment. Secondly, commercial banks tend to favour risk-free lending to the government in the form of "easy" T-Bills rather than riskier investments through lending to the private sector. Consequently, risk-taking behaviour is discouraged, which limits economic growth and diversification through the aforementioned channels. With the monetary policy tightening observed in the post-Covid time period, the cost of borrowing via domestic debt has significantly risen — the policy rate of the SBP currently stands at 20.5 per cent, slightly below its 22 per cent rate at the start of 2024. Higher costs of borrowing result in a greater burden of debt on the government, leading to reductions in the development budget and increases in both direct and indirect taxation.

Moreover, restrictions on borrowing from the SBP reduce the amount of domestically available funds for the government. As there is only so much debt the government can raise from the domestic market, the government turns towards external debt to finance its budgetary requirements and meet its needs. Therefore, the SBP Amendment Act, 2021 can be argued to be a primary factor behind the rising levels of foreign debt.

Figure 5 shows a rise in Pakistan's external debt in 2021 from previous years to nearly 80 billion US dollars, with debt remaining near this level in the following three years. External debt brings with it various challenges, including a higher cost of borrowing, foreign currency exposure, and IMF restrictions in the case of multilateral debt. Hence, it can further be argued that the potential unintended consequence of promoting external debt has far greater implications for the economy than the inflationary impact of borrowing from the SBP.

Figure 5

External Debt ($US Billion)



Source: SBP

At the provincial level, the amount of debt that can be raised by provinces is set according to their share in the NFC award. Two main issues emerge from this, firstly since the allocation of funds to a province depends upon factors such as population, development and poverty rather than actual needs or the efficient use of funds, as there are no safeguards in place to ensure productive uses of debt. Secondly, as revenue collection falls under the domain of the federal government, provinces have little to no incentive to use their funding responsibly, as this funding is obtained from either their allocated share or from raising debt, with the entire burden of financing debt and revenue generation falling upon the federal government. Hence, this polarity in those responsible for collection of revenue versus those who spend it leads to inefficiencies. While the drawbacks of the NFC award are beyond the scope of this paper, the debt allocation portion of the award remains a cause for concern.

Parliamentary Space

The preceding discussion suggests that parliament has good space to play an effective role in ensuring responsible public borrowing, leading towards ending the debt trap. The parliament lies at the forefront of tackling unsustainable debt and reducing the debt burden through closely monitoring public spending and borrowing along with keeping a watch over the debt levels, reporting mechanisms and overall transparency.

There are multiple positive prospects present to enhance parliament's approach to responsible debt management. Firstly, the parliament remains the optimal venue to end the debt crisis through legislation which imposes debt ceilings and targets responsible borrowing and spending practices along with promoting debt accountability and transparency.

Despite the current politically charged environment, there is a margin within which the parliament can have a proactive role in debt management. An understanding and consensus exist among all major political parties on the severity of the debt crisis and the urgency of addressing it. Furthermore, the parliament has an open approach to debating the issue, including discussions on current and future debt reduction initiatives. While a difference of opinion may exist on the tools that must be used, political parties remain welcoming and on the same page for debt discussions and for prioritising action through legislation.

Secondly, the parliament in Pakistan remains decentralised, with each province being empowered through its own provincial assembly. This allows for the provinces to set their own financial policies and debt borrowing limits independently. As opposed to a centralised structure, where the federal government would impose its own debt strategies, provinces do not have to wait for the federal government to take initiatives but can do so on their own. Furthermore, the parliamentary institutions are free from external influences, allowing them to make decisions that are in the best of their interests. Hence, decentralisation and independence enable the parliaments, both provincial and national, to address and manage their debt issues effectively through discussion and legislation.

Lastly, one of the conditions of the current IMF staff level agreement on the disbursement of a three billion US dollar loan standby arrangement[17] further broadens the space available for the parliament. In specific, under the agreement the government must seek parliamentary approval for any policy or reforms which include the fiscal decisions and expenditures the government plans to undertake (Kiani 2024).

This condition provides the National Assembly with the opportunity to use its mandate to implement comprehensive reforms aimed at tackling debt issues and promoting debt justice. The assembly can ensure transparent and accountable management of public finances and debt by thoroughly reviewing and improving the government's policies before granting them approval. Furthermore, the parliament can leverage its current position to monitor government spending and public debt closely to prevent any decisions that are harmful in the long run.

Recommendations

Given the space available to the parliament on the debt front, various measures can be undertaken to ensure responsible public borrowing. Parliamentary interventions can be divided in stages, starting with:

Strengthening enforcement of existing legislation

Pakistan already possesses the framework for managing its debt both at the federal level

17 For more information visit: https://www.imf.org/en/News/Articles/2023/06/30/pr23251-imf-reaches-staff-level-agreement-with-pakistan-on-a-us-3-billion-stand-by-arrangement

(FRDL Act 2005) and at the provincial level (Provincial debt and Fiscal Responsibility Acts) which outline the targets of sustainable debt management and debt reduction along with the outlines for fiscal oversight. Additionally, as discussed previously, the parliament is empowered by the constitution to have oversight on debt borrowing. There is, however, a need to establish an enforcement mechanism which pushes the government to achieve debt and fiscal targets.

As a starting point, the optimal role of parliament in debt management may be to strengthen existing laws. Pakistan already has the foundations in place, in the form of legislative frameworks, that guide fiscal and debt management. The country needs only to strengthen the enforcement of existing debt management mechanisms. In this regard, Pakistan must focus on areas such as empowering debt management offices to promote sustainable borrowing and expenditure practices along with improving the availability of debt statistics and information to ensure borrowing transparency.

Furthermore, the parliament must work towards establishing enforcement mechanisms such as introducing penalties for the government if it fails to meet monetary, fiscal and debt targets identified in previous legislation. As is evident by the debt levels rising beyond the mandated threshold in recent years, without clear consequences there is little to no incentive on part of the government to achieve debt sustainability goals. Without a proper enforcement framework in place any new legislation, or amendments to existing ones, will have limited success. Therefore, the initial and optimal role of parliament in achieving sustainable debt management is to strengthen existing legislature and ensuring enforcement of existing policies to attain responsible borrowing practices.

Ensuring robust implementation of financial management reporting mechanisms

To further improve parliamentary oversight in debt management, the parliament must require the government to give reports on Public Expenditure and Financial Accountability (PEFA) and Public Investment Management Assessment (PIMA), which is also a tool used by the IMF. The aim of PEFA must be to analyse the effectiveness of government in public financial management through I) financial reporting and auditing of revenues and expenditures and II) budget execution reports. These must be presented to the parliament on an annual basis to enhance accountability. Secondly, as most public-sector projects are financed through debt, PIMA is required to manage and oversee public investments. The goal of requiring this assessment is for the parliament to ascertain that debt is going towards public projects rather than current budgetary financing.

Set Up a Bipartisan Caucus for Debate and Legislation

The National Assembly needs to set up a parliamentary caucus consisting of members from different political parties. The sole focus of this caucus must be to stimulate debates on debt within the parliament along with forming legislation after successful debating. The legislation must focus on areas such as:

- → Implementing stringent borrowing limits.
- → Ensuring transparent debt management.
- → Strengthening the legal framework for debt management.
- → Enhancing revenue generation.
- → Promoting fiscal consolidation.

- → Aligning debt objectives with social and economic development.
- → Strengthening institutional capacity.

Proactive Role of Standing Committees

Pakistan has standing committees dedicated to fiscal spending at the federal level, such as the Finance and Spending standing committee, and at the provincial level, with the newest one being formed in Punjab in 2024 (Finance and Development). As these committees share a responsibility for debt oversight, they must play a more proactive role. These committees should incorporate debt into their agendas along with fostering debate on debt at the parliamentary level. Additionally, parliamentary special parliamentary sessions can be allocated to improving parliamentarians' understanding of debt and associated challenges along with monitoring of borrowing and spending. Furthermore, the doors to these committees must be opened to major stakeholders and experts in the fields of economics, finance, and public policy.

Increasing Parliamentarian's Sovereign Debt Literacy

A prerequisite for tackling the debt crisis within the bounds of the parliament is a sound understanding by parliamentarians of sovereign debt and all its parameters along with an understanding of how to use the debt management tools made available to them by the constitution. To ensure that parliamentarians are equipped with the appropriate tools and information set for decision-making and legislation, sovereign debt literacy programmes can be created. These programmes should cater to parliamentarians, with an agenda that focuses on creating a comprehensive understanding of debt through the simplest possible means. These programmes are especially needed in provincial assemblies where sovereign debt knowledge remains low as compared to the federal level. For example, the National or Provincial Assembly can dedicate a special session to understanding Pakistan's current debt structure, major debtors, debt instruments and maturities.

SDGs Framing of Public Debt

Framing debt within the perspective of the Sustainable Development Goals (SDGs) increases the buy-in from and outreach to parliament and parliamentarians. In this context, a partnership with SDG units, established at the level of the Federal Planning Commission of Pakistan and provincial development and planning departments, can bring significant gains. In partnership with SDG units, a series of sessions for parliamentarians from across the parties highlighting how debt can hurt Pakistan' progress on SDGs and the life of the common people can strengthen ownership of the debt justice agenda. Awareness sessions on debt justice and role of parliament in this regard can pave the way for enhancing parliament's oversight on sovereign borrowing.

Identify Global Debt Best Practices and Case Studies

In addition to increasing debt literacy, the parliament may also turn towards the experiences of countries of a similar standing that have successfully addressed their debt issues. This learning experience can include identifying the legislative policies adopted by the more successful countries. Pakistan can also collaborate with these countries through the hosting of legislative workshops in the parliament, where representatives from these countries can brief the assembly members on their best practices. One example is Benin, located in Sub-Saharan Africa. The country reformed its debt management by strengthening its legal framework as well as harmonising its debt and macro-economic policies (Kouame and Yavuz 2023).

At the provincial level, where the current debt stock remains relatively low and provinces are moving towards obtaining their own debt, the standing committees on debt have an even more proactive role to play. This includes training provincial legislators and parliamentarians on debt issues to enhance their understanding of debt sustainability. Equipping law makers with relevant knowledge will ensure responsible debt practices when the provinces eventually turn towards decentralised borrowing.

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8. Background Paper on Sri Lanka

Background Paper on Sri Lanka

by Ermiza Tegal & Ahilan Kadirgamar

Introduction

Sri Lanka was going through its worst economic crisis since independence, and it defaulted on its external debt for the first time in its history in April 2022. This unprecedented moment, particularly with a debt crisis and efforts to find a solution to it, have placed unique economic, political and legal challenges before the country. Sri Lanka is going through a debt-restructuring process and a questionably related International Monetary Fund (IMF) programme. (Chandrasekhar et al. 2023) Indeed, through the debt-restructuring process the IMF and the creditors are now pushing through measures with much more leverage than they might have done without the debt crisis. In this context, there is little domestic debate, limited space for civil society intervention and, for that matter, understanding of pathways of alternative socially-just debt resolution and ensuring non-recurrence of such debt crises.

At the then political moment in Sri Lanka, the regime in power governed without the legitimacy of public confidence. While the tremendous peoples' protests before the debt default and the IMF programme led to the overthrow of the then president, the remnants of the regime installed as President a member of the legislature who was not even elected by the people to Parliament. This meant the government of the day in fact had no social legitimacy to pass new laws until a new government was formed after presidential and parliamentary elections are held. The then president and government also failed to support scheduled local government elections in early 2023, further suppressing the democratic will of the people. It is in this context that the government sought to push through various laws had indeed already passed a number of laws over the preceding two years.

In this article we look at the tension between the need for international and domestic laws to ensure similar crises do not recur, while also considering the importance of democratically deriving such legal changes. Furthermore, we articulate the importance of legislation both at the international level and the domestic level to ensure that international and domestic actors, including the IMF, bilateral creditors, commercial creditors including bondholders and domestic leaders, are held accountable.

Legal background

Sri Lanka is a democratic socialist republic and is governed by its written Constitution of 1978. The Constitution sets up an Executive President who is elected by the citizens and, with a Cabinet of Ministers, forms the government. The legislature is unicameral, elected from a system of District-based proportional representation with seats also distributed to National List candidates. Constitutional recognition of decentralised power sharing in 1987 has been politically fraught and stood suspended at the time by the then President failing to release funds for local government elections in early 2023. Furthermore, despite long-standing demands for institutional change to deepen democracy and for transitional justice and reconciliation particularly post the protracted war, there has been no political commitment to power-sharing or addressing the root causes of several internal conflicts.

The constitutional safeguards protecting the independence of the judiciary are weak: superior court judges are appointed by recommendation of the Executive President; judicial review excludes post-enactment review and permits only a two-week period for pre-enactment review; superior court judges are a mix of career judges and senior state attorneys from the Attorney General's Department. Fundamental rights guaranteed to citizens by the Constitution are strictly limited to civil and political rights, and economic, social and cultural rights are not justiciable. Citizens are only able to challenge executive or administrative actions as being unreasonable or as constituting an infringement of their fundamental rights.

The preliminary stages of the law reform process are ad hoc. Ministries do not share policy or background documents publicly before or during the announcement of a proposed law. Often citizens are first alerted to a new law when the Cabinet of Ministers takes a decision to initiate reform, and only once a draft law is published in the government gazette is the public deemed to be aware of the law. There is no research, explanation or other note that accompanies, or is required to accompany, the gazetted proposed law. Citizens are expected to review a legally worded document without any introduction to the policy or scheme proposed. Once gazetted, the law can be placed before Parliament any time after the lapse of seven days. Once tabled before Parliament, citizens have a mere two weeks to challenge the law or any of its provisions as being unconstitutional. The jurisdiction of the Supreme Court is to review constitutionality of specific provisions or the law as a whole, and the Court does not evaluate the policy motivations of the law, including whether or not a policy conforms with or is against the mandate given by the people.

A poor constitutional framework protecting economic, social and cultural rights has given way to the erosion of socio-economic indicators and gains made by commitments to public education and health in the 1940s and 1950s. The failure to invest in the socialist goals of the Constitution and abide by constitutional directions on state policy have led to poor infrastructure, insufficient coverage of healthcare, education and social protection services, corruption- and problem-riddled administrations, and systems that are technologically lagging. Labour rights have also not seen significant gains and have failed to respond to exploitation in the free market economy, particularly with the neoliberal reforms that came with the Structural Adjustment Programmes of the IMF and World Bank in the late 1970s.

There has been no development of laws specific to improve transparency and accountability to Parliament for the IMF agreements as well as for debt contracts or any borrowing in foreign currency to avoid repeatedly having to turn to the IMF to prevent defaults. The reality is that, even with Sri Lanka's 17th IMF agreement, parliamentary approval has remained a rubber stamp after the Executive Board Approval of the IMF agreement of March 2023.

Increasingly authoritarian measures have also been part of Sri Lanka's recent past. Several attempts to introduce wide unchecked police powers have occurred in the form of proposals for new counter-terrorism laws, continued systemic police violence, torture and degrading treatment, administrative measures and legal proposals to severely curtail non-governmental organisations, several attempts to legally restrict freedom of expression and several cases initiated by the police against legitimate peaceful protestors, dissent and critique.

Laws adopted

It is in the above legal context that Sri Lanka experienced the economic crisis of 2022. Mass citizen protests caused a change of President in July 2022; however, the Cabinet of Ministers and the majority presiding over Parliament largely remained the same. After the outbreak of the economic crisis, new laws or amendments to existing laws were immediately initiated by the Government.

A sudden increased interest in laws curbing civil and political rights, especially freedom of expression and assembly, was apparent. Relating to economic policy and social security, the law reform agenda was driven by pre-crisis law reforms that did not have popular support, and which were re-packaged as being necessary to address the economic crisis and law reforms that were advocated for by actors such as the IMF. Based on the 17th IMF Agreement and related documents, Sri Lanka has agreed to the following types of legal reforms: (1) Anti Money Laundering/Countering Financing of Terrorism (AML/CFT), (2) Tax reforms, (3) Cost recovery on previously subsidised essentials fuel and electricity (4) Social safety, (5) Governance relating to public debt management, Central Bank and the banking sector, and (6) Economic policy touching on liberalising trade and investment, female labour force participation, climate change, access to transport and financial services, flexible working arrangements and affordable childcare, technical and vocational education programmes to close the skills gap, etc. Below is a snapshot of how these commitments are being rolled out.

In May 2024, the president declared that the government had passed 75 new laws in the previous two years amidst the economic crisis. Laws on tax reforms were enacted.[1] By way of AML/CFT law reform, the Anti-Corruption Act No. 09 of 2023 was enacted. The law was based on a draft of 2018 and one of the main criticisms against it was that it penalised complaints deemed false and thereby essentially discouraged complaints. The Inland Revenue (Amendment) Act No. 14 of 2023 was enacted and compelled retirement funds to agree to restructure treasury bonds held by the retirement funds to address domestic debt. (Kadirgamar et al. 2023) Claiming oversight over public finance the Central Bank Act of 2023 was enacted.

These legal changes came in tandem with economic reforms in the context of obedience to IMF programme targets that have creditor interests at heart, negatively affecting working people. The reform of the Ceylon Petroleum Corporation comes with market pricing of fuel, drastically increasing the price of fuel, including by tripling or quadrupling the price of kerosene oil used by small-scale fisherfolk for their outboard motor engines and farmers' irrigation pumps. In August 2022, for the first time in nine years, the Ceylon Electricity Board (CEB) raised electricity tariffs, causing 3.14 million households who use fewer than 60 units a month to experience a rise in the cost of electricity of 211 per cent with further revisions thereafter. For a developing country that had universal access to electricity (close to 100 per cent), now 1.3 million electricity connections have been disconnected[2].

In April 2023, under the Welfare Benefits Act, No. 24 of 2022, a social welfare payment scheme was introduced without consultation or transparency on the qualifying criteria. Social spending was advised to be at 0.6 per cent of GDP, and the new scheme was to be deployed by the Welfare Benefit Board and financed by the World Bank. While at the end of 2022, 2.6 million more people were pushed into poverty, the scheme catered to 1.9 million people in poverty and introduced temporal limits whereby every six months the beneficiary numbers were targeted for reduction. Particularly vulnerable populations such as estate populations, identified rural populations and urban poor were not specifically addressed (Feminist Collective for Economic Justice 2023).

1 Value-added taxes were increased from 12 per cent to 15 per cent by way of Extraordinary Gazette No. 2295 dated 31 August 2022, and thereafter further increased to 18 per cent by Extraordinary Gazette No. 2363/22 dated December 19, 2023. The personal Income tax threshold was decreased from three million Sri Lanka Rupees to one million Sri Lanka Rupees in October 2022. Corporate income tax was increased from 24 per cent to 30 per cent in October 2022. A Social Security Contribution Levy of 2.5 per cent of liable turnover was introduced in October 2022. The Betting and Gaming Levy increased from 1 January 2023.

2 "30 million Red Bills : Minister reveals electricity disconnection numbers", Newswire, 8 May 2024. Found at https://www.newswire.lk/024/05/08/30-million-red-bills-minister-reveals-electricity-disconnection-numbers/

Of the laws enacted that directly impacted civil and political rights, particularly the freedom of expression and freedom of assembly, was the Online Safety Act No. 09 of 2024.

Laws proposed and contemplated

Some of laws formally proposed by then government of Sri Lanka that were pending passage before Parliament include the Anti-Terrorism Bill gazetted on 15th September 2023, the Microfinance Credit and Regulatory Authority Bill published on 30th October 2023 and the Economic Transformation Bill announced on 22nd May 2024. Public concern was expressed over the authoritarian nature of powers in the anti-terrorism law, the lack of regulation of finance companies engaged in exploitative practices in the proposed micro credit law and the fixing in law of economic policy goals without adequately safeguarding labour and socio-economic rights of citizens engaging with and within the economic zones to be created under the economic transformation law.

The new Sri Lanka Electricity Bill will aggravate this process by breaking up the Ceylon Electricity Board and paving the way to privatise electricity service and further raise the costs to consumers. Similar reforms have been hinted at for the Ceylon Petroleum Corporation.

The Minister of Labour announced unprecedented reforms to unify and reform all labour laws applicable in the country in May 2023. Drafts of proposals indicated abandonment of state protection for workers on basic issues such as working hours and increased thresholds to form unions. The basic premise of workers having weak bargaining power and requiring legal protections was undermined with regard to several issues.

Long-standing governmental interest to exert greater control, oversight and in some ways interfere with non-governmental organisations in the form of amendments to the Voluntary Social Service Organisations Act of 1980 also resurfaced. Financial Action Task Force (FATF) guidelines on risk-based legal measures for the non-profit sector were not adopted and broad-based legislation requiring mandatory registration of all social services entities and empowering broad powers for interference were favoured in the draft law. Similarly, a draft law on a Broadcasting Regulatory Commission with broad powers over media institutions was proposed.

The red flags in the host of laws enacted and contemplated were (1) dangers of broadly defined executive power increasing the potential for abuse and rent-seeking in a country that is grappling with bribery and corruption at all levels, (2) expanding criminal law exerting greater control on the citizenry and criminalizing poverty, and (3) expanding authoritarian powers in a context of citizens engaging in dissent and citizen feedback which was crucial for citizen-focused or responsive decision making. On all of the laws proposed above, public concern included lack of public consultation and transparency of the process of development of the proposed laws.

The key concern, especially in an economic crisis, must be the building of public trust and confidence. To this end, public consultation and transparent lawmaking, regardless of the merits of the laws proposed, must be valued. The short turnaround times for law making experienced in Sri Lanka undermine democratic due process, including assessment of long-term impacts, including on the environment and climate change, and impacts on vulnerable populations.

Successful experiences and practices

The debt crisis in Sri Lanka with its severe austerity measures has had a severe impact on the lives of working people, who are excluded from both the process of policymaking and deliberations in the courts in relation to the fallout of the debt crisis. In this context, the battles outside the courtroom including protests, mobilisations, debates by and within trade unions and co-operatives, gain importance. Given the technical character of financial governance including sovereign loans and debt-restructuring processes, the relationship between laws, proceedings within courts and public debate become important.

In this context, in recent times the challenges by free trade zone (FTZ) workers who have demanded to know where their hard-earned foreign earnings had disappeared to, the struggles by trade unions against domestic debt restructuring that greatly reduced their retirement funds, and the convening of a workers' tribunal of plantation workers are examples of the importance of broader social understanding of justice in relation to debt and debt restructuring. In recent months the coalescence of academics, lawyers, researchers, activists and representatives of peoples' movements to form 'Yukthi', a new domestic debt justice movement, facilitated broader discussions about the debt crisis and alternative pathways for debt justice and resolution. The challenge of course is to transform such discussions and debates into the judicial domain, including legislation by a legitimate government after elections.

Sri Lanka has had some success with legal changes drawing from its own history and lessons learnt after mass human rights violations during periods of internal armed conflicts and the recognition of a need for transparency that has arisen during these conflicts. Sri Lankan citizens have increasingly engaged with the national Human Rights Commission, particularly when commissioners have been demonstrably independent, and the constitutional and legislative recognition of the Right to Information. Such institutions and legal tools have empowered citizens to raise concerns and also hold errant officials accountable. The principles and independence of these mechanisms must be valued in the law reforms proposed for addressing the debt crisis as well.

There have also been private member bills by opposition members in Parliament seeking routine transparency in government decision-making. In February 2023, a member proposed a bill requiring routine disclosure of information including on investments, on the Employees Provident Fund (EPF), the largest retirement fund in the country holding mandatory contributions on behalf of all private-sector workers. Currently, this information is not available even to workers who are members of the fund. No support was extended by the government and there was no progress made on this proposed law reform.

Unintended consequences

The urgent passage of such a large number of new laws is contributing to increasing uncertainty and apprehensiveness about how new executive powers introduced by the new laws will be utilised. In a country contending with corruption, political patronage and eroding rights and protections of the most vulnerable, public feelings of uncertainty and apprehensiveness is to be expected. Suspicion and distrust of public officials, eroding public confidence and trust in legitimate institutions are a growing concern.

New laws, regardless of their substance, even if progressive, if proposed by an illegitimate government and passed by a Parliament which had lost the confidence of the people, may see a backlash after elections. There may be attempts to reject and undermine laws created in undemocratic settings.

The new laws are also creating a number of new institutions without the safeguards of public consultation and routine transparency, and this thereby further deepens public mistrust and the frustrations of having newer and multiple executive agencies to hold responsible and seek information from. In a context where information requests, including on national economic concerns, are refused and evaded by diverting requests to other agencies, it is critical that this bureaucratic build-up does not tie citizens up in further dilemmas when engaging with the government.

In a worrying move, the Economic Transformation Act enshrined economic policy targets in the IMF agreement into law (IMF 2023). The policy targets were themselves not a reflection of the mandate given by the people of Sri Lanka to their elected representatives. By legally fixing such targets, the government in effect binds future governments, immediately prior to a Presidential election no less. Economic policies driving investment embedded in a law granting broad powers to the Minister of Finance, which post is held by the President, and also new executive institutions create opportunity for abuse of power, corruption and rent seeking. When policy decisions on economic transformation suffice to be adopted and implemented by the government in power, there is no reason to enshrine policy goals in law. Whether such law reforms are measures to reassure organisations such as the IMF and by extension international bond holders is a serious concern.

The independence of the judiciary and respect for international norms could be eroded when international actors and processes are seen to be complicit in bringing about changes by an authoritarian regime. The room for international cooperation will decline. Furthermore, the high-handed approach of the IMF and World Bank in pushing austerity and privatisation can lead to a xenophobic backlash against the Western world. Such extreme nationalist mobilisations after a period of unprincipled international engagement are indeed possible; this happened with the much-internationalised peace process when president Wickremesinghe was prime minister between 2002 and 2004. That backlash against the Norwegian peace mediators in the mid-2000s eventually turned inward in polarising communities and bringing about the rise of an even more authoritarian populist regime.

Recommendations

A Parliament without legitimacy should not pass new laws prior to a fresh mandate from the electorate. If laws are rushed through, as with the laws passed by legislators who lacked legitimacy, it will create problems in the future by potentially also undermining the legitimacy of the judiciary. A slew of amendments to and withdrawals of laws is likely in the years ahead with the laws that have already been passed.

Following elections and with a fresh mandate, parliament must set out a prescribed process for new laws that embodies principles of transparency, public consultation and accountability to the public. A law must be adopted to ensure there is oversight by the Parliament of all future foreign borrowings, agreements with the IMF and debt-restructuring processes to ensure transparency. Oversight could be in the form of parliamentary approval for foreign borrowings and agreements with international actors, routine review of progress, and the power to initiate renegotiation of terms of agreements. This creates opportunities for public scrutiny over decisions taken in the public interest. It would also be necessary to set out the principles and values that ought to guide oversight such as the protection and promotion of human rights, including socio-economic rights of the people. Principles embodied in the 2014 UN General Assembly Resolution on Basic Principles on Sovereign Debt Restructuring and the UNCTAD principles on responsible sovereign borrowing and lending may be adopted as criteria for review. Indeed, with the likelihood of another default and another debt restructuring process and more IMF agreements (Kadirgamar 2024), there should be greater public transparency over negotiations and parliamentary oversight over agreements.

Domestic debt restructuring has led to large cuts to retirement funds, undermining the future of working people. The new government should redress these losses to ensure the retirement funds do not lose any returns. The Central Bank cannot continue as the guardian of the fund. Domestic debt-restructuring measures should be undertaken with full transparency and provide sufficient time for citizens to engage, suggest alternatives and raise grievances, so that decisions are taken in the best interest of those most affected.

Sri Lanka must support and facilitate spaces for citizens to engage with new laws and express concerns and aspirations. Democratic space must be protected and promoted particularly during times of crisis to better gauge the impacts of policy and legal decisions.

When it comes to international engagement, the new government of Sri Lanka should work with other countries in the Global South to lobby for legislation on foreign borrowings in the metropolis. Such a debtor's coalition can also better renegotiate existing external debt in the case of debt restructuring and better terms for any future borrowing. Furthermore, through participation in international fora, demands should be made on actors like the Paris Club that debt restructuring should not require an IMF programme.

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9. Background Paper on Tunisia

Background Paper on Tunisia

by Imène Cherif

Summary of the Tunisian Debt situation

Tunisia's economic challenges have deep roots, dating back to well before the 2011 revolution. High unemployment, low economic growth and increasing reliance on external borrowing were significant issues that contributed to widespread public dissatisfaction and ultimately sparked the revolution. The post-revolution period did not alleviate these issues; instead, political instability further exacerbated the economic situation. The debt-to-GDP ratio has continued to climb, driven by both external and domestic borrowing to cover fiscal deficits, with the debt-to-GDP ratio reaching 81.9 per cent in 2024 (IMF 2024). The external debt component is significant, accounting for about 85.7 per cent of GDP in 2023 (IMF 2024). This high level of external debt is a major concern, given the country's economic instability and limited growth prospects.

Additionally, Tunisia has been paying significant surcharges[1] to the International Monetary Fund (IMF) due to its high levels of borrowing. According to CEPR, surcharges add two to three per centage points to lending rates on top of regular interest rates and service fees of the credit arrangements (CEPR 2024).

The economic situation and debt in Tunisia have consistently been a source of contention among civil society and the political class. This persistent scrutiny has led to numerous debates and initiatives aimed at addressing these financial challenges.

Legislative initiatives in Tunisia

The Tunisian debt crisis is complex and multifaceted. The lack of a unified legislative framework specifically dedicated to debt management makes the mission of addressing the legal framework around debt challenging in the country. Legislation concerning debt is scattered across various laws and regulations, creating a fragmented and sometimes contradictory legal landscape. Articles related to debt management are found in multiple financial laws, including the Finance Acts, directives from the Ministry of Finance and provisions within the Public Finance Code. The Tunisian legal system also includes references to debt management in the law that organises the Central Bank of Tunisia and various other articles that delineate the administrative roles of ministries such as the Ministry of Economy and the Ministry of Foreign Affairs.

These dispersed legislative references make it challenging to develop a coherent and effective strategy for managing public debt. This complicates the management and oversight of the country's financial obligations. It also makes the mission of civil society advocates and parliamentarians very difficult and leads to inefficient actions.

The 2022 Constitution does not directly address public debt. However, it does stipulate that international loan agreements are legally considered to be international conventions. According to the Constitution, these agreements must be signed by the President of the Republic and then ratified by the parliament, thus adopting them as

1 Surcharges are additional fees imposed by the IMF on countries that have large outstanding balances or have been using IMF resources for an extended period. In total, 22 countries are now subject to surcharges.

ordinary laws. This process underscores the critical role of the President and the parliament in debt management but also highlights a significant gap in the constitutional framework regarding specific provisions or guidelines for managing public debt. Moreover, the classification of international loan agreements as ordinary laws suggests that they do not hold precedence over other national laws.

The political situation and legislative initiatives in Tunisia

Civil society organisations' (CSOs') action before 2011 was very limited because of the authoritarian nature of the regime. During the revolution, Tunisian civil society quickly highlighted the country's debt issue. CSOs called for the cancellation of what they deemed "odious debt" incurred by the former authoritarian regime.

The role of parliamentary opposition and Transitional Justice_

Tunisia elected its first "democratic" parliament in late 2014. Since then, the role of Tunisia's parliamentary opposition in legislation related to debt has been significant, yet challenging. Opposition parties, including left-wing and progressive groups, have consistently criticised debt management in the country and argued that loans have come with stringent austerity measures that hurt the socio-economic fabric of the country. It is worth mentioning that after the July 2021 constitutional coup the role of the parliament became very limited.

The opposition has also introduced various initiatives aimed at curbing the negative impacts of debt. One notable effort was a proposal for a parliamentary commission to oversee all foreign loan agreements, ensuring greater transparency and accountability. This initiative sought to involve more stakeholders in the decision-making process and prevent the executive branch from unilaterally deciding on matters that had long-term economic implications. However, these proposals often met with resistance from the ruling parties and were not always successful in altering the course of government policy.

In 2016, the left-wing parliamentary bloc "Front Populaire" proposed a law (No. 36/2016)[2] for auditing the public debt. The law aimed to establish procedures for auditing Tunisia's external and internal public debt. It defined terms such as "odious debt" and "illegitimate debt" and sought to identify any portions of the debt that might be considered "illegitimate". The law proposed creating a "Truth Commission on Tunisian Public Debt", comprising members from parliament, the judiciary, anti-corruption agencies and civil society, to ensure transparency and accountability in public finance management. This commission would have the authority to audit all loan agreements since July 1986[3] and report its findings to the government and to the citizens.

The proposed law was never adopted or thoroughly discussed in parliament. This was primarily because the political bloc Front Populaire, which championed the proposal, did not have the necessary majority to advance it. Additionally, the law was considered unrealistic and not taken seriously by many legislators, as it failed to provide clear alternatives for financing the state budget. This lack of concrete solutions rendered the proposal ineffective in addressing the financial challenges it aimed to tackle.

The same bloc tried to create a limit in the per centage of the public budget (finance law) for the financial resources coming from loans between 2015 and 2021. These amendments were rejected as the parliamentary bloc was also not able to provide alternative resources to finance the national budget. The limited timing for the discussion of the national budget and the lack

2 https://legislation-securite.tn/ar/latest-laws/
3 Adoption of the Structural Adjustment Program with the IMF

of transparency from the side of the government in issues related to loans and budget finances were two of the reasons behind the failure of these initiatives.

The "Magaloulnech" campaign

In 2013, Tunisia started its first IMF programme after the revolution, sparking significant opposition from civil society, left-wing political parties and activists. In response, a campaign called "Magaloulnech"[4] was launched (CADTM 2013). This campaign demanded transparency and called for citizen participation in such agreements. While the campaign did not significantly impact the country's public debt policies, it played a crucial role in mobilising and educating a new generation of activists and associations. These groups became increasingly engaged with economic and financial issues, acquiring the knowledge and expertise necessary to advocate for greater accountability and public involvement in economic decision-making. The "Magaloulnech" campaign thus marked the beginning of a broader movement focused on transparency and citizen engagement in Tunisia's economic justice.

In 2014, Tunisian civil society specifically addressed the European Union, one of Tunisia's main creditors, urging it to cancel Tunisia's debts rather than extend new loans. This request aimed to alleviate the financial burden on the country and provide more flexibility for its democratic transition. Various informal groups and civil organisations alternated between awareness campaigns and protests focusing on the weight of Tunisia's debt. However, these nascent campaigns struggled to gain traction due to an elitist approach and the failure to make debt a central public issue.

Current Civil Society Action

Civil society actions around debt have primarily taken the form of social movements, mobilisations, public meetings and other types of gatherings. The trade unions also resisted debt and austerity measures related to employment and salaries in the public sector through strikes and negotiations with the government. Trade union resistance forced the government to renegotiate its agreement with parliament relating to some of the austerity measures. Although civil society has started proposing alternatives to debt, such as improving tax collection efficiency and implementing progressive tax system reforms, a clear and comprehensive legislative proposal has yet to emerge.

Despite the efforts of regional and international civil society, the role of national civil society remains largely focused on contestation and the publication of informative analytical reports. While this role is important and necessary, it remains insufficient. As well as these national efforts, many international opportunities for change, such as those offered by the Financing for Development (FfD) process, appear to have been largely unknown. In July 2024, with the support of the African Forum and Network on Debt and Development (AFRODAD), Tunisian civil society will have a gathering to discuss issues related to public debt and mobilise for future actions. It is still not clear if this gathering will lead to a legislative — or any other concrete — initiative from the side of civil society.

Ruling elite action relating to debt

The Tunisian government has implemented three programmes with the IMF since the revolution and reached a fourth agreement on the technical level in 2022. The fourth agreement

4 Meaning "they didn't inform us" in Tunisian dialect.

was interrupted by the President of the Republic[5] in October 2022. The relationship between Tunisia and the IMF has encountered complications following the President's position on the measures required by the IMF. President Saied has expressed reluctance to implement certain austerity measures, including subsidy cuts and privatisation of state-owned enterprises, citing potential social unrest and economic hardship for the Tunisian population.

The President's actions, particularly regarding debt and the IMF, have been interpreted in two contrasting ways. One perspective views the President as populist, accusing him of steering the country back into authoritarianism, especially with the shrinking civic space over the last two years. On the other hand, some civil society actors and part of left-wing activists see the President as taking sovereign actions, commending his bravery in tackling debt issues.

Despite these divergent views, the President has not implemented any clear legislative measures to address or manage the debt efficiently. Instead, while he halted the agreement with the IMF in 2022, he did not provide any alternative financing solutions for the national budget. Consequently, the national budget was adopted with significant gaps, leading to major challenges in exporting food and other essential products.

Successful experiences and practices

Since 2013, social movements and civil society campaigns in Tunisia have achieved notable success in raising awareness about debt justice. These actions have been crucial in mobilising public opinion and creating a broader movement focused on economic and social rights. The Tunsian General Labour Union (UGTT) has played a pivotal role in this movement. As a significant political actor, the UGTT has consistently opposed debt-related policies, often indirectly, by challenging the austerity measures required by international lenders like the IMF.

The UGTT's stance has not only influenced national policy debates but also compelled international financial institutions to reconsider their approach. For instance, in the IMF's Article IV Consultation in 2021, the Fund explicitly called for the involvement of social actors in discussions related to the new agreement, acknowledging the union's significant influence and the necessity of its cooperation for the options of conditionalities.

However, the path to debt justice in Tunisia is fraught with challenges. Despite the successes of social movements, entrenched political and economic interests continue to dominate the decision-making process. The government, often constrained by the need to secure international loans and maintain economic stability, finds itself in a delicate balancing act between implementing necessary reforms and addressing the demands of civil society. Additionally, the technical complexity of debt issues can sometimes alienate the general public, making sustained engagement and advocacy difficult.

Unintended consequences

These initial efforts by Tunisian civil society to address the country's debt crisis have highlighted several challenges. Firstly, these groups lacked the necessary expertise to engage effectively in the highly technical and complex discussions surrounding public debt. Mainstream economists and government experts have domi nated the debate in traditional media, arguing that debt cancellation was unrealistic and would harm Tunisia's reputation. Over time, this has enabled CSOs to become more informed and capable advocates for transparency and citizen participation in economic matters.

5 On July 25, 2021, 10 years after the revolution, President Saied issued an emergency declaration firing the prime minister, freezing the work of parliament and assuming all executive power.

As an alternative to IMF loans, the Tunisian President is increasingly involving the country in security-based agreements with the European Union. These agreements, particularly with Italy, aim to protect European borders by preventing Tunisian and Sub-Saharan African migrants from travelling illegally to Europe. In exchange, Tunisia receives financial loans and other forms of aid. However, these measures come with significant human and humanitarian costs, as migrants face dangerous conditions and human rights abuses both during their journey and upon interception or return.

Recommendations

The ongoing struggle for debt justice in Tunisia underscores the broader global issue of debt sustainability and economic sovereignty. To overcome these challenges, action is needed from policy makers with the participation of civil society.

1. At the political level, all the needed reforms will not be possible without democracy and robust democratic and independent institutions in the country.

2. Transparency measures should be implemented to ensure that all debt-related transactions and agreements are publicly accessible. This includes clear communication on the terms of loans, their intended uses and repayment plans.

3. Strengthen the role of Parliament in overseeing debt management by mandating regular reports from the executive branch on debt status and requiring parliamentary approval for major debt agreements.

4. Consolidate existing scattered legislative articles related to debt management into a comprehensive public debt law. This law should cover all aspects of debt management, including borrowing, utilisation, repayment and transparency requirements.

5. Amend the law governing the Central Bank of Tunisia to enhance its role in public debt management, including clear guidelines on its participation in international borrowing and domestic debt issuance.

6. Civil society needs to continue building capacity and expertise on debt-related matters. Education and awareness campaigns can demystify the technical aspects of debt and make them more accessible to the public.

7. National civil society needs more engagement in constructive dialogue with policymakers and international institutions. This can help to identify mutually agreeable solutions that align with both economic realities and social justice imperatives.

8. While social movements are crucial for political change, it is necessary to develop and propose clear and viable alternatives for debt financing. This includes exploring domestic revenue generation methods and seeking innovative financial instruments.

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10. Background Paper on United States

Background Paper on United States

by Aldo Caliari

Legislative initiatives

Developing countries' debt levels and vulnerabilities are on the rise, worsened by the pandemic shock and its aftermath, as well as interest rate hikes by major central banks. Existing debt workout processes such as the G20 Common Framework have proved incapable of providing timely, orderly and lasting restructuring with fair burden sharing among creditors.

In the absence of any global bankruptcy-like institution, a more fragmented creditor landscape has made coordination on internationally-agreed solutions more difficult (Talero 2022). More than 60 per cent of developing country debt is owed to private creditors (World Bank 2022). More than 90 per cent of those debts are issued under New York and English jurisdictions (IMF 2019), whose courts provide individual creditors with an avenue to sue for full payment even when and while collective talks or international community initiatives for debt relief are ongoing.

As a result, there has been increased interest in exploring how changes to legislation in key jurisdictions that govern private debt instruments can reset incentives for private creditors, thus improving the efficacy of the sovereign debt restructuring framework. This paper focuses on the status of these proposals in New York, which is one of those jurisdictions and covers more than half of debt contracts (IMF 2019).

Proponents of initiatives to introduce changes in New York State law argue that correcting flaws in the international debt restructuring machinery is essential for enabling developing countries to free up the money they need to spend on education, health, food, jobs and poverty reduction programmes. Implementing these proposals would also carry benefits for residents, consumers, workers, businesses and the economy in New York and the United States. The proposals would cut the US and New York taxpayer bailouts of private banks and creditors that lend based on profit; protect New York and US residents' long-term savings in pensions, retirements funds, and other investment vehicles; safeguard real wages, supply chains and jobs; prevent and mitigate the impacts of pandemics, climate change and other global challenges; as well as reduce inflation risks.

The reforms proposed in New York can be classed as three different approaches. One approach (hereinafter "Model Law"), originally introduced by Senator Gustavo Rivera and Assemblymember Maritza Davila, seeks to make restructuring agreements supported by a supermajority of creditors binding on the minority. The bill creates a sovereign debt restructuring process that a debtor can trigger in the New York jurisdiction and would apply to claims governed by New York law or the law of any other jurisdiction that had enacted legislation in substantially similar form.

The process envisions appointing an independent monitor who would be acceptable to the debtor and to the majority of its creditors holding claims under New York law. The debtor submits a restructuring plan that designates different classes of claims and explains how each class of claims would be restructured.

A plan approved by at least two-thirds of the debt amount and more than one half in number of the voting members of each class becomes binding on the sovereign debtor and its creditors. The debtor is then discharged of all claims within the classes, except as provided for in the plan. For a number of years after the plan becomes binding, the bill bars the debtor from filing for a new restructuring for a period that, in the original bill, was 10 years – diminished to five in the Sovereign Debt Stability Act version of this approach.

The bill also stipulates a procedure that allows the debtor to borrow money while the restructuring is ongoing, with approval from a majority of creditors whose claims are being restructured. The repayment of such new loans subsequently gets priority repayment status, similar to the way "debtor-in-possession" regimes operate in domestic bankruptcy frameworks.

For adjudication of disputes that may emerge, the bill provides that the independent monitor may request a court of competent jurisdiction to appoint a referee or special master to make recommendations.

A second approach (hereinafter referred to as "Champerty"[1]), introduced by Senator Liz Krueger and Assemblymember Jessica Gonzalez-Rojas, seeks to amend Section 489 of the New York Judiciary Law.

Section 489 forbade the assignment of a claim "with the intent and for the purpose" of bringing an action on that claim. In 2004, the New York Legislature amended Section 489 to exempt from its coverage assignments having a purchase price in excess of 500,000 US dollars, which exempted from this defence most claims that private creditors are likely to bring against a sovereign debtor in New York. It is worth noting that before this amendment courts had already largely emasculated Champerty by interpreting that it did not apply if the creditor had bought the debt to get repaid in full, or otherwise to litigate (Guzman 2016).

The proposed legislation would remove the exemption – therefore allow opposition of the Champerty defence – for claims against a foreign state or claims that were guaranteed by one. The bill enables the court to consider any facts and circumstances it deems relevant in assessing the intent and purpose of the purchase and provides a list of examples from where intent and purpose can be inferred. In different formulations of the bill examples included the history of the creditor (or affiliates) in transactions involving the debts of other debtors, a pattern of "participating in good faith . . . in consensual resolutions of such situations" ,"acquiring claims . . . at significant discount from face value, refusing to participate in consensual workouts and instead resorting to legal enforcement of the acquired claims", or "having refused to participate in a consensual settlement of the claim if holders of not less than two-thirds (by outstanding amount) of similar claims . . . agreed to accept the terms of the settlement".

A third approach, the New York Taxpayer and International Debt Crises Protection Act (hereinafter referred to as "NYTIDA") limits recovery of claims owed by indebted countries benefiting from an "international debt relief initiative" as defined in the bill, to the proportion that bilateral creditors agreed to recover under such initiative. It was initially introduced by Senator Brad Hoylman-Sigal and Assemblymember Patricia Fahy in May 2022.

1 Although technically the bill is not champerty in the traditional sense, it has become so widely known as such that this paper uses it. According to common law, champerty was the practice of someone (not otherwise involved in a lawsuit) agreeing to help finance the costs of a suit in return for a share of any recoveries in the action (Buchheit 2023, email on file with the author).

It builds on the "Debt Relief (Developing Countries) Act 2010" that the UK passed in 2010, which limited recovery in UK courts by private creditors suing beneficiaries of the Heavily Indebted Poor Countries/Multilateral Debt Relief Initiative.

Unlike the UK legislation, however, instead of naming a particular debt relief initiative, NYTIDA follows the approach of providing a general definition, thus enabling coverage of any current or future initiative that meets certain characteristics. The bill defines international debt relief initiatives as "any mechanism, framework or initiative in which the United States government and other sovereign states have engaged with international financial institutions and official and commercial creditors to advance the implementation and improvement of prompt and effective debt relief among eligible states".

To set the recovery limit, the bill defers to the burden-sharing standards set by the particular initiative. It uses as a proxy of a bilateral creditor's share "the proportion of the eligible claim that would have been recoverable by the United States federal government under the applicable international initiative if the United States federal government had been the creditor holding the eligible claim".

Successful experiences and practices

Each of the approaches tackles important issues that hobble sovereign debt workouts. They were introduced as separate bills in the 2023-2024 New York State Legislature session.

The Model Law prevents situations where a minority holdout creditor refuses to accept a majority agreement. A typical case is Argentina's 2005 and 2010 debt restructuring, which covered 93 per cent of bondholders and was challenged in court by a subset of non-participating creditors who demanded full payment plus past-due interest. The NYTIDA approach protects inter-creditor equity (or comparability) in situations where there is an international debt relief initiative and is particularly useful where private creditors en masse refuse to restructure – or to restructure in parity with the private sector. This is a common situation, as statistics reveal that private creditors usually get paid first and, on average, 20 per cent more than public creditors (Schlegl et al 2019). The Champerty approach protects against so-called "vulture funds" – private firms that purchase distressed debt at deep discounts with the intention of refusing participation in restructurings and suing for full payment.

In addition to providing responses to different problems, the approaches also operate in different ways. The Model Law requires the debtor to initiate bankruptcy-like proceedings in New York courts – therefore requiring, by design, use of the judicial system. NYTIDA and Champerty, on the other hand, operate as defenses that the debtor can utilise if being sued by a creditor under certain circumstances. They incentivize creditors to join negotiations and cooperate in consensual restructurings, and disincentivise their use of the judicial system to bypass such negotiations and agreements. While NYTIDA only limits the recovery for a creditor to what it would have received if it had participated in the negotiated restructuring, a successful Champerty defense results in the lawsuit being thrown out altogether.

In May 2023, the NYTIDA bill cleared the Judiciary committee in the Assembly, with bipartisan support, becoming the first bill on debt relief to move in the Legislature in 20 years.

While the different issues in sovereign debt restructuring that the bills tackle made them potentially complementary, the existence of multiple bills added to the challenges of communicating to lawmakers. Sovereign debt is a complicated topic with international finance and foreign policy dimensions that rarely come to the attention of New York State lawmakers. The experience of that first half of the session convinced proponents of NYTIDA and the Model Law that they could make gains by consolidating approaches in a single bill and they worked towards one bill with the two approaches during the fall of 2023.[2]

Senator Gustavo Rivera and Assemblymember Patricia Fahy introduced the consolidated bill, the Sovereign Debt Stability Act, in early 2024. Under the merged bill, debtor states would have the option to benefit from either the Model Law or the NYTIDA approach, by opting for one of them. They have the right to change their choice to the other regime once, any time before a restructuring is complete. The bill contains a severability clause that means if one of its provisions is held invalid, the invalidity will not affect other provisions, including that a sovereign can exercise its option to switch regime even if it before chose another that was subsequently declared invalid.[3]

In parallel, sponsors of the Champerty bill introduced an amended version in May 2024. Upon receiving comments from stakeholders, the bill was further amended and eventually cleared the Senate in early June. In the Assembly, however, by the end of the session the bill had not moved out of the Ways and Means Committee and did not get to a vote.

The May 2024 version of Champerty offered additions that could have gone some way to address problems targeted by the other bills.

It prescribed that instruments governed by the law of the state of New York imposed a duty on the holder to participate in good faith in a qualified restructuring affecting the instrument. For these purposes it defined a qualified restructuring as one where the IMF assessed the country's debt as unsustainable within the prior twelve months, provided that holders of at least two-thirds in amount and one-half in number of instruments accepted the modification.

The May 2024 version also tackled the pre-judgment interest rate that plaintiff creditors collect, currently a 9 per cent pre-judgement penalty on all overdue payment of interest. This high penalty is an incentive for bondholders to sue, especially in times when market interest rates are low (Rashid & Stiglitz 2020). Former US Undersecretary of Treasury for International Affairs Jay Shambaugh supported "indexing prejudgment interest rates to market rates." (2024) The bill set the rate in line with the market – using as a benchmark the "weekly average one-year constant maturity Treasury yield. . . for the calendar week proceeding [sic] the date of entry of the judgment awarding damages."

Media reports and commentary contrasted private creditor groups' support for this Champerty bill as a more targeted way to address sovereign debt restructuring concerns with their pushback against the Sovereign Debt Stability Act (Duguid & Cotterill 2024; Makoff, Setser and Weiss 2024). However, comments such groups and their allies submitted to the Champerty sponsors were very critical. The final form in which the bill was tabled and passed the Senate reflected this criticism by further narrowing down its application and limiting its provisions.

The bill that passed the Senate eliminated the provision establishing a duty of good faith. It also narrowed the bill's application. While the legislative intent in the May 2024 version excluded "conventional investors" from its application, this version also excluded an additional category called "cooperative investors". These are "distressed debt investors that regularly purchase debt at a discount in the secondary market and have a record of supporting the consensual resolution of sovereign debt distress through serving as a member of creditor committees or by generally participating in transactions accepted by other creditors following a negotiation". So, while the bill creates some meaningful obstacles

2 Although the initial attempt was to merge the three approaches, sponsors of Champerty decided to keep their bill separate.
3 A more integrating proposal consolidating the three bills has been attempted by Senior Counsel at Chatham Partners, Daniel Reichert-Facilides (2024).

to so-called vulture funds, it muddies the waters for debtors trying to use the defense. It does not conclusively prevent the action of these funds or enable a debtor to safely ignore their demands. The Senate-approved version maintained the reduction in the pre-judgment interest rate.

Unintended consequences

None of the reviewed bills passed yet, but claims about their alleged unintended consequences have played an important role in fueling opposition to them (ACLI et al 2023; International Institute of Finance 2024; Goss 2024). Because the types of reforms the bills promote are innovative and almost lack precedent, there is fertile ground for allegations that are not based on fact but rather on assumptions and speculation. Where one precedent exists, the 2010 UK legislation, it actually bolsters the case for the reforms.

It is worth noting that the arguments on unintended impacts that private creditors and allies wield resemble those they made to oppose the said UK legislation (UK HM Treasury 2010). In fact, because of the potential impacts, the UK Parliament passed the legislation initially on a temporary basis, with the intent to review it within a year. One year later, seeing that none of the consequences opponents warned about had materialised, Parliament made the law permanent. Several of the same arguments were raised in the late 1990s to reject the then emerging innovation of Collective Action Clauses (CACs) (Gugiatti and Richards 2003).

Below are in summary version the most recurrently argued unintended consequences and the way supporters of the bills answer them (Jubilee USA 2023; Fahy 2023; Caliari 2024).

→ **The legislation will bring uncertainty and disrupt markets, increasing the cost of borrowing for the debt-ridden countries it purportedly intends to help**

The proposals do not alter risk assessments for countries that determine the cost of borrowing, they only limit free-riding by any creditor at the expense of others. To suggest that this will affect borrowing rates implies that currently risk assessments by private institutions factor in an expectation of free-riding on bailouts from taxpayers or other private institutions. To the extent this actually happens, it would not be a sound practice or one to encourage.

→ **Sovereign debt contract issuance will move to other jurisdictions**

New York is a preferred place of financial operations because it is the foremost financial centre, and has liquidity, network externalities and agglomeration economies that no other jurisdiction can match. It is a favourite place for debt issuance because of the prestige it brings as a legal jurisdiction, with law that has been highly tested and jurisprudence built over decades. Issuing under another state would be too costly a move, not in parity with the size of impacts the legislation is expected to have. It is worth noting that emerging market and developing economies' sovereign debt continues to be a highly profitable asset, in spite of defaults and restructurings (Meyer et al 2019).

→ **Pension funds and other institutional investors will suffer losses that will negatively affect the assets of workers and individuals they manage**

On the contrary, pensions and savers with direct or indirect investments in emerging market and developing economies or companies based in them lose as a result of protracted debt restructurings that take a long time to bring an insolvent country back to profitability. The proposals will protect and boost pensions and others' savings by reducing the length and cost of debt crises and removing the distortion that free-riding lenders create in the lending industry.

→ **The legislation will disrupt emerging consensus on voluntary solutions and ongoing negotiations towards improvements in the sovereign debt restructuring regime, such as the Global Sovereign Debt Roundtable**

None of the remedies in the legislations is of mandatory use for any debtor. This means that there is no contradiction between the proposals and the consensual and market-based approach that some private actors seek to draw. On the contrary, to the extent that the latter approach works satisfactorily, there will be no need for the use of these remedies the legislation creates. Their existence, however, will be an important safeguard to hasten and smooth the process in such voluntary approaches and set incentives right.

Recommendations

People power matters

The legislation gathered support from a broad coalition of unions, major religious institutions, development and anti-poverty groups, diaspora leaders, notable economists, finance ministers from debtor countries, environmental organisations, as well as global debt networks and partners, and high-level United Nations officials (Jubilee USA 2024). Eventually, enlisting grassroots and grasstops' support across a breadth of constituencies translates into more cosponsors and brings bills higher up in prioritisation by leadership and the Governor, who can pull levers to advance them. The New York State Senate has 63 members and the Assembly 150. By mid-2023 the NYTIDA bill had 49 cosponsors (35 in the Assembly, 14 in the Senate), and the Model Law bill 38 (26 in the Assembly and 12 in the Senate). As the Sovereign Debt Stability Act combined efforts and constituencies that did not fully overlap before, it attracted the impressive number of 55 (43 in the Assembly and 12 in the Senate).

One might be sceptical about the relevance of sponsor numbers given that it was the Champerty bill, with fewer cosponsors (28 in the Assembly and 7 in the Senate), that moved furthest ahead. However, it is unlikely that bill would have gathered so much momentum if it were not seen by opponents as a more palatable alternative to more far-reaching bills that had a great amount of support.

Message benefits to debtor countries and also to the bond-governing jurisdiction/country and international financial system

The benefits from the legislation to residents, consumers, workers, businesses and the economy in New York and the United States need to be messaged at the same level as the benefits they will bring abroad. While this is a generally important advice campaigning in any advanced economy, it acquires special relevance with state-level lawmakers, such as in New York, which usually deal with more localised issues that can be easily connected to their constituents.

Align with US federal policy

It is a peculiarity of the US system that the law of choice that governs more than 50 per cent of sovereign debt contracts is not federal, but State level legislation, and it is also a State prerogative to regulate access to the courts that adjudicate them. The US federal government is cautious about any statement that may be seen as interfering with the legislative orbit of states.

However, given New York's position as a leading financial centre and the implications of the debt restructuring bills for global financial markets, state-level lawmakers do check the alignment of the legislation with US federal policy. Therefore, it is important to craft proposals in a way that aligns with US federal policy and that supporters be able to address questions about how the bills are compatible with and help promote such policy.

Evaluate tradeoffs between depth of reforms and ability to pass them – but don't fully buy into them

The legislative approach that moved closest to passage, Champerty, is the one with the narrowest scope of the three. By the time it reached the Senate floor, the influence of private creditors' groups had limited it further with loopholes that open questions about its capacity to operate as an effective remedy even for the limited range of actors and behaviours that it covers. At the same time, it is likely that in the existing political economy and given the powerfully resourced opposition, this was the price that had to be paid for the legislation to pass.

It may be easy to draw the disheartening conclusion that comprehensive and systemic solutions should not be tried. But that would be a premature conclusion to reach after the relatively short time span of two years – less than one if one takes the Sovereign Debt Stability Act — to campaign for such significant reforms. And one should not forget that the Champerty bill alone might have been without chances were it not for the presence of other more comprehensive approaches in play with real people power – thus, likelihood of becoming law — behind them.

A single focus on whether bills passed or how far they went may fail to capture the positive by-products of vibrant campaigning. The bills put private creditors in the spotlight and under pressure to behave in a more cooperative way. While a counterfactual is hard to estimate, since the bills have been under consideration few creditors have attempted to use the courts to sue countries that are renegotiating debt, and it is doubtful that "vulture funds" are pursuing their business model as usual. Free riders are on notice that taxpayers' and citizens' tolerance towards such behaviour and the associated consequences for people in debtor and creditor countries is not endless. The bills can also be credited with the renewed energy directed at finding concerted solutions in the Global Sovereign Debt Roundtable and other forua regarding matters that had hitherto eluded attention (e.g. standards for comparability of treatment). There is greater recognition of the gaps in existing solutions that result in a failure to involve private creditors in debt restructurings and the need for innovation.

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11. Germany and others financial centers

The Potential of national Legislation in Germany and other non-major financial centers on Private Sector Participation in international debt restructurings[1]

by Malina Stutz

Introduction

Over the last four years the debate on the potential of national legislation to ensure the participation of all creditors in international debt restructurings has gained new momentum. Since 2020 several bills have been introduced in the New York State Legislature aiming to restrict creditors' ability to sue debtor states and bring about enforcement. Those bills have been further modified and partly merged in recent years and have reached different stages in the formal legislative process (Caliari 2024). In Belgium – where a so-called "anti-vulture-fund law" has already been in place since 2015 (Belgian Legislator 2015) – the adoption of an even more comprehensive law has also been discussed over the past two years (Belgian Legislator 2023). When the bill was initially not adopted in a vote in Parliament in April 2024, this held up the process but did not yet end it. The adoption of a corresponding law is also being discussed in the UK by politicians (Debt Justice UK 2023), civil society (CAFOD, Debt Justice UK, 2023) and academics (Connelly et al. 2024). However, in the UK a new legislative proposal has not been introduced into the ordinary legislative process to date. The situation is very similar in Germany (see below, section 2.4). Thus, debates on the introduction of corresponding laws are taking place within the two most important financial centres (London and New York) as well as outside those jurisdictions (Belgium and Germany). This background paper aims to contextualise the current legislative initiatives and reflect on their potential while posing a special focus on legislation outside the major financial centres.

Legislative initiatives

Context of the debate on national legislation on private-sector participation

The current debates and legislative initiatives must be understood against the following background:

First, the debt crisis in countries of the Global South has worsened dramatically over the last decade with a major hike since 2020 (UNCTAD 2024); second, with a share of around 60 pecent, private creditors hold the majority of outstanding claims against countries in the Global South (Stutz 2024); third, the slow and patchy participation of the private sector continues to be one of the central challenges for equitable and efficient sovereign debt restructurings (Zucker-Marques 2023); fourth, legal action by private creditors against defaulting debtor governments increased steadily over the 1990s and 2000s, with 50 per cent of restructuring negotiations in

1 *The paper was finalised in 2024.*

the mid-2010s being accompanied by legal action from individual creditors against the defaulting debtor state and 50 per cent of these lawsuits being accompanied by seizure attempts (Schumacher et al. 2018); fifth, when discussions on national legislation reemerged in 2020-2021, there was no political will in the international community to create an international sovereign debt workout mechanism, nor any developments that suggested progress on the multilateral level. Particularly with the perspective of the Fourth International Conference on Financing for Development (FfD4) this has changed today, and this change must be considered when formulating recommendations (see below section 5).

The negative consequences of lawsuits and seizure attempts

To understand the potential of national laws in different jurisdictions to ensure private creditor participation in debt restructurings, it is first necessary to understand the various costs associated with litigation and seizure attempts.

First and most obvious, there are direct financial costs associated with lawsuits, as debtor countries have to pay the costs for defense in legal disputes. Further, debtor states are charged high interest on arrears for the duration of the lawsuit. If plaintiffs successfully obtain a legal title in court for full repayment and debtor states service these claims, this process leads to more financial burdens and limits the scope of debt relief effectually granted within a restructuring.

Second, litigation makes it more difficult to bring restructuring negotiations to a successful conclusion. The willingness of other creditors to accept debt cancellation may decrease because they fear that their concessions will only be used for preferential payments to the holdout creditors. In the current litigation case *Hamilton Reserve Bank v. Sri Lanka* the court actually granted a stay because it feared that a ruling could disrupt the debt restructuring negotiations and provoke a rush to the courthouse by other creditors (Cote 2023). Further, debtor countries may often find themselves being confronted with conflicting demands from the different creditors: on the one hand they might be confronted with the legal ruling to pay back a plaintiff in full; on the other hand, they might have entered a restructuring agreement with their other creditors that oblige them to seek a comparable treatment from all creditors. Recently, it has become more popular to include so-called most favoured creditor clauses in debt restructuring agreements. In this case, compliance with the judgement to fully compensate a plaintiff creditor would result in other restructuring agreements with other creditors losing their effectiveness — or more precisely, most favoured creditor clauses would oblige the debtor country to compensate its other creditors in a similarly advantageous manner to that enjoyed by the plaintiff creditor.

Third and most important, non-compliance with the judgement to fully compensate a plaintiff creditor may lead to sensitive economic cost, though such costs are very difficult to predict. In recent years, 50 per cent of litigation cases were accompanied by seizure attempts (Schumacher et al. 2018). Seizure attempts remain a very risky business and are by no means always successful, as a large share of the assets of debtor states located abroad are protected by state immunity. In very rare cases, however, creditors were highly successful: The emblematic New York court ruling against Argentina in 2012 prevented Argentina from servicing the claims of good-faith creditors and threatened to make these funds accessible to the plaintiff, forcing Argentina into a second default and ultimately into repayment to the plaintiff creditor (ibid. p. 42). Similarly, the series of attachment attempts launched by some US-based hedge funds against the Republic of Congo from early 2000 onwards led to the Republic of Congo's oil exports being blocked for years (ibid. p. 69). Further, scholars have found evidence that pending litigation and seizure attempts make access to the capital markets more difficult for the debtor state – possibly also due to the risk that plaintiffs could obtain access rights to the proceeds of newly issued bonds or repayments to creditors (ibid.).

Finally, it must be stressed that the real costs lie in the mere possibility of litigation and the uncertainty of the associated costs. The associated economic costs are especially hard to predict, but in rare cases can be very damaging. Thus, this uncertainty alone substantially increases the bargaining power of creditors vis-à-vis the borrowing country. It can be assumed (and sometimes heard in informal conversations with government officials) that the fear of lawsuits prevents governments of debtor countries from being more demanding in negotiations with their creditors and from insisting on more extensive debt cancellations. Currently we do not see many litigation cases with *Hamilton Reserve Bank v. Sri Lanka* being the only current case (Stutz 10.04.2024). However, we do also not see debtor countries being very demanding in the restructuring negotiations but are rather tending to accept debt restructurings with "too little" debt cancellation (Stutz 2024). Furthermore, the threat of lawsuits strengthens governments in the implementation of creditor-friendly policies at home vis-à-vis the domestic opposition. It is difficult for the opposition to present a more demanding stance vis-á-vis foreign creditors as a real policy option given the uncertain costs of possible lawsuits.

The potential of national legislation outside the major financial centres

In general, national legislation on private-sector participation does — in most cases — not formally oblige the private sector to participate in debt restructurings but limits the amount that is legally enforceable to the amount agreed upon in a debt restructuring. National laws therefore seek to reduce the various costs associated with litigation and seizure attempts and create more certainty for debtor states and good-faith creditors.

It is most urgent to have these laws adopted in the UK and New York, as virtually all bond contracts of countries in the Global South that are not governed by the law of the borrowing country are governed by the laws in those jurisdictions. This concentration of applicable law means that most lawsuits are brought before New York or British courts. However, the power of creditors is also based on the fact that the civil procedure laws of most countries and an increasing number of international treaties allow creditors to sue for their claims before other courts and to enforce claims obtained in New York or in other jurisdictions. For example, German-based creditors have brought lawsuits against Greece (BVerfG 2 BvR 331/18) and Argentina (BVerfG 2 BvR 824/15, BVerfG - 2 BvM 1/03) in the context of the respective restructurings before German courts, even though their claims were not governed by German law. In the emblematic case of Argentina, the plaintiff NML capital had obtained a judgment in a New York court. However, when NML capital tried to enforce the judgment, the hedge fund also tried to seize an Argentine naval vessel anchored off the Ghanaian coast and an Argentine dinosaur fossil that was on expedition in Europe (Schumacher et al. 2018, p. 13). These seizure attempts were ultimately not successful. However, the uncertainty created by those attempts might have been one reason why Argentina was not able to issue new international bonds at that time (ibid.). When NML Capital finally managed to obtain the right to access payments made by Argentina to its cooperative creditors, the New York judge also issued an order to Euroclear to not carry out any debt-service payments in the Argentina case (Reuters 2015). Euroclear is a Brussels-based clearing house through which many countries in the Global South process their payments to creditors.

These examples show that laws to limit a creditor's rights to sue and enforce judgements are also helpful outside the major financial centres. They can make the respective jurisdiction in which those laws are enacted a so-called "Safe Harbour" for the debtor states: creditors who have obtained a judgement elsewhere would then be unable to enforce that judgement by seizing assets located in or transferred through a jurisdiction that has enacted a corresponding law. This reduces in particular the associated economic costs that are hard to predict but can in rare cases be very damaging (see above). In principle, the adoption of such laws would make sense everywhere – not only in the most important financial centres and not only in Global North countries. Any such law in any country would somewhat limit the power of creditors, and somewhat reduce the negative costs associated with seizure attempts for debtor states. However, the larger a country's foreign trade and financial sector are, the greater the protective effect of a corresponding law.

Legislative initiatives in Germany.

Since Germany has a very large foreign trade sector and a relevant financial sector, the adoption of a Safe Harbour law could also make an important contribution in Germany.

In Germany, as elsewhere, the debt crisis in countries of the Global South moved more strongly on to the political agenda as the situation worsened due to the Covid-19 pandemic in 2020. In the 2021 parliamentary elections, all parties that finally made it into Parliament – with the exception of the far right-wing party – stressed the need to reform the international debt architecture in their election manifestos (SPD 2021, p.62, FDP 2021 p.50, Grüne 2021 p.244, Linke 2021 p.117, CDU/CSU 2021 RN686-688). After the 2021 elections, a governing coalition was formed between three parties – the Social Democrats, the Liberals and the Green Party. All three parties had stressed the need to involve the private sector in debt restructurings in their election manifestos, although with slightly different colourings. The Green Party had further formulated the ambition of enacting a national law to ensure private-sector participation. In the coalition agreement, the goal was finally agreed "to support an initiative for a codified international debt workout mechanism that includes all creditors and implements debt cancellation for particularly vulnerable groups of countries" (SPD, Grüne, FDP 2021, p.154). In the coalition agreement the parties have agreed on common goals for their time in government. Although this agreement is not a legally binding document, it is easier to implement political measures if they have already been agreed as a common objective in the coalition agreement. Further, the coalition agreement is an important basis for parties and MPs to hold their own government representatives accountable.

In Germany, issues relating to international debt policy are primarily dealt with by the Ministry for Economic Cooperation and Development and the Ministry of Finance, with the latter generally taking the lead. In 2022 the Federal Ministry for Economic Cooperation and Development commissioned a study to examine the potential and feasibility of various measures that the government could use to improve the participation of private creditors in debt restructurings. The study was published in May 2024 titled "Statutory and Policy Measures to Enhance Private Sector Participation in Sovereign Debt Restructuring" (Hinrichsen et al. 2024). It concludes that the enactment of safe harbour legislation is the most promising option:

> *"Limiting enforcement action through the court system is the most direct and efficient domestic tool to implement comparability of treatment across all creditor groups and enhance private creditor participation. Among domestic measures, safe harbour legislation also corresponds most closely to the agenda to promote rules for sovereign debt relief across all relevant creditor groups, which the German government has set itself in the 2021 coalition agreement"*

Within the Parliament, there was cooperation between key representatives from all three governing parties, who were working towards a corresponding law being passed before the end of this legislative period (i.e. by end-2025).

Since 2021, the debate on safe harbour legislation has also intensified within academia. In particular, the lawyer Daniel Reichert-Facilides published a first draft of a model law in 2021 and has since amended it several times (Reichert-Facilides 2023). erlassjahr.de has also been intensively involved in the debate since 2021 and has presented a list of elements that it believes should be included in a corresponding law (Stutz 2023). At present, it is necessary to wait until a bill is introduced into the ordinary legislative process.

Successful experiences and practices

As no corresponding law has yet been passed in Germany, no conclusions from successful experiences and practices can yet be derived. However, lessons can be learnt from the adoption of similar laws elsewhere. Specifically, there are already comparable laws in Belgium, France and the UK, all of which have certain weaknesses (for a detailed analyses of the strengths and weaknesses of the different pieces of legislation see Stutz 2023).

The intent of the British Debt Relief (Developing Countries) Bill was to curb lawsuits against Heavily Indebted Poor Countries (HIPC) states (British Legislator 2010). This target was mostly met: While a total of 12 lawsuits were brought against HIPC states in British territory up until 2009, only one creditor brought a lawsuit before British courts after the 2010 law was adopted (Stutz 2023 and sources cited therein). Since the law also restricts the enforcement of already disputed legal titles, it has also helped to enforce more favourable solutions for debtor states even in cases where a judgement had already been made before the law was adopted. This happened in *Hamsah Investments and Wall Capital Ltd. v. Liberia*. In 2009, a British court condemned Liberia to repay 20 million US dollars to the suing investment fund. This was much more than the amount creditors would have received for their claims if they had participated in the HIPC initiative. The law improved Liberia's negotiating position, and the two parties were able to reach an out-of-court agreement on a repayment amount of 1.3 million US dollars in 2010 (Dearden et al. 2010).

In addition to the fact that the number of lawsuits filed against HIPC countries decreased significantly after the law was passed, further lessons can be learnt from the discussion at the time before the law was enacted and the arguments put forward by the various parties: In July 2009, the British government announced its intention to take corresponding statutory measures and consulted stakeholders in public hearings until October 2009 (British Treasury 2009). As part of the public consultation process, international law firms and the Emerging Markets Trade Association argued that the law would jeopardise the attractiveness of London as a financial centre, unlawfully encroach on creditors' property rights and make it more difficult for HIPC countries and other low- and middle-income countries to receive finance in the future (Townsend 2010). As a result of these concerns, the law finally obtained the necessary majority in May 2010 only through the inclusion of a sunset clause. This clause provided that the law was to expire after one year. In 2011, the British government stated that no negative side-effects had been observed, whereas the law had created relief for some HIPC states. Thus, the permanent effect of the law was confirmed.

Similar lessons can also be learnt from the discussion on the adoption of the Belgian law in 2015: shortly after the announcement of the legislative initiative, pressure from national and international financial lobby groups in opposition to the law became stronger. Lobbyist groups, including the Belgian Financial Sector Federation and the Institute of International Finance, as well as the Belgian Central Bank, intervened, with the Minister of Finance and the chairperson of the Parliamentary Finance Committee arguing that the functioning of secondary markets would be harmed by the law and that contractual rights of creditors would be unduly restricted by arbitrary criteria (Sourbron, Vereeck 2017). However, legislators rejected all objections raised, and the law was finally passed in July 2015. After the law was passed, NML Capital brought legal action before the Belgian Constitutional Court on the grounds that the law was unconstitutional because it infringed NML Capital's property rights, discriminated between creditors in an improper way, and arbitrarily recognised some claims as legitimate and others as illegitimate (Wozny 2017, p.743). The fact that NML Capital, a classic hedge fund, has filed a lawsuit against the law, must be seen as a sign that it saw its position weakened by the passing of the law — even though Belgium is not a major financial centre. The Belgian Constitutional Court dismissed the lawsuit in 2018 and maintained the law in its entirety (Iversen 2019).

Parliaments intending to pass corresponding laws must be aware that massive resistance from the financial industry is to be expected. This was already evident when the British and Belgian laws were passed. The counter-pressure is likely to be many times greater if the law seeks not only to safeguard initiatives that have already been completed, as in the British law, and if, unlike the Belgian law, it is designed to have an effect on all creditors and not just on classic vulture funds. Both Belgium and the UK have been able to create legislation despite massive lobbying against it. Furthermore, they have done so without endangering the attractiveness of their financial jurisdiction or causing other negative consequences, for example, increasing the costs of lending to low- and middle-income countries. When introducing national laws to limit the enforceability of claims, it is therefore essential that parliaments learn from the experience of previous battles.

Unintended consequences

Most frequently the financial industry argues that corresponding laws could jeopardise the attractiveness of the financial jurisdiction enacting a corresponding law and reduce the willingness of private lenders to lend to countries in the Global South. Both threats have proved to be empty in the past (see above). Nevertheless, poorly designed laws may potentially have both these effects. However, these undesirable side-effects can be avoided if the relevant laws are designed sensibly. In order not to jeopardise the attractiveness of one's own financial centre through a corresponding initiative — which could make it more difficult to obtain a majority for the initiative — laws should be designed in such a way that they not only restrict the enforceability of claims made under one's own law, as this would disadvantage creditors who choose this law in their contracts. Rather, the enforceability should be restricted irrespective of the law under which the claims were issued. This is also the case in all existing laws in the UK, Belgium and France (Stutz 2023). In order not to reduce the willingness of private creditors to give loans to Global South countries, laws should be formulated as precisely as possible and create little uncertainty that legal action may also be restricted in cases that were not intended by the legislator.

However, there are other unintended consequences to consider when adopting national laws. The biggest pitfalls can arise in determining the circumstances when legal action and enforcement should be restricted. It would be most desirable to reduce the legally enforceable amount to the level considered sustainable in an international fair and transparent restructuring procedure that respects and prioritises the fundamental human rights of the population of the debtor countries. However, there is no such procedure at the international level. Therefore, when formulating corresponding laws, a balance must be found so that these laws enforce private-sector participation in debt restructurings that are currently taking place (e.g. within the G20 Common Framework) while staying open for future progressive developments that can only be achieved within a multilateral process. Thus, it is most important not to define international debt restructurings for the purpose of a corresponding law by features that characterise current international restructurings but that are not desirable from a debt justice perspective.

Recommendations

Erlassjahr.de has listed a number of elements that should be considered when formulating national legislation to restrict the legal action of creditors and sorted them according to the two criteria of efficiency and equity (Stutz 2023). However, the requirements of different jurisdictions and political systems must be considered when drafting corresponding laws, so that it is not possible to create a blueprint that can be used in all jurisdictions. However, from the point of efficiency the following aspects would be desirable. First, all countries, regardless of their income status or other classifications, should benefit from the protective effect of a corresponding law. Second, a corresponding law should not solely focus on particularly aggressive creditors such as the so-called “vultures” but rather limit the legal action for all private and public creditors to the amount agreed upon in an international restructuring. Third, unlike the UK Debt Relief (Developing Countries) Act of 2010, which only retroactively protected the so-called HIPC debt relief initiative, national laws should be constructed in a forward-looking manner and thus also safeguard future restructurings. Fourth, a corresponding law should have an effect on all claims, regardless of the law under which they were issued. Fifth, the enforcement of legal titles and arbitral awards obtained elsewhere should be limited to the extent that could be obtained in national courts within the meaning of the law.

From the point of equity, the following aspects should be considered: First, the goal of minimising the negative effects of debt crises on the economic, social and cultural human rights of the debtor country’s population should be explicitly stated. Second, a corresponding law should provide the possibility of protecting international debt restructurings that are not approved by a (super-)majority of creditors since it is not to be expected that a majority of creditors will always be willing to provide the amount of debt cancellation that is needed from a human rights perspective. Third, a law that aims to protect the outcome of international restructurings should be formulated in such a way that it remains open to future developments at the international level. Thus, current frameworks and their characteristics – such as those of the Paris Club or the Common Framework – should not be cited as the only point of reference for defining international debt restructurings for the purpose of a corresponding law. Fourth, debtor countries should be strengthened in the negotiations with their creditors by granting a temporary protection against enforcement for the period of the negotiations and by limiting the default interest that creditors may legally enforce. Fifth, ways should be explored to improve the legal defence on the basis of the odiousness of certain claims and the incompatibility of debt repayment with public obligations to protect the human rights of a debtor country’s population. Sixth, consideration should be given on how transparent disclosure of creditors can be increased by the enactment of a corresponding law.

Finally, when combining forces to fight for international debt justice, the current dynamics at the international level and the fact that there will be a Fourth UN Conference on International Development Finance (FfD4) in 2025 must be considered. With regard to the issue of national legislation, this means two things. First, the international debt justice movement may advocate that the creation of corresponding laws is formulated as a goal in the final communiqué of FfD4, going beyond the agreement in the Addis Ababa Action Agenda (AAAA). The AAAA encouraged countries to enact so-called anti-vulture fund laws (UN 2015, p.45). Second and most important, FfD4 provides an opportunity to make progress with regard to the international debt architecture which, unlike the enactment of national laws, cannot be achieved step-by-step but requires a genuine multilateral process. This includes, in particular, the initiation of an intergovernmental and binding decision-making process to reform the international debt architecture – possibly in the form of a UN debt framework convention. Among the elements that could be agreed within such a framework are the establishment of a UN-based institution to coordinate negotiations in the event of debt restructurings and the development of alternative, human-rights-based debt sustainability analyses. These opportunities, which were not available in 2020-2021 when the discussion about national laws gained momentum, should not be ignored by focusing primarily on national legislation issues.

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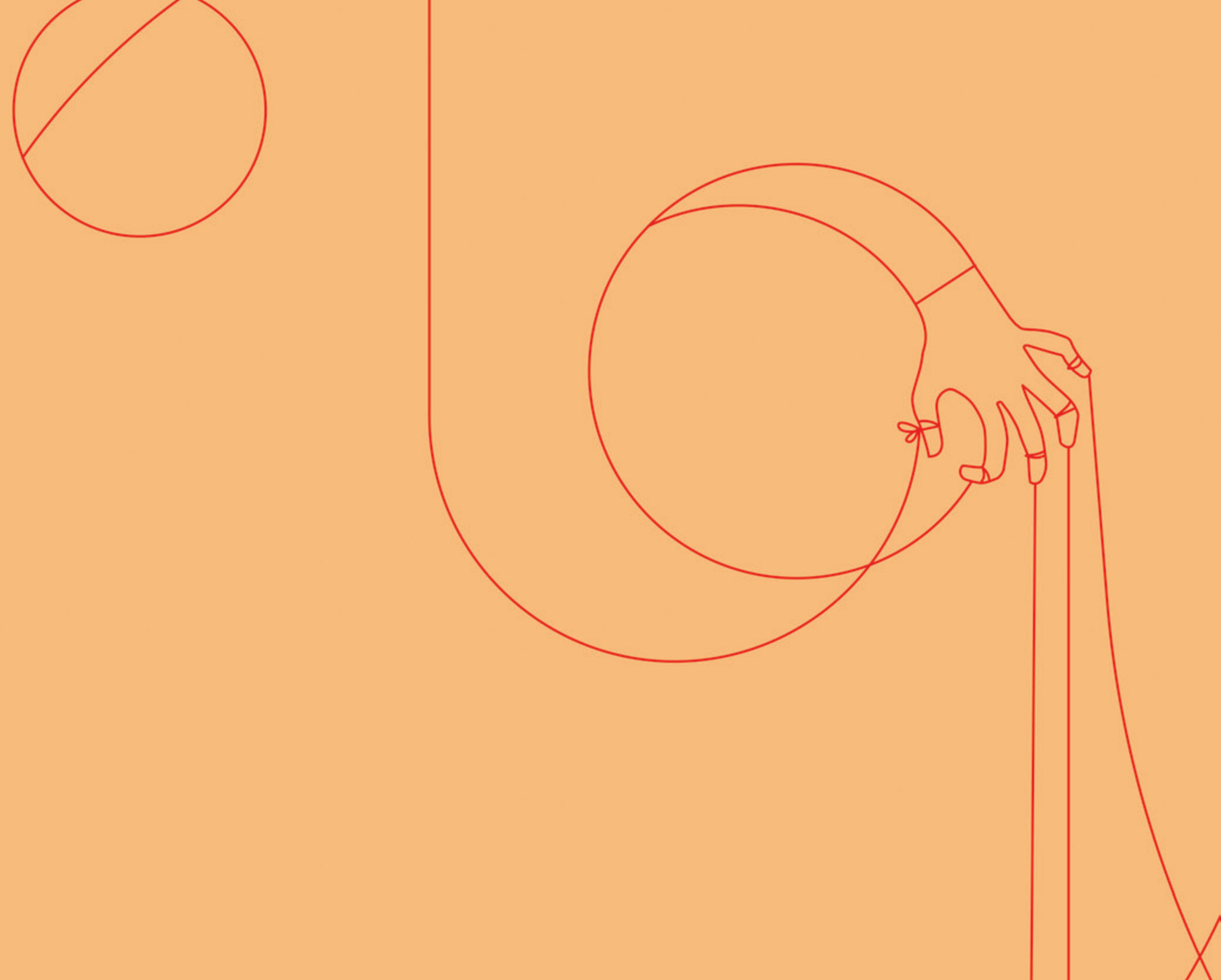

Conclusions

Conclusions

The findings presented in the Dossier highlight a clear reality: the debt crisis faced by developing countries is not inevitable but stems from systemic failures in debt management frameworks, inadequate parliamentary oversight, and insufficient transparency requirements.

Advocating for stronger legislative oversight—such as increased transparency in international financial agreements—and greater public participation is not just timely, but also urgent. Parliaments have a crucial role in driving accountability by exercising their oversight powers, amplifying citizens' voices, and ensuring that governments make decisions that truly serve the best interests of the people.

The experiences of countries like South Africa, Kenya, Ghana, and others, as exposed by the Dossier, demonstrate that unchecked borrowing undermines socio-economic equity, fosters dependency, and exacerbates fiscal vulnerabilities. To escape from these cycles, countries should adopt legislations that promote transparency, fiscal responsibility, incorporate social and environmental impact assessments, and strengthen the role of both parliaments and the public in financial decision-making. In Argentina, for instance, the establishment of Legal frameworks like the Public Financial Management Law in the ‘90s, improved state capacity for debt management and transparency. It also enhanced legitimacy and accountability of the debt cycle by allowing Congress' involvement.

Improving domestic legislation is not only a technical imperative but also a moral and political one, as sustainable debt management is, and demonstrated by the experiences of countries, essential for upholding human dignity and fostering equitable growth. Public policies and international actions play a vital role in capacity development. Ultimately, it is crucial to understand and address these challenges faced by lawmakers when designing future capacity-building initiatives to ensure their success. That is why, the End the Debt Trap Project becomes a crucial initiative that could add significant value in the current juncture.

End the debt trap

This publication examines case studies from Sub-Saharan Africa, South Asia, Latin America, and the Middle East to highlight systemic weaknesses in debt governance. Through comparative analysis and experiences of concrete countries, the Dossier advocates for legislative reforms that emphasize transparency, accountability, oversight, and sustainability in public finance management.

By connecting these reforms to human rights, economic equity, and environmental sustainability, the Dossier contributes to the international debate by providing a practical roadmap for nations to escape the debt trap and protect their developmental goals. The chapters, authored by experts and civil society representatives, offer lessons learned, actionable recommendations, and insights into the unintended consequences of selected cases.

This initiative is led by the Friedrich-Ebert-Stiftung, that is activating its global network of over 100 offices and partner organizations to help end the debt trap. It stems from the international advisory group "End the Sovereign Debt Trap," which brings together experts and political actors committed to a profound reform of the international financial architecture. The group aims to influence political and technical debates, engage with global decision-making processes, and bring progressive perspectives into key spaces.

Further information on this topic can be found here:
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