



**FORUM 2000: BRIDGING GLOBAL GAPS CONFERENCE  
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**OUTCOME OF THE WORKSHOP**

**External Debt: Issues of Sustainability and Legitimacy**

**Current state of the problem:**

The question of legitimacy of claims on southern countries is normally ignored when a sustainable level of debt is determined. Such a practice legitimizes such debt and will cause lenders to behave irresponsibly again in the future. Iraq with a total debt of approximately 380 bn US/Dollars and a GNP of 25 bn is a star case of not just an unsustainable burden, but also of highly questionable claims by creditors who financed the dictator's military buildup and affluent lifestyle.

As it is clear that financial crises will be reoccurring in the middle-income countries, the need for a comprehensive workout mechanism for unsustainable foreign debt is undeniable. However, the Sovereign Debt Restructuring Mechanism proposal didn't receive the necessary supermajority of 85% to be approved by the member states of the IMF. Even though, 70% of the IMF constituency wanted to continue discussing the mechanism on the grounds of the IMF, the position of USA has shelved the proposal.

The HIPC initiative although it has been a step forward in providing a framework for debt relief didn't fulfill the initial goals and has to face a reform in the near future.

The Millennium Development Goals cannot be reached without having more resources available via debt relief and additional aid.

**Areas of agreement:**

- It is desirable and necessary to include the issue of legitimacy in standard procedures in international debt management.
- If democracies were lending irresponsibly to illegitimate governments, the tax-payers should assume the burden of such mismanagement. However in cases where the lending government cannot be considered legitimate itself a new standard of accountability needs to be established.
- If a more representative voting structure cannot be found in the IMF, alternative approach (like the NGO proposal for a Fair and Transparent Arbitration Process) has to be found.

- Code of conduct that would not legally bind the creditors into a debt-workout cannot be the basis of a debt-restructuring framework.
- Accountability of the creditors needs to be ensured:
  - Bilateral donors (ie. governments of the developed states) should be held accountable through the pressure of the tax-payers who would in effect pay for an irresponsible behavior of their governments.
  - Odious (ie. illegitimate) debt doctrine is a promising concept, which may be used in some cases to put responsibility on the shoulders of the creditors.
- To ensure the accountability of both the creditors and the debtors lendings must be transparent.
- HIPC 2 initiative is definitely not sufficient to provide necessary debt relief for poor countries.
- The current definition of debt sustainability has to be redesigned and must include a broader range of use from non-creditor institutions to reflect better the real impact of debt cancellation on poverty reduction. The definition must explicitly take into account the resource needs for reaching the MDGs.

#### **Areas of disagreement:**

The participants didn't agree

- Whether the Odious debts doctrine can be applied given the critical issues of implementation.
- In what form the multilateral lenders (IMF/WB) should be financially responsible for their mistakes or even culpable for them.
- Whether it is feasible at all to approve and implement a worldwide insolvency framework or restructuring mechanism outside of the Bretton-Woods institutions and whether such agreement could be enforceable.
- Whether additional international financial institutions write-offs could be financed out of the institutions reserves without endangering in the short term their financial standing.

#### **Recommendations:**

- The legitimacy of debts inherited from oppressive regimes has to be evaluated and governments should cooperate in providing all the necessary documentation to both official and independent assessors.
- To ensure transparency, accountability and have a better picture of the legitimacy of debts, independent forensic auditing should be used as much as possible to assess the validity of debts.

- All market participants as well as civil society should be encouraged to work on further proposals regarding an independent debt workout mechanism which would comply with standards of the rule of law.
- For the imminent case of Iraq's foreign debt it is recommended that
  - Under a public and transparent process external debts are assessed for their validity and legitimacy before any debt servicing is resumed.
  - A political initiative is taken to organize a comprehensive debt conference after the donor conference taking place next week in Madrid, which would include all stakeholders, particularly Iraqi civil society groups.
- Redesign HIPC 2 so that
  - more countries are involved,
  - more flexibility in the application of conditionalities and evaluation of country performance for the countries that go off track are applied,
  - higher debt relief is provided.
 If it doesn't deliver after that, then it needs to be substituted by a new framework.
- The civil society as well as the international institutions have to increase the pressure on the governments of the developed north in order to make them comply with their previous pledges in particular the MDGs and the Monterrey Consensus. This includes an increase in the amount of aid and the assessment of debt sustainability, which explicitly takes into account the amount of resources needed to achieve the MDGs.
- More considerations must be given to assessing the most efficient use of additional resources. Particularly, the tradeoff is between debt relief and other forms of financing and assistance.

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