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Chapter 9/11?

Resolving international debt crises – the Jubilee Framework for international insolvency

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An NEF report by Ann Pettifor

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"An invasion of armies can be resisted; but not an idea whose time has come."

Victor Hugo

Executive summary

Origins of the Jubilee Framework

Jubilee 2000 first began campaigning for an independent framework for resolving international debt crises in 1995, when a global petition calling for a 'fair and transparent process' for writing off debts was drafted. This was subsequently signed by 24 million people in more than 60 countries of the world.

The **Jubilee Framework** has evolved as a result of debate, over many years, in both the north and the south, on the most appropriate, and most democratic mechanism for resolving debt crises. The British movement has worked closely with campaigns in Europe, Asia, Africa and Latin America; with the UN Secretary-General; with Yilmaz Akyuz, chief economist of UNCTAD and his staff; and with academics, including Professors Kunibert Raffer of the University of Vienna and Prof. Jeffrey Sachs of Harvard – in developing the concept.

Chapter 9 or Chapter 11?

The debate, over many years, has focused on whether Chapter 9 of the US legal code (which applies to governmental organisations like municipalities) or Chapter 11 (which applies to corporations) is the appropriate model. The Jubilee movement, on the whole, prefers the Chapter 9 model, because US law protects the rights of taxpayers and employees to participate in, and if necessary object to, the outcome of the governmental insolvency process.

Why now?

The relevance of the Jubilee Framework to the international financial system has been clearly highlighted by the devastating insolvency of Argentina. The report briefly examines the situation in that country, and the co-responsibility of both creditors and debtors for the crisis.

This report shows that, contrary to the assertion of Ms Kreuger of the IMF, the Jubilee Framework could be put in place immediately to resolve the crisis in Argentina.

The essential characteristics of the Jubilee Framework

- The very existence of a framework, enabling any indebted nation to file for a standstill on debt payments; or for her |creditors to declare her insolvent, will be a form of regulation of international capital flows; and will discipline both lax lenders and reckless borrowers.

- The **Jubilee Framework** could apply to **all** indebted countries, not just those the IMF deems insolvent.

- The criteria for petitioning for a standstill would be determined by the debtor nation. For the Jubilee movement, debts that can only be repaid at a cost to the fundamental human rights of the population, are deemed unpayable debts.

- The **Jubilee Framework** would remove international creditors, like the IMF, from playing the role of plaintiff, judge and jury in the event of international debt crises. Central to the framework would be the independence of the insolvency court.

- The court would be an ad-hoc body, appointed to deal with each individual petition for insolvency. It would not require an international treaty.

- The **Jubilee Framework** would accept the IMF as a 'portal' or 'gateway' to the process, given the vital role that the Fund will play in assembling working capital for the sovereign debtor during the debt standstill period.

- However under the **Jubilee Framework**, the IMF would not be able to influence the appointment or the proceedings of the ad-hoc, independent panel. The role of ensuring the independence of the panel should be assigned to the *Secretary General of the United Nations*.

- The composition of the court would be determined by the sovereign debtor on the one hand, and creditors on the other. Both sides would nominate one representative each; the two representatives would then choose a third, in whom they both have confidence – to act as the judge.

- Within the **Jubilee Framework**, the proceedings of the court will be transparent and accountable both to creditors; but most importantly, to the citizens of debtor nations.

- The court will assess all debts; and ascertain if they were contracted legitimately.

- Fundamental to the **Jubilee Framework** is *public participation* in the proceedings of the court, and in the resolution of crises involving public money. Accountability to the electorate of government officials responsible for reckless borrowing in *debtor* nations; and for lax and corrupt lending in *creditor* nations, will, we believe, introduce discipline into the lending and borrowing process, and challenge corruption.

- The **Jubilee Framework**, like Chapter 9 of the US legal code, will give rights to citizens to comment on the economic soundness of the court's 'composition plan'; and give taxpayers the right to object to the plan.

- The **Jubilee Framework** is the first vital step towards democratising international capital markets, and thereby, the project known as 'globalisation'.

The Jubilee Framework

Introduction

by Ann Pettifor[1], London, January 2002

With this report, we are promoting an international insolvency framework – **the Jubilee Framework** – that will involve citizens in the resolution of international debt crises, and will, we believe, be the first vital step towards democratising international capital markets and therefore the global economy as a whole. The de-regulation of capital markets, from 1979 onwards, has led them to become detached from democratic institutions in nation states. Introducing an insolvency framework will introduce regulation and discipline over the flows of international capital – through lending and borrowing. It will do so not just in bankrupt states; but in states where lax lending and excessive borrowing could lead to bankruptcy. In other words, the very existence of the framework could help regulate capital movements, and prevent future crises.

If our framework is adopted, it will be possible for citizens of poor borrowing nations, and citizens in rich, lending nations to strengthen their monitoring and control over the international lending and borrowing policies of their governments; and through them, affect international capital markets. Such democratic surveillance of international capital markets will, we believe, help discipline the unfettered and liberalised capital flows that have been central to the 'globalisation' project.

Of course such democratisation will only occur if our framework is adopted. And that will only happen if people around the world mobilise and struggle for these changes in the positive and constructive way they mobilised and struggled behind the global Jubilee 2000 movement for debt cancellation. Only by imposing the democratic will of the people on international capital markets, will it be possible to ground these markets in the reality of human societies and human rights, in the reality of endangered environments; and in the reality of democratic political relations.

We know it can be done. By mobilising and protesting, the international Jubilee 2000 movement, in just four years of campaigning, pushed third world debt to the top of the global agenda; and forced the world's most powerful creditors, the G7, to agree to cancel $100bn of the debts of the poorest countries.

As we note in the opening chapter, the ordinary people of Argentina, using pots and pans, have, without political leadership, and in just a few days, deposed a President and a powerful finance minister; unsettled international markets; imposed losses on international creditors; reversed long-standing economic policies; weakened the authority of the IMF; and are now demanding democratic elections of reluctant politicians. How much more can a global movement of ordinary citizens achieve?

We in the international Jubilee 2000 movement are seeking to reverse the malign influence of neo-liberal economists who have embarked on what the Austrian economist Karl Polanyi described as a starkly utopian project: the disembedding of the 'globalised' economy from society, from the environment and from democratic institutions.[2] We are determined to transform the international financial system into one that is embedded – in democratic, social, environmental and political relations.

That is the ambition of the wider Jubilee 2000 movement. And that, and nothing less, is the ambition of this report and of the 'the Jubilee Framework.'

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1 I am grateful to a number of people for help in producing this report. First among them is Professor Kunibert Raffer of the University of Vienna, whose ideas and arguments form the basis for this report. But I am also hugely indebted to Jurgen Kaiser of the German Erlassjahr campaign; and to my colleagues in the Indonesian, Argentine, Ecuadorian, Australian and African Jubilee 2000 campaigns.

2 See 'The Great Transformation' by Karl Polanyi, published by Beacon Press, 2001, with an introduction by Fred Block of the Dept. of Sociology, University of California, Davis.

Why now? Argentina's urgent need for crisis resolution

As we go to press, in January, 2002, an economy that was once the world's seventh largest – Argentina's – is effectively in liquidation. The crisis has only just reached a head, but back in October, 2001, Michael Mussa, (until recently the IMF's chief economist) noted that Argentina was 'not solvent by any stretch of the imagination.'[3]

This bankruptcy of a once vibrant economy is taking place in a brutal, uncivilised and inhumane manner - one that denies basic human rights to the people of Argentina, and that is inconsistent with either the spirit, or the framework of bankruptcy law. In all civilised nations bankruptcy law protects the human rights of debtors, as well as creditors, and for more than a century, has been central to the economic and political health of growing economies. Not so for sovereign debtors like Argentina – or indeed in any of the other 80 severely indebted nations of the world.

Responsibility for Argentina's bankruptcy cannot be laid at the door of her politicians alone. It has taken two to tango in Argentina's international financial markets. On the one hand there are the obvious culprits – the reckless, undemocratic and corrupt politicians, military leaders, bankers and judges, who over fifty years, have used the secret and opaque procedures of international capital markets to bankrupt their people.

On the other, there are those who financed and colluded in the corruption; and who designed and dictated Argentina's economic policies over the same period. (The IMF has been lending to, and advising Argentina for almost fifty years now). These economic policies, including Argentina's ten-year old currency peg to the dollar, was backed by the IMF, other IFIs, and leading US economists.

As Paul Krugman has noted[4] 'the currency board….returned the country to the gold standard, except that US greenbacks took the place of ingots….the rigid monetary system, designed to protect against inflation, precludes actions that countries normally take to fight deflation, like cutting interest rates or letting currency depreciate. Instead Argentina has gone through wave after wave of fiscal austerity, each time with the promise that the latest round of wage and job cuts would restore confidence and produce economic recovery. But austerity has not brought recovery. On the contrary, it has worsened the recession, increased social tension and further reduced confidence. Unfortunately that old-time economic religion (monetary orthodoxy), with its narrow-minded insistence on monetary rectitude at the expense of every other consideration, has had a revival in recent years, thanks largely to the promotional efforts of right-wing think tanks. And that ideology, more than anything else, is responsible for Argentina's looming catastrophe.'

The currency board, like dollarisation and the gold standard, had one overwhelming objective, linked closely to the objective of 'taming inflation": namely - to protect the value of assets held by foreign creditors and investors, and the foreign assets of wealthy Argentines.

Despite belatedly distancing the IMF from the pegged-currency policy of Domingo Cavallo (Argentina's neo-liberal finance minister), the Fund's leading shareholders went on lending to his government until December, 2001, disbursing $10.5bn in 2001. As all governments who do not conform to the IMF's austerity programmes well know, the IMF does not lend if it does not support the policies of the borrowing government. Staff

3 Quoted in the *International Herald Tribune*, 17 October, 2001.
4 'Argentina gets crucified on a cross of US dollars', International Herald Tribune, 8 November 2001.

went even further, and acted as cheerleaders for the now discredited Cavallo. As late as September, 2001, Tom Dawson, the IMF's chief spokesperson wrote to the Los Angeles Times in these terms: '*…Argentina's recipe for reform is the right one, well deserving of strong international support.*'[5] Yet today IMF staff and shareholders are notable for their silence, and for their absence from the scene of Argentina's economic havoc, leaving their protégé to be consumed by the flames of liquidation.

There are others who share responsibility for Argentina's crisis including domestically-based foreign companies that had their foreign debts nationalised, and Argentina's international creditors and investors – many of them apparently respectable bankers and investors in Wall St., the City of London and Madrid.[6]

In the absence of a just and orderly insolvency framework for managing the crisis, these groups of international creditors have largely been able to cut their losses and run. They deny any responsibility, blame the victims and shirk the burden of losses. Instead the burden – and the blame - is transferred overwhelmingly to the sovereign debtor government and to millions of innocent Argentine citizens.

International creditors may wish to argue that they are facing losses as the country defaults and devalues, and the collection of usurious interest rates on loans are halted. But creditors have been compensated in advance for this (widely predicted) risk in the form of premiums as high 25% on Argentine loans and bonds. They and their representatives, the G7 leaders of the international financial institutions, are beating a hasty retreat having extracted and transferred substantial assets out of Argentina – through debt transfers, privatisation assets and lower commodity prices.

G7 finance ministers, led by Gordon Brown, chair of the IMF's most powerful committee, announced in 1999 that they were setting up a $90bn 'Precautionary Fund' – precisely to prevent the sort of crises we are now witnessing in Argentina. But they too, like the staff of the IMF, have suddenly gone quiet, and, hoarding their ample funds, have retreated into the shadows.

Under any national bankruptcy law, no judge would allow creditors to escape responsibility so easily. And in circumstances of bankruptcy, sovereign debtors would have their human rights protected from the greed of predatory creditors.

The consequences of lawlessness in the management of international debt crises are tragic. The businesses, jobs, indeed the very futures of millions of innocent Argentines are in jeopardy. Already protesters have died in the streets, and tens of thousands go hungry. There is a real threat of a return to fascist policies and authoritarian rule.

We read press reports of poor people looting supermarkets and of the middle classes joining in street demonstrations. The poor are desperate to find food. The middle classes are using unconventional means to find a voice; banging pots and pans, they are insisting on being heard by politicians that have contracted huge unpayable debts on their behalf, without consultation or accountability.

It need not be thus. This report sets out to explain just how an orderly, transparent and accountable insolvency framework could help to resolve the debt crisis which has struck Argentina. Furthermore, we show that, contrary to IMF assertions, such a framework does not require an international treaty or court. The Jubilee Framework could be put in place tomnorrow, and could begin the urgent process of restoring stability, order and justice to Argentina.

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5 Earlier, the cheerleading was even louder. In May, 1999, Stanley Fischer, IMF deputy managing director, said: 'Argentina is to be commended for its continued prudent policies. As with a number of other countries in the region, Argentina has had to bear the adverse consequences of external shocks, which have taken a significant toll on economic performance. Nevertheless, the sound macroeconomic management, the strengthening of the banking system and the other structural reforms carried out in recent years in the context of the currency board arrangement, have had beneficial effects on confidence, and have allowed the country to deal with these challenges.'

6 For a more detailed discussion of the corruption that lies behind much of Argentina's foreign debts, see the New Economics Foundation/Jubilee Plus report 'It takes two to tango: creditor co-responsibility for Argentina's crisis – and the need for independent resolution,' by Ann Pettifor, Liana Cisneros and Alejandro Olmos Gaona, published by the New Economics Foundation in September, 2001. Available at the Jubilee Plus website: www.jubileeplus.org

International insolvency: key principles

An international insolvency process would have to begin by adopting the key legal principles underlying all insolvency procedures.[7]

The first principle is that any process should be based on *the application of justice and reason*. The process should not be viewed as an act of mercy.

The second principle is that any process *should protect the human rights, and the human dignity of the debtor*, as well as the rights of creditors.

The third principle is fundamental to the Rule of Law; namely that it is not possible to be judge in one's own court. In other words, *neither creditors nor the debtor can control the court of bankruptcy, or decide on their own claims or payments*. The judge has to be independent of both debtor and creditors, and to resolve the crisis within a framework of justice that recognises the human rights of the debtor.

Fourthly, we would add a vital principle, central to bankruptcy law for governmental organisations in the US; namely *that citizens affected by a debt crisis, have a legal right to have their voices heard in the resolution of that crisis*. In other words *freedom of information, transparency of process and accountability to the public* must be central to an international insolvency framework.

We, in the Jubilee movement are promoting a new international insolvency framework – a Jubilee Framework – because the purpose of all insolvency law is defined as *granting the debtor a new financial life*. Or as Section 101, note 63 of the US legal code states: '*the opportunity to accumulate new wealth unhampered by pressure and discouragement of pre-existing debts.*' Because the debtors we are concerned with are public sovereign debtors, we are promoting this new framework to strengthen *democratic participation* in a) the resolution of a crisis; b) the prevention of future crises and c) the development of a '*new financial life*' for the country as a whole.

A just, transparent and democratically accountable framework for resolving debt crises would contrast dramatically with the reality faced by hundreds of millions of people living in more than 80 sovereign debtor nations, as they struggle to deal with powerful creditors in forums dominated by creditors. The differences are contrasted in the following table.[8]

7 Most of the material in this chapter is based on the work of Professor Kunibert Raffer of the University of Vienna, and in particular his report for the Austrian Institute for International Affairs 'Solving Sovereign Debt Overhang by internationalising Chapter 9 procedures', June, 2001.
8 I am grateful to colleagues in the German Jubilee 2000 campaign, Erlassjahr, and in particular to Jurgen Kaiser, for this illuminating table.

Insolvency principles	*Sovereign debtors' reality*
Guiding principles	
a) '*Survival in dignity*' b) *Burden sharing between debtor and creditor*	a) *Exact maximum debt payments* b) *Shift burden to debtor*
Who participates?	
All creditors, on an equal basis.	*Fragmented approach; creditors treated unequally*, in different forums. Commercial creditor repayments subordinated to the repayments of 'preferred creditors' – like the IMF and World Bank. A premium for creditors willing to 'hold out' against collective agreements of other creditors.
Participation of citizens	
Under Chapter 9 of the US legal code, special taxpayers, and representatives of employees of the municipality are given a legal 'right to be heard'; a right to be consulted about the economic viability of a composition plan; and the right to block any composition plan.	Citizens in debtor and creditor nations are on the whole, denied information about new lending / borrowing agreements. Citizens in debtor nations play very little role in determining the outcome debt relief negotiations, and the economic conditionality programmes attached to these; although the IMF and World Bank are under increasing pressure to increase such participation. Negotiations with creditors both in contracting new loans; in negotiating conditions; and in negotiating debt relief are conducted in secret, and behind closed doors. The Paris Club of western government creditors is a powerful closed, cartel. The Board of the IMF does not vote on decisions relating to new lending or debt relief – nor does it deal directly with elected politicians in debtor nations. Information on the portfolio of debts – on why loans were contracted, and how the loans were used, is seldom made public. Creditors often spring new 'nationalised' debts on the sovereign debtor in debt relief negotiations.
Cash flow effects	
An automatic stay on debt payments, as debtor seeks protection from their creditors under bankruptcy codes – like Chapter 11 of the US legal code.	*No stay on debt payments*; but instead an asset grab by different creditors. The IMF and World Bank use their status as 'preferred creditors' to continue exacting debt repayments from the debtor.
Viability of debtor - the touchstone	**Viability of debtor – under HIPC and other procedures**
The final 'composition plan' of a Chapter 9 insolvency procedure is only defined as feasible if the debtor emerges from the *re-organisation with reasonable prospects of financial stability and economic viability; including sufficiency of capital.*	As the World Bank has admitted, and as demonstrated by Jubilee Plus and other NGOs, most of the sovereign debtors emerging from the protracted and complex Highly Indebted Poor Countries Initiative (HIPC) – are '*unsustainable*', *i.e. insolvent, even under World Bank criteria; and still* suffer *substantial shortages of capital.*

How would the Jubilee Framework work in practice?

Chapter 9 of the US legal code as the model

A Jubilee Framework would be modelled on existing practice in the United States, where US law provides for the bankruptcy of governmental organisations, so-called municipalities, under *Chapter 9* of the US legal code.

Under Chapter 9 municipalities may 'file for protection from their creditors', if they are insolvent or unable to pay. They must

- desire to effect a plan to adjust such debts.
- have obtained the agreement of creditors / or tried to work out a plan without success.

This petition results in an automatic stay (halt) on debt payments. The jurisdiction of the court depends on the debtors' volition.

US law protects the governmental powers of the debtor. In other words, creditors cannot prevent municipalities from carrying out vital services, or subordinate these services to debt repayment. The US Supreme Court has rejected the idea that a city has unlimited taxing powers, with which to raise funds for the repayment of debts. Furthermore, a municipality cannot be taken over and operated for the benefit of creditors. A municipality's politicians – elected democratically – cannot be removed from office – except by voters at the next elections.

US law also protects individuals affected by the final 'composition plan' mandated by the court. Employees and 'special taxpayers' affected by the plan are given the right, in law, to voice their views. Taxpayers have the right to block the plan by objecting to its confirmation. Representatives of employees have the legal right to be heard on the economic soundness of the plan. The Court can allow any interested entity to intervene. As a result the process is open, transparent and accountable to the innocent citizens who could be become victims of the debt crisis.

The final re-organisation (of debts) plan must be *fair, equitable and feasible*. It must be in the best interest of creditors – which is tested by what they could reasonably expect to be paid.

Finally the 'composition plan' is defined as 'feasible' if the debtor emerges from the reorganisation of the debts with reasonable prospects of financial stability and economic viability, including sufficiency of capital.

Below we outline the steps that are necessary for a just and democratically accountable process for resolving a debt crisis.

Step One: Declaring insolvency

Insolvent? Under the 'Jubilee Framework', the first step taken by a sovereign debtor would be to determine at what point repayment of foreign debts are being made at a cost to the human rights or dignity of the people of that country. If repayment of debts are in this sense unpayable, then the debtor would try and negotiate debt reduction with international creditors. If this failed, they would petition for a 'standstill' on debt payments.

The debtor's unconditional right to petition: Under the 'Jubilee Framework' the sovereign debtor, supported by civil society, would have the unconditional right to *petition* for a standstill in debt payments. This decision would be made on the basis of criteria laid down by the sovereign debtor, and would of course, be subject to the court acceding to it.

Parallels with the corner shop and Macy's. Any sovereign debtor would be free, under the 'Jubilee Framework' to petition for a standstill on debt payments. In this sense an international insolvency framework would mimic domestic bankruptcy law, where both a small corner shop, and big major companies have the right to 'file for protection from creditors'. In just the same way both a country as small as Rwanda or as large as Indonesia could petition for a standstill on debt payments.

Informed civil society. Of course it will be vital for **civil society** (e.g. the media, opposition parties, NGOs and the churches) to have access to information about a government's indebtedness, and to be free to make a judgement on the sustainability of their government's debt. Organisations will have to monitor:

- the government's borrowing policies on a continuous basis;
- what share of the government's budget is devoted to debt service payments, compared to expenditure on more productive activities – information that should be freely available.

If civil society organisations deem the debts to be unpayable, they should assert this loudly and clearly and invite the government to file for a standstill on debt payments. This civil society role will be vital in **debtor** nations. But it will important for campaigners in **creditor** nations to give support, by scrutinising loans guaranteed by their governments to the debtor nation.[9]

Bankruptcy no incentive for default. Such a step towards insolvency would not be taken lightly, as we know from domestic bankruptcy practice. The existence of bankruptcy law has never been an incentive for companies to go bust. On the contrary. Not only does bankruptcy limit access to new capital; but it damages reputations for sound economic management.

But – debtors made viable: The attraction of Chapter 9-type proceedings is that they would make sovereign debtors economically viable again and thus re-open access to capital markets. A crisis, in contrast, closes down access to capital markets.

Resistance from debtor? One might expect resistance from sovereign debtor politicians, and international creditors, to a petition for a debt standstill. Negotiating new loans to pay off old loans is, on the whole, much more attractive - to both the irresponsible borrower, and the lax lender. There is also a great deal of corruption associated with international borrowing – so the associated gains provide a major incentive for local politicians to continue borrowing.

It is at this juncture that **civil society** could play a vital role.

Step Two:

Petitioning for a standstill in debt payments, and seeking protection from creditors

The insolvency court: Under Chapter 9 procedures, the sovereign debtor government would file a petition with an **insolvency court** for protection from its creditors.

However there is no such international insolvency court, nor indeed is there any international law governing this process.

Prof Raffer and others have argued powerfully that there is no need for an International Court. Instead an ad hoc **mechanism**, modelled on many well established arbitration procedures, could be used to quickly establish **an independent panel**. Raffer demonstrates that there are precedents for de-factor insolvencies in the case of Germany in 1953 and Indonesia in 1971. In both these cases, an ad-hoc, independent, but authoritative debtor/creditor framework was quickly assembled, and massive debt cancellation agreed by both debtor and creditors.

9 For example, local campaigners for debt cancellation for Indonesia, have worked closely with campaigners in Britain, to put pressure on the British government to ensure that loans guaranteed by the government for military exports to the authoritarian ex-president Suharto are declared odious, and written off by the British government. And in the last weeks of 2001 a major row erupted in Britain over the Labour government's decision to guarantee a $40 million loan to Tanzania for the purchase of satellite equipment from British Aerospace Systems.

IMF as judge and jury? The IMF, an important creditor, and the representative of all major creditors, does not agree. They suggest that at this point, the sovereign debtor could petition **the IMF and through it, the powerful G7 shareholders on the Board**. These shareholders would then have to agree on whether or not to **accede** to an immediate standstill on debt repayments. Such backing, argues the IMF, would help to protect sovereign debtors from litigation by creditors based within the jurisdiction of G7 governments. The IMF has the recent appalling case of rogue creditors and Peru in mind.[10]

We beg to disagree: in reality there are just two possible jurisdictions which can challenge a sovereign government wishing to declare a standstill on debt payments: these are the courts of New York and London. It would therefore require we believe, just two governments to remove jurisdiction over international debt negotiations from their courts – the governments of the US and the UK. There would thus be no need to refer to all the governments represented on the full Board of the IMF.

Rejecting sovereign immunity: This legislation could take the form of a general rejection of the waiver of sovereign immunity. It would not be necessary to wait, as the IMF suggests, for 'two or three years' until legislation becomes 'universal'.

Unequal treatment of creditors? The IMF proposes this critical role for itself in order, its representative asserts, to ensure that the sovereign debtor negotiates 'in good faith with its creditors, and refrains from treating some creditors more favourably than others'.[11] IMF staff do not believe that the institution itself, a major creditor, should be included in the 'debt standstill' agreement. In other words they are asking the sovereign debtor make an exception of the IMF, and to therefore treat 'some creditors more favourably than others'.

This preferential treatment of creditors, like the IMF, that have made major errors in lending and policy advice, is clearly unacceptable. Especially for an institution that lives by the rule of the market. In the words of Raffer 'it is the most basic precondition of the market mechanism that economic decisions must be accompanied by (co)responsibility. Whoever takes economic decisions must also carry financial risks'. The IMF is asking to be treated in the way state-backed industries in the USSR, manufacturing one-size-fits-all brassieres for women, were once treated. There, in the absence of a market, the link between risk and responsibility was severed, and millions of inappropriately sized bras were produced. The IMF cannot de-link itself from responsibility for economic decision-making. And it cannot therefore de-link itself from debt standstills. Anyway, the precedent of cancellation of multilateral debts was set by the HIPC initiative, and cannot be reversed.

The IMF backs independent outcome. The IMF, while seeking to defend its past errors, is nevertheless very clear on the need for a bankruptcy court, and on the need for independent adjudication. In her latest speech on the subject, Ms Kreuger notes that her organisation's role should be confined to '*mandating the process within which a restructuring would be negotiated, but not the* ***outcome****.' …..There is an obvious analogy here with a domestic bankruptcy regime……..We would need some way to ensure that these aspects of the (debt) workout were seen to be carried out in a fair and transparent way.*[12]

The need for working capital: There is one other important factor: during any standstill, it will be vital for the sovereign debtor to have access to **working capital**. This will largely be provided through the IMF. The loans (and they will have to be loans; grants would be a major incentive for countries to go bankrupt) would have to be

10 The IMF is concerned that rogue creditors, like Elliott Associates of New York, could defy sovereign debtors, by challenging them in the friendly courts of local jurisdictions. As Ms Kreuger of the IMF explains: 'In 1997 Elliott Associates bought $20 million of commercial loans guaranteed by Peru. Rather than accepting the Brady bonds offered when Peru tried to restructure its debt, Elliott demanded full repayment and interest. In June, 2000 it obtained a judgement for $56 million and an attachment order against Peruvian assets, used for commercial activity in the US. Elliott targeted the interest payments that Peru was due to pay to its Brady bond holders who *had* agreed to the restructuring. Rather than be pushed into default on its Brady bonds, Peru settled.' From the speech cited above: *A new approach to sovereign debt restructuring*, 26 November 2001.

11 Ms Anne Kreuger, as above, page 7, para 2.

12 Ms Anne Kreuger, address given at the Indian Council for Research on International Economic Relations, Delhi, India, December 20, 2001.

treated differently to old unpayable loans. In this sense it will be necessary to differentiate between new loans or working capital, and old loans, and protect the former from being written off under the insolvency framework.

The IMF is arguing that *all* of its loans should be protected in this way. We disagree strongly. Many of the IMF's loans have been badly misjudged; and responsibility for those debts rests as heavily with IMF lenders as it does with the sovereign debtor. So the IMF must also face losses, and only a neutral court could impose such losses equitably on all creditors.

However a neutral court is not yet in place. This report is a contribution to the international debate that must begin to shape both the democratic processes around international insolvency; but also the character and duties of the independent panel.

In the meantime, sovereign debtor nations urgently need to resolve their debt crises.

Recognising that the IMF will play an important and legitimate role in organising and assembling creditors; in providing information on the country's debt; and in mobilising new finance for the debtor, we make the following proposal.

That, in the interim, while an independent panel/arbitration court international is being assembled, the IMF should act as ***a portal, a gateway*** *between the sovereign debtor and international creditors; enabling the sovereign debtor to file a petition for an immediate standstill on debt payments and for protection from creditors.*

This petition, must however, be subsequently heard by an ***independent*** *panel or court, which will rule on the petition, oversee the proceedings, ensure equitable burden sharing amongst all creditors, while guaranteeing the human rights of the people of the sovereign debtor nation.*

In order to guarantee independence in the process of nominating panel members, we propose that the Secretary General of the United Nations oversee the appointment of the panel.

How would panel be made up? The court would be made up of equal numbers of nominees made by both the sovereign debtor and representatives of international creditors. If the debtor nominated one, and the creditors another, they could both nominate a third (someone in whom they both have confidence) to act as judge, arbiter or chairperson. This would be all that would be required to establish a neutral panel.

Involving Parliaments. The sovereign debtor could propose that nominations to the independent panel be made by the Parliament. In any case, the process of nomination should be open and transparent, and should be supported by civil society.

Nominating creditor representatives: The creditor representatives could be chosen from the IMF, the Paris or London Clubs, or various bondholder committees. (However commercial creditors, like Commerzbank in Germany, have already expressed concern at the involvement of the Washington-based institutions, noting that the BWI's 'will be concerned with protecting their own balance sheets rather than with fair 'burden sharing'.[13])

The panel might need administrative and logistical support – a secretariat possibly; but this need not be large or costly.

The panel's proceedings should be open, transparent and accessible to civil society in the debtor nation.

13 Taken form Commerz Bank's 'Emerging Markets this week', no. 26/1999 of October 15 and cited in raffer, page 28, as above.

Step Three:

The responsibilities of the court

Determining whether sovereign debts were legally and properly contracted. All claims would have to be verified loan-by-loan, ensuring that all outstanding claims were contracted legitimately by the sovereign debtor and her creditors. Such a process would dismiss some of the debts contracted illegally and fraudulently by Argentina's military during the period of 1976-1983 – debts for which no formal records remain.

Involving civil society in this process. The debate about the outstanding portfolio of debts should be a public debate, with Parliaments and cso's scrutinising outstanding debts, to ascertain whether they were properly contracted within the formal procedures of the state.

Checking whether debts have been retroactively 'nationalised'. In many countries, governments have been forced by creditor cartels like the Paris Club to retroactively assume losses from private lending – initially undertaken without any government guarantees or involvement. In Argentina many multinational companies, with branches in Buenos Aires, arranged for their foreign debts to be nationalised during the time of the military regime.[14] The IMF and World Bank have turned a blind eye to such dubious legal practices. These 'nationalised' private debts must be declared null and void.

Ensuring symmetrical treatment of creditors: There is no reason why any particular class of creditors, and in particular public creditors like the IMF and World Bank, should be given preferential treatment in an insolvency process. A major reason for the IFIs not to be granted preferential treatment is outlined by Raffer[15]: Commercial banks may have lent aggressively, but they have usually not interfered with their clients' economic policy. Multilaterals have strongly influenced the use of loans, and exerted massive influence on their debtors' economies. 'In other words, IFIs take economic decisions, but refuse to participate in the risks involved. IFIs insist on full repayment, even if damages caused by negligence of their staff occur, damages which have to be repaid by the borrower… ..The striking contrast between free-market recommendations made by IFIs and their own protection from market forces, must be abolished. Symmetrical treatment of creditors is more than justified.'

Capital Flight. The debtor government, with the support of the court, will have to take measures to prevent rich nationals from exporting their assets via the Central Bank, in the form of 'capital flight'. In a radical departure from previous policy, and in a major concession, the IMF has indicated that the 'the imposition of exchange controls for a temporary period of time' would be necessary.[16] We agree. Furthermore, we argue that an international Chapter 9 framework should provide for the possibility of overruling banking secrecy, if suspicion exists that money was obtained in the first place by criminal activities, such as corruption, theft or embezzlement.

Civil society, will again, at this stage, play a crucial role in exposing such criminal activities in to the members of the court.

Protecting the human rights of citizens of the sovereign debtor. It is essential that schemes to protect the fundamental human rights of the citizens of the debtor nation, should be part and parcel of every debt workout plan. In an analogy with the protection granted to the population of an indebted municipality by Chapter 9, the money to service a country's debt can not, and must not be raised by destroying basic social services, fundamental to the defence of human rights. Subsidies and transfers necessary to guarantee these minimum rights for the poor, must be defended and maintained. Funds for sustainable economic recovery must be set aside.

Civil society will have a crucial role to play during these sessions of the independent arbitration court, to defend these human rights.

14 See: 'It takes two to tango' by Jubilee Plus.
15 In Raffer, as above, page 29.
16 Speech by Ms Anne Kreuger, 26 November, page 6, para 1.

Any international treaty devised to facilitate international insolvency should have these rights enshrined within it.

Mandating the final debt workout – or 'composition plan'. The court would have to bind all creditors, and the debtor, to a debt reduction agreement which is 'fair, equitable and feasible'; in which losses would be shared; and the debtor nations' human rights would be given precedence over bona fide claims.

Civil society's role in shaping the final debt workout plan. As in Chapter 9 proceedings, representatives of government employees and taxpayers of the sovereign debtor nation should be given the right to comment on the soundness of the final plan binding the government and her creditors; and to object to the final debt workout. This is a right that will have to be fought for, as independent panels are established, and their procedures developed.

Conclusion

This report has sought to outline, in skeletal form, what we believe to be the key elements necessary to a democratic and accountable framework – a Jubilee Framework – for resolving debt crises. Clearly our views are not, nor can they be, definitive; nor do we claim that our perspective is representative of the wider movement.

However we hope that these ideas will help stimulate debate within civil society as a whole; and above all stimulate civic involvement in international debt crises. Much greater democratic involvement by ordinary people in crises that impact directly on the quality of their lives, will we believe, transform the project that has come to be known as 'globalisation', and embed it more firmly in political, social and environmental relations.

Appendix 1

International Insolvency: the history of an idea

1776 **Adam Smith** - advocated a 'fair, open and avowed bankruptcy process' for nations. He wrote in the 'Wealth of Nations' – 'when it becomes necessary for a state to declare itself bankrupt, in the same manner as when it becomes necessary for an individual to do so, a fair, open and avowed bankruptcy is always the measure which is both least dishonourable to the debtor, and least hurtful to the creditor'. (Page 93).

1981 **C.G. Oechsli**. 'Procedural Guidelines for Renegotiating LSC Debts: An Analogy to Chapter 11 of the US Bankruptcy Reform Act. Virginia Journal of International Law 21 (1981) pp. 305.

1984 **D. Suratgar** in A.N Malagardis, Ein 'konkursrecht' fur Staaten? Zur Regelung von Insolvenzen souveraner Schuldner in Vergangenheit und Gegenwart. Baden-Baden: Nomos 1990. Suratgar backed by Prof. Jeffrey Sachs and other economists.

1980s **Lawrence Klein**, Nobel Laureate promotes Chapter 11 for sovereign debtors.

1986 **Sidney Dell** in UNCTAD, Trade and Development Report, 1986.

1986 **Raffer, Kunibert**, Die Verschuldung Lateinamerikas als Mechanismus des ungleichen Tausches. Zeitschrift fur Lateinamerika (Wien) No. 301/31 (1986) pp. 67 ff.

1987 **Thomas Kampffmeyer** 'Towards a Solution to the Debt Crisis: Applying the Concept of Corporate Composition with Creditors.' Berlin: German Development Institute (DIE) 1987.

1990 **Raffer, Kunibert**. Applying Chapter 9 Insolvency to International Debts: An Economically efficient solution with a human face. World Development 1990, vol.18, no. 2 pp 301.

1993 **Raffer, Kunibert**. 'What's Good for the United States Must Be Good for the World: Advocating an International Chapter 9 Insolvency.' In Bruno Kreisky Forum for International Dialogue (ed) From Cancun to Vienna. Can also be found on Raffer's homepage: http://mailbox.univie.ac.at/rafferk5.

1995 **Prof. J. Sachs**: 'Do we need an International Lender of Last Resort?' - Frank D. Graham Lecture, Princeton University, April 20, 1995.

1999 **Ann Pettifor and Joe Hanlon**: 'Kicking the Habit: finding a lasting solution to addictive lending and borrowing – and its corrupting side-effects.". Published by the Jubilee 2000 Coalition, London, UK.

2001 **UNCTAD** - Yilmaz Akyux, Chief Economist, UNCTAD, Trade and Development Report, 2001. Part Two, Chapter VI – Crisis Management and Burden Sharing.

Appendix 2

The Jubilee Framework: history of a campaign. A personal view. by Ann Pettifor

Since 1995 the Jubilee 2000 campaign in the UK has campaigned vigorously for a new framework of justice for resolving international debt crises – to replace the current international framework biased in favour of creditors. In drafting our petition at the end of 1995, signed later by 24 million people in more than 60 countries, we inserted the demand for a 'fair and transparent' process for negotiating debt cancellation. We had in mind an international insolvency framework based on Chapter 9 of the US's code for bankrupt municipalities.

At the time we were mocked and derided for our naïveté – 'it will never happen in a lifetime' we were told by our critics in the media, in the British government, the IMF and World Bank. Many of our own supporters dismissed our ideas and questioned our grip on reality. 'The IMF will never give up its pivotal role as plaintiff, judge and jury in the court of international debt,' they assured us, refusing to back what they regarded as a futile campaign.

"It was an odd way to drop a bombshell. Anne Kreuger, second-in-command at the International Monetary Fund, floated one of the most radical changes to international finance in a generation, with no prior warning, at a dinner in Washington, late on Monday night."

Financial Times, reporting on the IMF's proposal for a bankruptcy plan, 29 November, 2001.

In dropping her bombshell that night in November 2001, Ms Kreuger proved our critics wrong – the IMF, under a new management, are willing to consider major changes to the international financial architecture so that the resolution of debt crises is carried out 'in a fair and transparent way.'[17] Above all, she demonstrated that we were far from alone in our bold and innovative thinking.

Unknown to us, as far back as 1995, powerful central bankers were expressing dismay at the debacle of Mexico's debt crisis and the cost of the IMF's subsequent bail-out of Wall St. investors. Some, including Alan Greenspan of the US Federal Reserve and Mervyn King of the Bank of England, began to raise with colleagues, the necessity for greater regulation of international lending and borrowing – through an international insolvency process.

These proposals are not new: the idea was first mooted by Adam Smith in 1776; promoted by a range of academics in the 1980's; and then pressed vigorously by the United Nations Conference on Trade and Development (UNCTAD) in its ground-breaking 1986 Trade and Development Report.

While central bankers worked deftly but secretly behind the scenes, Jubilee 2000 campaigned loudly in the streets and on demonstrations for greater justice for debtor nations, and for an end to creditor domination of the international financial system. Some of the sister Jubilee 2000 campaigns in major creditor countries were reluctant to back calls for a new framework, preferring to stick to the demand for debt cancellation by the year 2000. One exception, however was the German Erlassjahr campaign, which made excellent use of the precedent whereby Germany was granted debt cancellation under an independent arbitration framework in 1953. Indeed after the 1999 Cologne Summit, Erlassjahr gave up campaigning for deeper debt

17 Address by Ms Anne Kreuger, given at the Indian Council for Research on International Economic Relations, Delhi, India, December 20, 2001.

cancellation by the year 2000 – and concentrated almost exclusively on the need for an independent framework for debt cancellation.

In the south the campaign was spearheaded by Afrodad, the African Debt and Development Coalition, and the Ecuadorean Jubilee 2000 movement. Indonesian debt campaigners were also active, spurred on by the precedent set when ex-President Suharto had been given massive debt cancellation under an independent process in 1971.

The movement was greatly encouraged when on 3 April, 2000, in preparation for the UN's Millennium Summit of world leaders, Kofi Annan, UN Secretary General produced a report in which he said: 'I would go a step further and propose establishing a debt arbitration process to balance the interests of sovereign debtors and to introduce greater discipline into their relations.' At the Summit itself, many world leaders expressed support for our proposal.

However, by the end of the year 2000, many in Britain felt disappointed, after a a massive worldwide campaign, at the amount of actual debt relief delivered by rich creditor nations. We were proud of the achievements of the Jubilee 2000 campaign, including the G7's promise to cancel $100bn of debt. Nevertheless we knew we had fallen well short of our goal of 'cancelling the unpayable debts of the poorest countries.' As this report goes to press (January, 2002) only $35.8bn of the $100bn promised (in nominal terms) has so far been committed in debt reduction. Only four countries have gone all the way through the labyrinthine framework set up by creditors and led by the World Bank, the IMF and the Paris Club. A further 20 countries are between their 'decision' and six-year 'completion' points, with a committed reduction in debt of only $24.51bn.[18] In the meantime, middle-income countries, excluded from the HIPC process, continue to endure painful, unresolved debt crises – countries like Indonesia, Turkey, Pakistan and most dramatically, Argentina.

In the British Jubilee 2000 campaign, we became convinced that only by altering structural injustice, i.e. the balance of power between international creditors and sovereign debtors could we achieve our goal. Only by introducing justice into international debt negotiations, could genuine debt sustainability be achieved for a wide range of effectively insolvent states.

With the passing of the millennium deadline, the Jubilee 2000 campaign closed. Drop the Debt, a short-term campaign, focused on the Genoa G7 summit of 2001, and proved extraordinarily effective at maintaining pressure on world leaders. But after the Summit, campaigners began to disperse, and momentum began to be lost.

In Germany, the Erlassjahr campaign for a Fair and Transparent Arbitration (FTAP) Process (FTAP) continued to gather momentum, with effective lobbying of the UN Financing for Development process, the German government, the Bundesbank and German representatives on the board of the IMF and World Bank. The Indonesian campaign renewed its activities; and the Ecuadorean campaign persisted in its work.

Here in London, the New Economics Foundation[19] took up the baton, and by establishing the transitional Jubilee Plus programme, made sure that an independent, international insolvency framework remained central to NEF's mission for global economic justice and greater civil society participation in international governance.

Despite producing excellent reports[20] and extensive advocacy, in the UK, the US, Indonesia, Africa and Latin America, our voices seemed no more than cries in the wilderness.
Then came the devastating attacks on New York on the 11th September, which seemed to shake the

18 See NEF's Jubilee Debt Programme website: www.jubileeplus.org
19 The chair of the New Economics Foundation, Ed Mayo, had been one of the founders of the Debt Crisis Network in the UK, and had chaired the Jubilee 2000 Coalition Board for the duration of the campaign. See the NEF website at www.neweconomics.org.
20 'HIPC – flogging a dead process: the need for a new, independent and just debt work-out for the poorest countries' by Ann Pettifor, Bronwen Thomas and Michela Telatin, published by the New Economics Foundation, September 2001; and 'It takes two to tango: creditor co-responsibility for Argentina's crisis – and the need for independent resolution', September, 2001, by Ann Pettifor, Liana Cisneros and Alejandro Olmos Gaona, published by the New Economics Foundation; and 'Drops of Oil in a Sea of Poverty: the case for a new debt deal for Nigeria' by Kwesi Owusu, published by the New Economics Foundation, September 2001. All available on the website at www.jubileeplus.org.

confidence of many influential policy makers. Soon after, on the 21st September, Paul O'Neill, US Treasury Secretary made the following statement to the US Senate Banking Committee. 'I think now is the time that we need to take the action that's been talked about for years and that's never been done, we need an agreement on international bankruptcy law.'

This remark was quickly dismissed, with prominent voices in Washington think-tanks assuring us that Mr. O'Neill was a 'lame duck' whose views were not taken seriously.

However O'Neill's statement was followed rapidly by a paper published jointly by the Bank of England and the Bank of Canada, and presented to a meeting of finance ministers at the IMF's annual meeting in Ottowa in November, 2001. [21] This paper echoed the Jubilee movement's calls for a fair, transparent and orderly framework for the resolution of debt crises. Furthermore it called on international creditors to take losses. 'If debt is unsustainable' argued senior policy analysts from these two Central Banks, 'creditors will be required to reduce their exposures in net present value terms' - a radical notion in the world of international finance. 'Standstill guidelines' they argued in the cautious language of central bankers 'provide one means of ensuring that the debt work-out process is efficient, equitable and expeditious.'

And then on 26th November, 2001, came the IMF's capitulation.[22] Yet further evidence of the power that civil society has in exposing deep-seated injustice; and setting the agenda on international financial matters.

21 The Resolution of International Financial Crises: private finance and public funds' by Andy Haldane, International Finance Division, Bank of England, and Mark Kruger, International Department, bank of Canada. Obtainable from the Bank of England website at XXXx

22 'International Financial Architecture for 2002: A new approach to sovereign debt restructuring,' address by Anne Kreuger, First Deputy Managing Director, International Monetary Fund, given at the National Economists' Club annual Members' Dinner American Enterprise Institute, Washington DC, November 26, 2001.