Curtailing Vulture Funds in Low-Income Sovereign Debt Litigation: American and British Legislative Responses

Eloy A. Peral*

The wielding of official might by Western governments to influence developing country private debt restructuring is nothing new in the modern age. From the proverbial gunboats to the Brady Plan, this exercise of power has ranged from armed conflict to the sponsorship of "quasi-voluntary" sovereign debt restructurings and the enactment of incentives to spur debt reduction among private creditors. Central to the history of sovereign debt defaults and restructuring has been the transformation of sovereign immunity from an absolute immunity to a qualified immunity, which prevails today in the United States and the United Kingdom. This change has had a significant impact on sovereign debt litigation and consequently on the sovereign debt market. Consistent with this history, the United States has been active in exerting its foreign policy machinery to influence the disposition of sovereign debt litigation in U.S. courts.

The erosion of sovereign immunity in the United Kingdom and the United States, combined with the diversification of sovereign debt-holders from bank syndicates (which were the standard during the 1980s) to bondholders today, have created what are pejoratively referred to as "vulture funds." Official U.S. reaction toward these funds has been muted in comparison with that of the British government. The historical reasons for official involvement in private sovereign debt restructuring, particularly the attempt to manipulate the viability of sovereign debt litigation, are varied, complex, and disputed. Regardless of one's viewpoint, it is clear that the post-Cold War consensus among the industrialized world has been to implement, via international financial institutions, debt relief initiatives for the most economically deprived nations, which are largely located in Sub-Saharan Africa. These debt relief initiatives have collided with the rise of sovereign debt enforcement through litigation in American and British courts. Official participation in sovereign debt crises has been characterized by the pushing and prodding of relevant parties in order to reach desired outcomes. Despite restricted sovereign immunity, until recently bright-line prohibitions on the enforcement of sovereign debt by secondary market actors have been resisted.

Regardless of one's viewpoint, it is clear that the post-Cold War consensus among the industrialized world has been to implement, via international financial institutions, debt relief initiatives for the most economically deprived nations, which are largely located in Sub-Saharan Africa.

In the U.K., enactment of the Debt Relief (Developing Countries) Act 2010 (Debt Relief Act) emerged as a result of the confluence of the forces described above. The swift passage of the Debt Relief Act was the product of a sustained campaign by non-governmental organizations (NGOs) directed toward Members of Parliament (MPs) in the British government. Prior to the introduction of the Debt Relief Act in Parliament, several pieces of legislation, including a bill in the U.S. House of Representatives, a (now defunct) bill in the U.K. House of Commons, and a public consultation issued by Her Majesty's (HM) Treasury—the precursor to the Debt Relief Act—represented the continuum of solutions to the perceived problem. Generally, all three proposals and the Debt Relief Act limit the amount creditors are permitted to recover defaulted "poor" country debt in national courts. However, the scope of applicability and potential impact of each piece of legislation—notably what level of poverty qualifies a country for protection and the mon...
etary limits on recovery—vary dramatically. The growing urge to curtail vulture funds, as manifested in these legislative acts, came to the surface after Donegal International Ltd. \textit{v. Republic of Zambia}, where a hedge fund purchased Zambian trade debt owed to Romania since 1979 and sued to enforce the debt in U.K. courts. 

\textit{Donegal} and the introduction of these legislative proposals have paralleled an outcry from government officials and civil society over vulture fund "profiteering" from debt enforcement against the poorest countries. The overarching public policy aim of these legislative proposals is to support multilateral debt relief programs, such as the Heavily Indebted Poor Countries (HIPC) initiative, a debt relief initiative that received broad support from the international community and that is designed to minimize the impact of excessive public sector debt on domestic poverty reduction programs. But in the wake of the \textit{Donegal} case, little attention has been paid to anti-vulture fund legislative proposals that ignore any adverse impact some imbalanced provisions may have on the same countries purported to benefit from the legislation. Many international actors continue to frame the issue in terms morality and have not considered whether such radical approaches to curtailing low-income sovereign debt enforcement could increase the cost of borrowing for such countries or eliminate the market. More fundamentally, these entities either ignore a country’s ability to pay or conflate it with the country’s willingness to pay. In addressing the problems unveiled by \textit{Donegal}, do these legislative proposals go too far and perhaps impair multilateral initiatives to aid impoverished, highly-indebted countries? And will these legislative proposals really contribute to the ability of low-income countries to cope in the current economic climate?

This article aims to provide a framework in which to discuss these issues. In addition, it analyzes the three proposals and the enacted Debt Relief Act. Part I explains the facts of the \textit{Donegal} case. Part II discusses how the original legislative proposals incorporate and seek to address the problems revealed by \textit{Donegal}. Part III begins by explaining the international aid programs that provide the country classifications used by these proposals to determine which countries receive protection, then analyzes each legislative proposal and the enacted Debt Relief Act. Part IV offers a general critique of overly broad anti-vulture fund legislation that is motivated more by populist sentiment than by efforts to guard the integrity of multinational debt relief programs.

\textbf{I. DONEGAL INTERNATIONAL LTD. \textit{v. REPUBLIC OF ZAMBIA}}

In 2007, Donegal International Ltd., a special-purpose vehicle based in the British Virgin Islands and incorporated by Delaware-based Debt Advisory International LLC, sued Zambia in U.K. court to recover more than $55 million in connection with official debt assigned to Donegal by its original holder, Romanis. The debt was owed on a credit agreement originated in 1979 to finance Zambia’s acquisition of agricultural machinery from Romania. Starting in 1992, Romania and Zambia began trying to restructure that debt. In 1997, Debt Advisory International offered to purchase the debt from Romania, suggesting a 90% discount. After an offer from Zambia to buy back the debt for an 89% discount through the World Bank’s Debt Reduction Facility, Romania assigned the debt to Donegal in 1998 for $3.2 million, an 89% discount. After failed negotiations between Zambia and Donegal, in 2003 Zambia concluded a settlement agreement with Donegal, which included a broad waiver of Zambia’s sovereign immunity and under which Zambia agreed to pay $15 million plus additional interest payments. The agreement provided that upon default Zambia would be liable for the full amount of principal and interest due under the original agreement. At the recommendation of Zambia’s Task Force on Corruption, established to investigate misappropriation of public funds under a previous president, Zambia suspended payment under the settlement agreement. Despite concluding, \textit{inter alia}, that Donegal provided misleading information to courts in three countries, that Donegal’s actions in obtaining confidential information about the validity of the debt from government officials was unlawful, and that the interest rate provisions in the settlement agreement were penal, the English High Court found Zambia liable for the debt. However, in a later decision, a judge reduced Donegal’s $55 million claim and awarded Donegal a judgment of just over $15 million plus interest. Donegal has been criticized for failing to "set down clear guidelines for how to assess damages due to default on sovereign debt purchased on the secondary market," thus causing uncertainty as to secondary market holders’ legal entitlement to repayment.

Although unusual partly due to the low proportion of HIPC debt held by private creditors, sovereign debt claims brought by assignees are not unique. Liberia, Republic of the Congo, Uganda, Honduras, and Sierra Leone have all been the target of lawsuits. Recently, London’s High Court awarded two Caribbean-based investment funds over $18 million due to Liberia’s nonpayment of a $6 million loan issued by U.S.-based Chemical Bank in 1978. The award was the enforcement of a 2002 New York court $18 million judgment.

\textbf{II. AFTER DONEGAL—PUBLIC POLICY FIXES}

Other than inspiring general distaste for the enforcement of the debt of a country classified among the world’s poorest countries, Donegal’s efforts to enforce the full value of the debt was seen as counteracting multilateral debt relief initiatives available only to low-income countries, notably the HIPC Initiative. In 2005, Zambia became eligible for $2.5 billion in debt relief, which represented a 62.6% reduction in its public debt. The link between debt relief for low-income countries and poverty...
creditors to realise a loss and to be repaid an equal all.

certain creditors may recover on defaulted low-income sovereign in this position, insolvency-law generally provides for consultation. Although all four endeavours to limit the amount that debt is therefore correspondingly low. For companies and the predecessor to the Debt Relief Act, HM Treasury enacted Debt Relief Act, the Keeble Bill, the U.S. Vulture Act, expected to be unable to meet all of its repayment four pieces of legislation that are the subject of this paper: the nominal value of the debt: the debtor country is This section describes the structures and features of the creditors' debts is often much below the all value of the debt: the debtor country is

III. LEGISLATION

The link between debt relief for low-income countries and poverty reduction and development has been the bedrock of multilateral debt relief initiatives.

First, some view the enforcement of HIPC debt in national courts, despite long-established commitment by the international community to debt relief, as transferring the benefits of debt relief from its intended beneficiaries, the low-income countries, to vulture funds. All three original legislative proposals give this concern considerable weight. For example, the House of Representatives' Stop VULTURE Funds Act (U.S. Vulture Act) has likened low-income sovereign debt judgments to preferential payments from multilateral creditors to vulture creditors. The facts found by the House of Commons Developing Country Debt (Restriction of Recovery) bill (Keeble Bill) and is clearly expressed as a finding in the U.S. Vulture Act. Low-income countries such as Zambia, with weak governmental institutions and histories of political and economic exploitation and corruption, are especially vulnerable to private actors seeking improper influence. Problems of non-transparency in the secondary market for sovereign debt are addressed by the disclosure requirements in the Keeble Bill and U.S. Vulture Act. Feeding off the current political climate, these disclosure requirements have been suggested as a vehicle for financial regulatory reform. The facts found by the Donegal court illustrate the basis for these concerns. Lastly, a consideration not examined in Donegal is the extent to which payment of adverse judgments in connection with sovereign debt litigation exacerbates the social and economic conditions of countries such as Zambia. This question will be briefly examined in Part IV.
debt, their scope and potential impact vary substantially. In this respect, enactment of the Debt Relief Act represents a victory for proponents of balanced measures against the threat vulture funds pose to multilateral debt relief initiatives. Although the Keeble Bill is now largely irrelevant due to enactment of the Debt Relief Act, its provisions serve as an analytical counterpoint to the Debt Relief Act. Furthermore, by revealing its radical provisions, the Keeble Bill should serve as caution to the anti-vulture fund debate in other countries.

The core features of the proposals include: (1) indicators to determine whether a country qualifies for protection; (2) the height of the recovery ceiling; (3) a determination of whether the prohibitions apply to new borrowing; and (4) disclosure requirements. In addition, the proposals each have their own unique features. All four proposals rely, to different extents, on World Bank country classifications to determine what sovereign debt is covered. The World Bank and its branches use these classifications to determine whether a country qualifies for certain assistance and debt relief programs.69 The Keeble Bill extended its protections to IDA-eligible countries and “low and middle income” countries. The U.S. Vulture Act covers a class of IDA-eligible countries further limited by its own set of criteria.70 Consistent with its underlying public policy, the Debt Relief Act only applies to HIPC-eligible countries.71

A. World Bank Country Classifications

The IDA provides interest-free, deeply concessional loans (known as credits) and grants for “programs that boost economic growth, reduce inequalities, and improve living conditions.”72 Two criteria are used to determine which countries can access IDA resources: (1) relative poverty, defined as gross national income (GNI) per capita below an established threshold;73 and (2) “lack of creditworthiness to borrow on market terms and therefore a need for concessional resources to finance the country’s development program.”74 “Blend countries” are those that are eligible for IDA assistance but sufficiently creditworthy to borrow from the International Bank for Reconstruction and Development (IBRD).75 Non-blend countries are ineligible for assistance from the IBRD.76 Currently, seventy-nine countries are eligible for IDA assistance, including Zambia.77 Noably, India, a blend country and an emerging global economic power, is eligible for IDA assistance.78

The HIPR Initiative, complemented by the Multilateral Debt Relief Initiative,79 aims to alleviate the burden that excessive levels of debt payments impose on the ability of poor countries to provide poverty reduction programs.80 To be available for debt relief, a country must be IDA-eligible, “face an unsustainable debt situation even after the full application of traditional debt relief mechanisms,” and “have a proven track record in implementing strategies focused on reducing poverty and building the foundation for sustainable economic growth.”81 Once a country is eligible for the HIPR Initiative there are two stages to gaining debt relief—decision point and completion point.82 To reach decision point a country must have a satisfactory record of poverty reduction and must have achieved macroeconomic stability.83 Once a country reaches decision point, official creditors begin to provide debt relief, although they maintain the right to revoke.84 At decision point, the International Monetary Fund (IMF) and World Bank agree with the country on triggers that the country must meet to complete the initiative.85 Once the triggers are met, completion point is reached and the Paris Club and participating creditors cancel their debt in proportion to the common reduction factor.86 The common reduction factor is the “proportion of a country’s debt which all creditors will need to cancel in order to bring the debt to a sustainable level.”87 Currently, twenty-eight countries have reached completion point, seven countries have reached decision point, and five countries remain potentially eligible for HIPR debt relief.88 Lastly, the debt reduction facility complements the debt reduction goals of IDA and the HIPR Initiative.89

B. The Keeble Bill

The Keeble Bill, if enacted, would have had the most pronounced impact on primary and secondary sovereign debt markets. The Keeble Bill would have barred courts from awarding a “creditor of the defaulted debt of a Low or Middle Income country the right to recover in excess of the maximum recovery amount . . . .”90

“Low or Middle Income Country” was defined as “any country whose income group is classified as low income, lower middle income, or higher middle income” by the IBRD and the IDA.91 Consequently, the Keeble Bill was applicable to 144 countries, including the BRIC countries92 and other emerging economies such as Chile, Argentina, Turkey, and Mexico, and emerging European countries like Latvia, Poland, Lithuania, and Romania.93 Currently, the maximum amount a creditor can collect on covered debt is the amount paid for the debt plus the lower of 8% as calculated from the date the debtor acquired the interest94 and the interest rate under the sovereign debt agreement.95 Moreover, any amount recovered in U.K. courts must have been “reduced by a sum equal to any amounts recovered from other actions related to the same defaulted debt.”96

Under the Keeble Bill, before commencing an action in the U.K. to recover “any amount of defaulted sovereign debt,” a creditor “must make an application to, and receive the consent” of a U.K. court.97 The disclosure requirements needed in the consent applications98 would therefore have imposed additional costs on creditors seeking payment of defaulted sovereign debt that fell outside the Keeble Bill’s coverage.99

The Keeble Bill’s limit on recovery was intended to apply to “a business carrying on business in the United Kingdom” and to British citizens who successfully recover in foreign courts.
or through some dispute resolution procedure in excess of the maximum recovery amount. In such a case, the debtor country or interested party would have standing to force the creditor to "repay to the debtor country the amount that exceeds the maximum recovery amount." Lastly, there is no indication from the text of the Keeble Bill that its provisions would not have applied to debt originated after its enactment, i.e., to new borrowing. In addition, the Keeble Bill did not expressly exclude original creditors from its provisions.

C. U.S. Vulture Act

The U.S. Vulture Act would make "sovereign debt profiteering," whether direct or indirect, illegal not only for any U.S. citizen, but also for anyone operating in the United States. "Sovereign debt profiteering" is defined as:

any act by a vulture creditor seeking, directly or indirectly, the payment of part or all of defaulted sovereign debt of a qualified poor country, in an amount that exceeds the total amount paid by the vulture creditor to acquire the interest of the vulture creditor in the defaulted sovereign debt (excluding any amount paid for attorneys' fees or other fees and costs associated with collection), plus 6 percent simple interest per year on the total amount, calculated from the date the defaulted sovereign debt was so acquired, but the term does not include the purchase or sale of such a debt, or the acceptance of a payment in satisfaction of the debt obligation, without threat of, or recourse to, litigation.

Thus, the maximum amount that would be recoverable is the amount paid by the creditor to acquire an interest in the debt, plus 6% interest, calculated from the date the debt was acquired. Furthermore, as is evident from the final clause of the definition, the U.S. Vulture Act implicitly exempts consensual negotiations from its prohibitions, unless there is a threat of litigation. Parties found to willfully engage in sovereign debt profiteering would be "fined an amount equal to the total amount sought by the person through sovereign debt profiteering."

The legislation defines a "vulture creditor" as "any person who directly or indirectly acquires defaulted sovereign debt at a discount to the face value of the obligation so acquired . . . ." Thus, the U.S. Vulture Act would not apply to original lenders and trade creditors. Furthermore, the U.S. Vulture Act would not apply when a secondary creditor acquires the debt at face value.

The U.S. Vulture Act covers debt of "qualified poor countries." Under the Act, a qualified poor country includes those eligible for assistance from the IDA, but not from the IBRD. Additionally, the county must not be deemed to: "engage in pattern of gross violations of internationally recognized human rights" as defined by the Foreign Assistance Act of 1961; have "an excessive level of military expenditures;" provide support for acts of international terrorism; or fail to cooperate with the United States on international narcotics control matters. The first prong of the definition would extend the qualified poor country status to approximately forty-seven countries. It is uncertain to what extent the second prong of the definition would narrow the group of countries covered by the U.S. Vulture Act. Currently, Sudan is the only IDA-eligible country that has been designated as a sponsor of international terrorism by the State Department. In 2010, six IDA-eligible countries were among those identified by President Barack Obama, pursuant to requirements in the Foreign Relations Authorization Act, as major drug transit or major illicit drug-producing countries.

Several more were highlighted in the State Department's 2009 Country Reports on Human Rights Practices because of U.S. concerns about human rights abuses.

Like the Keeble Bill, the U.S. Vulture Act would require disclosure of specified information before suing in U.S. courts to recover qualified defaulted debt. The disclosure requirements are substantially similar to the disclosure requirements in the Keeble bill. However, these fairly onerous disclosure requirements are inapplicable unless the sovereign at issue is a qualified poor country.

The U.S. Vulture Act grants standing to "interested parties" to contest the furtherance of litigation that violates the Act. Lastly, like the Keeble Bill, there is no indication from the language of the U.S. Vulture Act that its prohibitions are limited to debt originated before the date of enactment.

D. HM Treasury Proposal

Of the three original proposals, the HM Treasury Proposal was the most tailored to advance and protect the goals of multilateral debt relief embodied in the HIPC Initiative. In its rebuttal to opposition consultation responses, the British government concluded that its proposals were "tightly targeted . . . at a fixed, historical stock of debt" and that "an extension beyond the HIPC Initiative would be unjustified and harmful." Notwithstanding the uncertainty as to which IDA-eligible, non-blend countries would be exempted from the U.S. Vulture Act under that bill's definition of qualified poor countries, the HM Proposal covered the smallest number of countries out of the three original legislative proposals. The HM Proposal also relied on the HIPC Initiative terms to determine the maximum recoverable amount. The HM proposal favored applying a Common Reduction Factor on "traditional terms," i.e., 67%. Thus, under the HM Proposal's preferred method, the maximum recoverable amount would be 67% of the face value of the debt. Second, the HM Proposal cautiously disfavored applying recovery limits to original creditors, new borrowing, and debts contracted after decision point. Furthermore, the proposed
legislation would have applied only to existing judgments that had yet to be enforced.\textsuperscript{127}

Additionally, the HM Proposal differed from the Keeble Bill in two other important respects. First, it opposed the imposition of disclosure requirements as a prerequisite to litigation because the requirements would impose "additional procedure and transaction cost[s]" and would be "insufficient to be a robust deterrence."\textsuperscript{128} Second, the HM Proposal supported granting courts discretion to vary the terms of the law if they consider it just and equitable to do so.\textsuperscript{129}

E. Debt Relief (Developing Countries) Act of 2010

As noted above, the Debt Relief (Developing Countries) Act of 2010 (the Act), in general, codifies the HM Proposal. The Act provides that the amount of a "qualifying debt" or any cause of action relating to a qualifying debt is the "relevant proportion" of the amount that would otherwise be recoverable under the terms of the qualifying debt or cause of action.\textsuperscript{130} The Act defines a "qualifying debt" as the debt of a country "to which the [HIPC] Initiative applies" or of those countries that are potentially eligible for the HIPC Initiative.\textsuperscript{131} A "potentially eligible Initiative country" is a country that has been identified by the IMF and World Bank as eligible for debt relief under the HIPC Initiative, but has yet to reach decision point.\textsuperscript{132} A country to which the HIPC Initiative applies is a country currently receiving HIPC debt relief, i.e., a country categorized as "post-decision point" or "post-completion point."\textsuperscript{133} Whether a country is eligible or potentially eligible may affect the amount recoverable.

The Act excludes from the definition of "qualifying debt" those debts incurred after commencement of the Act and debts contracted after a country's decision point has been reached.\textsuperscript{134} Once the Act took effect, forty countries were eligible or potentially eligible for HIPC debt relief.\textsuperscript{135} Furthermore, the Act precisely defines "debt."\textsuperscript{136} Much of this was included in order for the Act's terminology to conform with the terms used by the World Bank and IMF when determining which debts are covered by the HIPC Initiative. For example, the Act generally excludes "short-term" debts and trade debt from coverage.\textsuperscript{137}

The maximum recoverable amount, i.e., the "relevant proportion" under the Act, may turn on whether the debt being enforced is that of a country "to which the [HIPC] Initiative applies" or a "potentially eligible [HIPC] Initiative country." For countries currently eligible for HIPC debt relief, the "relevant proportion" is 67%—the traditional common reduction factor—and, if applicable, a "topping up" of assistance to further reduce the common reduction factor, divided by the amount of the debt before the reduction.\textsuperscript{138} Accordingly, the maximum a creditor could recover from covered debt would be 67% of its face value. The "relevant proportion" for debts of a potentially eligible HIPC Initiative country is 67%.\textsuperscript{139} The amount recoverable under agreements that reduce the debtor's obligations through a rescheduling or compromise agreement is limited to the amount that would have been recoverable if no such agreement had been made, i.e., if a compromise or refinancing agreement would otherwise entitle the creditor to an amount that exceeds the "relevant proportion" by which the amount recoverable would be reduced.\textsuperscript{140} In addition, the limit on recovery only applies to domestic and foreign judgments and arbitral awards given prior to the Act taking effect.\textsuperscript{141} The Act expressly applies the limits on recovery to those causes of action related to "qualifying debts," such as damages claims.\textsuperscript{142}

The Act materially departs from the original HM Proposal in several ways. First, the Act does not authorize courts to vary the terms of the law if they consider it just and equitable.\textsuperscript{143} In fact, the government ultimately agreed with the detractors of such a provision, stating that "it would be difficult for courts to apply in the absence of precedent... and would remove the legal certainty and clarity provided by [the] legislation."\textsuperscript{144} Second, in order for sovereign debtors to avail themselves of the Act, the debtor must "make an offer to compromise the proceedings on comparable Initiative terms."\textsuperscript{145} This provision does not apply to proceedings to enforce domestic judgments awarded before commencement of the Act.\textsuperscript{146} Third, the Act includes a sunset clause whereby the Act would expire one year after commencement unless it were extended, either for another year or permanently, by order of HM Treasury with statutory approval by each House of Parliament.\textsuperscript{147} The sunset amendment was proposed as a way to allow the bill to proceed while assessing whether its provisions increased the risk premium on qualifying debt.\textsuperscript{148} Fourth, the Act exempts enforcement of foreign judgments and arbitral awards if their enforcement would be inconsistent with European law or an obligation of the United Kingdom.\textsuperscript{149} Lastly, and most significantly, there is no indication in the Act that non-trade, original creditors are excluded from the Act's provisions. This would seem to be an extraordinary provision that would significantly increase the risk premium on qualifying debt. This risk is mitigated, however, as qualifying debt incurred after the Act takes effect would not be affected.

F. Potential Adverse Side Effects and Design Flaws

1. Moral Hazard—Here We Go Again

When discussing sovereign debt and financial crises, moral hazard is perennially used to challenge robust government action to stem the causes and effects of the spread of distressed debt. The U.S. Vulture Act, by failing to exclude new lending from its coverage, may be especially vulnerable to attacks on the grounds that it generates moral hazard among covered sovereign debtors. It should be noted, however, that the proposals do not simply seek to enact incentives to influence the substance of low-income sovereign debt litigation. When forum-shopping for a favorable litigation environment is limited,\textsuperscript{150} often the optimal choice...
for covered sovereign debtors holding distressed debt may be to default. \(^{151}\) When drawing the line between covered and non-covered countries, failing to make the distinction between the highly impoverished and indebted, such as Zambia, and developing countries that are not IDA-eligible would seriously exacerbate the moral hazard problem. Ecuador’s recent declaration of default and subsequent buy-back at a heavy discount illustrates the potential risk. \(^{152}\) The Debt Relief Act expressly addresses the problem of increasing moral hazard by exempting debts contracted after decision point and those originated after enactment from the Act’s protections. \(^{153}\)

**Such legislation would increase the risks of covered debt in the secondary market and may directly affect the primary market as well in the case of legislation, such as the U.S. Vulture Act, that does not exclude new lending.**

2. **The Secondary Market and the Theoretical Costs of Borrowing**

Economic reasoning suggests anti-vulture fund legislation may increase the cost of borrowing for covered sovereign debtors. An active secondary market in sovereign debt, of which vulture funds are prominent participants, is “a fundamental feature of sovereign borrowing and lending.” \(^{154}\) Such legislation would increase the risks of covered debt in the secondary market and may directly affect the primary market as well in the case of legislation, such as the U.S. Vulture Act, that does not exclude new lending. \(^{155}\) The unnecessary distortion that the U.S. Vulture Act creates (and any other proposals modeled after it and the Keable Bill) does not stop there. Under the U.S. Vulture Act, recovery on covered debt is capped by the price paid for the debt plus 6%, rather than by HIPc terms, as in the Debt Relief Act. \(^{156}\) This means that, under the U.S. Vulture Act and similar proposals, otherwise identical debts may entitle holders to different repayments simply because the debts were bought and sold at different times. \(^{157}\) This is an attack on the fair treatment of creditors of equal seniority, the prevention of which is a core public policy aim of insolvency law. \(^{158}\)

Moreover, the effects on the secondary market are also likely to indirectly influence the primary market for covered debt. \(^{159}\) Limiting the contractual right to recover on defaulted debt would decrease the amount for which original creditors can sell the debt on the secondary market—i.e., the recovery value—thereby potentially increasing interest rates for the debtors. \(^{160}\) The resulting reduction in liquidity in the primary and secondary market for covered debt \(^{161}\) by potentially increasing the burden of servicing debt would be contrary to the goals of the HIPc Initiative. \(^{162}\)

3. **Why It Matters**

A fundamental question (perhaps the fundamental question) in the debate concerning anti-vulture legislation is the extent to which payments pursuant to judgments or settlement agreements affect the economic growth of low-income nations and direct limited resources away from crucial public services. Somewhat surprisingly, there is a dearth of economic studies investigating this question. The conditions facilitating Africa’s “poverty trap,” however, have received constant attention and study. \(^{163}\) Unlike other developing countries, low-income countries such as Zambia face overwhelming public health challenges, such as the high proportion of individuals affected by HIV/AIDS in African populations. \(^{164}\) Therefore, the marginal effect of one dollar redirected from public health programs to paying sovereign debt judgment is much higher than the effect on other non-IDA developing countries. Indeed, this rationale is the cornerstone of the HIPc Initiative. A cursory review of the current picture on sovereign debt litigation suggests that such litigation does have the potential to be disastrous for low-income countries. At the end of 2007, awards on sovereign debt claims ranged from 0.5% of the debtor’s GDP to 49% of the debtor’s GDP, as in the case of Liberia. \(^{165}\) The recent enforcement in London High Court by vulture funds of over $18 million in Liberian debt amounted to 5% of Liberia’s 2009 budget. \(^{166}\) Liberia is a country still reeling from the aftermath of a civil war between 1989 and 2003, a country that ranks 208th in per capita income, above only Democratic Republic of Congo and Burundi. \(^{167}\)

IV. **CONCLUSION**

In light of the existing international commitment to poverty reduction and debt relief, anti-vulture fund legislation motivated by a desire to punish an amorphous group of “vulture” investors could contribute little and detract much. Anti-vulture fund legislation that is not carefully calibrated to advance the goals of debt relief while minimizing the adverse effects that may result from tampering with credit markets, such as a reduction in liquidity, will be counter-productive. The British Parliament succeeded in striking the right balance: a product of informed and reasoned debate. If the U.S. Congress decides to move forward with anti-vulture legislation in the future, the Debt Relief Act and its surrounding debate should serve as a model.

The Debt Relief Act should provide several guiding principles. First, punitive legislation is unproductive. Selecting civil fines as the remedy, rather than directly empowering defendants, is at best an inelegant and inefficient solution to the problem and is at worst disingenuous. Second, legislators should design anti-vulture fund legislation that aims to accomplish their stated
goal: to prevent investors from redirecting the benefits of multilateral debt relief programs, principally the HIPC Initiative, away from recipient countries and toward secondary market investors. Imposing an arbitrary recovery ceiling, as the U.S. Vulture Act does, not only seems unfair as it would lead to the same debts having different values merely based on when they were bought, but has no relationship with the HIPC Initiative.

ENDNOTES

1. See generally Lex Riffel, Restructuring Sovereign Debt: The Case for Ad Hoc Machinery 150–51 (2003) (explaining the main features of the Brady Plan, namely the conversion of Latin American countries’ bonds into new bonds after defaults by those countries in the 1980s and the corresponding impact on commercial banks involved in lending to those countries).

2. Lee C. Buchheit, You’ll Never Eat Lunch In This Conference Room Again, 11 INT’L FIN. L. REV. 11, 11 (1992) (describing the paradoxical terms that were commonplace during the sovereign debt restructurings of the 1980s).


4. See Foreign Sovereign Immunities Act (FSIA), 28 U.S.C. §§ 1605–11 (2006) (codifying in U.S. law the extensive protections afforded to sovereign states against litigation in other jurisdictions). According to Argentine Republic v. Amendoa Bros. Shipping Corp., 488 U.S. 428 (1989), the FSIA is the sole basis for obtaining jurisdiction over foreign sovereigns in U.S. courts; however, Semtex v. Youth, 150 S. Ct. 2278 (2010), indicates immunity is also conferred by preempting common law. The FSIA codifies international law’s modern definition of sovereign immunity, which states immunity should be “restricted” to acts of a foreign state that are sovereign or governmental in nature, rather than commercial in nature or normally associated with private persons. The traditional exceptions to sovereign immunity are waivered by the sovereign; activity deemed to be commercial rather than governmental in nature property taken in violation of international law, tortious act or omission under the home jurisdiction’s law; and contractual consent to arbitration.


7. See Press Release, HM Treasury, Legislation to Ensure Effective Debt Relief for Poor Countries (July 24, 2009) (defining vulture funds, generally, as investment funds that purchase distressed or defaulted debt at a discount and then seek to make a profit on the debt by reselling the debt, negotiating a settlement with the debtor, or litigating the defaulted debt for face value).

8. See, e.g., Zambia Law ‘Vulture Fund’ Case, BBC News (Feb. 15, 2007), http://news.bbc.co.uk/2/hi/3654333.stm [hereinafter BBC News Zambia]; see also Written Ministerial Statement by Mr. Gordon Brown, C. of the Exchequer to the House of Commons (May 10, 2007), http://www.publications.parliament.uk/pa/cm200607/cmhansrd/cm070510/wmstatement/070510n0001.htm (‘‘I explore the activities of so-called vulture funds that seek to profit from debts owed by the poorest countries in the world . . .’’).

9. See, e.g., Peers & Weissman, supra note 3, at 701 (arguing the “United States has used bank loans in the world system as a dominant factor of imperialism”); see also Joseph K提示, The Mexican Rescue 1–24 (1984) (explaining the prevailing view at the time of the Mexican crisis was that not responding to the crisis would destabilize Mexico and thus adversely affect U.S. interests).


15. Stop VULTURE Funds Act, H.R. 2932, 111th Cong. (2009); see discussion infra Part III.


17. Public consultation in Commonwealth countries is a regulatory process that serves a similar function as the notice and comment procedure under U.S. state and federal administrative law. See generally DELIA RODRIGUEZ & PEDRO ANDRES ABO, ORG. FOR ECON. CO-OPERATION & DEV., BACKGROUND DOCUMENT ON PUBLIC CONSULTATION, http://www.oecd.org/dataoecd/4/43/36785341.pdf.

18. HM TREASURY, Ensuring Effective Debt Relief for Poor Countries: Consultation on Legislation 2009–10 [hereinafter HM Treasury Consultation]; see also discussion infra Part III.

19. The Government, represented by Economic Secretary to the Treasury Ian Pearson, indicated that it supported the Bill and assisted in the preparation of its explanatory notes. See Debt Relief (Developing Countries) Bill Research Paper, H.C. Research Paper 10/17 at 32 (2010).

20. [2007] EWHC (Comm) 197 (Esg.).

21. See, e.g., 6 May 2009, PARL. DEB., H.C. (2009) 175 (statement of Ms. Sally Keeble) [hereinafter Keeble statement] (noting the Donogah case as illustrative of “profiteering” that the Developing Country Debt (Restriction of Recovery) Bill is meant to address); see also Michael Whil, An Elusive Quest After the Donogah Case, Compensation for Sovereign Defaults Remains Uncertain, 26 Int’l Fin. L. REV. 32, 32 (2007) (“The case has generated considerable controversy, due to perceived abuse of the HIPC Initiative.”).

22. See BBC News Zambia, supra note 8 (quoting Jubilee Debt campaigner Caroline Pearce, “Profiteering doesn’t get any more cynical than this. Zambia has been planning to spend the money released from debt cancellation on much-needed nurses, teachers and infrastructure. This is what debt cancellation is intended for, not to line the pockets of businessmen rich in countries.”).

23. For more information on the HIPC Initiative, see supra Part III.

24. See, e.g., Mfinga Ngoyi, Deriving Maximum Social Benefits from Debt Relief: A Case of Zambia, 9 AM. VIEWPOINT (2009); see also The Basics About Debt, THE JUBILEE DEBT CAMPAIGN, http://www.jubileedebtcampaign.org.uk/fid-98 (asserting that “[d]ebts should be cancelled because they are unjust in terms of their origin, and also because they worsen poverty”).


26. Throughout, dollar amounts are in U.S. dollars.

27. Donogah I, [2007] EWHC (Comm) 197 [1], [6], [23], [24].

28. Id. at [6].

29. See Waldb, supra note 21, at 32.
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30 Id.

31 See infra notes 43-44 and accompanying text (describing the World Bank Debit Reduction program).

32 Donegal, [2007] EWHC (Comm) at [2], [6], [9]-[11].

33 See Waibel, supra note 21, at 52 ("In 2001, Donegal proposed an immediate cash settlement at 37%, about $30 million. Zambia responded with a 10% offer consistent with comparable treatment under the HIPC initiative, which Donegal called completely unacceptable.").

34 See id.

35 HMT Treasury Consultation, supra note 18, at 15.

36 See id.


38 Waibel, supra note 21, at 33 (citing Donegal, [2007] EWHC (Comm) 397).

39 Donegal, [2007] EWHC (Comm) 397 at [6] (reducing also Donegal's costs by one-third due to dispositive evidence presented to the court by Donegal witnesses and reinstating narrower freezing relief).

40 Waibel, supra note 21, at 33.

41 See Anna Gelpem, Odissa, Not Debt, 70 LAW & CONTEMP. PROBS. 81, 82 (2007).


43 See CANUTO & MOGHADAM, supra note 42, at 62.


45 See id.


48 See Arewa, supra note 66, at 644 (discussing how Zambia has also negotiated a loan reduction agreement with the Paris Club, an informal group of largely developed world creditor countries).

49 See, e.g., HMT Treasury Consultation, supra note 18, at 11 ("Debt relief contributes to poverty reduction and development for low income countries by reducing the unmanageable burden of debt that many had built up in the decades to the 1990s.").

50 See id. ("Debt relief frees up resources for these priorities — for example, countries that have benefited from relief have raised average spending on health and education from 7 per cent to 9 per cent of Gross Domestic Product and now spend an average six times more on them than they do on debt service. There is also some evidence that countries that have received relief benefit on average from an improved macroeconomic position, with higher economic growth and lower inflation."). (internal footnote omitted) (citing IMF and World Bank studies).

51 See Anna O. KUHUIER, INT'L MONErNY FUND, A NEW APPROACH TO SOVEREIGN DEBT RESTRUCTURING (2002), Ashley Seager & James Lewis, How Top London Firms Help Vulture Funds Devour Their Prey, THE GUARDIAN, Oct. 17, 2007, at 27 ("Liberal Democrat international development spokesperson Lynne Featherstone says that Mr. Brown has the power to do more. "He needs to legislate and make it illegal to use London's high court for this. One wants the law firms to come to the conclusion this is a dirty business they don't want to be involved in.").


54 This term refers to transactions made shortly before an entity files for protection within the insolvency system that facilitate the distribution scheme set forth in the applicable insolvency law. WILLIAM WAREN & DANIEL BUBEL, BANKRUPTCY 349-98 (7th ed. 2006). Under U.S. bankruptcy law, the trustee (or debtor-in-possession) may, in certain circumstances, undo certain of these pre-bankruptcy transactions and recover the payments for the benefit of the estate. Once recovered, the transferred property becomes part of the bankruptcy estate and may be distributed to creditors under a liquidation plan or a restructuring plan. 11 U.S.C. §§ 547, 550(a) (2006).

55 See H.R. 2932, § 2(0)-(9).

56 See STURZENEGGER & ZETTELMEYER, supra note 5, at 62-65 (describing the collective action problems that exist in sovereign debt litigation and describing the major sovereign debt cases as illustrative).


58 See discussion infra Part III.


62 See Gelpem, supra note 41, at 32.

63 See id.

64 See supra note 23 and accompanying text.

65 See, e.g., Keeble statement, supra note 21 (explaining that the bill has four main provisions: stopping excessive profiteering, introducing accountability, ensuring greater transparency, and combating corruption).


67 H.R. 2932, 111th Cong. § 2(16) (2009) ("To be effective . . . in an area affecting the foreign relations of the United States, national legislation is required that will mandate the public disclosure of relevant information concerning the acquisition, ownership, and consideration provided by creditors in obtaining . . . interests in the defaulted sovereign debt of poor countries.").

68 See Keeble statement, supra note 21 (explaining that a principal aim of the bill was to regulate hedge funds, a much needed regulatory reform highlighted by the "under-regulation of various financial market actors" revealed by the recent economic crisis).

69 See Waibel, supra note 21, at 32-33.


71 See H.R. 2932 § 6(a) (requiring the U.S. Department of the Treasury to maintain lists of IDA-eligible countries, but also listing other restrictions on eligibility, such as recognition of human rights, level of military expenditures, involvement with terrorists, and failure to cooperate with U.S. narcotics authorities).

72 See Debt Relief (Developing Countries) Act 2010 c. 221(6).


75 Id.

76 See id. The following are currently blind countries: Cape Verde, Zimbabwe (inac­ tive), Papua New Guinea, Armenia, Azerbaijan, Bosnia-Hercegovina, Georgia, Uzbekistan, Dominica, Grenada, St. Lucia, St. Vincent and the Grenadines, India, Vietnam, Bolivia, and Pakistan. Id. In addition, countries designated as "small island economies"
are exempted from the per capita GNI threshold requirement. **What is IDA?**


80 HM Treasury Consultation, supra note 18, at 11.

81 IBRD — Frequently Asked Questions, supra note 76.

82 Debt Relief and Development, supra note 79.

83 See id. (announcing that the requirement a country must meet at decision point include a poverty reduction strategy and debt burden indicators above specific HIPC Initiative thresholds).

84 Id.

85 See id. (interpreting the completion point triggers as a series of measurable goals necessary to complete the HIPC Initiative).

86 See id. (explaining the common reduction factor "is calculated to bring the country’s debt (both to 150 percent of exports (or in certain cases 250 percent of fiscal revenues))."

87 HM Treasury Consultation, supra note 18, at 12.


89 See discussion supra Part II.

90 Developing Country Debt (Restriction of Recovery) Bill, 2009, H.C. Bill [91], art. 2 (U.K.).

91 Id. at 5.


95 As defined by the Keeble Bill, the maximum recovery amount equaled:

(a) the amount paid by a creditor to acquire the interest the creditor has in the defaulted sovereign debt (excluding any legal fees or other fees and costs associated with collection); and

(b) interest, calculated as simple interest only, on the amount the creditor paid to acquire the interest in the defaulted sovereign debt, from the date the creditor acquired rights over the defaulted sovereign debt, and at an interest rate which is the lower of:

(i) the interest rate in the loan agreement for the sovereign debt; or

(ii) the interest rate set in accordance with section 17 of the Judgments Act 1838 (c. 110).

Developing Country Debt (Restriction of Recovery) Bill, 2009, H.C. Bill [91], art. 3 (U.K.) (emphasis added).

96 Id. (emphasis added).

97 Id. at 6.

98 The disclosures in the consent application included, inter alia, the amount paid by all persons who would receive a financial benefit of more than 1% from the recovery proceeding; information on the creditor’s business including, for example, accounts for the previous financial year and a statement that the creditor, or any of its agents, has not improperly influenced any of the debtor’s government officials in connection with acquisition of the debt. Id. at art. 6(a)(g).

99 Considering the broadness of the sovereign debt covered by the Keeble Bill, it appears that in practice the disclosure requirements would have never applied to non-covered sovereign debt, as the Keeble Bill only excluded "high-income economies" from its provision. Compare id. at [91], cl. 1 ("[L]ow or Middle Income country’ means any country whose income group is classified as low income, lower middle income or higher middle income by the International Bank for Reconstruction and Development and the International Development Association.") (emphasis added), with Country and Lending Groups, supra note 93 (categorizing all countries as either low income, lower middle income, higher middle income, or high income).

100 H.C. Bill [91] art. 9.

101 See id.

102 The Keeble Bill could have been interpreted to apply only to secondary market creditors and not original creditors, because it referred to the amount the creditor "paid" to acquire the interest in defaulted sovereign debt. However, this is not the only conceivable construction. Lenders "pay" for the stream of interest payments under loan agreements or such other consideration that may be agreed upon. If original lenders were seen as covered under the Keeble Bill, the amount "paid" by the creditor to acquire the interest in the debt could be based on the net present value of the debt at time of its origination. This interpretation and valuation would be a complicated task for anyone. In any case, whether the Keeble Bill applied to original lenders would have been of little practical consequence. It is hard to envision when a lender would receive more from enforcing a debt obligation through litigation than accepting their consideration under the loan agreement.

103 See VULTURE Funds Act, H.R. 2932, 11th Cong. § 4(a) (2009).

104 Id. § 3(4) (emphasis added).

105 Id.

106 Id. § 4(b).

107 Id. § 3(4) (also excluding the U.S. government, or any of its agencies, foreign states, and international financial institutions from the definition).

108 See id.

109 Thus, blend countries, those are eligible for both IDA and IBRD assistance, would not be covered by the U.S. Vulture Act. See supra notes 75-76 and corresponding text.

110 Id. § 6(d). There additional requirements would allow the Secretary of the Treasury to maintain a list of those countries meeting the parameters for qualified poor country status. See Id. § 3(6) (the term "qualified poor country" means a foreign state identified on the list maintained by the Secretary of the Treasury under section 650(2)).

111 Country and Lending Groups, supra note 93 (arriving at forty-seven by taking the sixty-three countries eligible for IDA aid and subtracting the sixteen blend countries).

112 Compare State Sponsorship of Terrorism, U.S. DEP'T OF STATE, FOREIGN POLICY, 3-9 (2010) (listing countries that raise concerns because of human rights issues during times of conflict, including the IDA-eligible Afghanistan, Myanmar, Democratic Republic of the Congo, Nigeria, Sri Lanka, and Sudan, and because of general discrimination against vulnerable minority groups, which included the IDA-eligible Uganda).

113 See id.; see also Treaty of December 5, 2000, International Monetary Fund, http://www.imf.org/external/np/exr/facts/2000/071400.htm (listing countries that raise concerns because of human rights issues during times of conflict, including the IDA-eligible Afghanistan, Myanmar, Democratic Republic of the Congo, Nigeria, Sri Lanka, and Sudan, and because of general discrimination against vulnerable minority groups, which included the IDA-eligible Uganda).

114 See U.S. EM’Y of STATE, 2000 HUMAN RIGHTS REPORT (March 11, 2010), available at http://www.state.gov/g/drl/hr/2009/finreport/135936.htm (listing countries that raise concerns because of human rights issues during times of conflict, including the IDA-eligible Afghanistan, Myanmar, Democratic Republic of the Congo, Nigeria, Sri Lanka, and Sudan, and because of general discrimination against vulnerable minority groups, which included the IDA-eligible Uganda).

115 See H.R. 2932 § 5(b).


117 See H.R. 2932 § 5(b)(1)-(3).

118 See id. § 5(b) ("If it appears to a court in... of the United States that an action brought in the court constitutes, or is in furtherance of, sovereign debt profiteering, the court shall, on its own initiative or at the request of any interested party, promptly dismiss the action.").

119 HM Treasury, Ensuring Effective Debt Relief For Poor Countries: A Response to Consultation § 2.27 (2010).

120 See supra notes 115-120 and corresponding text.

121 See HM Treasury Consultation, supra note 18, at 25 ("One legislative approach would be to make HIPC Initiative terms the binding reference point for commercial creditors.").

122 See supra note 86 and corresponding text (explaining the Common Reduction Factor).
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bill added to the (2010)(providing...apts from the Common DebtReliefAct,ExplanatoryNotes~ see also id.

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146 DebtRelief(DevelopingCountries)Act,ExplanatoryNotes,2010, ch. 22, §4 (defining "comparable Initiative terms"); see DebtRelief(DevelopingCountries)Act,ch.22,§2. 

145 H.C.RESEARCH PAPER NO. 10117, supra note 19, at 16. 

144 Compare DebtReliefAct, ch. 22, with HM TREASURY CONSULTATION ON LEGISLATION, supra note 18, §4.12. 

143 DebtReliefAct, ch. 22, §6(1); see id. §2 (defining "comparable Initiative terms"); see also Debt Relief (Developing Countries) Act, Explanatory Notes, 2010, ch. 22, §30 (specifying the discount rate applied in association with the HIPC Initiative is the relevant Commercial Interest Reference Rate, as published by the OECD and explaining the requirement's purpose: to encourage the debtor to participate in negotiations).

142 Id. § 3(1). 

141 DebtReliefAct, ch. 22, § 5(1); DebtRelief (Developing Countries) Act, Explanatory Notes, 2010, ch. 22, § 16. 

140 H.C.RESEARCH PAPER NO. 10117, supra note 19, at 26. 

139 Compare DebtReliefAct, ch. 22, § 7(1); see also id. § 7(2) (listing several types of foreign judgments that are per se excluded under the Act).