

Stop Them Circling: Addressing Vulture Funds in Australian Law

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Abstract

Vulture funds are private investment funds that trade in the defaulted or soon-to-default sovereign debt usually issued by the world's most Heavily Indebted Poor Countries. They use their rights as creditors to obtain profitable returns from sovereign debtors, potentially expanded beyond the debt's original value by interest, penalties and other associated costs. In November 2010, vulture funds entered Australian law when the New South Wales Supreme Court ordered the Democratic Republic of Congo to pay out nearly A\$12 million in an action seeking repayment. Yet in the three years since that decision, no Australian legal analysis has arisen to examine either vulture funds and their business here or the policy contradiction between Australia's commitment to reduce global poverty and our common law's facilitative role in assisting such activity. This article examines the nature of vulture funds, the circumstances that have led to their existence and possible methods to limit their activities. It argues that Australia should adopt a solution closely resembling the legislative approach of the United Kingdom, which deters vulture fund activity but does not undermine the global market for sovereign debt.

I Introduction

In 1980 and 1986, the government of the country then known as Zaire entered into two contracts with Yugoslav company Energoinvest to provide the country with electricity generation and transmission infrastructure. To fund these transactions, the regime of Mobutu Sese Seko and Zaire's national electricity company, Société Nationale d'Électricité, entered a credit arrangement with Energoinvest containing International Chamber of Commerce ('ICC') arbitration clauses for dispute resolution purposes.¹ Unfortunately, by the late 1980s, both the government and its electricity company had defaulted on their debt. Eventually, in 2003, two ICC arbitrations led to a pair of arbitral awards requiring that the now-Democratic Republic of the Congo ('DRC') repay Energoinvest US\$11 725 844.96 and US\$18 430 555.47 plus interest of nine per cent and costs.² Subsequent litigation

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¹ Teresa Cheng and Adrian Lai, *Lessons Learned from the FG Hemisphere v DRC and Huatianlong Case* (9 December 2011) International Council for Commercial Arbitration, 1–2 [3] <http://www.arbitration-icca.org/articles.html#articolo_138>.

² *Ibid* 2 [4].

in the United States District Court for the District of Columbia confirmed each award in 2004 and 2005 respectively, ensuring enforceability within United States jurisdictions.³

On 16 November 2004, Energoinvest sold its interests in these decisions to FG Hemisphere LLC ‘at a discount ... [but representing] market price’, ostensibly because it ‘needed liquidity’.⁴ FG Hemisphere (today called ‘FG Capital Management’) is an investment firm ‘specialising in uncovering, investigating and managing alternative investment opportunities and special situations within the emerging markets’.⁵ Having acquired this debt, FG Hemisphere sought a plaintiff’s first request for production from the District Court of the District of Columbia in 2005, compelling the DRC to provide detailed information on any valuable state-owned assets located throughout the world.⁶ The order was granted soon after filing, before the DRC had even translated FG Hemisphere’s application from English to French.⁷ Given the diversion of economic and bureaucratic resources necessary to meet this order, the DRC did not follow up on it for three years. In response, FG Hemisphere filed a further motion in the District Court on May 2008 to hold the DRC in contempt.⁸ By March 2009, the DRC was being penalised US\$5000 per week for its failure to comply, rising every four weeks to a maximum of US\$80 000 per week.⁹ Once FG Hemisphere was furnished with the desired asset information, allowing it to bring legal action against the DRC in the Bahamas, Australia, Hong Kong, Jersey, South Africa, and the United States, the total sum sought for repayment had reached US\$125 924 407.72 by way of principal, costs and interest.¹⁰

The DRC is one of the two lowest ranked countries (186th) in the 2013 UN Human Development Report, with GDP per capita of PPP\$329 and 45.9 per cent of its people living in severe poverty.¹¹ Following the country’s pillaging by dictator Mobutu Sese Seko in the 1980s and 1990s,¹² the DRC has been involved (sometimes involuntarily) in a series of regional conflicts, most recently a now 15-year-old civil war that has claimed ‘at least 30 times as many lives as the Haiti

³ Cephias Lumina, *Report of the independent expert on the effects of foreign debt and other related international financial obligations of States on the full enjoyment of all human rights, particularly economic, social and cultural rights*, UN HRCOR, 14th sess, Agenda Item 3, UN Doc A/HRC/14/21 (29 April 2010) 8, 9.

⁴ Peter Grossman, *FG Hemisphere Associates Responds to Inaccurate and Misleading Media Reports* (2 December 2011) FG Hemisphere Associates LLC <<http://www.fgcap.net/statement.html>>.

⁵ Heather Stewart and Ashley Seager, ‘Vulture Fund Swoops Down on Congo over \$100m Debt’, *Business, Media and Cash, The Observer* (London), 9 August 2009, 1.

⁶ *FG Hemisphere Associates LLC v Democratic Republic of Congo*, 603 F Supp 2d 1 (DDC, 2009).

⁷ Michael Stulman, ‘Indebted Nations Fight off Vulture Funds’, *Asia Times Online* (online), 8 July 2009 <http://www.atimes.com/atimes/Global_Economy/KG08Dj02.html>.

⁸ Lumina, above n 3, 8.

⁹ Stulman, above n 7.

¹⁰ Cheng and Lai, above n 1, 2 [5]; Lumina, above n 3, 8.

¹¹ United Nations Development Programme, *Human Development Report 2013* (2013), 160, 165.

¹² Charlotte Denny, ‘Suharto, Marcos and Mobutu Head Corruption Table with \$50bn Scams’, *The Guardian* (online), 25 March 2004 <<http://www.guardian.co.uk/world/2004/mar/26/indonesia.philippines>>.

earthquake'.¹³ It is noteworthy that, although there is no evidence to prove correlation, the litigation claims initiated by FG Hemisphere against the DRC throughout the world have almost perfectly coincided with this ongoing humanitarian disaster, which understandably consumes most of the DRC government's attention. This case emphasises the lengths to which sovereign states can be coerced by creditors into meeting debt obligations that they are in no position to repay.

Given their method of deriving profit, it is unsurprising that FG Hemisphere and similar investment vehicles are labelled 'vulture funds';¹⁴ such investors proverbially feed on, or more accurately pick the bones of, the vulnerable members of the global community. On 1 November 2010, this 'scavenging' entered the Australian legal system, when the New South Wales Supreme Court handed down an *ex tempore* judgment in favour of FG Hemisphere, after the DRC gave up trying to defend its case.¹⁵ The total award from the NSW Supreme Court exceeded US\$31 million, and required the DRC to liquidate its share assets in Australian mining interests in order to repay FG Hemisphere.¹⁶ The large award conferred is unsurprising in vulture fund cases: the African Development Bank Group ('AfDB') estimates that vulture funds achieve immense returns between 300 and 2000 per cent of capital invested, even after deducting legal fees and other costs.¹⁷ Of course, this is to the detriment of the nations sued, where the potential impact of such court awards ranges from 0.5 per cent of a debtor country's GDP to 49 per cent in one particular example.¹⁸ In the FG Hemisphere case, it is thought that the fund purchased the underlying debt for US\$3.3 million,¹⁹ making a 939 per cent return on the Australian suit alone.

The content of Hammerschlag J's one-page judgment is a straightforward summary of international arbitral law within Australian jurisdictions. Beyond that, the case demonstrates how easily vulture funds can claim income and property from Heavily Indebted Poor Countries ('HIPC'),²⁰ the common target in these cases. HIPCs tend to have limited resources with which to fend off such claims in various jurisdictions, and are left little or no alternative but to repay the relevant

¹³ Nicholas Kristof, 'Orphaned, Raped and Ignored', *The New York Times* (online), 30 January 2010 <http://www.nytimes.com/2010/01/31/opinion/31kristof.html?_r=0>.

¹⁴ See, eg, Lumina, above n 3, 1; David Bosco, 'The Debt Frenzy' (2007) 161 *Foreign Policy* 36, 36, 38; Jonathan Goren, 'State-to-State Debts: Sovereign Immunity and the "Vulture" Hunt' (2010) 41 *George Washington International Law Review* 681.

¹⁵ *FG Hemisphere Associates LLC v Democratic Republic of Congo* [2010] NSWSC 1394 (1 November 2010) (Hammerschlag J) [14].

¹⁶ Cephas Lumina, 'Preying on the Poor: "Vulture Funds", Foreign Debt and Human Rights in Developing Countries' (Speech delivered at the Castan Centre for Human Rights Law, Monash University, 10 February 2011).

¹⁷ AfDB, *Vulture Funds in the Sovereign Debt Context* <<http://www.afdb.org/en/topics-and-sectors/initiatives-partnerships/african-legal-support-facility/vulture-funds-in-the-sovereign-debt-context/>>.

¹⁸ Lumina, above n 16.

¹⁹ Greg Palast, Maggie O'Kane and Chavala Madlena, 'Vulture Funds Await Jersey Decision on Poor Countries' Debts', *The Guardian* (online), 16 November 2011, <<http://www.theguardian.com/global-development/2011/nov/15/vulture-funds-jersey-decision>>.

²⁰ As will be discussed below, 'HIPC' is a term formed by the World Bank to describe specifically vulnerable sovereign debtors that qualify for particular comprehensive debt relief programs set up in conjunction with the International Monetary Fund ('IMF').

vulture fund. The litigious strategy used hinges upon legally sound ideas: creditors that own debts should be allowed to bring claims enforcing their legal rights against their debtors. No domestic or international laws are necessarily breached in such actions, and no inappropriate pressure outside of the courtroom needs to be exerted.²¹ Consistent with the neutral role of courts within common law systems, the Supreme Court of New South Wales gave no consideration to the relative positions of either party, nor did it consider the wider implications that this judgment would have for the millions of impoverished citizens within the DRC. Instead, the Court played a facilitating role in FG Hemisphere's 'vulture' behaviour, not because it was 'corrupt or unmoved ... but simply because current law favours certainty, predictability, and the enforceability of contract'.²² Given Australia's commitment to addressing global poverty, the use of our common law to further such ends is problematic. Yet, in the three years following this decision, no Australian legal analysis has arisen to examine vulture funds and their business here.

This article aims to fill this gap, examining vulture funds and the circumstances in which they are formed, and seeking a method to limit their litigious pursuits within Australian courts. It argues for the imposition of a legislative solution consistent with Australia's development-aid efforts, but recognises that such a solution must not undermine the financial market for sovereign debt. It begins by explaining what is meant by the term 'vulture funds' and the legal mechanisms that allow the owners of such funds legitimately to seek repayment for the debts they own, with examples provided for emphasis. Second, it discusses the problems represented by vulture funds, at both international and domestic levels, and why Australia should seek limitations on their claims. Finally, it examines existing methods of combating vulture funds from around the world, and articulates a proposed Australian answer to this problem. Ultimately, it is argued that any Australian legislative solution should cap HIPC-related claims at levels established by existing international debt relief programs, in imitation of the model enacted in the United Kingdom.

II What is a Vulture Fund?

'Vulture fund' is a negative term most often associated with distressed debt funds that trade HIPC-issued debt within the sovereign debt market. Distressed debt funds are those that operate in secondary debt markets, acquiring defaulted or soon-to-default ('distressed') debts at a significant discount in order to seek repayment of the total debt.²³ Using dispute resolution processes such as litigation, negotiation or arbitration, the investors behind distressed debt funds gain attractive returns upon repayment, often swollen beyond the debt's original value by interest, penalties, and other associated costs. In cases not involving sovereign debtors, such

²¹ In at least one case, the United Kingdom High Court Queen's Bench Division considered whether Donegal had bribed the Zambian government into accepting UK jurisdiction, but was unable to rule on this matter due to lack of evidence: *Donegal International Ltd v Republic of Zambia* [2007] EWHC 197 (Comm) (15 February 2007) [472].

²² Goren, above n 14, 700.

²³ AfDB, above n 17.

a fund may gain equity in the debtor as an alternative form of compensation, providing valuable shares should the debtor recover.²⁴ These funds are secondary creditors that assist both sides of a debt relationship: initial/primary creditors guarantee themselves a return on debts regardless of risk or default, and debtors appear less risky as a result, making overall capital-raising easier. Of course, such a business model has inherent risks: if a struggling debtor does not recover, bankruptcy and insolvency laws often lump creditors together into the same situation, leaving each to eke out a return from the remnants.

A *The Sovereign Debt Market*

The relationship dynamics of distressed debt trading change dramatically in cases where sovereign debt is traded. As with privately issued debt, sovereign debt has numerous legal rights and obligations of repayment attached. These can be found within the relevant loan agreements.²⁵ However, the involvement of states and their governments introduces a geopolitical dimension into the ‘merely’ financial relationship usually involved in the issuing of debt. When countries take loans, politics and other significant non-financial factors affect their ability to repay.²⁶ In the case of HIPCs, which are the primary concern of this article, unique and extreme concerns (such as military uprisings, stagnant economies, natural disasters, and regional conflict) make timely repayment even harder.²⁷ The result is that fiscal consolidation (the ability to collect and spend government revenue) — let alone fiscal responsibility (the ability to balance a budget) — becomes difficult at best. The danger of financial mismanagement translates into greater financial risk that must be borne by creditors, requiring a correspondingly higher return for their investments. However, unlike corporations or individuals, sovereign nations are neither protected nor constrained by laws that might otherwise apply to private parties burdened with debt; countries cannot declare insolvency,²⁸ nor can they be coerced into repayment through enforcement mechanisms such as asset seizure or foreclosure.²⁹ As a result, primary creditors to sovereign nations (and, in particular, HIPCs) face increased risk in the very process of lending, but with lessened flexibility to demand repayment in the event of distress or default.

²⁴ David McIntyre, ‘Distressed Debt Funds Eyeing Australia’, *Sydney Morning Herald* (Sydney), 13 April 2009 <news.smh.com.au/breaking-news-business/distressed-debt-funds-eyeing-australia-20090413-a4bh.html>.

²⁵ AfDB, above n 17.

²⁶ Harvey Asiedu-Akrofi, ‘Banks, Bonds and the American Bench: Exercising Judicial Discretion to Discourage Rogue Sovereign Bond Litigation Claims’ (2011) 7 *Cambridge Student Law Review* 42, 53.

²⁷ Some of the countries eligible for HIPC status include Afghanistan, Haiti, the DRC, Liberia, Rwanda, and Uganda: The World Bank, *Heavily Indebted Poor Countries* (24 January 2012) World Bank Economic Policy and Debt <<http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTDEBTDEPT/0,,contentMDK:20260049~menuPK:64166739~pagePK:64166689~piPK:64166646~theSitePK:469043,00.html>>.

²⁸ Although there is an argument for such processes to be made available to nations: see Part IV(A) below.

²⁹ Paul Beford, Adrian Penalver and Chris Salmon, ‘Resolving Sovereign Debt Crises: the Market-based Approach and the Role of the IMF’ (June 2005) *Financial Stability Review* 92 <<http://www.bankofengland.co.uk/publications/Documents/fsr/2005/sovdebt.pdf>>.

This limited capacity for enforcement is not of great concern to larger primary creditors, which are historically large banking institutions that began sovereign lending in the late 20th century.³⁰ Even today, these creditors tend to hold vast amounts of sovereign debt belonging to both HIPCs and non-HIPCs. When first issued in the 1970s and 1980s, sovereign debt had limited capacity for trade or conversion,³¹ with institutional investors confident that developing countries could maintain repayment of their debts and provide them with lucrative profits indefinitely.³² Citigroup Chairman Walter Wristen once claimed, '[c]ountries don't go out of business ... their assets always exceed their liabilities, which is the technical reason for bankruptcy ... that's very different from a company'.³³ This erroneous belief in slow economic development fuelled a surge in easy credit, leading banks to overinvest in debt.³⁴ As the resources primarily traded by less-developed economies began selling for lower prices and currency values depreciated, governments were left with significantly diminished funds with which to repay their debts. The corresponding skyrocketing of interest rates left banking syndicates facing the impending prospect of default by their less-developed sovereign debtors. Although the United States government tightened monetary policy and the IMF scrambled to stave off catastrophic default,³⁵ it became clear that any institution vigorously pursuing its debt would only exacerbate the financial distress. By the early 1980s, the IMF, the banks, and their debtors looked to restructure this debt and renegotiate economic policy the world over to prevent mutually assured financial disaster.

The United States-led Baker Plan was the initial attempt to reinvigorate sovereign debtors by providing them with more credit while simultaneously pressuring them for repayment.³⁶ However, this process proved fruitless, creating little faith in the sufficient prevention of default. A sovereign debt market began to take shape, as some creditors opted to cut their losses by selling their debts at a discount rather than waiting for a resolution.³⁷ Through trading activity, over-exposed banks could shift parts (or in some cases, all) of their sovereign loan portfolios onto interested investors, most of whom wanted to make equity investments in the developing world and did not wish to resort to inefficient and expensive currency trading.³⁸ It was the United States' Brady Plan of March 1989 that accelerated the growth of this sovereign debt market by allowing sovereign loans to be converted into bonds.³⁹ 'Brady bonds' (as these instruments came to be known) were freely tradeable and could be offered up on the open market,

³⁰ Asiedu-Akrofi, above n 26, 49–50.

³¹ Devi Sookum, *Stop Vulture Fund Lawsuits — A Handbook* (Commonwealth Secretariat, 2010) 8.

³² Jeffrey Sachs, 'Making the Plan Work' (1989) 68(3) *Foreign Affairs* 87, 89.

³³ IMF, *Money Matters: An IMF Exhibit — The Importance of Global Cooperation* <http://www.imf.org/external/np/exr/center/mm/eng/mm_dt_01.htm>.

³⁴ In 1982, United States banks had lent 287.7 per cent of their collective bank capital to developing countries: *ibid*; Asiedu-Akrofi, above n 26, 50.

³⁵ Sookum, above n 31, 8.

³⁶ Asiedu-Akrofi, above n 26, 50–1.

³⁷ Philip J Power, 'Sovereign Debt: The Rise of the Secondary Market and its Implications for Future Restructurings' (1996) 64 *Fordham Law Review* 2701, 2716.

³⁸ *Ibid*.

³⁹ Emerging Markets Trade Association, *The Brady Plan* (2009) <<http://www.emta.org/template.aspx?id=35>>.

introducing even more parties to sovereign debt.⁴⁰ In this way, sovereign debt evolved into a commodity to be ‘cashed in’ like any other financial instrument. Where in the past the risk/return problems of this borrowing were minimised while institutional creditors forestalled repayment with restructuring, the new market dynamic brought secondary creditors into the fold, some of which had no intention of negotiating with sovereign debtors. Such investors looked instead to identify the previously non-existent arbitrage (‘buy-low, sell-high’) opportunities in the market made possible by the speculative possibilities of market trading.⁴¹

B Enter Vulture Funds

In the case of HIPC, the bad publicity associated with reports of large corporate interests suing Third World countries make many primary creditors hesitant or unwilling to follow up on these debts. In one notable 2002 case, multinational food company Nestlé withdrew its claim against historically famine-ravaged Ethiopia after a ‘name and shame’ campaign was waged against it by the media and groups including Oxfam.⁴² Admittedly, Nestlé was seeking US\$6 million, which is estimated to equal an hour’s turnover for the multinational.⁴³ Smaller bondholders tend to lack the resources necessary to take sovereigns to court, since successful litigation against countries often requires patience and an ability to maintain expert legal counsel over long periods of time.⁴⁴ More recently, international moves to forgive Third World debt, such as the World Bank’s HIPC Initiative⁴⁵ or the more informal Paris Club program⁴⁶ (discussed below) make debt-holders even less likely to pursue their third-world debtors, lest prevailing international popular opinion overwhelm their other avenues of profit-making. The result is that primary creditors can be motivated to offload their debt to interested third parties. To them, this represents a better outcome than participating in drawn-out, and often indeterminate, restructuring or rescheduling processes.⁴⁷

Where other creditors are hesitant to be seen pursuing HIPC for repayment, vulture funds willingly do so. Once they have acquired rights to repayment, vulture funds ‘do not hesitate to take legal action’ in order to claim compensation,⁴⁸ especially since the view taken by vulture fund investors is that ‘you will always recover a sufficient amount to cover your costs’.⁴⁹ By their own admission, this legal action is not limited to litigation (although this is usually the means by which they ultimately conclude such transactions); negotiation and other

⁴⁰ Sookum, above n 31, 9.

⁴¹ Power, above n 37, 2719.

⁴² Charlotte Denny, ‘Retreat by Nestlé on Ethiopia’s \$6m Debt’, *The Guardian* (online), 20 December 2002 <<http://www.guardian.co.uk/world/2002/dec/20/marketingandpr.debtrelief>>.

⁴³ *Ibid.*

⁴⁴ Goren, above n 14, 693.

⁴⁵ The World Bank, (*HIPC*) *The Enhanced Heavily Indebted Poor Countries Initiative* (20 March 2012) <<http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTDEBTDEPT/0,,contentMDK:20260411~menuPK:64166739~pagePK:64166689~piPK:64166646~theSitePK:469043,00.html>>

⁴⁶ Club de Paris, *Welcome to the Paris Club* <<http://www.clubdeparis.org/>>.

⁴⁷ *Ibid.*

⁴⁸ Sookum, above n 31, 1.

⁴⁹ Michael Sheehan, quoted in *Donegal International Ltd v Republic of Zambia* [2007] EWHC 197

(Comm) (15 February 2007) [76].

alternative dispute resolution processes are often conducted in efforts to swap debt for other government interests (in natural resources or infrastructure projects) analogous to corporate ‘equity’.⁵⁰ Vulture funds view their activities with a detachment that makes no accommodation for the struggles of HIPC debtors, seeing only opportunity for investment that brings ‘much needed transparency into how a country’s leadership is managing [its] resources’.⁵¹ Although individual claims may represent relatively small sums given the large debts deferred or erased by other creditors, one estimate of HIPC-related litigation suggests that the aggregate value of 54 separate cases against 12 different HIPCs has reached US\$1.5 billion.⁵²

Given the impression that these investment vehicles leave on the wider public, it is unsurprising that they are usually opaque and try as hard as possible to avoid the glare of both the media and the wider public.⁵³ The United Nations Independent Expert on the Effects of Foreign Debt and other Related International Financial Obligations on Human Rights, Cephias Lumina, has gone so far as to claim that many vulture funds are established just to pursue certain debts, with ownership obscured and deliberately hidden behind corporate veils.⁵⁴ In many cases, incorporation occurs in offshore tax havens: Donegal International Ltd, which sued Zambia in 2006, was incorporated in the British Virgin Islands, while Hamsah Investments Ltd and Wall Capital Ltd, which sued Liberia in 2008, are registered in the British Virgin Islands and the Caymans respectively. Such devices help shield vulture funds from both stringent tax liability and public attention.

As discussed, vulture funds rely on some relatively simple legal principles to drive their cases; as secondary creditors, they are entitled to exercise the rights for repayment that they own, given the obligations of HIPC debtors. Despite having strong cases at law and being well-resourced to pursue them single-mindedly, vulture funds still use tactics in and out of court that might appear underhanded. As seen in the FG Hemisphere case, HIPCs can be forced to submit by using heavy court-sanctioned fines, but others may surrender where political coercion is brought to bear.⁵⁵ Even then, as in the UK High Court case of *Donegal International Ltd v Zambia*, vulture funds may ‘deliberately [withhold] documents because they contradicted the case they were seeking to advance’,⁵⁶ use witnesses who give ‘vague and inconsistent’⁵⁷ evidence, and generally act in a manner that is ‘deliberately evasive and even dishonest’.⁵⁸ However, since vulture fund cases

⁵⁰ See, eg, *Donegal International Ltd v Republic of Zambia* [2007] EWHC 197 (Comm) (15 February 2007); Grossman, above n 4.

⁵¹ Grossman, above n 4.

⁵² Club de Paris, *Creditors Litigating against HIPCs* <<http://www.clubdeparis.org/sections/themes-strategiques/2009-8217-action-du-club>>.

⁵³ Meirion Jones, ‘Vulture Fund Threat to Third World’, *BBC Newsnight* (online), 14 February 2007 <<http://news.bbc.co.uk/2/hi/6362783.stm>>.

⁵⁴ Lumina, above n 3, 6.

⁵⁵ *Donegal International Ltd v Republic of Zambia* [2007] EWHC 197 (Comm) (15 February 2007) [472], [474]: Zambia’s lawyers alleged that the settlement agreement central to this case was entered into due to corrupt payments by Donegal to Zambian officials.

⁵⁶ *Ibid* [64].

⁵⁷ *Ibid* [127].

⁵⁸ *Ibid* [51].

depend on questions of substance (does the vulture fund have properly assigned creditor rights to enforce?) rather than form (should a vulture fund be allowed to recover even where its owner was so ‘misleading in his evidence’ that he ‘must have realised his responses gave a wholly false impression’?),⁵⁹ these strategies are not subjected to great scrutiny, as the HIPC’s must ultimately meet the promises they have made under law.

C *Features of Sovereign Debt Loan Agreements*

The loan agreements found in sovereign debt transactions follow the same general formula found in written contracts used in everyday borrowing scenarios: the parties are identified, the obligations are set out and the terms and conditions that govern the overall loan are made clear for the sake of expediency.⁶⁰ As with any loan, each individual agreement may take on features unique to the transaction itself and/or the parties involved. In the case of debt issued by governments, certain templates are available from international organisations such as the IMF, World Bank or the AfDB to create consistency in treatment and enforcement.⁶¹ When the debt is sold on, the loan agreements pass all the rights and obligations available to the previous creditor on to the new ‘owner’ of the debt.⁶² In the case of vulture funds, it is often by exploiting non-standard terms that the fund gains the scope necessary for successful litigation.⁶³ Two kinds of clauses are of particular interest: applicable law clauses and collective action clauses.

Applicable law clauses establish the jurisdiction of the law that will govern any disagreements that might arise between parties. Where dispute resolution is a concern, parties tend to rely on a stable jurisdiction with a well-developed body of law in order to protect each party’s rights. As a result, the United Kingdom and New York tend to be popular,⁶⁴ especially given their ‘creditor-friendly’ images.⁶⁵ The choice of governing law is often designed to stop parties from being drawn into other jurisdictions with which they might be unfamiliar, confining the legal concepts and procedures that are to apply and ensuring a level playing field. Even where distinct mechanisms for dispute resolution are identified, as in the FG Hemisphere case where ICC arbitrations were required, the choice of law remains important in explaining how the contract should function. The Commonwealth Secretariat Legal Debt Clinic in particular cautions sovereign debtors against submitting to jurisdictions not provided for in the loan agreement, as in the case of

⁵⁹ Ibid [186].

⁶⁰ Sookum, above n 31, 13–15.

⁶¹ See, eg, AfDB, *General Conditions Applicable to the African Development Bank Loan Agreements and Guarantee Agreements (Sovereign Entities)* (31 December 2008) <<http://www.afdb.org/fileadmin/uploads/afdb/Documents/Legal-Documents/30774810-EN-NEW-GENERAL-CONDITIONS-ADB-SOVEREIGN.PDF>>; The World Bank, *General Conditions for Loans* (12 March 2012) <http://siteresources.worldbank.org/INTLAWJUSTICE/Resources/IBRD_GC_English_12.pdf>.

⁶² *Pravin Banker Associates Ltd v Banco Popular del Peru*, 109 F 3d 850 (2nd Cir, 1997).

⁶³ Sookum, above n 31, 14.

⁶⁴ Ibid 16.

⁶⁵ Lumina, above n 3, 6.

Donegal International Ltd v Republic of Zambia,⁶⁶ because refusing to submit is ‘a powerful legal argument against the creditor which will undoubtedly lead to the withdrawal of the lawsuit’.⁶⁷ In any event, submission to the laws of a certain jurisdiction can also compromise the sovereign immunity that countries would otherwise enjoy, as it is viewed as a waiver of this immunity.⁶⁸

Many loan agreements also include collective action clauses: devices that benefit sovereign debtors. These clauses, originally found in bond agreements, permit the restructuring of debt so long as a majority of creditors approve.⁶⁹ This represents an effective inverse of what is known as a *pari passu* clause, which requires that creditors be treated equally and repaid pro rata after a debtor goes into bankruptcy. Collective action clauses weaken a vulture fund’s capacity to hold out from debt restructuring and streamline the entire process as well. Although relatively exclusive to bond-based debt,⁷⁰ collective action clauses have been endorsed in principle by the G10⁷¹ and the IMF as recently as 2002.⁷² Unfortunately, the very appeal of these clauses for sovereign debtors (their ability to coerce minority creditors into restructuring) can make them unattractive to smaller prospective lenders, possibly raising the cost of borrowing or simply being dismissed outright during negotiations.⁷³

D Case Study: *Elliott Associates and Peru*

The status of the ‘original vulture fund case’ is sometimes attributed to *Elliott Associates LP v Banco de la Nación*,⁷⁴ a decision in the District Court of New York seeking repayment of a debt guaranteed by the government of Peru. The facts of this case, and the decisions subsequently handed down, provide vulture funds with the example followed to this day, demonstrating the profit margins on offer and the powerlessness of courts to reject claims regardless of any irregularities on the part of the vulture fund. The case also demonstrates the holding to ransom-like tactics used by these funds to prioritise their own interests ahead of all other creditors, even if such tactics forestall more constructive debt restructuring efforts and much-needed economic assistance.

In the 1980s, Peru was hit hard by debt crises that required a suspension of payments on external debts in March 1983.⁷⁵ By the 1990s, Peru’s prospects had

⁶⁶ [2007] EWHC 197 (Comm) (15 February 2007) [17]: after failing to have standing in the Cayman Islands and the British Virgin Islands, Donegal ‘convinced’ Zambia to submit to the jurisdiction of the UK in future disputes, leading to a finding against Zambia.

⁶⁷ Sookum, above n 31, 17.

⁶⁸ Goren, above n 14, 694–6.

⁶⁹ Sookum, above n 31, 19.

⁷⁰ *Ibid* 20.

⁷¹ Group of 10, *Report of the G-10 Working Group on Contractual Clauses* (26 September 2002) Bank for International Settlements <<http://www.bis.org/publ/gten08.pdf>>.

⁷² Yan Liu, *Collective Action Clauses in International Sovereign Bonds* (30 August 2002) IMF <<http://www.imf.org/external/np/leg/sem/2002/cdmfl/eng/liu.pdf>>.

⁷³ Sookum, above n 31, 20.

⁷⁴ 194 F 3d 363 (2nd Cir, 1999).

⁷⁵ Christopher Wheeler and Amir Attaran, ‘Declawing the Vulture Funds: Rehabilitation of a Comity Defence in Sovereign Debt Litigation’ (2003) 39 *Stanford Journal of International Law* 253.

improved, the country having received IMF support in reforming economic policy and reached settlements with all but one of its 180 lenders. In January 1996, Peru reached a Brady Plan agreement with these creditors to exchange virtually all US\$4.4 billion of its commercial debt for cash and bonds. It was at this point that Elliott Associates ('Elliott'), a New York-based investment fund, began purchasing US\$20.7 million worth of capital loaned to Nación Banco Popular del Peru ('Nación'), a bankrupt Peruvian bank, guaranteed by Peru's government.⁷⁶ While Peru negotiated the terms for debt restructure with all other commercial creditors, Elliott refused to participate, instead sending Nación and Peru's government a notice of default and demanding repayment of the debt.⁷⁷

On 18 October 1996, 10 days before Peru's exchange agreement was scheduled for execution, Elliott filed suit in the Southern District Court of New York.⁷⁸ In its decision, the Court ruled against Elliott under New York's *champerty* statute, which makes it unlawful to purchase debt with the sole intention of bringing an action or proceeding.⁷⁹ It particularly focused on the suspicious timing of Elliott's purchase, its lacklustre attempts to collect on the debt without resorting to litigation and the experience that Elliott's owners had in suing sovereigns.⁸⁰ Unfortunately, the Second Circuit Court of Appeal reversed the decision one year later, finding no such *champerty*: Elliott's 'principal aim was to obtain full payment'⁸¹ such that bringing suit was incidental and contingent to that aim. Hence, Nación and Peru had breached their obligations to repay Elliott for the debt it owned, and Peru was therefore required to compensate Elliott for US\$55.7 million.⁸² This stalled Peru's Brady Plan restructure, as the orders prevented Peru from making any other payments, including those required by the first round of obligations under their other, newly bond-backed debt. Peru was therefore at considerable risk of another decade of economic stagnation,⁸³ and so decided to acquiesce to Elliott instead.

However, this was not the end of Elliott's efforts. As Peru had opted to pay all its creditors through Euroclear, a Brussels-based clearing bank, the vulture fund decided to cement its award by gaining priority in repayment. Bringing an *ex parte* claim in Belgium's courts, Elliott sought an injunction against any payments to all of Peru's other creditors.⁸⁴ Although initially unsuccessful, on appeal Elliott got its injunction in a controversial Belgian decision requiring minority creditors be compensated on their own terms.⁸⁵ Defeated once more, Peru settled with Elliott

⁷⁶ Despite the more than US\$20 million value of this debt, Elliott Associates is estimated to have paid only US\$11.4 million to acquire it: *Elliott Associates LP v Banco de la Nación* 194 F.3d 363 (2nd Cir, 1999) 366–7.

⁷⁷ Sookum, above n 31, 35.

⁷⁸ *Elliott Associates v Republic of Peru*, 12 F.Supp. 2d 328 (SDNY 1998).

⁷⁹ NY Jud Ct Acts §5289 (McKinney 1983).

⁸⁰ *Elliott Associates v Republic of Peru*, 12 F.Supp. 2d 328, 336, 342, 333 (SDNY 1998).

⁸¹ *Elliott Associates v Banco De la Nación* 194 F.3d 363, 378 (2nd Cir, 1999).

⁸² Sookum, above n 31, 35–6.

⁸³ IMF, *Peru: Article IV Consultation and Request for Stand-by Arrangement 48* (19 March 2001) <<http://www.imf.org/external/pubs/cat/longres.cfm?sk=3993.0>>.

⁸⁴ *Elliott Associates LP v Banco de la Nación* General Docket No 2000/QR/92 (Court of Appeals of Brussels, 8th Chamber, 26 September 2000).

⁸⁵ *Ibid.*

on 29 September 2009, paying out US\$56.3 million, or 500 per cent of Elliott's initial investment.⁸⁶ Only then could Peru meet its Brady bond obligations. By subverting notions of 'fairness' in debt repayment, acting as a 'free-rider' that held out from debt restructuring, and doggedly pursuing Peru in the courts, Elliott guaranteed itself an enormous profit at the expense of a disadvantaged sovereign debtor. Since this case, Elliott has continued its business in sovereign debt, most recently winning a comprehensive victory against Argentina in the United States Court of Appeals for the Second Circuit.⁸⁷

E *FG Hemisphere and the DRC (again)*

In the Australian case of *FG Hemisphere Associates LLC v Democratic Republic of Congo*,⁸⁸ the decision against the DRC was met by liquidating its sovereign-owned share assets. Unfortunately for the DRC, its willing acceptance of international arbitration waived any sovereign immunity it may have relied upon here. In other jurisdictions, FG Hemisphere deliberately sought alternative streams of income to avoid sovereign immunity protections as applied elsewhere. In certain jurisdictions where sovereign immunity is enforced strictly, such as China (giving limited to no exception for purely commercial activities conducted by sovereigns), FG Hemisphere has brought legal action against non-sovereign entities seeking their income or assets as a form of 'repayment'. In 2001, FG Hemisphere sued CMS Nomeco, a Texan oil and gas company, for payments that it owed to the Republic of Congo,⁸⁹ and, in 2008, went to the High Court of Hong Kong to force the China Railway Group to hand over its infrastructure investments in the DRC.⁹⁰ Although both actions were ultimately unsuccessful, these cases represent a dangerous prospect for HIPCs seeking to build infrastructure or foreign investment opportunities generally. Threatening litigation against corporations and groups that work with HIPCs is a significant disincentive for ongoing trade and investment, reducing further hopes of development over time.⁹¹ Such threats also stall any wider efforts by HIPC governments to normalise their relationships with the international business community.⁹² In this way, vulture fund activities damage HIPC economies, as immediate resources and long-term investment are both diverted away.

⁸⁶ G Mitu Gulati and Kenneth N Klee, 'Sovereign Piracy' (2001) 56 *The Business Lawyer* 635, 636.

⁸⁷ *EM Ltd v Republic of Argentina*, 695 F 3d 201 (2nd Cir, 2012); see also Joseph Stiglitz, 'We Need a Fair System for Restructuring Sovereign Debt', *The Guardian* (online), 5 September 2013 <<http://www.theguardian.com/business/2013/sep/04/we-need-fair-system-for-restructuring-sovereign-debt>>.

⁸⁸ [2010] NSWSC 1394 (1 November 2010) (Hammerschlag J)

⁸⁹ *FG Hemisphere Associates v Republique du Congo*, 455 F 3d 575 (5th Cir, 2006).

⁹⁰ *FG Hemisphere Associates LLC v DR Congo & China Railway Groups* [2008] CACV 373; *FG Hemisphere Associates LLC v DR Congo & China Railway Groups* [2009] CACV 43.

⁹¹ Lumina, above n 3, 17.

⁹² *Ibid* 18.

III The Problem for Australia

Despite all the moral outrage directed at vulture funds by reporters and politicians,⁹³ their business activities are legitimate under contract law.⁹⁴ Their claims rely on the principles that contractual obligations freely entered into should be met and that debtors should not be allowed to default. These are concepts so vital to day-to-day business that their significance in contract law is largely undisputed. Hammerschlag J's brief reasons in the FG Hemisphere case demonstrate this, in that Australia's legal obligations to international arbitration⁹⁵ were merely a means to an end. The decisive reason for the Supreme Court of New South Wales upholding the arbitral awards against the DRC was that '[t]he benefit of the right of enforcement has been assigned to [FG Hemisphere] which is accordingly entitled to the relief which it seeks'.⁹⁶ For a jurisdiction like Australia, regulating commercial activity requires a balancing of competing policy agendas; although the undesirable activity and its effects must be limited, the market and the law cannot be incapacitated generally. Vulture funds are an especial problem because their legal activities do not manipulate statutory loopholes, which can be closed, or precedents, which can be overruled.

Restricting vulture fund activities therefore requires particular justification, given that secondary creditor enforcement is usually desirable in credit markets. In other words, why should Australia seek to impede certain kinds of creditors (vulture funds) from enforcing their debts against certain kinds of debtors (HIPCs)? The answer lies outside black-letter law. The servicing of debt by sovereign nations, like any debtor, means that potential expenditure in other fields is reduced, and where HIPCs are concerned, this usually results in poor humanitarian outcomes. HIPCs stand out from other debtors (both public and private) at an economic and foreign policy level by virtue of severe disadvantage. Their residents have limited to no access to healthcare and education, their borders are marred by warfare and violence, and their governments are often unstable.⁹⁷ Accordingly, HIPCs receive special treatment from other countries and international bodies in terms of aid, trade, and development assistance. Hence, the primary justification for Australian action on vulture funds stems from the nature of HIPCs themselves. Australia's particular involvement in debt relief is the strongest justification for unifying executive and legislative policy towards consistency, reducing wastage, and preventing exploitative 'free-riding' on the processes of debt relief.

⁹³ See, eg, Goren, above n 14, 682–3; John Dizard, 'Distressed Debt Returns to the Spotlight', *Financial Times* (London), 30 July 2007, 7; Gordon Brown is quoted as saying vulture fund activities are 'morally outrageous': Jones, above n 53.

⁹⁴ Laura Alfaro, Noel Maurer and Faisal Ahmed, *Gunboats and Vultures: Market Reaction to the "Enforcement" of Sovereign Debt* (April 2010) UCLA Economics, 16 <<http://www.econ.ucla.edu/workshops/papers/History/Maurer.%20Gunboats%20and%20Vultures,%20version%205.2.pdf>>.

⁹⁵ *FG Hemisphere Associates LLC v Democratic Republic of Congo* [2010] NSWSC 1394 (1 November 2010) (Hammerslag J).

⁹⁶ *Ibid.*

⁹⁷ Lumina, above n 3, 11–12.

A *Australia's Commitment to Debt Relief*

Successive Australian governments have shared the view that worldwide poverty reduction is a cornerstone of Australia's foreign policy. Grounded in the idea of 'a fair go for all',⁹⁸ Australia has dedicated itself to a variety of international and regional initiatives that have sought to reduce global inequality. Most efforts are associated with formal aid programs involving conditional financial grants or in-kind deployments of advisers, which directly address specific problems: for example, Australia's campaign since 2003 to reduce malaria in Vanuatu and the Solomon Islands, or Australia's assistance in constructing and developing schools throughout Indonesia.⁹⁹ Since 2007, Australia has pledged to increase its aid budget to 0.5 per cent of Gross National Income.¹⁰⁰ Australia has indirect methods for promoting development as well. These less well-known aid activities provide overseas partners (including, but not limited to, HIPC) a degree of autonomy away from foreign influence. Debt relief initiatives are a good example of indirect aid: governments can use the freed-up funds otherwise used to service sovereign debt on outcomes that they themselves identify. Australia has, over the years, demonstrated a commitment to debt relief processes, and continues to use considerable funds to ensure their effectiveness.¹⁰¹ The significance of these debt relief efforts is typified by two international debt relief programs: the World Bank's HIPC Initiative and the Paris Club of creditor countries.

B *Australian Leadership on Debt Relief: the HIPC Initiative and the Paris Club*

Perhaps the most important debt relief project currently is the 'first international response to provide comprehensive debt relief to the world's poorest, most heavily indebted countries': the HIPC Initiative.¹⁰² Originally developed in 1996 and

⁹⁸ AusAID, *An Effective Aid Program for Australia — Making a Real Difference — Delivering Real Results* (July 2011) Australian Government, 5 <<http://aid.dfat.gov.au/Publications/Documents/AidReview-Response/effective-aid-program-for-australia.pdf>>.

⁹⁹ *Ibid* 12.

¹⁰⁰ AusAID, *Australia and the World Bank — Saving Lives, Creating Opportunity* (July 2011) Australian Government, 4 <<http://aid.dfat.gov.au/partner/Documents/ausaid-worldbank.pdf>>; this aim was originally going to be reached by 2015–16, but successive 2012–14 budgets have postponed this pledge to 2016–17: AusAID, *Summary of Australia's Overseas Aid Program 2013–14* (14 May 2013) <<http://www.ausaid.gov.au/Budgets/Documents/budget-highlights-2013-14.pdf>>; as of 2013, the newly elected Coalition government has since pledged to cut foreign aid by \$4.5 billion to focus instead on infrastructure spending, which will effectively renege on this pledge: Emma Griffiths, *Coalition Costings: Joe Hockey, Andrew Robb Reveal Foreign Aid to Take \$4 Billion Hit*, ABC News (online), 5 September 2013 <<http://www.abc.net.au/news/2013-09-05/foreign-aid-cops-244bn-hit-as-coalition-releases-costings/4938218>>.

¹⁰¹ See, eg, Alexander Downer, *Australia's Overseas Aid Program 2002–03* (14 May 2002) AusAID <http://aid.dfat.gov.au/Publications/Documents/budget_2002_2003.pdf>; Alexander Downer, *Australia's Overseas Aid Program 2006–07* (9 May 2006) AusAID <http://aid.dfat.gov.au/Publications/Documents/budget_2006_2007.pdf>; Kevin Rudd, *Australia's International Development Assistance Program 2011–12* (10 May 2011) The Treasury, <http://www.budget.gov.au/2011-12/content/ministerial_statements/ausaid/download/ms_ ausaid.pdf> 71, 100.

¹⁰² The World Bank, *Heavily Indebted Poor Countries Initiative (HIPC)* (2011) Economic Policy and Debt <<http://web.worldbank.org/WBSITE/EXTERNAL/COUNTRIES/AFRICAEXT/0,,contentMDK:20236241~menuPK:488504~pagePK:146736~piPK:226340~theSitePK:258644,00.html>>.

consolidated in 1999, the now-‘Enhanced’ HIPC Initiative recognises the crippling effects of debt on poor economies and prompted the present-day trend of helping economic sustainability via large-volume debt relief.¹⁰³ With the cooperation of the World Bank and its members, the HIPC Initiative split sovereign debtors into ‘Highly Indebted Poor Countries’ and non-HIPCs based on (1) their eligibility for IMF/World Bank highly concessional financial assistance; (2) whether they have an ‘unsustainable debt situation even after the full application of traditional debt relief mechanism[s]’; and (3) their commitment to implementing poverty reduction and economic growth strategies.¹⁰⁴ Those eligible HIPCs are granted amnesty for all external public and publicly guaranteed debt up to predetermined Initiative thresholds deemed sustainable by the World Bank. These thresholds are calculated at a ‘decision point’: when a track record of economic stability, poverty-reduction planning and debt sustainability has been established.¹⁰⁵ But the decision point is only the beginning: if an HIPC can maintain its track record and continually implement reforms towards debt sustainability, it reaches ‘completion point’, becoming eligible for full and irrevocable debt reduction.¹⁰⁶ In July 2006, the HIPC Initiative was supplemented by the IMF-led Multilateral Debt Relief Initiative (‘MDRI’), a program providing full and unqualified debt relief to eligible HIPC countries, free from the ‘sustainability’ condition.¹⁰⁷ In both cases, Australia has been a consistent and active participant, despite its limited financial interest as ‘a minor creditor with little outstanding bilateral debt’.¹⁰⁸ Since the inception of both programs, Australia has voluntarily contributed more than A\$300 million in additional assistance, forgiven all the debts of Ethiopia and Nicaragua (the only HIPCs with direct debts to Australia), and continues to identify opportunities for reducing multilateral debt.¹⁰⁹

Given Australia’s longstanding involvement with both the World Bank and the IMF, Australian participation in these programs might suggest a bare-minimum involvement with the cause of debt relief. However, the Australian government’s permanent involvement in the Club de Paris (‘Paris Club’) emphasises its much stronger engagement in this field. The Paris Club is an informal group of creditor countries that meets monthly to discuss the external debt situations of distressed debtor countries. Although little known outside of the finance community and

¹⁰³ The World Bank, *The Enhanced HIPC Initiative — Overview* (2011) Economic Policy and Debt <<http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTDEBTDEPT/0,,contentMDK:21254881~menuPK:64166739~pagePK:64166689~piPK:64166646~theSitePK:469043,00.html>>.

¹⁰⁴ The World Bank, *Frequently Asked Questions* (2011) Economic Policy and Debt <<http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTDEBTDEPT/0,,contentMDK:20259564~pagePK:64166689~piPK:64166646~theSitePK:469043,00.html>>.

¹⁰⁵ The World Bank, *HIPC At-a-Glance* (13 April 2012) Economic Policy and Debt <http://siteresources.worldbank.org/INTDEBTDEPT/Resources/468980-1256580106544/HIPC_Spring2012_ENG.pdf>.

¹⁰⁶ IMF, *Debt Relief under the Heavily Indebted Poor Countries (HIPC) Initiative* (1 October 2013) <<http://www.imf.org/external/np/exr/facts/hipc.htm>>.

¹⁰⁷ IMF, *Factsheet — The Multilateral Debt Relief Initiative* (15 December 2011) <<http://www.imf.org/external/np/exr/facts/mdri.htm>>.

¹⁰⁸ When compared with the USA/Japan/Germany/the UK: Jubilee Australia, *Debt and Development — Australia as a Creditor Nation* (October 2011) <<http://www.jubileeaustralia.org/page/work/debt-and-development>>.

¹⁰⁹ AusAID, *The Values and Virtues of Debt Relief* (7 May 2010) (document no longer available online).

having no official legal status, the Club acts as a unified front to assist sovereign debt repayment negotiations.¹¹⁰ Its operations often address purely bilateral or regional obligations falling outside of the largely multilateral debts governed by the IMF or World Bank. The large financial interests represented by the Club (other permanent members include the United States, Russia, the United Kingdom, France, Germany, and Switzerland) provide it with considerable influence, so it often acts not only as a concerned third party, but as the creditor(s) as well. In general, the Paris Club tries to persuade creditors away from vigorous enforcement, and instead towards debt relief and rescheduling, provided the relevant debtor demonstrates a 'track record' of poverty-reduction planning consistent with relevant IMF programs.¹¹¹ When it acts, the Club's key principles of 'consensus' and 'solidarity' require that decisions be made only with the unanimity of all participating creditors, and only if all Paris Club members act uniformly in relation to any particular debtor country.¹¹² At its best, the Paris Club represents the willingness of most creditors to renegotiate debts where possible, or to forgive them entirely if necessary.¹¹³

By participating in the Paris Club, Australia provides greater assistance to the more advanced processes of debt relief, reflecting the broad international opinion that no positive outcomes are achievable when creditors are inflexible. As a member, Australia works to further the same goal of debt relief espoused by the IMF/World Bank: alleviating poverty in debtor countries so that they can better handle their economic burdens in a sustainable fashion.¹¹⁴ It is important to note that the Club readily admits to one non-altruistic motive for its efforts, which is perhaps embodied in the most important principle underpinning Paris Club-assisted debt relief: 'comparability of treatment'. In practice, Paris Club agreements require debtor countries to seek, where possible, treatment by all creditors on comparable terms to those negotiated through the Paris Club,¹¹⁵ mostly where non-Paris Club countries and private creditors are involved. This qualification, supported by flexible reporting and assessment procedures, provides Paris Club taxpayers with some assurance that their government's financial interests (and their own 'claims') are preserved, without being 'subordinated to those of other creditors'.¹¹⁶

¹¹⁰ Club de Paris, *Paris Club Meetings* <<http://www.clubdeparis.org/sections/composition/fonctionnement-du-club/reunions>>.

¹¹¹ Club de Paris, *The Five Key Principles* <<http://www.clubdeparis.org/sections/composition/principes/cinq-grands-principes>>.

¹¹² *Ibid.*

¹¹³ For example, the Paris Club cancelled half of the DRC's debt in 2010: Club de Paris, *The Paris Club Agrees on a Reduction of the Debt of the Diplomatic Republic of Congo in the Framework of the Enhanced Heavily Indebted Poor Country initiative* (17 November 2010) <<http://www.clubdeparis.org/sections/communication/archives-2010/rdc>>.

¹¹⁴ Club de Paris, *What Does Comparability of Treatment Mean?* <<http://www.clubdeparis.org/sections/composition/principes/comparabilite-traitement>>.

¹¹⁵ *Ibid.*

¹¹⁶ *Ibid.*

C *The Counterproductive Status Quo*

Australia's involvement in these programs (among others, such as the International Development Association's Debt Reduction Facility and the Commonwealth Secretariat's Legal Debt Clinic) requires significant investment of government time and resources. An analysis of the abstract moral or ethical concerns raised by vulture fund behaviour is not covered by this article. Rather, by simply focusing on the more tangible gains made by debt relief proponents (including Australia), it is sufficient to see that these opportunities go squandered while vulture funds are left free from scrutiny or regulation.¹¹⁷ After all, creditors do not necessarily support debt relief because they do not value repayment per se. Rather, they recognise that if all creditors demanded repayment, HIPC economies would collapse, and no return would be received by anyone.¹¹⁸ Hence, they relieve debt burdens to avoid perpetuating hardship and to provide scope to allow HIPCs to develop into economies more capable of handling sovereign debt. Creditors participating in debt relief judge that providing HIPCs with a much-needed reprieve is a more valuable outcome than collecting on dollars owed.¹¹⁹ Unfortunately, vulture funds take the opposite approach, seeing these altruistic majority-creditor 'windfalls' as an exploitable profit for a sufficiently motivated minority creditor.¹²⁰

Jurisdictions outside of Australia have already recognised that permitting vulture fund activity endangers existing debt relief and development generally,¹²¹ encouraging pro-debt relief creditors to roll back their activities (if 'comparability of treatment' cannot be assured), sell off their holdings, or end capital investment within HIPCs altogether.¹²² Any of these outcomes defeats the purpose of debt relief, which is to give HIPCs greater latitude in developing (or rebuilding) their economies without the weight of debt curtailing them. Vulture funds only profit so long as others abstain from copying their behaviour: they are the quintessential 'free-riders', benefiting only from the hard work and sacrifice of others, with limited contribution on their own part. It is therefore unsurprising that both the UN and the Paris Club have issued admonitory statements against vulture creditors. Paris Club members have even 'committed to avoid selling their claims on HIPCs to other creditors who do not intend to provide debt relief'.¹²³

Australia is unusual in that it does not hold large quantities of sovereign debt and does not sell off what little it owns, yet remains financially and politically engaged with debt relief. However, it is also home to at least one legal jurisdiction that has willingly upheld a vulture fund's claim against an HIPC, so it should seek to halt future claims to prevent further negative impacts on HIPCs, or at the very least to ensure policy consistency. Correcting the discrepancy whereby Australian

¹¹⁷ Lumina, above n 16.

¹¹⁸ United Kingdom, *Ensuring Effective Debt Relief for Poor Countries: A Response to Consultation* (HM Treasury, 2010).

¹¹⁹ This is why World Bank and IMF policy requires that a minimum of 80 per cent of all a sovereign's creditors participate in the HIPC and MDRI Initiatives before 'completion' is possible.

¹²⁰ Lumina, above n 3, 12.

¹²¹ United Kingdom, above n 117, 7–8.

¹²² Sookum, above n 31, 96–7.

¹²³ Club de Paris, above n 52.

law enables vulture funds but Australian *policy* assists HIPC's would better serve Australia's overall debt-relief agenda. Taking action allows Australia to prevent wastage of taxpayer dollars committed to debt relief, demonstrates consistency of policy and action, and provides an unmistakable sign that discourages 'free-riding' vulture activity. It also gives HIPC's clear legal protection that acknowledges their relative disadvantage when facing vulture funds in court and shields them from the tactics that might be deployed. To do nothing would be 'illogical' (as stated by the UN Independent Expert)¹²⁴ and renders Australia a country inadvertently harming the global community's most vulnerable members.

IV Addressing the Vulture Fund Problem

How to find a way to stop vulture fund litigation is a difficult question for Australian lawmakers. After all, the problem with vulture funds is not the business model they follow, the manner in which they use the courts for that business, or even the role they play in the wider financial market. This article is not arguing against secondary creditors using courts and other dispute resolution techniques to pursue debts. Nor is it arguing against the very existence of distressed debt funds. Rather, the problem to be addressed is whether such investment vehicles should be allowed to target HIPC's and extract large amounts from them, given the important and expensive debt relief efforts currently in place that strive to help millions of impoverished people in the developing world.

Many of the proposals against vulture funds presented by anti-vulture fund activists (including the Jubilee Debt Coalition¹²⁵ and Eurodad¹²⁶) have tended to emphasise measures involving international or multilateral cooperation. Although these are briefly considered below, a better approach would be to use domestic measures that overcome problematic voluntary participation by commercial creditors.¹²⁷ Not only would this sidestep the immense difficulties of creating global consensus necessary in international law, it would also allow for careful customisation of objectives, which might otherwise be compromised by interests unrelated to one jurisdiction's particular concerns. A purely Australian response could be developed, debated and implemented relatively quickly, especially where sufficient motivation exists within Parliament. Consequently, this part begins with a brief discussion of international solutions to curb vulture behaviour, before examining the various attempts that have been brought forward in continental Europe, the United States, and the United Kingdom. Finally, it proposes that the ideal solution for Australia is one based heavily on the British approach of limitation rather than outright prohibition, building upon existing debt relief

¹²⁴ Lumina, above n 16.

¹²⁵ The Jubilee Debt Coalition, based in the UK, is a collection of national organisations dedicated to the erasure of all debt owed by the developing world to more advanced economies; in Australia, it is represented by Jubilee Australia: Jubilee Debt Campaign, *About Us* (2010) <<http://www.jubileeaustralia.org/page/about>>.

¹²⁶ 'Eurodad' is the shortened name for the European Network on Debt and Development, a network of European non-government organisations focusing on debt, developmental finance and reducing poverty: Eurodad, *About* <http://eurodad.org/?page_id=10119>.

¹²⁷ Lumina, above n 16.

foundations and making Australia a leader, rather than a follower, in addressing this particular problem.

A *International Institutional Proposals*

Some commentators have addressed vulture funds in close conjunction with the question of how to resolve sovereign debt crises.¹²⁸ This is unsurprising given that the sovereign debt secondary market grew out of such crises. As outlined in Part II(A), when sovereign debtors — for whatever reason — become less able to handle their liabilities, their debts become distressed and riskier, creating opportunities for secondary creditors such as vulture funds. In the past, sovereign debt crises have been resolved through strategies influenced by the financial trends of the times; for example, securitisation in the 1980s¹²⁹ and comprehensive debt restructuring in the 1990s.¹³⁰ More recently, proposals have centred on an international insolvency framework that provides sovereign nations with the same protection and assistance that individuals receive when declaring bankruptcy. This would limit the threat of predatory creditors by freezing repayments on all debts while the distressed debtor develops a plan out of insolvency. Theoretically, this framework grants debtors a state of reprieve that could not be circumvented by enthusiastic litigation, since all creditors would be required to participate in an independently approved repayment plan drawn up with input from all relevant parties.

A Sovereign Debt Restructuring Mechanism was suggested to the IMF in 2001, but this was abandoned in 2003 because of lack of support from the United States and the private sector.¹³¹ Another option advocated by the Jubilee Debt Coalition is the formation of an international arbitration mechanism that mirrors Chapter 9 (Title 11) of the United States *Bankruptcy Code* (allowing municipalities to declare insolvency).¹³² This second solution has been proposed on both an ad-hoc basis (much as international arbitration is conducted currently) and as a permanent standing court (resembling institutions such as the International Court of Justice).¹³³ Each of these frameworks has similar features: independent (or at least, arm's-length) decision-makers, a comprehensive assessment of the debtor's situation with clear disclosure obligations, legally enforceable processes, legally binding outcomes, and a shared view towards debt sustainability.¹³⁴ Unfortunately, they still require governments to bind themselves and their residents voluntarily.

¹²⁸ See, eg, Owen C Pell, *Nations Need Bankruptcy Process* (8 February 2002) White and Case <http://www.whitecase.com/files/Publication/b5fcea31-cb8e-4845-8a4a-e05570d0c9d8/Presentation/PublicationAttachment/a4d59aef-4348-441b-8ba3-e3424b567f43/article_nations_need_bankruptcy_process_pell.pdf>; Luke Fletcher and Adele Webb, 'Alternatives to Debtors Prison: Developing a Framework for International Insolvency' (Research in Development Series Report No 4, Australian Council For International Development, October 2011).

¹²⁹ Sookum, above n 31, 8–10.

¹³⁰ Jürgen Kaiser, 'Resolving Sovereign Debt Crises — Towards a Fair and transparent International Insolvency Framework' (Study, Friedrich Ebert Stiftung, September 2010) 5–10.

¹³¹ *Ibid* 18–19.

¹³² Fletcher and Webb, above n 128, 23–9.

¹³³ *Ibid* 24.

¹³⁴ Kaiser, above n 130, 21 (Table 1).

This would be problematic in and of itself, if not for the additional problem that, even after treaties are ratified and binding agreements are made, enforceability and compliance may remain elusive.¹³⁵ As has been the case with debt relief generally, the possibility would also remain that the private sector extricates itself from such norms through lobbying or outright rejection. It is therefore unsurprising that the UN Independent Expert, while welcoming multilateral initiatives, believes them to be insufficient so long as public and private players remain free to opt in or out.¹³⁶

B The European Experience: Belgium and France

Belgium was the first country in the world to institute a legal response to safeguard against vulture behaviour successfully.¹³⁷ As a large creditor to Africa, and especially its former colonies in the Congo,¹³⁸ Belgium makes considerable investments to support development in that region. At the same time, it has served as a venue for vulture funds seeking to enforce decisions handed down elsewhere. Identifying the futility of permitting both processes, Belgium's Federal Parliament unanimously adopted a legal resolution in January 2008 to 'safeguard Belgian funds disbursed towards development cooperation and debt relief from the actions taken by vulture funds'.¹³⁹ This forbids officially sanctioned development assistance from being 'seized' or 'transferred' between parties.¹⁴⁰ The law renders all funds or aid given by the Belgian government (towards an agenda of foreign sovereign development) illiquid; any interest owned by a non-sovereign creditor stemming from such 'income' cannot be converted into monetary value. This is so irrespective of whether the assistance is provided to a sovereign government, a corporation acting with a guarantee from its government, a central bank or 'any institution which executes the policy of development'.¹⁴¹ The vague language of the statute suggests that funds freed up by debt relief and direct aid given in kind or otherwise are covered, with no exceptions at all.

An alternative approach to combat vulture funds was proposed by Marc Le Fur to the French National Assembly in June 2006.¹⁴² Although it was not passed,¹⁴³ the Bill to 'fight against the actions of financial funds known as "vulture

¹³⁵ The United States' reluctance to submit to international criminal law is an ominous harbinger here: John Bolton, 'The Risks and Weaknesses' of the International Criminal Court from America's Perspective' (2001) 64(1) *Law and Contemporary Problems* 167.

¹³⁶ Lumina, above n 3, 14–15.

¹³⁷ Sookum, above n 31, 88.

¹³⁸ *Ibid* 88.

¹³⁹ The Chamber of Representatives, *Projet de loi visant à empêcher la saisie ou la cession des fonds publics destinés à la coopération internationale, notamment par la technique des fonds vautours* [A Bill to safeguard Belgian funds disbursed towards development cooperation and debt relief from the actions taken by vulture funds] (2008) Belgian Federal Parliament <<http://www.lachambre.be/kvvcr/showpage.cfm?section=/flwb&language=fr&rightmenu=right&cfm=/site/wwwcfm/flwb/flwb/lwbn.cfm?lang=F&legislat=52&dossierID=0762>> [author's trans].

¹⁴⁰ *Ibid* art 2 [Devi Sookum trans].

¹⁴¹ *Ibid*.

¹⁴² Sookum, above n 31, 91.

¹⁴³ The text is still available in French on the National Assembly's website: Assemblée Nationale, *Proposition de Loi No 3214* (28 June 2006) <<http://www.assemblee-nationale.fr/12/propositions/pion3214.asp>>.

funds”¹⁴⁴ was justified as a way to stop holdout creditors from undermining the French government’s debt-relief efforts.¹⁴⁵ The Bill built on the French Civil Code’s rule of *champerty*, stating at art 1699:

A person against whom a litigious right has been assigned [may be] released by the assignee by reimbursing him for the actual price of the assignment with the expenses ... fair costs, and with interest from the day when the assignee has paid the price of the assignment made to him.¹⁴⁶

This allows primary creditors that assign their debts (with their associated litigious rights) to buy back the debts if they so choose. Such a mechanism works well against vulture funds because it restricts the return on investment to the amount spent buying the debt, rather than the full face value, if and when ‘litigious rights’ are sought for return. The suggested law goes further, giving French courts discretion to forbid payments of sovereign debt owed to a creditor,¹⁴⁷ rendering questions of return moot. The discretion was only qualified by a court’s consideration of how much the sovereign debtor had been assisted by public sources and other creditors and the debtor’s future economic prospects.¹⁴⁸ When put before the French lower house, it was argued that, if this discretion were bestowed, French courts should deny all requests for payment on sovereign debt (including requests to enforce foreign decisions) so long as the debt was bought by a party ‘speculating on possible litigation which could be introduced against the debtor, and not so much taking into account the market value of the debt’.¹⁴⁹ This legislative ability to influence the courts is made easier in civil law traditions, where judicial service ‘is analogous to a career in the civil service ... limited by strict notions of legislative supremacy’.¹⁵⁰ Essentially, this French solution would ban any secondary creditors that operate for profit and consider litigation a legitimate means to ensure repayment.

C *America’s Stand against ‘Debt Profiteering’*

Perhaps the most promising bid to combat vulture funds was a Bill introduced twice into the United States Congress by Representative Maxine Waters, on 1 August 2008 and 18 June 2009. Unfortunately, the ‘*Stop Very Unscrupulous Loan Transfers from Underprivileged countries to Rich, Exploitative Funds Act*’ (‘*Stop VULTURE Funds Bill*’) has been referred to committee on both occasions, effectively leaving it ‘dead’ according to GovTrack.us, an online database for

¹⁴⁴ The original French is: ‘*lutter contre l’action des fonds financiers dits “fonds vautorous”*’ [Patrick Wautelet trans].

¹⁴⁵ Patrick Wautelet, *Vulture Funds, Creditors and Sovereign Debt: How to Find a Balance?* (March 2011) The Open Repository and Bibliography, 18 <<http://orbi.ulg.ac.be/bitstream/2268/87549/1/Vulture%20funds%20and%20sovereign%20debtors%20Wautelet.pdf>>.

¹⁴⁶ *Code civil* [Civil Code] (France) art 1699 [Georges Rouhette and Anne Rouhette-Berton trans].

¹⁴⁷ Wautelet, above n 145, 17.

¹⁴⁸ *Ibid* 17.

¹⁴⁹ *Ibid* [Patrick Wautelet translation from the original French].

¹⁵⁰ James Apple and Robert Deyling, *A Primer on the Civil-Law System* (1995) Federal Judicial Centre, 30 <[http://www.fjc.gov/public/pdf.nsf/lookup/CivilLaw.pdf/\\$file/CivilLaw.pdf](http://www.fjc.gov/public/pdf.nsf/lookup/CivilLaw.pdf/$file/CivilLaw.pdf)>.

United States legislature.¹⁵¹ Intended '[t]o prevent speculation and profiteering [defined within the Bill] in the defaulted debt of certain poor countries', the passage of the *Stop VULTURE Funds Bill* would have substantially impeded vulture funds worldwide, given their preference to seek initial judgments from American courts.¹⁵²

The first part of the *Stop VULTURE Funds Bill* prohibits 'sovereign debt profiteering' from being carried on inside the United States by any person acquiring defaulted sovereign debt at a discount (a 'vulture creditor'). 'Sovereign debt profiteering' translates to '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' plus '6 percent simple interest per year on the total amount'.¹⁵³ The Bill backs up the prohibition with a penalty for wilful violation: a fine equal to the total amount sought by the vulture creditor,¹⁵⁴ which voids any gains received and punishes the violator as well. Here, a 'qualified poor country' is not narrowed to mean only an HIPC, but any country eligible to borrow from the International Development Association, the World Bank's concessional loan facility. The result is problematic; it extends the *Stop VULTURE Funds Bill's* protection to a much larger class of debtors, while placing hefty disincentives on virtually all secondary creditors, due to the very wide net of 'profiteering'.

The second, even more stringent, part of the *Stop VULTURE Funds Bill* blocks courts in or of the United States from issuing 'a summons, subpoena, writ, judgment, attachment, or execution, in aid of a claim under any theory of law or equity a purpose of which would be furthering sovereign debt profiteering'.¹⁵⁵ This ban is unequivocal, stopping any creditor from seeking anything above the statute-imposed minimum described above. A creditor may only seek this minimum (by definition, not 'profiteering') but even then it must provide the relevant court with a long list of affidavits sworn under oath. This includes, but is not limited to: 'a statement that written notice of the claim ... has been provided to ... the [United States] Treasury', 'a statement of the names and addresses of all persons who, directly or indirectly hold any interest in the claim against the foreign state' and 'a statement of the total amount paid by all persons, directly or indirectly holding an interest in the claim, to acquire the interest'.¹⁵⁶ These comprehensive disclosure requirements leave creditors open to careful scrutiny by the courts and more, forcing transparency on sovereign debt transactions whether the parties want it or not.¹⁵⁷

¹⁵¹ GovTrack.us, *HR 6796 (110th Congress)* (2009) <<http://www.govtrack.us/congress/bills/110/hr6796>>; GovTrack.us, *H.R. 2932 (111th Congress)* (2009) <<http://www.govtrack.us/congress/bills/111/hr2932>>.

¹⁵² Since 'experience has shown that when it comes to enforcing judgments obtained in the US, sovereign debt creditors were almost always forced to look for assets outside of the United States': Wautelet, above n 145, 22.

¹⁵³ Stop Very Unscrupulous Loan Transfers from Underprivileged Countries to Rich, Exploitative Funds Bill, HR 6796, § 3, 110th Congress (2009).

¹⁵⁴ *Ibid* §4(b).

¹⁵⁵ *Ibid* §5.

¹⁵⁶ *Ibid* §5(b).

¹⁵⁷ Lumina, above n 3, 15.

The *Stop VULTURE Funds Bill* is the primary legislative attempt at addressing vulture funds in the United States. Some American commentators have suggested alternative judicial solutions that would expand existing concepts to address sovereign debt litigation specifically: broadened sovereign immunity,¹⁵⁸ a return of the comity defence,¹⁵⁹ and even an across-the-board liberal interpretation of an existing judicial discretion to deny an order to attach¹⁶⁰ are three prominent examples. As with the French example, relying on the judiciary to limit vulture activities is unsatisfying; given that vulture funds are already predisposed to legal action as their primary business activity, making them well equipped and well funded as a result, it is hard to see how this would function as an effective deterrent. Unless the discretion were paired with a particular emphasis to stop vulture fund activities — as in the French civil law system — it would simply encourage vulture funds to extend their attrition tactics, arguing on the side of legitimate legal rights in successive courts until they receive a judgment in their favour. Even assuming that common law courts could be guided by objective criteria that permitted appropriate assessments of a sovereign debtor's reliance on debt relief or a vulture fund's speculative motives, in the short term this discretion would introduce an unpredictable element, injecting greater risk into sovereign lending. In the longer term, the experience of HIPC's as poorer parties with limited legal acumen, forcing them to give up in protracted legal struggles (as the DRC did in the New South Wales Supreme Court) makes a judicial solution even less persuasive. Finally, since vulture funds rely on the letter, if not the spirit, of the law, precedent-based solutions would be inconclusive until a superior court could issue an unambiguous statement of secondary creditor rights in sovereign debt cases — one would hope in favour of HIPC's. Otherwise, vulture funds will simply accrue decisions that, on legal principle, largely favour them. For the sake of expediency and clarity, clear-cut legislation is to be preferred.

D *The British Approach: Legislative Limitation*

The most important move against vulture funds to date is the passing of the *Debt Relief (Developing Countries) Act 2010* ('*DRDCA*') in the United Kingdom. Following extensive public consultation on how to limit sovereign debt recovery from HIPC's,¹⁶¹ a Private Member's Bill was introduced by Andrew Gwynne MP in December 2009 and passed with bipartisan support.¹⁶² Although originally the legislation was to last for one year following commencement,¹⁶³ it has since been entrenched in the law of England and Wales, with permanent effect as of 25 May 2011.¹⁶⁴ A more refined effort than its Euro-American counterparts, the *DRDCA* builds on the United Kingdom's existing commitments under the HIPC Initiative and enhances them by limiting what anyone, including private parties, can claim

¹⁵⁸ Goren, above n 14.

¹⁵⁹ Wheeler and Attaran, above n 75.

¹⁶⁰ Asiedu-Akrofi, above n 26.

¹⁶¹ United Kingdom, *Ensuring Effective Debt Relief for Poor Countries: A Consultation on Legislation* (HM Treasury, 2009).

¹⁶² Lumina, above n 3, 16.

¹⁶³ *Debt Relief (Developing Countries) Act 2010* (UK) c 22, s 9.

¹⁶⁴ *Debt Relief (Developing Countries) Act 2010 (Permanent Effect) Order 2011* (UK) SI2011/1336, O 2.

from a HIPC debt under the law of Great Britain and Northern Ireland. The close legal heritage between the United Kingdom and Australia suggests the legislation's suitability for Australia's purposes, but as of May 2013 it remains untested in British courts.

Section 1 defines the relevant 'qualifying debt' as:

a debt incurred before the commencement [of the *DRDCA*] that —

- (a) is public or publicly guaranteed,
- (b) is external,
- (c) is a debt of a country to which the [HIPC] Initiative applies or a potentially eligible [HIPC] country, and
- (d) in the case of a debt of a country to which the [HIPC] Initiative applies, is incurred before decision point is reached in respect of the country.

Unlike the other examples discussed so far, this *DRDCA* definition is nuanced, excluding short-term debts (discharged in less than a year from the time it was incurred) and liabilities for goods or services delivered to a HIPC.¹⁶⁵ The distinction is crucial: it confines the legislation's effect to those older debts favoured by vulture funds, issued before sovereign debt markets and debt relief programs ever existed. This means that the *DRDCA* does not grant HIPCs a 'free pass' for all the debts they have had or ever will have. It requires HIPCs to honour their less onerous (and more financially manageable) short-term debts and ensures responsibility where goods and services are provided. This counters the 'moral hazard' argument put forward by vulture funds themselves:¹⁶⁶ that to simply forgive or forget the contractual obligations of distressed debtors is commercially unfair and encourages reduced accountability, greater government corruption, and financial wastage.¹⁶⁷ By also reserving the right of HIPCs to seek new loans or financing agreements (acknowledging the practical reality of capital-driven economic development), the *DRDCA* encourages HIPCs to learn from hindsight and experience for sustainable future debt (presumably by seeking better terms on their debt).

The *DRDCA* also restricts the recovery on qualifying debt and related causes of action to levels permitted by the HIPC Initiative when a country reaches 'completion point'. This levels all creditors to the IMF/World Bank's thresholds that are already applicable to large-scale creditors, simultaneously accommodating for 'tailoring' to an individual HIPC's circumstances based on the negotiations that were conducted at completion point. Hence, the cap imposed builds on existing obligations without exceeding them and differentiates debtors. Although the *DRDCA* does not technically apply to compromise agreements (that compromise claims for qualifying debts or associated causes of action) and refinancing agreements (varying the terms of repayment or replacing the debt entirely), the amount recoverable under either arrangement is also restricted to HIPC Initiative

¹⁶⁵ *Debt Relief (Developing Countries) Act 2010* (UK) c 22, s 2.

¹⁶⁶ More specifically, their representative body, the Emerging Markets Trade Association: Lumina, above n 3, 16–17.

¹⁶⁷ Goren, above n 14, 691.

levels.¹⁶⁸ Additionally, the *DRDCA* applies to judgments on qualifying debt claims, fixing recovery irrespective of whether the judgment was given by a UK court before the *DRDCA*'s commencement, is a foreign judgment, or an award made through arbitration conducted under law.¹⁶⁹ The result of these configurations is that the *DRDCA* covers all the typical litigious means by which a creditor might seek recovery.

The final factor that makes the *DRDCA* so persuasive is best represented by s 6 of the legislation: the 'Exception where debtor fails to make offer to pay recoverable amount'. Section 6 excludes the Act from applying to any relevant claims, foreign judgments or arbitral awards where 'the debtor does not, before the relevant time, make an offer to compromise the proceedings on comparable [HIPC] Initiative terms.' In other words, the *DRDCA* is designed to protect proactive debtor nations. It will not protect lazy HIPC's, which themselves 'free-ride' on debt relief, and do not at least attempt to negotiate with their creditors. This is another guard against that moral hazard problem discussed above. Section 6 acknowledges that anti-vulture fund measures can encourage apathy by HIPC's, so the *DRDCA* makes its protection contingent on responsible behaviour and genuine engagement with debt relief. Requiring an offer of compromise gives creditors a chance to be treated on equal terms voluntarily (rather than compulsorily under the Act) and leaves the decision whether to engage in vulture behaviour in the creditors' hands. Hence, the *DRDCA* rewards HIPC's trying to give equal treatment to all their creditors, and ensures no-one can recover more than what majority creditors would already receive under their HIPC Initiative pledges in proceedings lodged in the United Kingdom.

E *An Ideal Solution for Australia*

The above solutions are different ways law can address the problem of vulture funds. Any method for reducing vulture fund excesses must (1) provide sufficient deterrence against vulture funds seeking to use Australian law to benefit them and (2) limit the flow-on effects that might impede acceptable corporate behaviour. This 'deterrence' factor to remove the incentives encouraging vulture behaviour must exist to motivate investors away from holding out and free-riding. However, while all the aforementioned proposals are primarily concerned with meeting the first outcome, only the *DRDCA* is tempered by the second goal. This latter objective, which might be labelled 'specificity', ensures that vulture funds are the sole parties regulated by the solution, distinguished from other creditors, and that the sole beneficiaries are HIPC's, which should be separately protected within the wider class of sovereign debtors. Ideally, an Australian response would be readily adaptable for the common law tradition as well, conscious of the role courts play in the common law tradition and capable of straightforward application.

Specificity also avoids unintended flow-on results, such as an increase in the cost of sovereign lending to prohibitively high levels, or the encouragement of bad debtor behaviour. Hence, active participation by all parties and subtle

¹⁶⁸ *Debt Relief (Developing Countries) Act 2010* (UK) c 22 ss 3(3)–(6).

¹⁶⁹ *Ibid* s 5(1).

distinctions between debts and debtors are good places to start. Another aspect of specificity is measured by unobtrusiveness: core concepts or processes underpinning sovereign borrowing/lending should be left unaltered, and existing obligations embraced by international debt relief should not be exceeded. In short, a persuasive model for Australia necessarily requires a degree of complexity that promotes fairness between creditors that willingly and unwillingly engage in debt relief, de-incentivises creditors from pursuing HIPC-issued debt for short-term gain, and retains HIPC involvement throughout. Given that the *DRDCA* achieves virtually all these outcomes, Australia should base its own model on this United Kingdom approach.

Legislation is a better mode of crafting a solution than is judicial method. The common law treats legislation very differently than in the civil law tradition, and implementing an Australian version of the French proposal particularly would require an adaptation of *champerty* and its ‘buy-back’ option, which is largely unknown in Australian law. This might upset existing practices of litigation funding and the assignment of litigious rights, and introduce a possibly unconstitutional broad judicial discretion (coupled with parliamentary suggestion) that might render it impossible to temper legislation or common law concepts of judicial independence and neutrality. Even if a purely judicial response were formed independent of the legislature (unlike the French example), its utility would still be limited. Trying to establish binding rules that do not infringe upon the principles of contractual obligation and debt repayment requires such judicial contortion that any precedent established would be confined to the unique characteristics of the parties and circumstances involved. The result is that HIPCs as a class would not be protected as required since *prima facie* no two distressed sovereigns are the same. In conjunction with the ‘attrition’ observations made earlier with respect to the American judicial alternatives, it is clear that a legislative approach should be preferred.

As indicated, private sector participation is vital to any solution; as vulture funds are privately owned and operated, attempts to curb their activities must apply equally to both public and private spheres. Although it is unlikely public sector creditors might initiate vulture litigation, everyone should be removed from the temptation to sell HIPC-issued debt to vulture investors. As for private parties, an ideal scheme would mandate participation, bringing all recovery (in any action seeking repayment or enforcement of extra-jurisdictional decisions) into line with levels consistent with existing debt relief efforts, such as the Enhanced HIPC Initiative. Not only would this work towards the consistency rationale stressed in Part III(C), but it would also make the most of the considerable work already completed by Australia in respect of debt relief. The *DRDCA* does precisely this, once again highlighting why it is the best option for Australia. An analogous scheme would remove the option of free-riding once all creditors (not merely the altruistic ones) are required to show a measure of generosity to their disadvantaged debtors.

Finally, an Australian solution must avoid being so heavy handed that it might undermine sovereign lending generally, or insert unpredictable discretion that encourages more protracted litigation in respect of sovereign lending. A

proposal that stops or impedes debt recovery would raise significant barriers for lending in the worldwide sovereign debt market, gradually driving interest rates to higher levels that would force riskier sovereign debtors (like HIPCs) out of borrowing entirely.¹⁷⁰ This result would be counterproductive: although vulture funds would be stymied, HIPCs would lose important streams of capital and their future development would be crippled. The Belgian law can be dismissed outright, as can the *Stop VULTURE Funds Bill*, which is equally unhelpful. In the latter model, the stringent measures and broad definitions involved essentially criminalise secondary creditor activities. First, the blanket limitation on recovery (the amount paid by a secondary creditor at purchase plus six per cent simple interest) removes all incentive for secondary creditors to trade sovereign debt (for fear of being labelled a ‘profiteer’), even if only at a HIPC-compliant level. Second, although the disclosure requirements would bring much-needed transparency into sovereign lending, compliance would become too significant a hurdle for ongoing sovereign lending. In the case of large institutional creditors such as banks, seeking repayment at levels consistent with the *Stop VULTURE Funds Bill’s* strict recovery floor requires the release of copious amounts of sensitive operational and ownership information onto the public record. This would alienate all creditors from ever seeking repayment, removing the rationale for debt entirely. In all these respects, the *DRDCA’s* HIPC Initiative-consistent thresholds for recovery (limiting what can be recovered, but not effectively stopping recovery itself) are much more useful. Once again, its careful adaptation to address vulture funds but not all secondary creditors, protecting engaged HIPCs without drastically reshaping sovereign creditor enforcement processes, makes it a specific but robust response to the problem of vulture funds. Australia should, for all these reasons, adopt a legislative scheme closely modelled on the United Kingdom’s *DRDCA*.

V Conclusion

This article has examined an issue that has so far received little attention in Australian law: vulture funds. Their hugely profitable business practices, centred on pursuing discounted debts owed by HIPCs, are in clear opposition to the international community’s agenda of reducing global poverty through debt relief. At their simplest, vulture funds exploit legitimate concepts of contractual obligation and debt repayment by ‘free-riding’ on the generosity of more forgiving creditors who wish to assist development in the world’s most disadvantaged economies.

Beyond the immediate diversion of resources away from HIPCs, questionable tactics are used by vulture funds in pursuit of their profits and take a disruptive toll on HIPC development. These are among the reasons why Australia should take decisive action against such activities. If anything, Australia’s substantial support of debt relief, opposed and hindered by vulture activities, provides sufficient justification to form some strategy that might restrict vulture funds in this jurisdiction. Without such a response, the litigation initiated by these funds would see Australia used as a venue for ‘hold-out’ behaviour that ‘free-rides’

¹⁷⁰ Goren, above n 14, 693.

on debt-related negotiation efforts. Only active efforts against vulture funds can address Australia's inconsistency in law and policy. A viable solution must be carefully customised to avoid unhelpful repercussions elsewhere.

Legislation resembling the United Kingdom's *DRDCA* should be adopted, because it is a model that focuses on vulture funds without imposing severe measures that might imbalance sovereign creditor/debtor relationships. Compared to other international and domestic proposals, the most attractive methodology is this British model, balancing deterrence and specificity. If a similar legislative scheme were adopted here, Australia would emerge as a leader among developed economies in recognising and addressing one of the world's most distressing, but largely unseen, problems.