These notes refer to the Debt Relief (Developing Countries) Act 2010 (c.22) which received Royal Assent on 8th April 2010

DEBT RELIEF (DEVELOPING COUNTRIES) ACT 2010

EXPLANATORY NOTES

INTRODUCTION

1. These Explanatory Notes relate to the Debt Relief (Developing Countries) Act 2010 which received Royal Assent on 8 April 2010. They have been prepared by Her Majesty's Treasury in order to assist the reader in understanding the Act. They do not form part of the Act and have not been endorsed by Parliament.

2. The Notes need to be read in conjunction with the Act. They are not, and are not meant to be, a comprehensive description of the Act. So where a section or part of a section does not seem to require any explanation or comment, none is given.

SUMMARY AND BACKGROUND

3. The enhanced Heavily Indebted Poor Countries Initiative ("the Initiative") is an international initiative to provide debt relief to heavily indebted low income countries. Under the Initiative, the International Monetary Fund ("the IMF") and World Bank calculate the proportionate reduction required in the country's external debts in order to return them to 150% of the country's annual exports[1], which is considered to be a sustainable level. All creditors – multilateral, bilateral and commercial – are expected to provide the proportionate reduction that will achieve this. At present, the Government, and many governments of other countries, multilateral lenders and commercial creditors do so.

4. 40 countries have been designated as eligible or potentially eligible for the Initiative. The current position of eligible or potentially eligible countries in the Initiative is given in the table below.

Eligible for the HIPC Initiative		*Potentially eligible for the HIPC Initiative*
Post-Completion Point (28)	*Post-Decision Point (7)*	*Pre-Decision Point (5)*
Afghanistan Benin Bolivia Burkina Faso Burundi Cameroon Central African Republic	Chad Côte d'Ivoire Democratic Republic of Congo Guinea Guinea-Bissau Liberia	Comoros Eritrea Kyrgyz Republic Somalia Sudan

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1 Countries with high exports relative to the size of their economy may also qualify under the 'revenue window', if their ratios of exports of goods and services to GDP and fiscal revenue to GDP exceed 30% and 15% respectively. For these countries, a ratio of 250% debt to fiscal revenue is assessed as sustainable and the HIPC Initiative expects the reduction that will lower their debts to this level. Subsequent references in these notes to sustainable levels of debt assume this point.

Eligible for the HIPC Initiative		*Potentially eligible for the HIPC Initiative*
Post-Completion Point (28)	*Post-Decision Point (7)*	*Pre-Decision Point (5)*
Republic of Congo Ethiopia The Gambia Ghana Guyana Haiti Honduras Madagascar Malawi Mali Mauritania Mozambique Nicaragua Níger Rwanda São Tomé Príncipe Senegal Sierra Leone Tanzania Uganda Zambia	Togo	

5. While many creditors reduce their debts in accordance with the Initiative, some creditors have instead sought to recover the full value of the debt plus accumulated interest and any associated charges owed to them. Repayment of these creditors diverts the resources provided through debt relief, which are intended to support development and poverty reduction in the country.

6. The Act addresses this by preventing creditors from recovering an amount in excess of that consistent with the Initiative. It also promotes the negotiated settlement of these debts on terms compatible with the Initiative by excluding from the scope of the legislation debts where the HIPC government does not offer to settle on such terms.

7. The Government issued a consultation document – *Ensuring effective debt relief for poor countries: a consultation on legislation* – on this issue on 21 July 2009 and has published a response to that consultation. Both are available on the HM Treasury website[2].

TERRITORIAL EXTENT AND APPLICATION

8. The Act extends to all parts of the United Kingdom.

COMMENTARY ON SECTIONS

Section 1 – Meaning of "qualifying debt" etc

9. *Section 1* defines the debts to which the Act applies. This is limited to those debts on which relief is expected under the Initiative, and which are incurred before commencement of the Act. It also limits the legislation so that future changes that might be made to the conditions for eligibility for the Initiative would not extend or reduce the debts to which the Act applies.

2 available from http://www.hm-treasury.gov.uk/consult_debt_relief.htm

10. *Subsection (3)* gives the broad definition of the debts to which the Act applies. The expressions used there are further defined in section 2.

11. *Subsections (3)(c) and (6)* extend the Act to the countries that have been identified by the World Bank and IMF as potentially eligible for debt relief under the Initiative on the grounds of their low income and high level of indebtedness, but which are yet to meet the conditions allowing the Boards of the World Bank and IMF to approve the country's entry onto the Initiative at Decision Point. Five countries currently fall into this category.

12. *Subsections (4) and (5)* cater for the restructuring of debts. The Act follows the practice of the Initiative in determining whether or not a debt is included in the Initiative on the basis of the nature of the original debt, rather than of a replacement that arises through a restructuring.

13. *Subsections (11) and (12)* restrict the legislation to apply to the debts of countries that meet the eligibility conditions for the Initiative as they stand at commencement. They stop the scope of the Act from expanding (or contracting) if a future policy decision were reached to change these conditions. The current conditions for a country to be designated eligible or potentially eligible for the Initiative include the following: (i) for the country's income levels currently and at the end of 2004 to be below the level for qualification for lending from the World Bank's International Development Association and the IMF's Extended Credit Facility and (ii) for its level of indebtedness at or before the end of 2004 to be such that it would remain above sustainable levels even after provision of a 67% reduction in the net present value of its debts through so-called traditional relief.

Section 2 – Qualifying debts: further definitions

14. *Section 2* defines in more detail the debts to which the Initiative applies and to which the Act applies. The definition is based on that used by the World Bank and IMF in determining which debts are included within the Initiative.

Section 3 – Amount recoverable in respect of claim for qualifying debt etc

15. *Section 3* reduces the amount recoverable on a debt to which the Act applies to the amount which the creditor could recover if the creditor provided the level of debt relief expected under the Initiative.

16. *Subsection (1)* reduces both qualifying debts and causes of action associated with those debts to the relevant proportion. A cause of action associated with a qualifying debt might, for example, be a damages claim.

17. *Subsections (3) and (4)* apply to instances where an agreement has been reached to reduce – "compromise" – a debt or related cause of action. For example, the creditor and debtor may have ageed to reduce a debt from £100 to £50, while the level of reduction expected under the HIPC Initiative is 90%. The effect of these sections is to apply that 90% reduction to the original £100, rather than the £50 value of the debt at the time the legislation is applied. In the example, the amount recoverable would be £10 rather than £5. The subsections ensure that a creditor that has agreed to such a compromise is not disadvantaged in comparison to a creditor that has not.

18. *Subsections (5) and (6)* have the same effect as *(3) and (4)* but cover agreements that reduced the debtor's obligations through rescheduling the terms of repayment or which replaced the original debt with a new debt. Subsection (5) refers to the net present value of future payments. The discount rate applied in association with the Initiative is the relevant Commercial Interest Reference Rate, as published by the Organisation for Economic Co-operation and Development ("the OECD").

19. *Subsection (8)* ensures that the reduction will apply when the qualifying debt is a secured debt, and the secured creditor attempts to enforce the security.

20. The effect of *subsection (9)* is that UK courts must apply the reduction even if they are applying foreign laws.

Section 4 – Meaning of "the relevant proportion"

21. *Section 4* defines the reduction in the amount of a debtor's obligations brought about by the Act.

22. *Subsection (2)* applies to the debts of countries that have reached Decision Point under the Initiative. It defines the relevant proportion of a debt by referring to the reduction in accordance with the Initiative. Practice under the Initiative is as follows. At Decision Point, the IMF and World Bank calculate the percentage reduction which is required from all creditors holding debts included in the Initiative in order to reduce the country's indebtedness to a sustainable level. These organisations publish within their Decision Point document the Common Reduction Factor. This sets the reduction expected from all creditors after they have provided so-called traditional relief of 67%. The amount the debt would be if it were reduced in accordance with the Initiative is the amount it would be if firstly reduced by the application of traditional relief at 67% and secondly if further reduced by the proportion set by the Common Reduction Factor.

23. For example, the Common Reduction Factor for an eligible country might be 33%. A debt of £100, if reduced in accordance with the Initiative, would first be reduced by 67% through traditional relief, to a new value of £33. Further reduction by the Common Reduction Factor gives the amount the debt would be if it were reduced in accordance with the Initiative (A) as £22, and hence the relevant proportion as 22%.

24. The assumption, if it is not the case, that Completion Point has been reached, is included for the following reason. While individual Decision Point documents set out the debt relief a country needs in order for that country's debt burden to become sustainable, under the Initiative debt relief need not be provided until a country reaches Completion Point. In practice, creditors who voluntarily participate in the Initiative give relief from Decision Point onwards, in the form of interim reductions in the debt service payments. The purpose of the Act is to ensure that once a country has reached Decision Point, creditors should only be able to recover that proportion of their debts that is consistent with the reduction expected in the IMF's Decision Point analysis. That is done by the assumption that countries have reached Completion Point.

25. Some countries are assessed as needing additional 'topping up' of assistance at Completion Point. In these instances, a higher Common Reduction Factor is published by the World Bank and IMF in the Completion Point documents. HIPC Initiative practice is to apply the most recently published Common Reduction Factor, and that is the outcome expected under this section.

26. *Subsection (3)* applies to the debts of countries yet to reach Decision Point. For these countries, the World Bank and IMF will not (in general) have calculated the Common Reduction Factor by which debts must be reduced in addition to the provision of the traditional reduction of 67%. To be designated as a country potentially eligible for the Initiative, its debts must be sufficiently high as to remain unsustainable even if creditors provided this traditional relief. It is known that, upon reaching Decision Point, the expected reduction will be assessed as at least 67%. As its value cannot be determined beyond this, the subsection applies the 67% reduction alone to these debts and sets the relevant proportion at 33%.

Section 5 – Judgments for qualifying debts etc

27. *Section 5* reduces the value of judgments and arbitration awards relating to debts to which the Act applies. It applies to judgments given in the UK before commencement of the Act, so that such judgments may be enforced only for the reduced amount. Section 5 also applies to the enforcement of awards and foreign judgments in the UK, and those awards and judgments may only be enforced for the reduced amount.

28. *Subsection (6)* has the effect of ensuring that a creditor that has compromised a claim is not disadvantaged, as with section 3(3) and (4).

Section 6 – Exception: debtor failing to make offer to pay recoverable amount

29. *Section 6* contains an exception to the legislation, excluding debts where the debtor does not make an offer to repay the amount which remains recoverable by the creditor under the terms of the Act. This provision does not correspond to an existing element of the Initiative. Its purpose is to increase the creditor's prospects for recovering the amount to which it remains entitled, and to encourage the debtor to participate in negotiations to agree settlement of the debt rather than oblige the creditor to recover the debt through the courts.

30. This provision will not apply to proceedings to enforce domestic judgments given before the commencement of this legislation (or proceedings to enforce foreign judgments registered before that date, or to enforce arbitration awards where permission has been given before that date for the award to be enforced as if it were a judgment.) In those situations, the reduction will apply to the judgment or award, without the need for the debtor to make an offer.

31. *Subsection (2)* refers to the net present value of future payments. The discount rate applied in association with the Initiative is the relevant Commercial Interest Reference Rate, as published by the OECD.

Section 7 – Exception for overriding EU or international obligations

32. *Section 5* applies the Act to certain foreign judgments or arbitration awards. The UK is obliged to enforce foreign judgments and awards under a number of international instruments. The reduction in this Act will apply where, under the relevant international instruments (for example EU Regulation 44/2001 – 'Judgments Regulation'), the UK is entitled to refuse to enforce judgments and awards, where to do so would be contrary to the UK's public policy.

33. *Section 7* excludes foreign judgments and arbitration awards from the effects of the Act where the UK is obliged under international instruments to enforce them in full, even where such enforcement is contrary to the UK's public policy.

34. *Subsection (2) (a) and (b)* exclude from the Act two procedures for fast-track enforcement under EU Regulations. Both procedures apply only to uncontested claims.

Section 8– Saving

35. *Section 8* prevents the Act from requiring repayment by the creditor of an amount already paid by the debtor in relation to any of the liabilities dealt with by the Act.

Section 9 – Duration of Act

36. *Section 9* provides that the Act will expire one year from commencement, unless it is extended - either for a further year or permanently - by order made by Treasury. The Treasury's order-making powers are subect to affirmative procedures in Parliament. If the Act expires by reason of section 9, it is to be treated as never having been in force, and any judgment given while the Act was in force will be treated as if it had not been reduced by the operation of section 3.

COMMENCEMENT

37. The Act will come into force two months after receiving Royal Assent.

HANSARD REFERENCES

38. The following table sets out the dates and Hansard references for each stage of the Act's passage through Parliament.

Stage	*Date*	*Hansard reference*
House of Commons		
Introduction	16 December 2009	Vol. 502 Col 978
Second Reading	26 February 2010	Vol. 506 Cols 559-584
Committee	9 March 2010	Debt Relief (Developing Countries) Bill Committee
Report and Third Reading	7 April 2010	Vol. 508 Cols 1044-1056
House of Lords		
Introduction	7 April 2010	Vol. 718 Col 1540
Second Reading and Remaining Stages	8 April 2010	Vol. 718 Cols 1695-1703
Royal Assent – 8 April 2010		House of Commons: Vol. 508 Col 1256
		House of Lords:Vol. 718 Col 1738