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Douglas L. Hymas

Robert P. Doane

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I. Introduction

Since the late 1970's, third world countries have been struggling to meet debt service payments on external debt. Proposed solutions to what has been called the "international debt crisis" are many, and are based on varying characterizations of the problem itself.

The U.S. Department of Treasury has maintained a role of leadership in urging a conservative approach to the debt crisis. Congress, on the other hand, initially did not become involved in international debt issues. But in 1987, Congress, finally recognizing a relationship between the debt crisis and U.S. foreign trade, expressed discontent with the Treasury Department's approach and began considering other proposals with a view towards including an alternative in the Omnibus Trade and Competitiveness Act of 1988 (hereinafter Trade Bill).[1] The result was the International Debt Management Act, which encourages the current administration to adopt a more active approach towards the debt crisis.

The Trade Bill, however, also provides the Treasury Secretary with some important loopholes with which he may avoid strict compliance with the statute's broad policy changes. This comment will briefly review the history of the international debt problem, followed by an explanation of the Treasury Department's current conservative approach. Then, Congress' alternative solution as set forth in the International Debt Management Act will be presented and analyzed to determine the probable effect it will have on current U.S. international debt policy.

II. Background of the International Debt Problem

A. *International Debt Before 1985*

In the early 1970s, Less-Developed Countries (LDC)[2] throughout the world found themselves with promising eco-

1. The Omnibus Trade and Competitiveness Act of 1988, Pub. L. No. 100-418, 102 Stat. 1107 (1988) [hereinafter 1988 Trade Act].

2. For purposes of this comment, Less Developed Countries include Latin America and other third world countries that have borrowed substantial sums from Western com-

nomic opportunities in international markets. Latin American countries in particular began industrializing, taking advantage of inexpensive labor and vast supplies of raw materials. Cheap oil prices facilitated not only production of goods, but also kept transportation costs low for importing and exporting.[3] At the same time, multinational banks found themselves with excess reserves resulting from large deposits by OPEC countries ("petro-dollars"). These banks saw the growth of LDC as creating a promising market in which to invest the excess reserves, and proceeded to finance LDC efforts to compete in international markets.[4]

At first, LDC easily met debt service requirements, allowing banks to realize profits on their investments. But several unexpected events soon ended this symbiotic economic arrangement. A rise in oil prices, initiated by OPEC, beginning in 1973, increased production and transportation costs worldwide. For LDC, higher costs resulted in the need for more loans.[5] More loans meant higher financing costs. Thus, the resulting higher production and financing costs made it increasingly difficult for the highly-leveraged[6] LDC to compete internationally. Furthermore, in late 1979, the U.S. tightened its monetary policy to combat domestic inflation, causing interest rates worldwide to rise to historic heights as the dollar strengthened vis-a-vis other major currencies. Higher interest rates meant even higher debt service costs for LDC.[7]

LDC debt service payments continued to climb even as increased production costs hampered their ability to compete in international markets. By 1983, principal amounts on third

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mercial banks. Also, references to debt owed by LDC include those owed by both LDC governments (sovereign debt) and LDC private borrowers.

3. *See generally* Comment, *Treasury Secretary James Baker's "Program for Sustained Growth" for the International Debt Crisis: Three Steps Toward Global Financial Security*, 4 Dick. J. Int'l L. 275 (1986).

4. LDC growth rates exceeded prevailing interest rates, kept low by the availability of petro-dollars.

5. *See* S. Griffith-Jones, International Finance and Latin America (1982).

6. "Leveraging" refers to a high level of debt financing as compared to the level of equity financing. The term "highly leveraged" indicates a high debt-to-equity ratio. A higher relative debt-to-equity ratio has the effect of amplifying profits (or losses) per share of equity holdings.

7. *See generally* D. Delamaide, Debt Shock: The Full Story of the World Credit Crisis 232-51 (1985). Since the early 1980s the U.S. federal deficit has also contributed to high interest rates worldwide by reducing the amount of credit available to the third world. *See also* Roett, *Democracy and Debt in South America: A Continent's Dilemma*, 62 Foreign Aff. 695 (1983).

world debt reached levels some countries found difficult to service.[8] Interest payments for Mexico and Brazil alone amounted to $22 billion in 1985.[9] Debtor countries were forced to curtail imports and aggressively promote exports to generate the foreign exchange necessary to meet debt service payments.[10] Though some debtor countries were able to attain a favorable trade surplus, 35% to 45% of their net export earnings were swallowed up by debt service payments.[11] In many instances, the level of debt service costs increased more rapidly than net export earnings.[12]

Many lenders viewed LDC struggles to meet debt service payments as a liquidity problem (i.e., a temporary shortage of foreign exchange), rather than as one of insolvency. They felt that when interest rates dropped and external conditions improved, LDC would again be able to compete effectively in international markets, and that as long as LDC growth was sustained, in the long run LDC would be able to meet debt service requirements. Thus, growth of LDC was considered the touchstone of any solution to the international debt problem.[13]

The International Monetary Fund (IMF)[14] assumed a greater role in helping debtors meet short-term cash requirements through increased lending. As a condition to receipt of assistance, it also imposed austere measures on LDC to encourage reform and promote growth.[15] These austerity measures,

8. *See* Cohen, *High Finance, High Politics*, in UNCERTAIN FUTURE: COMMERCIAL BANKS AND THE THIRD WORLD 107 (Feinberg & Kallab eds. 1984). By mid-1982, the total debt of the Latin American countries had reached nearly $300 billion, including $90 billion for Mexico, $75 billion for Brazil, $30 billion each for Argentina and Venezuela, and $15 billion for Chile. Two-thirds of this amount was owed to commercial banks.

9. Meltzer, International Debt Problems 1 (July 1986) (unpublished abstract available from the Department of Economics, Carnegie-Mellon University).

10. In Latin America alone, the trade balance moved from a deficit of $4 billion in 1981 to a surplus of $38 billion in 1984. S. REP. No. 1409, 100th Cong., 1st Sess. 36 (1987).

11. *See* Hormats, *The World Economy Under Stress*, 64 FOREIGN AFF. 455, 476 (1985).

12. *Id.*

13. *See* Wertman, *The "Baker Plan": A Remedy for the International Debt Crisis?*, CONG. RES. SERV. Aug. 16, 1988. *See also* Comment, *supra* note 3. All of the major proposals under consideration at that time, and even now, consider sustained economic growth within LDC's to be the solution. They differ, however, on how this economic growth can most effectively be sustained.

14. *See* Robichek, *The International Monetary Fund: An Arbiter in the Debt Restructuring Process*, 23 COLUM. J. TRANSNAT'L L. 143, 149 (1984).

15. IMF austerity measures generally consist of: attempting to reduce government expenditure by eliminating government subsidies and cutting back domestic credit; in-

however, made domestic investment in LDC less attractive to domestic investors,[16] and resulted in "capital flight".[17] To avoid continued capital flight, the IMF sought to increase funds available from external sources, particularly from commercial banks and other multilateral financial institutions.

Initially, banks and multilateral financial institutions complied with IMF requests to continue to extend loans to debtor countries under the assumption that when interest rates decreased LDC growth rates would outrun debt service requirements.[18] But even after interest rates dropped in the early eighties, LDC had trouble meeting debt service payments. As LDC debt levels rose to unsustainable levels, creditors began doubting the wisdom of extending loans to already financially troubled countries, and such lending decreased.[19]

In this setting, then U.S. Treasury Secretary James Baker, III, introduced in 1985 a comprehensive plan to increase lending to LDC. His plan quickly gained support from the Group of Seven (G-7)[20] countries and multilateral development banks,

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creasing foreign demand for domestic products while decreasing domestic demand for imports by devaluing the currency; and stimulating savings by increasing interest rates. *See* J. CAVANAGH, F. CHERU, C. COLLINS, C. DUNCAN & D. NTUBE, THE DEBT CRISIS NETWORK, FROM DEBT TO DEVELOPMENT: ALTERNATIVES TO THE INTERNATIONAL DEBT CRISIS (1986) [hereinafter DEBT CRISIS NETWORK].

16. S. REP. No. 1409, 100th Cong., 1st Sess. 36 (1987) ("Since the debt crisis, capital investment as a share of GDP [Gross Domestic Product] in the developing world has fallen by 5 percent, but it has dropped a staggering 27 percent in those countries where debt servicing problems have most dramatically shifted the resource transfer equation.").

17. *Id.* at 40. "Capital flight" occurs when 1) borrowed funds leave a debtor country via debt service payments or other foreign-exchange outflows, or 2) investors lose faith in domestic markets and invest abroad, thus drying up domestic capital and forcing the country to rely increasingly on foreign investment capital. *See* BUSINESS WEEK, Oct. 3, 1988, at 110.

18. The additional loans were primarily short-term, one to three years in duration. Therefore, the lenders, as a whole, were under the assumption that the shorter-termed loans would be timely repaid. This assumption proved erroneous as the already troubled debtor countries' economic situations worsened to the point that they could not even service their short-term commitments.

19. S. REP. No. 1409, 100th Cong., 1st Sess. 35 (1987). The sharp decrease in lending was precipitated in 1982 when Mexico found it difficult to meet its debt service payments:

> [T]he developing world increased its borrowing from private sources by $74 billion in 1981, the year before the Mexican crisis. In 1982, new borrowings fell to $48 billion, and they collapsed to $17 billion in 1983. The situation was far worse for the fifteen "heavily indebted countries" which saw net new lending of $56 billion [in] 1981 fall to $29 billion in 1982, only to drop to a negative $2.6 billion in 1983."

Id.

20. The Group of Seven include Canada, France, Great Britain, Germany, Italy, Ja-

such as the IMF and the World Bank, and has since been a dominating influence in the concerted effort to curb the international debt problem.

B. 1985 to 1988: The Baker Plan Era

On October 8, 1985, in Seoul, Korea, Secretary Baker presented his "Program for Sustained Growth"[21] to the Joint Annual Meeting of the IMF and the International Bank for Reconstruction and Development (World Bank). The "Baker Plan", as it has come to be called, set forth a conservative three-prong approach to the debt problem:[22] first, adoption by debtor countries[23] of austere economic reform measures similar to those required by the IMF;[24] second, continued lending by IMF and other multilateral development banks conditioned on the debtors' adoption of the reforms set forth in the first prong;[25] and third, increased lending by multinational commercial banks,[26] also conditioned on debtors' adoption of the reforms. The Baker Plan acknowledges the unique circumstances surrounding each debtor country and encourages the case-by-case strategy already adopted at the joint meeting in 1982.[27] It also stresses the need to keep worldwide interest rates low so that multilateral development banks such as the IMF and the World Bank can acquire funds and pass them on to debtor countries inexpensively.

The thrust of the Baker Plan is its commitment to continued lending as the sole remedy for the international debt problem. This approach is based on the assumption mentioned above that growth rates in debtor countries can be increased to match and outrun debt service burdens.

The Baker Plan has, however, met opposition on several

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pan, the United States and West Germany.

21. *See* Comment, *supra* note 3.

22. Comment, *supra* note 3, at 308.

23. Shortly after Mr. Baker presented his plan, the Treasury Department identified fifteen heavily indebted countries as proposed participants. The countries named were Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, Ivory Coast, Jamaica, Mexico, Morocco, Nigeria, Peru, Philippines, Uruguay, Venezuela, and Yugoslavia. Wertman, *supra* note 13.

24. Comment, *supra* note 3, at 278.

25. The Baker Plan called for increased lending by multilateral development banks in the amount of $9 billion over the three year period beginning in 1985. *Id.*

26. The Baker Plan called for increased lending by commercial banks in the amount of $20 Billion over the three years beginning in 1985. *Id.*

27. *Id.*

fronts.[28] First, commercial banks have been reluctant to extend more loans to already burdened LDC.[29] Second, certain U.S. congressmen complain that the plan anticipates the use of public funds to protect commercial banks from LDC default. By encouraging LDC to use new loan proceeds (some of which come from publicly funded development banks) to pay old debt service payments, the plan only perpetuates LDC insolvency while erroneously assessing that the debtor countries are credit-worthy. And finally, LDC claim that exorbitant debt service burdens have only increased under the plan without corresponding relief.[30]

Since its introduction the Baker Plan has been zealously advocated by the U.S. Treasury Department and has been followed by the G-7,[31] the IMF, the World Bank, and various multilateral development banks. By early 1987, however, members of Congress felt that LDC efforts to increase imports and decrease exports in order to meet debt service payments was a contributing cause of the increasing U.S. trade deficit; consequently, they believed that more active involvement in solving the international debt problem would help not only LDC, but also the U.S. Thus, Congress began calling for more direct involvement. It considered various new proposals for solving the international debt problem,[32] many of which involve debt restructurings,[33] debt

28. Senator Bill Bradley declared at a monetary conference in Washington in September, 1988 that the Baker Plan was dead. He stated further that the "only decent thing to do is bury it" and start over. He further stated that the major premise of the plan was miscalculated: "Any banker will tell you there's simply no way banks are going to lend the new money needed in highly indebted middle-income countries. The period when commercial bank lending dominated development has ended." Quoted in Silk, *Economic Scene: A Strident U.S. at I.M.F. Talks*, N.Y. Times, Sept. 30, 1988, at D2, col. 1.

29. *Bank for International Settlements, International Banking Developments and Financial Markets*, (various issues). Commercial banks have failed to increase their exposure by the 6% to 7% per annum which was initially called for in the Baker Plan, but instead reduced their lending to Latin America and Africa to $2.1 billion and $0.7 billion in 1985.

30. *See* DEBT CRISIS NETWORK, *supra* note 15, at 77 ("No mention is made of cutting interest costs or restructuring debt, for example. Moreover, by relying heavily on variable-rate bank loans as the source of new funds, the Baker Plan may only exacerbate an already precarious situation.").

31. *See supra* note 20.

32. Wertman, *The International Debt Problem: Congressional Proposals*, CONG. RES. SERV. Mar. 3, 1987.

33. "Restructuring" generally refers to rescheduling and refinancing of loans. Rescheduling usually involves an extension of the term of a loan, thereby decreasing the amount of the periodic payment. Refinancing, on the other hand, involves the offering of new credit on different terms than the original loan, i.e., lower interest rate, longer term,

write-offs,[34] or both. Several congressional committees charged with international debt issues[35] formulated the International Debt Management Act to be included in the Omnibus Trade and Competitiveness Act of 1988[36] as a statement of congressional disenchantment with the Baker Plan.

III. The International Debt Management Act

President Reagan signed the Trade Bill on August 23, 1988. As formulated by Congress, Subtitle B of Title III, entitled the International Debt Management Act (the Act), encourages the administrative branch to adopt a more active approach in dealing with the debt crisis.

A. Policy Changes in the Act

1. Justification for policy changes

Section 3102 of the Act sets forth Congress' reasoning for altering the Treasury's approach to third-world debt. Congress found that—

> (1) the international debt problem threatens the safety and soundness of the international financial system, the stability of the international trading system, and the economic development of the debtor countries;
>
> (2) orderly reduction of international trade imbalances requires very substantial growth in all parts the world economy, particularly in the developing countries;
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> (3) growth in developing countries with substantial external debts has been significantly constrained over the last several years by a combination of high debt service obligations

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etc. The principal of the new loan is used to satisfy the original loans. *See generally* Note, *Sovereign Debt Restructuring: The Rights and Duties of Commercial Banks* Inter Sese, 1987 Colum. Bus. L. Rev. 425.

34. *Third-world Debt: Hearings on Congressional Proposals before the Subcomm. on International Development Institutions and Finance of the House Committee on Banking, Finance and Urban Affairs*, 100th Cong., 1st Sess. (1987). A "write-off" involves the forgiving by a bank of all or part of a loan, allowing debtors to start anew. Opponents of write-off strategies argue that some creditors may not have sufficient reserves to cover the accompanying losses and that credit ratings of countries whose debts are written off would plummet, severely limiting those countries' ability to obtain subsequent loans.

35. The congressional committees involved were the House Committee on Banking, Finance and Urban Affairs, the Senate Committee on Banking, Housing, and Urban Affairs, and the Senate Committee on Foreign Relations.

36. 1988 Trade act, *supra* note 1.

and insufficient new flows of financial resources to these countries;

(4) substantial interest payment outflows from debtor countries, combined with inadequate net new capital inflows, have produced a significant net transfer of financial resources from debtor to creditor countries;

(5) negative resource transfers at present levels severely depress both investment and growth in the debtor countries, and force debtor countries to reduce imports and expand exports in order to meet their debt service obligations;

(6) current adjustment policies in debtor countries, which depress domestic demand and increase production for export, help to depress world commodity prices and limit the growth of export markets for United States industries;

(7) the United States has borne a disproportionate share of the burden of absorbing increased exports from debtor countries, while other industrialized countries have increased their imports from developing countries only slightly;

(8) current approaches to the debt problem should not rely solely on new lending as a solution to the debt problem, and should focus on other financing alternatives including a reduction in current debt service obligations;

(9) new international mechanisms to improve the management of the debt problem and to expand the range of financing options available to developing countries should be explored; and

(10) industrial countries with strong current account surpluses have a disproportionate share of the world's capital resources, and bear an additional responsibility for contributing to a viable long-term solution to the debt problem.[37]

Thus, Congress' justification for the Act stems from the adverse impact of the debt crisis on U.S. foreign trade and the lack of improvement under the Baker Plan.

2. *Policy changes*

Congress' desire to explore alternatives to the Baker Plan is reflected in two sections of the Act. A short section describes the subtitle's "purposes". The purposes stated are altruistic and broad in scope.[38] The other section in the Act sets forth U.S.

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37. *Id.* § 3102.

38. *Id.* at § 3103:

The purposes of this subtitle are—

(1) to expand the world trading system and raise the level of exports from

"policy" regarding the international debt crisis. In comparison with the purposes, the policies are more straightforward in expressing Congress' intent to broaden the U.S.'s current approach to the debt crisis.[39] Subparagraphs (2) and (3) illustrate the change:

> It is the policy of the United States that—
>
> . . . .
>
> (2) it is necessary to broaden the range of options in dealing with the debt problem to include improved mechanisms to restructure existing debt;
>
> (3) active consideration of a new multilateral authority to improve the management of the debt problem and to share the burdens of adjustment more equitably must be undertaken . . . .[40]

The very suggestion of restructuring third world debt cuts at the heart of the Baker Plan's conservative refusal to alter loan terms. Also, subparagraph (3)'s proposed creation of a multilateral entity to facilitate debt restructuring is similar to an earlier proposal expressly rejected by the Treasury Department.[41] Thus, Congress is calling for more active solutions to the international debt problem than the Treasury Department has been implementing.

The Act as first passed by the House of Representatives required strict adherence to the above policies.[42] However, the House version was greatly moderated in the Senate.[43] The final

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the United States to the developing countries in order reduce the United States trade deficit and foster economic expansion and an increase in the standard of living throughout the world;

(2) to alleviate the current international debt problem in order to make the debt situation of developing countries more manageable and permit the resumption of sustained growth in those countries; and

(3) to increase the stability of the world financial system and ensure the safety and soundness of United States depository institutions.

39. *Id.* § 3104.

40. *Id.* § 3104 (2), (3).

41. *Hearings Before the Subcomm. on International Development Institutions and Finance of the House Comm. on Banking, Finance and Urban Affairs*, 100th Cong., 1st Sess. 888 (1987). David Mulford, then Assistant Secretary for the Treasury on International Affairs, argued that a new debt facility would not be effective in helping ease debt service burdens because 1) there is already a secondary market for LDC debt; 2) growth rates of debtor countries would not be sustainable; and 3) reductions in market interest rates since 1984 have already provided $13 billion in annual debt service saving without the aid of a debt facility. *Id.*

42. H.R. 3, 100th Cong., 1st Sess., Title III, Subtitle B (1987).

43. Telephone interview with Gary Parker, Banking Committee Representative for

version contains only directives for the Secretary of the Treasury. He is directed to research the possibility and feasibility of creating a multilateral facility, which would be called the International Debt Management Authority[44] (IDMA). The Act requires no other affirmative steps toward reducing LDC's debt burden, and thus contemplates enforcement of its policy changes through the IDMA. Because the IDMA is meant to be the door through which the new policies will enter into the international debt arena, creation of the IDMA is a prerequisite to implementation of the Act's new policies.

B. *The International Debt Management Authority*

1. *Statutory specifications*

Part II of the Act,[45] directs the Secretary of the Treasury to study the "feasibility and advisability"[46] of creating the IDMA. If the Secretary concludes that attempts to create the IDMA would 1) materially increase the discount at which LDC debt is sold, 2) materially increase likelihood of default on LDC debt, or 3) materially enhance likelihood of failure or disruption of debt service payments, he is relieved of his duty to pursue creation of the IDMA. He must report to Congress in detail the grounds on which these conclusions are based.[47]

Unless the Secretary reaches one of the above conclusions, he is directed to initiate discussions with such other industrialized or developing countries as he determines to be "appropriate,"[48] regarding creation of the IDMA. The establishment and operation of the IDMA is governed by five general guidelines, summarized as follows:

> (1) Loan assistance provided by the IDMA should include return commitments by debtors to sound economic policies which will improve resource utilization and minimize capital flight, and to economic management plans which will provide sustained economic growth and allow the debtor to meet its restructured debt service payments.
> (2) The IDMA's financial support should be provided by indus-

Senator Jim Leach of Iowa (Oct. 13, 1988).

44. 1988 Trate Act, *supra* note 1, §§ 3111-12.
45. *Id.* §§ 3111-3113.
46. *Id.* § 1111(a)(1).
47. *Id.* § 3111(a)(2).
48. *Id.* § 3111(a)(3).

trialized countries, with more support being expected from those with strong current account surpluses.
(3) The IDMA should work closely with the IMF, the World Bank, and other regional development banks.
(4) The IDMA should, after capitalization, operate as a self-supporting entity, subject to prohibitions discussed below.
(5) The IDMA should have a pre-established termination date and a detailed proposal for accomplishing its purposes within that time.[49]

The IDMA would be given power to purchase the sovereign debt[50] of LDC's from commercial banks, thus helping them dispose of their third-world loan portfolios.[51] The IDMA itself would then become the creditor and would restructure the debt to ease LDC's debt service burdens.[52]

The IDMA, if created, will function as a multilateral facility for implementing the policies set out in the Act. This would be a marked improvement over the Baker Plan, which lacked a similar facility to implement its policies.

To be successful, the IDMA would need to develop a close working relationship with other multilateral development facilities such as the IMF and the World Bank. Coordination between these institutions will ensure more effective use of resources, whereas independence among them may lead to gaps or overlaps of relief. The IDMA should also maintain a close relationship with the commercial banks in order to solicit their participation in debt relief policies.

2. *The Treasury Secretary's responsibility*

As mentioned above, actual implementation of the Act's policies with respect to international debt are contingent on creation of the IDMA. The original House version of the Act required the Secretary of the Treasury to initiate discussions to

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49. *Id.* § 3111(b). The Senate Committee on Banking, Housing and Urban Affairs emphasizes international cooperation in forming the IDMA as fundamental to its success: "The debt problem is truly an international one, with U.S. domestic banks accounting for only about one-third of the total outstanding debt, and should be addressed on an international basis." S. REP. No. 1409, 100th Cong., 1st Sess. 39 (1987).

50. *See supra* note 2.

51. 1988 Trade Act, *supra* note 1, § 3111(a)(3)(A)-(C).

52. "Restructure" is not defined in the statute, but generally refers to some alteration of the original terms of the loan to reduce current debt service burdens. Restructures often involve a decrease in the interest rate, an extension of the repayment period, or some combination of the two. *See supra* note 33.

that end. But as moderated in the Senate, the enacted version places on him sole responsibility to research the "feasibility and advisability"[53] of creating the IDMA and to make recommendations to Congress based on his findings.

Within six months of the Trade Bill's enactment, the Act directs the Secretary to submit an interim report to congressional committees concerned with the international debt issues[54] and to consult with them regarding the progress being made as to creation of the IDMA.[55] Similarly, a second report must be filed within another six months.[56] Upon completion of the study, the Secretary is also required to submit a final report which shall include "such recommendation for legislation which [he] may determine to be necessary or appropriate" to establish the IDMA.[57] Thus, the enacted version of the Act places the Secretary in a key discretionary position to influence congressional opinions respecting the need to create the IDMA and, thereby, to influence implementation of the Act's new policies.

C. *Other Miscellaneous Items in the Act*

The Act also directs Federal banking regulatory agencies[58] to allow "the widest possible latitude" with respect to debt restructuring by commercial banks with high exposure to third-world debt.[59] It encourages the agencies to require those banks to seek "expanded recapitalization through equity financing" (i.e., "debt-equity" swaps)[60] in order to establish and maintain acceptable capital-to-total-asset ratios.[61]

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53. *See supra* note 46 and accompanying text.

54. *See supra* note 35.

55. 1988 Trade Act, *supra* note 1 § 3111(c). President Reagan signed the Trade Bill on August 23, 1988; the first interim report was thus due on February 23, 1989, but was submitted until early March.

56. *Id.* The second interim report is due August 23, 1989.

57. *Id.* § 3111(d).

58. Specifically, the Federal agencies to which this section applies are those which "regulate and oversee the operations of depository institutions (within the meaning given to such term by clauses (i) through (vi) of section 19(b)(1)(A) of the Federal Reserve Act)." *Id.* § 3121 (b)-(d).

59. *Id.* § 3121(b).

60. S. REP. No. 1409, 100th Cong., 1st Sess. 4 (1987):

> Debt-equity conversions involve conversion of a fixed or floating-rate loan made to an LDC government or company into an equity position in the company or country involved. More commonly referred to as "debt-equity swaps,' these transactions occur when a creditor sells a loan, usually at a discount, to a third party in return for equity ownership in the debtor.

61. 1988 Trade Act, *supra* note 1 § 3121(c).

It is worth noting that Part III of the Act contains no specific standards or measures with which the regulatory agencies must comply. Rather, it permits them to grant banks the necessary flexibility to handle their third world debt portfolios in ways previously disdained under the Baker Plan. Part III, then, is a natural extension of Part II's proposed creation of the IDMA to facilitate those transactions.

IV. The Act's Probable Effect on Current U.S. International Debt Policy

If created, the IDMA would be an effective means for supplementing Baker Plan policies of increased lending. It would assume a leadership role as a centralized facilitator and coordinator of debt relief transactions. Unmanageable debt service levels would be decreased without simultaneously eliminating LDC's access to funds when necessary.

However, the same result might be reached without creation of the IDMA if the Baker Plan were simply expanded to include such measures as restructurings, write-downs, debt-equity swaps, etc. In addition, in balancing its commitment to the Baker Plan against Congress' impatience with it, the Treasury Department may opt for allowing a broader Baker Plan rather than compromising its leadership role by creating the IDMA.

With respect to creation of the IDMA, the Act is silent as to how the Treasury Secretary should conduct the study called for in section 3111, nor does it mention variables or standards on which he should base his conclusions. It simply states that a conclusion unfavorable to creation of the IDMA must be adequately substantiated.[62] Thus, the Secretary has been given broad discretion as to how the study should be conducted. Accordingly, he may use that discretion to oppose creation of the IDMA, and a conclusion to that effect appears most likely.[63]

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62. *Id.* § 3111(a)(2) & (d).

63. Treasury Secretary Nicholas F. Brady, who only recently replaced James Baker, III, recently reaffirmed the Treasury Department's commitment to the Baker Plan in a joint annual meeting of the World Bank and IMF. L.A. Times, Oct. 4, 1988, § 2 (Metro), at 6, col. 1. Mr. Brady not only encouraged increased lending, but also rebuffed recent proposals to increase the role of governments and international financial institutions in solving the debt crisis, saying that shifting some of the burden to those entities would produce only an "illusion of progress." *See, also*, L.A. Times, Sept. 28, 1988, § 4 (Business), at 2.

Mary Chaves of the International Debt Policy Office at the Treasury Department indicated that though no official statement regarding the Secretary's study would be is-

In the event that the Secretary opposes the creation of the IDMA, it is unlikely that Congress would enact provisions mandating its creation. Even though the major proponents of the Act have convinced many congressmen that a more active policy is necessary to solve the international debt problem, they have not been successful in soliciting consensus on a single approach.[64] It seems unlikely, then, that absent a consensus on the IDMA as the optimum approach, Congress would be swift to mandate its creation.

Nevertheless, Congress feels that the current approach needs to be broadened, as indicated by its enactment of the Act. If the Treasury Department continues its support of the Baker Plan, Congress might promulgate supplemental legislation imposing more active policies in the form of mandates, rather than as mere directives. Therefore, Congress' concern for the need for a more aggressive approach should not be ignored by the Treasury Department if it intends to maintain its leadership role in international debt issues.

V. Current Developments

On March 10, 1989, Secretary Brady delivered a speech to the Brookings Institution and The Bretton Woods Committee Conference on third world debt[65] and, immediately thereafter,

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sued until its February due date, Secretary Brady's reaffirmation of the Baker Plan in the October meeting of World Bank and IMF should strongly suggest his commitment to the Baker Plan. Telephone Interview with Mary Chaves, International Debt Policy Office, Treasury Department (Oct. 13, 1988).

64. Even Representative John LaFalse of New York, who co-authored the Act, has since shown support for a recent proposal introduced by Japan. The "Miyazawa Plan", named after its author, Japan Finance Minister Kiichi Miyazawa, was presented in late October to the Joint Annual Meeting of the IMF and the World Bank in Berlin. It proposes splitting a debtor country's debt into two parts. One would be rescheduled, the other would be swapped for guaranteed bonds at a discount, which bonds would be guaranteed by a portion of the debtor country's own foreign currency to be held by the IMF. American Banker, Oct. 3, 1988, at 2; *see also* N.Y. Times, Oct. 5, 1988, at D2. If the Miyazawa Plan is implemented, the IDMA will no longer be necessary. Congressman LaFalse chided U.S. officials for ignoring Japan's proposal: "The Miyazawa Plan is a constructive and intelligent approach to helping heavily indebted countries to help themselves. . . . Ever since the Baker Plan was launched in Seoul, any proposal that even vaguely involved the notion of debt reduction has been ignored—until now." Wall Street Journal, Oct. 27, 1988, at A23. *Compare The International Economy*, Sept./Oct., 1988, at 100 (comparison of various proposed solution to international debt crisis).

65. Remarks by Nicholas F. Brady, Secretary of the Treasury, to the Brookings Institution and The Bretton Woods Committee Conference on Third World Debt, March 10, 1989 [hereinafter Remarks]. *See also* Department of the Treasury, First Report to the Congress Concerning World Bank Strategy and Lending Programs in

submitted to Congress the first interim report pursuant to section 3111(c) of the International Debt Management Act.[66] The report indicates that the Treasury Department still promotes the Baker Plan and has postponed serious efforts to create the IDMA. Of course, final determination will not be made until August when the final report is due.

In a statement accompanying the interim report, David C. Mulford, Assistant Secretary of the U.S. Treasury for International Affairs, stated that the approach urged in the report "builds upon the basic principles that guided international efforts in recent years. [The new approach] recognizes the continued vital importance of stronger growth, debtor reforms, external financial support, and a case-by-case approach to individual nations' problems."[67]

In his report, after recounting various successes of the Baker Plan, Secretary Brady admitted that there is still much to be accomplished in order to overcome the international debt crisis. Growth remains the primary objective. To attain it, the Treasury Secretary encouraged additional and more effective financial support from the commercial banks in the form of new lending and debt reduction. He also strongly suggested that the scope of alternatives be broadened in order to promote greater creditworthiness of the debtor nations. For example, he urged the increased the use of debt-equity swaps.[68] As creditworthiness improves, the report encourages new lending by the commercial banks.

Furthermore, the Treasury Department stresses the need for the IMF, the World Bank and other multilateral development banks to maintain an important, though indirect, role in debt reduction policies.[69] These institutions should facilitate debt reduction by financing collateralization through debt-for-bond exchanges[70] and replenishing reserves.

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66. *See supra* note 53 and accompanying text.

67. David C. Mulford, Assistant Secretary of the U.S. Treasury for International Affairs, Statement before the Subcommittee on International Finance and Monetary Policy, United States Senate, March 16, 1989.

68. *See* Remarks, *supra* note 58.

69. Secretary Brady stressed that "the negotiation of transactions will [should] remain in the market place — encouraged and supported but not managed by the international institutions." *Id.*

70. Of such transactions, Secretary Brady stated:

[Redirected financing] could be used to support debt for bond exchanges in-

The thrust of Secretary Brady's interim report centers on strengthening the foundation of the current strategy while expanding it to include debt reduction. Through a concerted effort by the parties involved, the Treasury Department predicts continued improvement. Therefore, with respect to creation of an International Debt Management Authority, Secretary Brady has postponed any further development pending implementation and success of the new remedial efforts.[71]

VI. Conclusion

The International Debt Management Act encourages creation of the International Debt Management Authority to supplement the Baker Plan's policy of increased lending with other forms of debt relief. However, it places the initial duties for creation of the IDMA on the Baker Plan's principal advocate, the U.S. Treasury Department. Therefore, implementation of the Act's policies may lie principally in the hands of the Secretary of Treasury, who has committed himself to continued adherence to the Baker Plan. Consequently, the Secretary may continue to pursue more conservative policies while nominally complying with the vague requirements in the statute.

However, the Secretary of Treasury should not ignore Congress' disenchantment with the Baker Plan, nor its implication that if broader policies are not adopted soon, stricter legislation may be forthcoming. Even congressional proponents of the Baker Plan currently appear to be less in favor of the plan itself than they are opposed to other alternatives presented thus far.[72]

> volving a significant discount on outstanding debt. They could also be used to replenish reserves following a cash buyback.
>
> Moreover, both institutions could offer new, additional financial support to collateralize a portion of interest payments for debt or debt service reduction transactions. By offering direct financial support for debt and debt service operations, the IMF and the World Bank could provide new incentives, which would act simultaneously to strengthen prospects for greater creditworthiness and to restore voluntary private financing in the future. This would lead to considerable improvements in the cash flow positions of the debtor countries.

Id.

71. Department of the Treasury, Interim Report to the Congress Concerning International Discussions on an International Debt Management Authority 7 (Mar. 1989).

72. Senator Jim Leach of Iowa, a noted supporter of the Baker Plan, feels that the Baker Plan's purpose was to buy time during which more effective approaches could be worked out to handle pressing situations, and this it has accomplished successfully. He maintains that conservatives in Congress were more opposed to the H.R. 3 version of the

Accordingly, though passage of the Act did not abrogate the Baker Plan, Congress' apparent readiness to pursue more active involvement in international debt issues should be seen by the Secretary as a warning of Congress' intent to broaden the scope of alternative solutions to the international debt crisis beyond merely increased lending to LDC's.

Douglas L. Hymas
Robert P. Doane, III

Act, which required strict compliance with its policies, than they are to the H.R. 4848 version, which allows for more flexibility. He believes that Baker Plan enthusiasts in Congress might now be prepared to give consent to more active approaches to the international debt problem, so long as they are sound and not simply reactionary. G. Parker, Telephone Conversation, Oct. 13, (1988) (Banking Committee representative for Senator Jim Leach of Iowa).