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In the Interest of Societal Development: Aligning Government and Business Interests to Address Foreign Debt

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I. Introduction

The literature around debt can be misleading. Statistics aggregate different types of debt, though funds owed to domestic versus foreign creditors have different implications for returns to the economy. Some reporting ignores financial sector debt while focusing on government debt, when both require analysis to understand a country's financial burdens. And sometimes reporting can appear overly complicated by statistics and figures as if deterring critical inquiry were its primary goal. But in simple terms, when it comes to foreign debt, it is not that future liabilities are inherently problematic, it is whether these liabilities successfully generate enough economic activity to enable their repayment.[1]

Today, foreign or external debt comprised of both government debt and individual debt owed to foreign creditors is overwhelmingly unsustainable.[2] Though some debt is incurred for sound growth strategy and not all debt indicates crisis; debt without corresponding assets, suggesting little prospect of repayment, is a problem which corrodes economies and societies over time. It makes recovery increasingly less likely and reduces funding for essential public services to address poverty and inequality.[3] The responsibilities of states to guarantee rights to their citizens; such as healthcare, welfare and education are "dependent on the sufficient allocation of state financial resources… but debt encumbrance [causes]… increasing poverty in

[1] Jubilee Debt Campaign, *The New Developing World Debt Crisis*, (2 November 2016), at 2.
[2] Tim Jones, *The New Debt Trap*, Jubilee Debt Campaign, (July 2015), at 15.
[3] International Monetary Fund, *Sovereign Debt Restructuring—Recent Developments and Implication for the Fund's* Legal and Policy Framework, (26 April 2013), at 15; and *Understanding the National Debt and Budget Deficit* , (2012), at 2:58, https://www.youtube.com/watch?v=3ugDU2qNcyg.

society" and deprives states and individuals of essential resources to promote and protect human rights.[4]

In a world where 8 people own about 17% of an estimated 256 trillion dollars in total global wealth- while another 17% is shared by 3.6 billion people, most individuals struggle to earn the necessary revenue to manage their livelihoods- let alone their debts.[5] Governments struggle too, both to facilitate economies that sell goods and services in order to generate enough earnings from its gross domestic product (GDP) and to tax earnings appropriately so that sufficient tax revenue can be devoted to debt management:[6] One way the extent of this struggle is monitored is through a measurement called the 'current account':

> This calculates the difference between what a whole country – both public and private sectors – spends on foreign goods and services, and what it earns from overseas. If it is spending more than it earns… a country covers the difference by borrowing from overseas…[which] allows more economic activity to take place now, at the cost of creating liabilities which must be repaid in the future.[7]

If debt were sustainable, it would be expected that the percentage of government revenue needed to fulfill a country's debt obligations would fall as investments funded by this debt generate income.[8] Instead, the proportion of debt obligations has increased in 43 low and middle-income countries from 2011- 2014 and calculations from International Monterey Fund (IMF) and the World Bank data predict further increases.[9]

This suggests that government revenue is not being efficiently generated to repay loans and interest but moreover it shows that the current framework for managing government debt

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[4] Vahan Bournazian, *The Impact of Economic Crisis and Foreign Debt on Human Rights*, Global Campus of Human Rights Research Programme, (2014-2015), at 2.
[5] Calculated from Camila Domonoske, *Gulf Between Richest and Poorest is Wider Than Previously Thought*, (2017), http://www.npr.org/sections/thetwo-way/2017/01/17/510271789/gulf-between-richest-and-poorest-is-wider-than-previously-thought-oxfam-says and Credit Sussie, *Global Wealth Report*, (2016), https://www.credit-suisse.com/ch/en/about-us/research/research-institute/global-wealth-report.html
[6] Silja Baller, et al., *The global competitiveness report*, (2016), http://reports.weforum.org/global-competitiveness-index/
[7] Jones, *supra* n. 2, at 6.
[8] *Id.* at 10.
[9] *Id.*

is unsustainable. Governments and individuals are often caught in a situation where they are borrowing to stimulate economic activity, but the investments supported by loans cannot enable their repayment. Without effective revenue strategy in place, there is no concrete path to escaping the debt trap: treading between financial need and financial obligation in a state of increasingly scarcer resources.

II. Foreign Lending and Debt Management Measures

Paradoxically, during the 2011-2014 period of an increasing percentage of debt obligations to government income ratio, IMF and the World Bank report GDP growth in low income and developing countries.[10] The average annual growth rate in GDP in these countries was 5.03%, more than two percentage points higher than the 3.68% average for the world.[11] But it is important to note that GDP growth is only the dollar value of economic output. Though presumably it is a viable indicator for debt sustainability, it does not itself indicate that enough revenue is spread throughout the private sector and to governments in order to alleviate their debt burdens. In fact, evidence that the benefits of GDP growth have instead spread unequally throughout economies dependent on international lending is more persuasive:

> Poverty is actually increasing in several…countries heavily dependent on foreign loans, despite high growth. For example, in Ethiopia the economy grew by 60% per person between 2005 and 2011, but the number of people living on less than $2 a day increased by 5.4 million.[12]

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[10] International Monetary Fund, *Macroeconomic Developments and Prospects in Low-Income Developing Countries: 2015*, (19 November 2015), at 1; and The World Bank, *GDP growth (annual %), GDP growth (annual %) | Data*, http://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?end=2014&start=2011 (last visited Feb 20, 2017).

[11] Calculated from The World Bank, *GDP growth (annual %), GDP growth (annual %) | Data*, http://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?end=2014&start=2011 (last visited Feb 20, 2017).

[12] Jones, *supra* n. 2, at 16.

One of the reasons for this is that conditions on borrowing from international lenders, like IMF and the World Bank, tend to exacerbate socioeconomic inequality.[13] Joseph E. Stiglitz, Nobel Laureate, former chief economist and senior vice-president at the World Bank, criticizes the set of policies that international lending institutions demand governments implement "reflecting the interests and ideology of the Western financial community".[14] In exchange for loans and the prospect of economic growth, countries are advised by international lending institutions to lower their corporate tax rate, reduce public spending, and soften labor protections.[15] In fact, "between 25 to 40 per cent of IMF programmes adopted until 2014 contained labour-related conditions relating to the public or the private sector."[16] While these measures may have addressed budget deficits, attracted new business operations, and allowed GDP growth to increase in some places, little benefit is being seen by poorer groups in society.[17] So, much to the dismay of the World Bank whose flagship goals are to "end extreme poverty… and boost shared prosperity;"[18] while the countries' most dependent on foreign lending have grown in GDP terms, "poverty and inequality have generally been increasing."[19]

Further, "it is not surprising that these countries, which are significantly dependent on foreign debt, have higher [GDP] growth rates, though this does not imply causation."[20] Even IMF itself is careful not to attribute GDP growth directly to foreign lending. In fact, for all

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[13] Joseph E. Stiglitz, Globalization and its Discontents, New York: WW Norton & Company, (2002).
[14] Joseph E. Stiglitz, Making globalization work: the next steps to global justice, Great Britain: Allen Lane: an imprint of the Penguin Group, (2007).
[15] Paul Krugman, *The austerity delusion*, The Guardian (29 April 2015), https://www.theguardian.com/business/ng-interactive/2015/apr/29/the-austerity-delusion
[16] United Nations, Human Rights Council, *Structural adjustment and labour rights*: report of the Independent Expert, A/HRC/34/57 (27 December 2016), at 5, available from undocs.org/A/HRC/34/57.
[17] Jones, *supra* n. 2, at 3.
[18] The World Bank, *About the World Bank*, (last visited 20 February 2017), http://www.worldbank.org/en/about
[19] Jones, *supra* n. 2, at 4.
[20] *Id.* at 16.

the statistics on debt and financial flow IMF collects, there is little reporting on the direct effects of their own lending. They do confirm that:

> [C]apital inflows to [low-income developing counties]…have grown sharply in recent years, augmenting domestic resources—but the usage of these resources, for consumption or investment, depends on national policy choices.[21]

Still, in spite of IMF's reporting language, which avoids conclusory misrepresentation, even this claim lacks accuracy. As mentioned above, policy autonomy of governments has more than on occasion been exchanged for funds from IMF and the World Bank and so the measure of these governments' economic stability or lack thereof, cannot be said to reflect national policy choices alone.

To that end, Human Rights Advocates echoes the findings of Independent Expert Mr. Juan Pablo Bohoslavsky in his latest report to the Human Rights Council.[22] The overwhelming strategy thus far to manage foreign debt has been counterproductive by persistently utilizing a tired arsenal of low corporate taxation and labor market deregulation in the misguided hope of stimulating economies.[23] Such policies do not promote long-term solvency, exacerbate inequality, and are counterproductive to debt relief and prevention agendas.[24] Policy which emphasizes corporate tax incentives and flexible labor regulation keep the workforce stagnant at their existing skill level, paygrade and socioeconomic status; stifles innovation, and causes governments to sacrifice needed potential revenue.[25] While revenue via GDP growth is what governments strategize to generate by borrowing funds and by implementing policy aimed at luring corporate investments, borrowing contingencies and contemporary financial policy

[21] IMF, *supra* n. 10.
[22] *Supra* n. 16, at 3.
[23] *Id.*
[24] Jones, *supra* n. 2, at 6.
[25] Esmé Berkhout, *Tax Battles: The dangerous global race to the bottom on corporate tax*, Oxfam Research, (December 2016), at 6.

instead block governments form collecting and redistributing the very revenue which would enable loan repayment.[26]

III. The Effect of Labor Deregulation on Inequality and Debt

There is a "mainstream assumption that labor rights are generally detrimental to economic development" by generating supposed monetary and productivity losses in spending toward compliance of workplace regulations, and in granting employees' time-off and livable wages.[27] The implication being that if employees could be forced to work indefinitely, if their pay were frozen at some minimum wage, and expenses did not have to be incurred toward working conditions; then businesses could be optimally successful. Subscribing to this belief in the past, "[t]he Organization for Economic Cooperation and Development (OECD), IMF and the World Bank have advocated that high labour protection standards are a driver of unemployment, among others, and should be scaled down."[28]

The Independent Expert notes that this belief has been challenged on theoretical and empirical levels- but the common use and negative consequences of such labor law reform is still readily apparent.[29] The "easing of labor market regulations is associated with [the contemporary phenomenon of] higher market inequality and income share of the top 10 percent… likely reflecting the fact that labor market flexibility benefits the rich and reduces the bargaining power of lower-income workers."[30] From a human rights perspective, the inequitable distribution of benefits and labor protections should be dismantled not only because it is unfair, self-perpetuating, and based on notions of equity constructed by and lobbied for by

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[26] *Id.*
[27] *Supra* n. 16, at 3.
[28] *Id.* at 15.
[29] *Supra* n. 16, at 3
[30] Era Dabla-Norris, *Causes and Consequences of Income Inequality: A Global Perspective*, International Monetary Fund Staff Note, (June 2015), at 26.

those who benefit from the disparity, but also because dismantling such inequality "would directly help create a more stable financial world." [31]

Intuitively, it can be understood why facilitating financial stability both for businesses and economies could not be achieved simply by cutting costs associated with labor protection. Stripped of labor rights, employee injury rates increase, competitors with marginally better work benefits poach laborers, and if the work offered is not a meaningful alternative to joblessness, employment will not be retained and economic output will not be stable:[32]

> [A] number of functions of labour law [have been identified] that render the economy efficient rather than encumbering it… [L]abour laws further economic coordination at both the company and market levels. In addition, laws regarding minimum wages or protection against dismissal tend to incentivize employers to utilize their workforce in an efficient manner, invest in technology and strive to improve their organization… In this regard, the role of labour legislation in correcting market failures is frequently acknowledged.[33]

Even taking into account that corporations are expected to lobby only for regulations which are in the interest of their own solvency, corporate and human rights interest can still be aligned. Wellbeing effects productivity, economic output, and market stability. This makes the promotion of labor protections good business decision-making and fiscally responsible.[34]

IV. The Effect of Contemporary Corporate Taxation on Income Inequality and Debt

In today's effort to stimulate economies, governments have entered into lending agreements contingent upon policy implementation detrimental to their economies. In addition to labor deregulation, a popular structural adjustment to manage countries' financial burdens is

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[31] Jones, *supra* n. 2, at 5.
[32] Sunil Ramlall, *Managing Employee Retention as a Strategy for Increasing Organizational Competitiveness*, 8 Applied H.R.M. Research 68, 68 (2003).
[33] *Supra* n. 16, at 15.
[34] John T. Addison & Barry T. Hirsch, *The Economic Effects of Employment Regulation: What are the Limits?*, Government Regulation of the Employment Relationship (1997) at 188–218.

the offering of tax incentives to corporate operations. But these tax incentives are undermining the very economic enrichment governments are seeking when attempting to lure local business development.[35]

Minimal corporate taxation as well labor market deregulation is central to many governments' growth strategies. They are either encouraged by lending institutions or persuaded that such deregulated and "tax-aggressive economies attract…businesses to invest or operate in a country. This doctrine is augmented by a powerful lobby that wields disproportionate influence over policy making to protect the interests of corporations" and as a result, there is an estimated $138 billion loss in potential tax revenue to governments from corporate tax incentives offered by developing countries.[36] The loss of this revenue cannot be afforded when governments are still struggling to repay their loans and further invest in the development of their societies.

Higher taxes on corporate wealth are needed to increase revenue and to mitigate accruing debts, yet "governments around the world are slashing corporate tax bills– damaging their own economies… in the process."[37] Governments are self- sabotaging as they utilize increasingly lowered corporate tax rates to compete with each other for localized business operations. In an effort to attract corporate resources and to overcome financial difficulty, countries become swept up in a rivalry to offer the most inexpensive price-tag for doing business.[38] "Globally, corporate tax rates have fallen from an average of 27.5 percent just ten years ago to 23.6 percent today and this process also shows signs of accelerating."[39] Corresponding to this fall in corporate tax rates, "net profits posted by the world's largest

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[35] Berkhout, *supra* n. 25, at 5.
[36] Berkhout, *supra* n. 25, at 3.
[37] *Id.* at 5
[38] *Id.*
[39] *Id.*

companies more than tripled in real terms, from $2 trillion in 1980 to $7.2 trillion by 2013."[40] At the same time increased corporate profits from tax cuts benefit shareholders and owners of corporations, there has been a further increasing gap between the rich and poor.[41] Yet there has been no decrease in the proportion of government revenue needed to fulfill low- and middle income country debt obligations.[42]

This indicates that low corporate taxation is not a sound revenue strategy to enable efficient loan repayment.[43] Corporate tax cuts do not effectively spread revenue to governments and individuals most burdened by debt. Instead, corporate owners and shareholders reap the benefits of low tax and little of that money is spent within the country of operation or given to laborers in the form of income.[44] While the high take-home benefits may attract investors, the economic activity generated is not a useful tool in debt relief unless the revenue from that activity is being spread to those with corresponding liabilities.

Moreover, tax rates are not the only factor corporations contemplate when choosing a place of business.[45] Corporations have a range of interests and government is one of the few entities in a position to incentivize and emphasize more mutually beneficial ones. According to the World Economic Forum's Global Competitiveness report, there are 16 factors which inhibit business interests to varying degrees in various countries. Any of the following could be improved by policy to make a country more attractive to investors: 1. Access to financing; 2. Foreign currency regulations; 3. Tax rates; 4. Inflation; 5. Inadequate supply of infrastructure;

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[40] *Id.* at 3.
[41] Economic Policy Institute, *CEO Pay Continues to Rise as Typical Workers are Paid Less,* (last visited 20 February 2016), http://www.epi.org/publication/ceo-pay-continues-to-rise/
[42] Jones, *supra* n. 2, at 10.
[43] *Id.*
[44] William Lazonick, Gautam Mukunda & Dominic Barton, *Profits Without Prosperity*, Harvard Business Review (12 November 2015), https://hbr.org/2014/09/profits-without-prosperity (last visited Feb 21, 2017
[45] *The global competitiveness report*, (2016), http://reports.weforum.org/global-competitiveness-index/ (last visited Feb 14, 2017).

6. Poor work ethic in national labor force; 7. Corruption; 8. Tax regulations; 9. Inefficient government bureaucracy; 10. Insufficient capacity to innovate; 11. Inadequately educated workforce; 12. Policy instability; 13. Crime and theft; 14. Government instability; 15. Poor public health; and 16. Restrictive labor regulations.[46] Right now financial policy reform concentrates heavily on "mitigating restrictive labor regulation" and "tax rates" in order to make a country a more attractive place for conducting business.[47] But there is no reason why reform could not align itself with human rights interests and work to mitigate "corruption" or "poor public health", for example, in order to attract new business.

Efforts to attract lucrative corporate ventures as revenue strategy for governments do not have to rely predominantly on offering tax incentives. In fact, there are no statically significant relationships between corporate tax rates and corporate investments.[48] As billionaire investor Warren Buffett explains:

> I have worked with investors for 60 years and I have yet to see anyone — not even when capital gains rates were 39.9 percent in 1976-77 — shy away from a sensible investment because of the tax rate on the potential gain. People invest to make money, and potential taxes have never scared them off.[49]

V. Shifting the Way Benefits of Financial Policy are Understood

There has been a marked effort to push "deregulation, downsizing the public sector and freezing or reducing… work-related social benefits in an effort to reduce government expenditure," as part of lending conditionality.[50] Tropes like "governments should operate like business and not spend more than they earn," became popularized in response to the 2008

[46] *Id.*
[47] Lazonick, et al., *supra* n. 44.
[48] *Recent Studies Find Raising Taxes on High-Income Households Would Not Harm the Economy*, (April 24, 2012), http://www.cbpp.org/research/recent-studies-find-raising-taxes-on-high-income-households-would-not-harmthe-economy
[49] Samantha Lewin, *Income Inequality and its Role in Sustainable Development*, Human Rights Advocates, (March 2016), http://www.humanrightsadvocates.org/wp-content/uploads/2016/03/CSW60-Income-Inequality-Report-1.pdf
[50] *Supra* n. 16, at 3.

global financial crises.[51] But the truth is businesses are not run that way.[52] Entrepreneurs do not wait 20 years until they have accumulated enough savings to promote and produce their innovations; they borrow from lenders who are later paid back by the revenue generated from sales.[53] The insistence on public sector budget cuts are based on the misguided assumption that minimizing government spending "will lead to economic growth and thus prevent or help overcome debt crises."[54] But minimizing spending is not a realistic answer to debt obligations when a meaningful design for increasing revenue is not in place.[55]

Further, public sector budget cuts not only lessen "the essential spending needed to reduce inequality,... poverty," and spread revenue responsively to debt obligations:[56] But evidence of their benefit is scarce and certainly do not demonstrate a necessary and non-discriminatory measure to "meet the economic needs of the country in a manner that fully protects" and complies with their core international human rights obligations.[57] Though making discerning spending choices can be an important aspect of managing debt, cutting funds toward government programs which hold the potential to mitigate inequality and poverty will not be the answer to a debt problem: a problem which is exacerbated by these very social issues. Similarly, continued labor deregulation may lure corporate operations by guaranteeing cheap labor, but ultimately the mistreatment of the workforce hurts a country's economy more than corporate enterprises have proven to help.[58] Instead governments should strategize to lure

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[51] John T. Harvey, *Why Government Should Not Be Run Like A Business Forbes* (5 October 2012), http://www.forbes.com/sites/johntharvey/2012/10/05/government-vs-business/#1095ed252685
[52] *Understanding the National Debt and Budget Deficit* , (2012), at 2:58, https://www.youtube.com/watch?v=3ugDU2qNcyg.
[53] *Id.*
[54] *Supra* n. 16, at 3.
[55] Krugman, *supra* n.15.
[56] Michael Quinlan, *The effects of non-standard forms of employment on worker health and safety,* in the Conditions of Work and Employment Series No. 67, (2015), at 4.
[57] *Supra* n. 16, at 9.
[58] Quinlan, *supra* n. 56 at 5.

business operations and investments from overseas through mutual interests- like a healthy, well-educated workforce.[59]

An example of how governments can emphasize policy which creates returns on mutual interests rather than serving interests which are predominantly corporate is through cuts to personal income tax. At no cost to corporations, governments could negotiate lower income tax rates for individual gains rather than corporate gains. This would benefit everyone in the workforce by allowing them to retain a larger portion of their earnings and would also work to increase the tax revenue stream to governments from the larger pool of corporate income. Another negotiated proposition could be to suggest lending institutions take a security interest in the corporate gains tax revenue of countries. This would incentivize governments to collect higher corporate tax so that lending institutions would receive faster returns on their loans. It would also incentivize a lobby from these institutions for higher corporate gains tax- a lobbying position missing prominence and power in the face of prevailing corporate, profit-seeking influence. The point being; that policy can be reimagined "to explicitly benefit the economy… and… can lead to investments that create jobs, improve worker health and thus productivity… spur important technological innovations," and address prevailing debt burdens.[60]

VI. Conclusion: Bridging Solvency and Human Rights Interests

Though"[d]ebt policies and debt management strategies designed and implemented by governments… rarely take into consideration [the] human rights implications" of financial

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[59] *Supra* n. 48.
[60] Isaac Shapiro & John Irons, *Regulation, employment, and the economy Fears of job loss are overblown*, EPI Briefing Paper, Economic Policy Institute (12 April 2011), http://www.epi.org/files/2011/BriefingPaper305.pdf

decision-making, there is much to be gained from rethinking this approach.[61] In 2015, IMF found and reported that progressive tax systems designed to redistribute wealth rather than feed corporate exceptionalism are one of the most effective ways for governments to reduce poverty and inequality as well as create sustainable growth.[62] In order to overcome debt burdens, it is in government's best economic interest to advocate for their workforce through policy and to redesign strategy for attracting corporate operations that emphasizes mutually beneficial interests. Policy should focus on better sharing and redistributing revenue generated by business development rather than subscribing to the trickle-down economics that promote subservience to corporate interests alone.

While financial deregulation and regressive corporate taxation may not inherently promote hierarchical income distribution, conflicts of financial and human rights interest, and de-emphasis of collaborative social development, at bottom, such measures make room for these impediments and need to be rethought. If instead financial policy were fashioned from a rights-based perspective, the advantages of business development could spread from their primary concentration in corporate prosperity to a better enrichment of government resources and a broad societal capability to prevent devastating financial crises and manage future liabilities effectively.[63]

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[61] United Nations, General Assembly, *Effects of Foreign Debt and other Related International Financial Obligations of States on the Full Enjoyment of all human rights*: Report of the Independent Expert, A/69/273 (7 August 2014), available from undocs.org/A/69/273.
[62] IMF Staff Report, *Fiscal Policy and Long-Term Growth*, IMF Policy Paper (2015).
[63] Berkhout, *supra n. 25,* at 6.

VII. Recommendations: Human Rights Advocates urges the Human Rights Council to:

A. Renew Independent Expert Mr. Juan Pablo Bohoslavsky's mandate and provide resources for him to:
   1. Further his research on financial policy and practice which incorporate a human rights based perspective;
   2. Develop strategies for monitoring and holding government's accountable to human rights considerations when transacting and negotiating with corporations;
   3. Liaison between international lending institutions like IMF and the World Bank and the United Nations to keep these institutions informed of the latest human rights research and the implication it has on lending policy and procedure.

B. To request of the General Assembly at its 72nd meeting session to address the IMF and World Bank about:
   1. The detriment of labor market deregulation lending contingencies;
   2. Clauses in their lending agreements to governments which contribute to the enrichment of the workforce without increasing risk of loan default. (i.e. income tax rate incentives rather than corporate incentives and security interests to lending institutions in corporate gains).

C. To urge State Parties to:
   1. Incorporate human rights data, dialogue, and standards into financial decision making;
   2. Work collaboratively with other governments to set floors for corporate incentivizing in order to prevent the undermining of economies by offering competitive and increasingly lower corporate tax incentives at the cost of much needed tax revenue.