

Michigan Journal of International Law

Volume 12 | Issue 4

1991

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Recommended Citation

Daniel D. Bradlow, *Debt, Development, and Human Rights: Lessons from South Africa*, 12 MICH. J. INT'L L. 647 (1991).

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DEBT, DEVELOPMENT, AND HUMAN RIGHTS: LESSONS FROM SOUTH AFRICA

*Daniel D. Bradlow**

INTRODUCTION

The debt crises of the 1980s have demonstrated that financial institutions are able to exert considerable influence over the social and economic policies of developing countries in financial distress. The International Monetary Fund (IMF) and the World Bank increased their influence over these countries by expanding the scope of the conditions attached to their financial support to include a broad range of economic and development issues.¹ Other official creditors have linked debt relief to the adoption of acceptable development policies.² Commercial bank creditors have used their leverage to force sovereign debtors to assume most of the costs associated with renegotiating their debt and, where applicable, to assume responsibility for private sector debt.³

While this situation is clearly a troubling challenge to the sover-

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1. There is extensive literature on this subject. For a discussion of the influence of these organizations in developing countries both prior to 1980 and thereafter, see generally R. FEINBERG, *BETWEEN TWO WORLDS: THE WORLD BANK'S NEXT DECADE* (Overseas Development Council Policy Perspectives No. 7, 1986); C. GWIN & R. FEINBERG, *THE INTERNATIONAL MONETARY FUND IN A MULTIPOLAR WORLD* (1989); C. PAYER, *THE DEBT TRAP: THE INTERNATIONAL MONETARY FUND AND THE THIRD WORLD* (1976); E. HUTCHFUL, *THE IMF AND GHANA: THE CONFIDENTIAL RECORD* (1987); R. BROAD, *UNEQUAL ALLIANCE: THE WORLD BANK, THE INTERNATIONAL MONETARY FUND AND THE PHILIPPINES* (1988); I.M.F. *CONDITIONALITY* (J. Williamson ed. 1983).

2. The Paris Club, the forum in which official debt is rescheduled, requires debtors to have an IMF approved adjustment program as a precondition to debt relief. See A. REIFFEL, *THE ROLE OF THE PARIS CLUB IN MANAGING DEBT PROBLEMS* (Essays in International Finance No. 161, 1985).

3. See generally H. GREEN, *THIRD WORLD DEBT RENEGOTIATION 1980-86 AND AFTER* (Institute of Departmental Studies, University of Sussex, Discussion Paper 223, 1986); UNITED NATIONS ECONOMIC COMMISSION FOR LATIN AMERICA CARIBBEAN, *TRANSNATIONAL BANK BEHAVIOUR AND THE INTERNATIONAL DEBT CRISIS* (1989); Mudge, *Restructuring Private and Public Sector Debt: Country Debt Structure*, 20 INT'L. LAW. 847 (1986); INTER-AMERICAN DEVELOPMENT BANK, *LATIN AMERICA SOVEREIGN DEBT MANAGEMENT: LEGAL AND REGULATORY ASPECTS* (R. Reisner, E. Cardenas, & A. Mendes eds. 1990).

eignty and freedom of action of the debtor countries, it does have some positive developmental consequences. Multilateral development organizations have recognized the need for greater participation by project beneficiaries in the design and implementation of sustainable development strategies.⁴ A few bilateral aid agencies have also acknowledged that sustainable development strategies must pay due regard to the human rights of a country's citizens.⁵ Even commercial banks have begun to contribute some of their debt to finance development projects.⁶

These lessons have not been lost on non-governmental human rights organizations, some of whom have argued that both official and commercial creditors should use their leverage to compel debtor governments that are particularly egregious violators of human rights to change their policies. The use of financial pressure for human rights purposes has been advocated against such countries as South Africa, Zaire, the Philippines, Turkey, Chile, Poland, Yugoslavia, Panama, Bolivia, Nicaragua, Guatemala, and Israel.⁷

It is easy to understand the attraction of using financial sanctions to achieve human rights gains in debtor countries. External creditors are already applying financial pressure to target countries and these creditors can be subjected to public pressure in their home countries. Official creditors can be held politically accountable for their actions and are therefore sensitive to charges that they provide financial support to governments which violate the human rights of their citizens.

4. See generally WORLD BANK, *WORLD DEVELOPMENT REPORT 1990* (1990); INTER-AMERICAN DEVELOPMENT BANK, *ECONOMIC AND SOCIAL PROGRESS IN LATIN AMERICA: 1990 REPORT* (1990).

5. Dutch, Norwegian and Canadian aid agencies have begun to build human rights and environmental criteria into their aid programs. See K. TOMASEVSKI, *DEVELOPMENT AID AND HUMAN RIGHTS* 50-56 (1989). See also *Donor Countries Linking Aid to Human Rights*, The Reuter Library Report, Dec. 5, 1990 (BC Cycle). On the linkage between development and human rights, see, for example, Stewart, *Basic Needs Strategies, Human Rights, and the Right to Development*, 11 HUM. RTS. Q. 347 (1989). The United States uses denial of aid to combat extreme human rights abuses. 22 U.S.C. § 2151n(a) states that the United States may not provide any assistance to "any country which engages in a consistent pattern of gross violations of internationally recognized human rights." 22 U.S.C. § 2151n(a) (1990).

6. See Burton, *Debt for Development: A New Opportunity for Nonprofits, Commercial Banks, and Developing States*, 31 HARV. INT'L. L. J. 233 (1990); Gibson & Curtis, *A Debt for Nature Blueprint*, 28 COLUM. J. TRANSNAT'L. L. 331 (1990); Comment, *The Debt-for-Nature Swap: A Long Term Investment for the Economic Stability of Less Developed Countries*, 24 INT'L. LAW. 1071 (1990).

7. See J. CAVANAGH, F. CHERU, C. COLLINS, C. DUNCAN & D. NTUBE, *FROM DEBT TO DEVELOPMENT* (1985) (suggesting that renegotiation of South African, Zairian, and Filipino debt be linked to human rights improvements); G. HUFBAUER, J. SCHOTT, & K. ELLIOT, *ECONOMIC SANCTIONS RECONSIDERED: HISTORY AND CURRENT POLICY* (2d ed. 1990). On sanctions generally, see B. CARTER, *INTERNATIONAL ECONOMIC SANCTIONS: IMPROVING THE HAPHAZARD U.S. LEGAL REGIME* (1988); M. MALLOY, *ECONOMIC SANCTIONS AND U.S. TRADE* (1990).

Commercial creditors are vulnerable to pressure from shareholders and consumer groups. While this pressure may not stop commercial banks from rescheduling outstanding debts, banks are unlikely to provide new credits to countries that are the targets of concerted public campaigns.

Financial sanctions, however, are a blunt policy instrument. They cannot easily be structured to affect only those elements of the target society that are the perpetrators of the human rights violations. A determined government and its allies can redirect financial resources so that the sanctions disproportionately affect the poor and powerless sections of the target society.⁸ Thus, the socioeconomic consequences of even a successful sanctions campaign may be to so weaken the sanctions' intended beneficiaries that they are unable to translate their victory into sustainable political and socioeconomic advances.

This suggests that if financial sanctions are to be used for human rights purposes, they must be viewed as part of an overall development assistance strategy that is designed to help improve the social, economic, and political conditions in which the poorest and weakest elements of the target society live.⁹ The possibility of developing such a strategy depends both on coordinating the punitive and developmental aspects of the sanctions and on establishing a means for identifying appropriate development activities and development financing mechanisms. In this context, "appropriate development" means development activities that are consistent with international human rights standards, that are environmentally, financially, and managerially sustainable, and that involve the beneficiaries in the design, implementation, and management of the development activity.¹⁰

This paper, through a case study of financial sanctions against South Africa, demonstrates that it is possible to design a development-oriented financial sanctions strategy against any country that violates the human rights of its citizens and in which government regulations, including exchange controls, result in foreign-owned financial assets

8. In most debtor countries the poor have suffered most from the debt crisis and attempts to deal with it. This has been reflected in infant mortality rates, nutrition standards, minimum wages, employment rates, education, and income distribution. See 1 ADJUSTMENT WITH A HUMAN FACE (G. Cornia, R. Jolly, & F. Stewart eds. 1987); INTER-AMERICAN DEVELOPMENT BANK, *supra* note 4, at 25-27.

9. In principle this can be achieved by linking sanctions to an aid program once the sanctions have produced the desired policy change in the target country. However, this strategy will not minimize suffering during the period in which sanctions are in force, nor will it help the future beneficiaries benefit from any development opportunities that arise while the sanctions are in force.

10. For a detailed discussion of the elements of this definition, see *infra* notes 129-51 and accompanying text.

being trapped in the target country. This strategy will both deprive the perpetrators of the human rights violations of new funds and will help redirect the blocked funds into activities that are designed to promote the political and socioeconomic development of the victims of the human rights abuses. The means for identifying appropriate development activities used in this strategy can also be used to test the human rights and developmental appropriateness of development projects that are not part of a sanctions campaign.

The South African case is particularly interesting because, based on recent developments in South Africa,¹¹ it appears to be an example of a successful financial sanctions strategy. In fact, the strategy of using South Africa's debt problems to promote change in the country cannot be considered a successful human rights campaign. Even though the South African Government (SAG) has been weakened by financial pressure, it has been able to renegotiate the country's debt without having any human rights or development conditions incorporated into its renegotiated financial arrangements.¹² In addition, the victims of apartheid have borne the brunt of the debt burden without being able to take advantage of the development financing opportunities created by the country's debt situation. The result is that, while the financial pressure on the SAG has been alleviated, the social and economic situation of the majority of South Africans has deteriorated.¹³

After a brief description of the country's political economy, this paper will analyze the evolution of the South African debt crisis and

11. Since June 1989, the South African Government has lifted the ban on the African National Congress (ANC) and other political organizations, released Nelson Mandela and many but not all political prisoners, allowed the return of some exiles, and taken the first steps towards negotiating a new democratic constitution for South Africa with the ANC. The government has also acknowledged that the country faces serious socioeconomic problems that cannot be solved as long as the apartheid system remains in place, and that the country is suffering from its relative exclusion from the international economy and international capital markets. See *After Apartheid, A Survey of South Africa*, THE ECONOMIST, Nov. 3, 1991. In February 1991, the South African Government announced that it would repeal the statutory foundations of apartheid: the Group Areas Act, the Land Acts, and the Population Registration Act. See Wren, *South Africa Moves to Scrap Apartheid*, N.Y. Times, Feb. 2, 1991, at 1, col. 1. The South African Parliament repealed the Group Areas and 1913 and 1936 Land Acts on June 5, 1991, see Wren, *New York Times*, June 6, 1991, at A3, col. 4, and the Population Registration Act on June 17, 1991. See Wren, *South Africa Scraps Law Defining People by Race*, N.Y. Times, June 18, 1991, at A1, col. 3.

12. The terms of the three Interim Arrangements negotiated between the SAG and the country's creditors are discussed *infra* notes 68-114 and accompanying text. For information on the First Interim Arrangement, see *infra* notes 68-73 and accompanying text; on the Second Interim Arrangement, see *infra* notes 74-91 and accompanying text; on the Third Interim Arrangement, see *infra* note 114 and accompanying text.

13. See discussion of South Africa's political economy *infra* notes 14-32 and accompanying text.

financial sanctions against South Africa. Then the paper will describe an alternate sanctions strategy that, if implemented, would have both maintained financial pressure on the SAG and provided financial assistance to qualifying development projects in the country. This alternate strategy includes both criteria for identifying such projects and a proposal for a development financing mechanism. It is important to note that even though sanctions against South Africa are being lifted, creditors still have financial assets trapped in South Africa that can be used to fund the developmental aspects of this strategy.

SOUTH AFRICA'S POLITICAL ECONOMY

The South African economy, like that of many developing countries, is characterized by substantial government participation in the economy and heavy regulation of private economic activity.¹⁴ The result in South Africa is an economy which creates wealth and economic power for a small elite, and poverty for the majority.¹⁵ Governmental control over the economy also distorts development by limiting the opportunities and the incentives for non-governmental development initiatives.¹⁶

A 1986 U.S. Department of Commerce report described South Africa as "a chronic debtor, import-starved, ridden with ethnic divisions, a repressive regime . . . whose only leverage is its ability to manipulate foreign governments and attract international attention."¹⁷ The report adds that even before sanctions, South Africa was a difficult place for

14. See, e.g., H. DE SOTO, *THE OTHER PATH* (1990) (discussing the inhibition of non-governmental initiatives in Peru); S. GEORGE, *A FATE WORSE THAN DEBT* (1988) (discussing the socioeconomic effect of development policies in Morocco, Zaire, and Latin America.) On South Africa's political economy, see generally S. LEWIS, *THE ECONOMICS OF APARTHEID* (1990); A. STADLER, *THE POLITICAL ECONOMY OF MODERN SOUTH AFRICA* (1987); *THE POLITICAL ECONOMY OF SOUTH AFRICA* (N. Natrass & E. Ardington eds. 1990); J. SAUL AND S. GELB, *THE CRISIS IN SOUTH AFRICA: CLASS DEFENSE, CLASS REVOLUTION* (2d ed. 1986); J. Knight, *A Comparative Analysis of South Africa as a Semi-Industrialized Developing Country*, 26 *J. MOD. AFR. STUDIES* 473 (1988).

15. In 1983, white South Africans had an annual disposable income per capita of R6,242, urban Africans had an income of R1,366, and rural Africans' income was R388. In 1980, it was estimated that about 50% of South Africans lived below subsistence levels. See F. WILSON & M. RAMPHELE, *UPROOTING POVERTY: THE SOUTH AFRICAN CHALLENGE* 17-20 (Report for the Second Carnegie Inquiry into Poverty and Development in South Africa, 1989); SOUTH AFRICAN INSTITUTE OF RACE RELATIONS, *RACE RELATIONS SURVEY 1987/88* (1988). Tito Mboweni, head of the African National Congress' economic policy department, estimates 5% of South Africa's population owns more than 88% of the personal wealth. Mboweni, *ANC Calls for Business Partnership*, *EUROMONEY*, Feb. 1991, at 69.

16. See sources cited *supra* note 14. The term "non-governmental" refers to both private commercial activities and all other development activities that are not initiated and controlled by the government and its instrumentalities.

17. Parks, *S. Africa Irked as U.S. Sees Troubled Business Climate*, *Los Angeles Times*, Oct. 24, 1986, at 13, col. 4, 16, col. 2.

U.S. companies to do business because of excessive government control of the economy and regulation of business activity.¹⁸

The South African development strategy, which is based on the government's apartheid ideology, has led to an irrational and inequitable allocation of resources.¹⁹ The country's white population has a surplus of 37,000 houses while the black population suffers from a growing housing shortage that in 1987 was between 700,000 and 1.4 million units and was expected to reach 2 million units in 1990.²⁰ In fact, the situation is so serious that there are now 7 million shanty dwellers and seventy percent of urban blacks have inadequate access to clean water and electricity.²¹

In the last decade over 190 white schools have been closed due to inadequate attendance, while black students are forced to attend overcrowded "black" schools and over 1 million children are unable to attend school at all.²² This educational crisis has resulted in an economy that suffers from both an unemployment rate of at least thirty percent²³ and a shortage of about 100,000 to 150,000 skilled artisans,

18. *Id.*

19. The South African Chamber of Business estimates the cost of remedying the racial inequities caused by apartheid to be R52 billion and a leading South African economist has estimated the costs to be between R20 billion and R30 billion per year over the next decade. Chester, *The Soaring Cost of Killing Apartheid*, *The Star*, Feb. 20, 1991, at 13; *Apartheid Barometer*, *The Weekly Mail* (Johannesburg, South Africa), Feb. 15-21, 1991, at 4. See also Savage, *The Cost of Apartheid*, 9 *THIRD WORLD Q.* 601 (1987). Wilson & Rampehele, commenting on the policies of the South African government, state that "these policies of separate development, anti-urbanization, forced removals, Bantu education, the crushing of organizations, and in more recent years, destabilization have been directly responsible for increased poverty amongst millions of people. Indeed it is precisely this dimension of premeditation or deliberate policy in impoverishing people that makes poverty in South Africa different from that in so many other parts of the world." F. WILSON & M. RAMPEHELE, *supra* note 15, at 230.

20. See SOUTH AFRICAN INSTITUTE OF RACE RELATIONS, *supra* note 13, at 198; Wren, *Bulldozers Visit a Township, Followed by Misery*, *N.Y. Times*, July 16, 1990, at A4, col. 2; Cowell, *For South African Squatters, Life Just Gets Harder*, *N.Y. Times*, Aug. 14, 1990, at A2, col. 1.

21. Sparks, *South African Population Shift Seen Fostering Urban Squalor*, *Washington Post*, July 23, 1990, at A1 (discussing shanty dwellers); F. WILSON & M. RAMPEHELE, *supra* note 15, at 144-51 (discussing access to water and electricity).

22. P. Molefe, *'Apartheid Education' Flounders to Another Year*, *The Weekly Mail* (Johannesburg, South Africa), Dec. 21, 1989 - Jan. 18, 1990, at 16. In 1990 the government did begin to address this issue by allowing white schools to admit black students, provided over 70% of white parents agree and there are vacancies in the school. See Wren, *South Africa Integrates Some Schools*, *N.Y. Times*, Jan. 10, 1990, at A3, col. 1; Kraft, *Dozen of White Schools Open Doors to Blacks*, *Los Angeles Times*, Jan. 10, 1991, at A4, col. 1.

23. According to the South African Institute for Race Relations in 1988, some experts estimate total African unemployment to be between 5.5 and 6.1 million persons and in some rural areas the unemployment rate is 50%. SOUTH AFRICAN INSTITUTE FOR RACE RELATIONS, *supra* note 15, at 293-95. It also states that the Congress of South African Trade Union claims the unemployment rate for women is three times that for men. *Id.* at 295. The general unemployment rate for black workers is now estimated to be at least 40%. See Rumney, *A Tiny Flicker of Light Amid the Gloom*, *The Weekly Mail* (Johannesburg, South Africa), Dec. 20, 1990 - Jan. 10, 1991, at 22.

about 212,00 management personnel, and about 200,000 people with technical skills.²⁴ "Black" hospitals have an occupancy rate of over 100%, while "white" hospital wards are closed for lack of demand.²⁵ Despite these conditions, in its fiscal year 1991 budget, the government allocated about fifty percent of its funds to the implementation of apartheid, including multiple departments of health, education, housing, and welfare, and to the State's security apparatus.²⁶ The fiscal year 1992 budget, despite a fifteen percent per annum inflation rate, provides for a sixteen and one-tenth percent increase in spending on education, an eight and nine-tenths percent increase in the health budget, and a fifty-three percent increase in the police budget.²⁷

The inefficiency of the government's development strategy is also demonstrated by the resources it expends to reward its supporters. The government spends about R700 billion per annum²⁸ to subsidize private firms that are willing to invest in locations that the government selects according to the dictates of apartheid rather than considerations of economic efficiency. A recent study shows that nearly seventy-four percent of the recipient firms are unprofitable.²⁹

The government continues to provide substantial financial support to white farmers. About ninety percent of all agricultural production is subject to government controls that affect both production and distribution. The degree of inefficiency of these policies allows the destruction of surplus agricultural products in some areas of the country, while in other areas of the country people experience serious food shortages.³⁰

24. Nel, *Inevitabilities of Change*, in THE SOUTH AFRICAN POLICY FORUM 31 (Third Conference, Aspen Institute, Apr. 12-15, 1990).

25. In the first half of the 1980s, black South Africans had an infant mortality rate (94-124 per 1000 live births) that was worse than those of such African countries as Kenya (76), Congo (77), and Zambia (84) and on a par with that of Burundi (119), while the rate for white South Africans (12) compared favorably with that of the United States. F. WILSON & M. RAMPHELE, *supra* note 15, at 107-08. Recently the government has begun to integrate hospitals.

26. Fabricius, *Barend Keeps Tight Rein on Purse Strings*, The Star, Mar. 21, 1990, at 12, col. 1.

27. *At A Glance*, The Star, Mar. 27, 1991, at 13.

28. Between 1986 and February 1990, the Rand-United States dollar exchange rate fluctuated between R2.03 to a \$1 and R2.78 to a \$1. See S. AFR. RESERVE BANK Q. BULL., Mar. 1990, at S-81. Prior to 1982, the exchange rate fluctuated between \$1.5 to R1 and \$1 to R1. R. BETHLEHEM, *ECONOMICS IN A REVOLUTIONARY SOCIETY: SANCTIONS AND THE TRANSFORMATION OF SOUTH AFRICA* 126 (1988).

29. The information in this paragraph is drawn from Waldmeir, *Survey on South Africa: Dumping Grounds of Apartheid*, The Financial Times, June 11, 1990, at IV.

30. Gawith, *Survey of South Africa: Difficulties Ahead—Agriculture*, The Financial Times, June 11, 1990, at VII.

This brief description of South Africa's political economy³¹ demonstrates that apartheid is a developmental as well as a human rights tragedy. In 1985, when the country's debt crisis erupted, the trade unions, community organizations, and democratic organizations in the country were all trying, on both a political and socioeconomic level, to address the country's development crisis.³² However, their efforts were constrained by the political situation in the country and by a lack of financial resources and technical skills.

The debt crisis, by trapping South Africa's creditors' assets in the country, offered an opportunity for resolving the country's development and political crises. We now turn to a consideration of how the crisis arose and was handled.

BACKGROUND ON THE SOUTH AFRICAN DEBT CRISIS

During the 1970s and 1980s, South Africa significantly increased its reliance on external debt to finance economic growth.³³ This development was particularly pronounced during the first half of the 1980s. Between 1980 and 1984, South Africa's total debt increased from \$16.9 billion (R12.66 billion, equal to twenty percent of GDP) to \$24.3 billion (R48.2 billion, equal to forty-six percent of GDP).³⁴ The growth in short term debt was even more dramatic. Short term debt as a portion of total debt increased from forty-nine percent in 1980 to over sixty-six percent by the end of 1984.³⁵ Even though the dollar value of South Africa's debt declined throughout the first half of 1985, adverse currency fluctuations meant that in Rand terms the debt burden increased.³⁶ By August 1985 the total external debt was equal to about fifty percent of GDP and most of this debt was short term, that

31. For more detailed information, see sources cited *supra* note 14, and F. WILSON & M. RAMPHELE, *supra* note 15.

32. F. WILSON & M. RAMPHELE, *supra* note 15, at 275-97. See also M. SINCLAIR, HOPE AT LAST: A GUIDE TO GRANTMAKING IN SOUTH AFRICA (1990). For a discussion of the development of the South Africa trade union movement, see S. FRIEDMAN, BUILDING TOMORROW TODAY: AFRICAN WORKERS IN TRADE UNIONS (1987).

33. S. LEWIS, *supra* note 14, at 65. In 1956 equity investments represented 75% of total foreign investment, but by the mid-1980s debt, particularly short-term debt, was the major form of external financing.

34. Hirsch, *Sanctions, Loans and the South African Economy*, in SANCTIONS AGAINST APARTHEID 27 (M. Orkin ed. 1989).

35. *Id.*; Harris, *South Africa's External Debt Crisis*, 8 THIRD WORLD Q. 807 (1986); Padayachee, *Private International Banks, The Debt Crisis and the Apartheid State*, 87 AFR. AFF. 367 (1988); Grant, *The Banks Abandon South Africa*, EUROMONEY, Dec. 1985, at 68. See generally G. HUFBAUER, J. SCHOTT, & K. ELLIOT, *supra* note 7, at 221-35.

36. By August 1985 South Africa's total external debt was \$23.9 billion. J. LIND AND D. ESPALDON, SOUTH AFRICA'S DEBT AT THE TIME OF CRISIS 1 (1986). This was equal to about R50 billion. Hirsch, *supra* note 34, at 272-73.

is, with a maturity of less than one year.³⁷

The increase in borrowing was partly due to a substantial shift in the direction of South African capital flows. In 1982 there had been a net inflow of R3.2 billion per annum. In the eighteen months prior to August 1985, there was a net outflow of R5.6 billion.³⁸ It is estimated that there was a net capital loss in the first half of the 1980s of between R20 and R30 billion.³⁹ This capital flight is attributable to a number of factors, including loss of confidence in the political leadership of the country and in the future of the economy, and to deregulation of the financial markets, which made it possible for South Africans to send their capital abroad.⁴⁰

Another significant cause of the increase in debt was the SAG's response to the recession experienced by the country when the price of gold began its steep descent from its 1980 peak of \$800 an ounce.⁴¹ By November 1982, the recession was severe enough that the SAG was forced to draw on the financial support of the International Monetary Fund.⁴²

In 1983, in an effort to deal with rising inflation and a deteriorating balance of payments position, the SAG deregulated the foreign exchange markets and allowed the Rand to float. It also allowed domestic interest rates to increase sharply, creating a substantial differential between domestic and international interest rates, and implemented measures designed to assist international traders and borrowers in hedging their exchange risks.⁴³ These actions made foreign financing so attractive that some South African commercial banks began to borrow in the short-term interbank market to fund medium term credits to South African public and private sector borrowers. They were counting on the large interest rate differential between their international borrowing and domestic lending rates to cover the costs of these risky operations.

The ease with which South African borrowers were able to obtain funds is surprising and raises questions about the prudence of the

37. Hirsch, *supra* note 34, at 272-73; Padayachee, *supra* note 35, at 371-74.

38. Martin, *The South African Credit Crisis of 1985*, 4 *TRANSAFRICA F.* 17, 21 (1986). See generally S. AFR. RESERVE BANK Q. BULL., *supra* note 28, at S-65.

39. See Martin, *supra* note 38.

40. See S. LEWIS, *supra* note 14, at 154.

41. For an analysis of these policies, see J. SAUL & S. GELB, *supra* note 14, at 22-32; Innes, *Monetarism and the South African Crisis*, 3 S. AFR. REV. 290 (1986).

42. Morell, *A Billion Dollars for South Africa*, INT'L POL'Y REP., Apr. 1983, at 1-3.

43. The interest rate differential could be as much as 10-12%. The exchange rate hedges involved the sale of foreign exchange for future delivery on terms that placed the risk of currency fluctuations on the SAG. See Padayachee, *supra* note 35, at 365.

banks' actions in South Africa⁴⁴ The heaviest borrowing activity occurred in 1983-84, after the onset of the debt crises that the banks faced with their Latin American and Eastern European borrowers. It also occurred at a time when the South African economy was stagnating and per capita income was falling.⁴⁵

Under these circumstances, it is difficult to understand the attraction of South African borrowers to the banks. This difficulty is compounded by the fact that South Africa, unlike most countries to which commercial banks extended credit, was, in effect, cut off from IMF financial support and policy advice. The IMF's 1982 decision to give financial support to South Africa had proven to be very contentious. A number of the Fund's executive directors and staff opposed the financing, arguing *inter alia* that South Africa was being given unduly favorable treatment.⁴⁶

The IMF's action led the U.S. Congress to adopt legislation instructing the U.S. Executive Director to "actively oppose" any use of IMF funds to assist South Africa because "the practice of apartheid results in severe constraints on labor and capital mobility and other highly inefficient labor and capital supply rigidities which contribute to balance of payments deficits in direct contradiction to the goals of the International Monetary Fund."⁴⁷ The banks, South Africa, and the IMF recognized that without U.S. support, there was no real possibility of the IMF providing financial support to South Africa.

The banks also based their decision to lend to South African borrowers on a flawed assessment of the country's ability to manage its debt. When the SAG deregulated the foreign exchange markets, it did not replace its previous regulatory scheme with any mechanism for prudent management of the country's external debt. Consequently, it had incomplete knowledge of the size or repayment schedule of the country's debt. In fact, by late 1984, banks were beginning to express concern about the country's ability to service its 1985-86 debt obligations. In March 1985 Citibank observed: "South Africa's external fi-

44. The borrowers were predominantly private corporations. The sanctions campaign made it difficult, but not impossible, for the public sector to directly raise funds in international markets. *Id.* at 366. For a general description of the sanctions campaign's effect on loans to South Africa, see J. HANLON & R. OMOND, *THE SANCTIONS HANDBOOK* 333-34 (1987).

45. Padayachee, *supra* note 35, at 365, 370. Hirsch, *supra* note 34, at 271.

46. South Africa was allowed to obtain most of the financing from the IMF's low-conditionality Compensatory Financing Facility at a time when most debtor countries were adopting austerity programs as a result of the IMF's stringent conditionalities. See Morrell, *supra* note 42, at 2.

47. 22 U.S.C. § 286aa (1988). For a general discussion of the debate over IMF support for South Africa, see Morrell, *A Victory Over Apartheid*, *INT'L POL'Y REP.*, April 1984, at 1-9.

nances are in total chaos."⁴⁸ It went on to state that the South African Reserve Bank had paid "no regard whatsoever . . . to the maturity structure of the debt."⁴⁹ Citibank concluded that "it is difficult to see how debt refinancing on the scale required . . . can possibly be achieved."⁵⁰

These growing financial problems were compounded by the political situation in the country and by a foreign reserve crisis caused by the collapsing value of the Rand. In order to protect the Rand, which had fallen in value from about eighty-eight cents to the dollar to about forty cents, the Reserve Bank had used up most of its reserves and had entered into a number of gold swap arrangements. The result was that foreign reserves were declining as debt payments were falling due.⁵¹

In mid-1985 South Africa's political and financial difficulties reached a crisis point. Its economy was experiencing the worst recession since the 1930s, and it was facing the most sustained period of political protest in the country's history.⁵² On July 20, in response to these developments, the government imposed a state of emergency, the first since the time of the Sharpeville massacre in 1960. Over the next week, the market value of the Johannesburg Stock Exchange dropped R11 billion; this was caused largely by selling by American, French, and British investors. The French government announced restrictions on French investments in South Africa, thereby giving official support to the international divestment campaign, and on July 31 Chase Manhattan Bank announced that it would not extend any new credits to South African borrowers nor would it roll over short term loans that were to fall due in late August. This announcement was quickly followed by a similar announcement from Security Pacific Bank. It soon became clear that other banks intended to take like action.⁵³

At the time, about eighty-five percent of U.S. bank exposure to South Africa, fifty-seven percent of U.K. bank credits to South Africa, and thirty-one percent of German credits were short term.⁵⁴ Since there was a "bunching" of debt payments falling due in the second

48. Hirsch, *supra* note 34, at 273.

49. *Id.*

50. *Id.*

51. See sources cited *supra* notes 34-35.

52. See sources cited *supra* notes 34-35. The following discussion of the unfolding of the South African debt crisis are based on these sources. For a chronology of the South African debt crisis, see G. HUFBAUER, J. SCHOTT, & K. ELLIOT, *supra* note 7, at 221-35.

53. Chase Manhattan was not the first bank to take such action but it was the first to do so publicly. Its actions had particular significance because of the influence that Chase Manhattan, as a money center bank, has with other banks. G. HUFBAUER, J. SCHOTT, & K. ELLIOT, *supra* note 7, at 223.

54. Hirsch, *supra* note 34, at 274.

half of 1985, it was obvious that if all these banks refused to roll over their debts as they fell due, South African borrowers would be unable to meet their obligations.⁵⁵

The situation was exacerbated by President Botha's "Rubicon" speech to the Party Congress in mid-August. Prior to this speech, the government had let it be known that the President was going to announce major reforms.⁵⁶ President Botha stated that the country had "crossed the Rubicon" on the road to reform, but that he would set the pace and choose the terms.⁵⁷ He ruled out political power sharing and blamed "barbaric communist agitators" for the social unrest in the country.⁵⁸

The reaction to the speech was dramatic. It was followed by a twenty percent drop in the value of the Rand and a substantial capital outflow. By August 27, the situation was critical and the SAG was forced to close the foreign exchange and stock markets. Before allowing the markets to reopen on September 2, the SAG announced that it was:⁵⁹

- (a) declaring a four month moratorium on the repayment of \$10 billion of payments falling due on short term debt, primarily interbank debt. Foreign government-guaranteed debts, trade credits, Eurobonds, and IMF funds were excluded from the moratorium; and
- (b) reintroducing the two tier currency, with the financial rand being reintroduced for the purpose of limiting outflows

55. For a detailed analysis of South Africa's debt profile at this time, see J. LIND & D. ESPALDON, *supra* note 36.

56. See R. BETHLEHEM, *supra* note 28, at 71-73. It has been suggested that a draft of the speech was shown to senior United States and British officials before it received cabinet approval. The cabinet subsequently insisted on major changes. *Id.*

57. The tone of President Botha's speech and his general understanding of the situation in the country are evident from the following quote from the speech,

But let me be quite frank with you. You must know where you stand with me. . . . I am not prepared to lead White South Africans and other minority groups on a road of abdication and suicide. Destroy White South Africa and our influence, and this country will drift into factional strife, chaos, and poverty. . . . We have never given in to outside demands and we are not going to do so. South Africa's problems will be solved by South Africans and not by foreigners. We are not going to be deterred from doing what we think best, nor will we be forced into doing what we don't want to do. The tragedy is that hostile pressure and agitation from abroad have acted as an encouragement to the militant revolutionaries in South Africa to continue with their violence and intimidation. They have derived comfort and succor from this pressure.

R. BETHLEHEM, *supra* note 28, at 72.

58. See G. HUFBAUER, J. SCHOTT & K. ELLIOT, *supra* note 7, at 223. See also Hirsch, *supra* note 34, at 274; Grant, *supra* note 35, at 69.

59. Proclamation R 157/1985, as issued by the State President of South Africa, Gov't Gazette Sept. 1, 1985, at 9926. These measures were eventually extended until March 31, 1986. See G.N.R 2868/1986, in Gov't Gazette Feb. 23, 1985 at 10054. The statutes are analyzed in Du Plessis, *South Africa's Foreign Debt Moratorium*, 8 MOD. BUSINESSMAN'S L. 24, 28 (1986).

through the capital account of the balance of payments.⁶⁰

The Government Proclamation specifically excludes from the scope of the moratorium debts of the SAG and debts owed to or guaranteed by other governments. The moratorium was, therefore, limited to debt owed by the South African private sector to private lenders.⁶¹ This meant that at the time of the initial debt negotiations the SAG was not legally responsible for the debt and was only seeking to establish an orderly repayment mechanism for private borrowers.⁶² It also meant that South Africa would not have to approach the Paris Club to renegotiate its official debt.⁶³ Thus, South Africa could not be subjected to official creditor pressure.

The banks' response to the SAG's action was to set up a committee of twenty-nine banks to represent the country's 233 bank creditors.⁶⁴ This committee negotiated with South Africa through a mediator.⁶⁵

The banks were aware of the political sensitivity of the South African debt negotiations. In the early stages of the crisis they appeared to be requiring the SAG to satisfy certain political demands as a precondition to a successful debt renegotiation. The preconditions were based on demands of the anti-apartheid movement, such as the release of key political prisoners and the lifting of the state of emergency.⁶⁶ In the end, a new one year debt arrangement was concluded in March 1986 without the SAG satisfying any of these political conditions.⁶⁷

THE FIRST INTERIM ARRANGEMENT

The terms of the First Interim Arrangement were that the SAG would make available sufficient foreign exchange to repay five percent (\$500 million) of the principal of the debt over the one year life of the

60. The two tier market consists of a Commercial Rand which is used for current transactions and a Financial Rand which trades at a discount to the Commercial Rand and is used only in capital account transactions. For a detailed description of the two-tier currency market, see The Bank of Lisbon and South Africa Limited, *The Financial Rand Market*, in *THE MECHANICS OF THE SOUTH AFRICAN FINANCIAL SYSTEM* 339-48 (3d ed. 1989).

61. The crisis was a serious one for the banks because a significant amount of the debt was interbank debt. See Harris, *supra* note 30, at 807. For a description of the interbank market's important role in international finance, see M. STIGUM & R. BRANCH, *MANAGING BANK ASSETS AND LIABILITIES* 128-30 (1983).

62. See Du Plessis, *supra* note 59, at 33.

63. See A. REIFFEL, *supra* note 2, at 8-10.

64. See Hirsh, *supra* note 34, at 274.

65. This was an unusual, but not unprecedented, procedure for renegotiating debt. It had been used to reschedule Indonesia's debt after the fall of the Sukarno government in 1966. Like the South African case, this was a politically sensitive debt renegotiation. Farber, *Renegotiating Official Debts*, *FIN. & DEV.*, Dec. 1990, at 20-21.

66. See sources cited *supra* notes 34-35.

67. See Harris, *supra* note 35, at 803.

arrangement and the banks would reschedule the remaining \$9.5 billion over twelve months with an interest rate of one percent to one and a quarter percent over pre-moratorium rates.⁶⁸ The banks also established a technical committee to represent them in future discussions with the SAG. Over the life of this agreement, the SAG actually made about \$2 billion of the scheduled \$3.6 billion interest and principal payments due on South Africa's total debt, indicating that some of the banks must have refinanced their credits.⁶⁹

Compared to the terms achieved by other debtor countries, this first interim arrangement seems unusually harsh. It provided no new funds, gave the South African debtors no grace period, and required them to repay about five percent of the principal of the outstanding debt. On the other hand, it did provide some significant benefits to a government that, prior to this arrangement, had been unable to raise money on the international markets.⁷⁰

The interim arrangement provided that if the banks and the original debtor did not reschedule the debt according to the agreed terms, the original debtor would make payments equal to the local currency equivalent of the original obligation into Special Restricted Accounts that matured according to a schedule stipulated in the Interim Arrangement. These accounts, credited to the original creditor, were held until maturity by the Permanent Investment Commission (PIC), a public sector entity that invests in public sector stock.⁷¹ The SAG was therefore free to use these deposits, subject only to the PIC's statutory authority, until the repayment obligation matured.⁷² Consequently, the arrangement enabled the SAG to utilize the assets of international banks at a time of significant economic difficulty in South Africa and at a time when it had no access to international financial markets.⁷³ Thus, overall the agreement was an attractive one for the SAG.

68. Hirsch, *supra* note 34, at 275. See also Harris, *supra* note 35, at 804. The banks were free within these parameters to reach their own agreements with their original debtors.

69. Hirsch, *supra* note 34, at 275.

70. See sources cited *supra* notes 34-35.

71. The PIC is a non-banking financial intermediary that receives funds from public sector entities and invests in fixed interest public sector stock. Its scope and responsibilities are set out in Public Investment Commissioners Act, Stat. of S. Afr. No. 45 of 1984. See The Department of Finance, *The Public Investment Commissioners*, in *THE MECHANICS OF THE SOUTH AFRICAN FINANCIAL SYSTEM* 109, 109-16 (3d ed. 1989).

72. See Du Plessis, *supra* note 59, at 33. It is important to recognize that this arrangement enabled the SAG to use budgetary resources for other purposes.

73. The funds available to the PIC from "other" sources (*i.e.*, unattributed sources) increased from R523 million in 1985 to R1920 million in 1986. It is reasonable to assume that a significant portion of this increase is due to debt payments. See S. AFR. RESERVE BANK Q. BULL., *supra* note 28, at S-44.

THE IMPOSITION OF SANCTIONS

By revealing the economic and financial vulnerability of the SAG, the debt negotiations, together with popular revulsion at the SAG's response to political developments in South Africa, resulted in an intensification of the international sanctions campaign. In 1985, the United Nations Security Council urged all Member States to ban all new investments and export credits to South Africa.⁷⁴ In 1986, the Member States of the European Community agreed to prohibit certain imports from South Africa and placed restrictions on new investments in South Africa, but did not prohibit European banks from rescheduling their outstanding South African credits.⁷⁵ The Commonwealth also sought to intensify its sanctions against South Africa.⁷⁶

Overriding a Presidential veto, the United States Congress adopted the Comprehensive Anti-Apartheid Act (CAAA) in October 1986.⁷⁷ The primary purpose of the CAAA is to help create a nonracial democracy in South Africa by using "economic, political, diplomatic, and other effective means to achieve the removal of . . . the apartheid system."⁷⁸ The CAAA implements this policy by barring most trade with South Africa and prohibiting new investments and new loans to South Africa. The definition of "loan" contained in the CAAA excludes rescheduling of existing debts.⁷⁹

The CAAA also states that it is the policy of the U.S. to assist the victims of apartheid "to overcome the handicaps imposed on them by

74. S.C. Res. 569, U.N. Doc. S/RES/569 (1985).

75. Decision 86/459/ECSC, 29 O.J. EUR. COMM. (No. L 268) 1 (1986) (suspending imports of certain iron and steel products from South Africa); Council Regulation No. 3302/86, 29 O.J. EUR. COMM. (No. L 305) 11 (1986) (suspending imports of gold coins from South Africa); Decision 86/517/EEC, 29 O.J. EUR. COMM. (No. L 305) 45 (1986) (suspending new direct investments in South Africa).

76. *The Commonwealth Accord on Southern Africa*, Oct. 20, 1985 (threatening, *inter alia*, to ban investments in South Africa and to terminate double tax treaties with South Africa); *Communique of Commonwealth Heads of Government Review Meeting*, London, Aug. 3-5, 1986 (committing Member States to implement sanctions specified in the 1985 Accord and to ban all new loans to South Africa and imports of South Africa uranium, iron, steel, and coal). The Accord and Communique are reprinted in BACKGROUND MATERIALS FOR COMMONWEALTH COMMITTEE OF FOREIGN MINISTERS ON SOUTHERN AFRICA, 4th Meeting, Canberra, Australia (Aug. 7-9, 1989) (Australian Overseas Information Service).

77. 22 U.S.C. §§ 5001-5116 (1988). The implementing regulations can be found in 31 C.F.R. § 545. For general discussion of the CAAA, see Nagan, *Economic Sanctions, U.S. Foreign Policy, International Law and The Anti-Apartheid Act of 1986*, 4 FLA. INT'L. L. J. 85 (1988); Clarizio, Clements, & Geetter, *United States Policy Toward South Africa*, 11 HUM. RTS. Q. 249 (1989). See also Butcher, *The Unique Nature of Sanctions Against South Africa, and Resulting Enforcement Issues*, 19 N.Y.U. J. INT'L L. & POL'Y 821 (1987)

78. 22 U.S.C. § 5013(a) (1988).

79. 22 U.S.C. § 5001(3) (1988) states that "the term loan does not include . . . rescheduling of existing loans, if no new funds or credits are thereby extended to a South African entity or the Government of South Africa."

the system of apartheid and to help prepare them for their rightful roles as full participants in the political, social, economic, and intellectual life of their country."⁸⁰ To this end, the CAAA permits private loans, donations, and investments in black-owned businesses and in projects designed to assist the victims of apartheid.⁸¹ The Act imposes no affirmative obligation on banks with outstanding South African credits either to use a portion of their renegotiated credits for this purpose, or to take these objectives into consideration in their future treatment of their outstanding South African credits. The anti-apartheid movement has not made any concerted effort to get the banks to use their renegotiated South African credits for these purposes.

THE SECOND INTERIM ARRANGEMENT

When the first interim arrangement expired, South Africa's financial position was improving and the SAG's political crackdown had succeeded in shielding the country's political crisis from international attention.⁸² Given this reduction in political and financial pressure, the banks, despite calls from South African anti-apartheid activists not to reach a new arrangement with the SAG unless certain political conditions were met, concluded a second interim arrangement with the SAG in March 1987.⁸³

This three year arrangement, which terminated on June 30, 1990, continued the basic framework of the first arrangement. It contained no grace period and required repayment of \$1.42 billion (thirteen percent) of the outstanding affected debt.⁸⁴ The interest rate charged depended on whether the banks reached an agreement with their original borrower or took advantage of the special restricted accounts with the

80. 22 U.S.C. § 5013(a) (1988).

81. 22 U.S.C. § 5013(b) (1988). The regulations stipulate that charitable contributions will not be treated as prohibited "new investments," 31 C.F.R. § 545.421 (1990), and states that specific licenses may be issued to financial institutions interested in making otherwise prohibited loans where it is determined that "the loans will improve the welfare or expand the economic opportunities of persons in South Africa disadvantaged by the apartheid system." 31 C.F.R. § 545.503 (1990). Neither the regulations nor the statute explain the standards to be used in making this determination.

82. See K. OVENDEN & T. COLE, *APARTHEID AND INTERNATIONAL FINANCE* 90-91 (1989); Hirsch, *supra*, note 34, at 277-79.

83. Hirsch, *supra* note 34, at 275. See also G. HUFBAUER, J. SCHOTT, & K. ELLIOT, *supra* note 7, at 229.

84. G. HUFBAUER, J. SCHOTT, & K. ELLIOT, *supra* note 7, at 229. This agreement consists of a letter from the South African Minister of Finance to the banks, dated March 25, 1987, that sets out the terms of the arrangement and stipulates that each letter to each bank is a separate offer which the bank may accept by acknowledging receipt of the letter. *Second Interim Arrangement Letter*. Appended to the letter was a technical memorandum that discussed how the interim arrangement would operate. *Aspects of the Second Interim Arrangements* [hereinafter *Technical Memorandum*].

PIC, that paid an interest rate of seven-eighths of one percent over the relevant market interest rate.⁸⁵ The SAG continued to have access to these funds subject to the statutory mandate of the PIC⁸⁶ and to the terms of arrangement, according to which the SAG was the obligor on these debts.⁸⁷

The Second Interim Arrangement also established two mechanisms through which creditors could "exit" the Interim Arrangement. First, the banks could convert their loans into ten year exit loans that would not be subject to any future rescheduling.⁸⁸ These exit loans, on which the borrower pays an interest rate of one and five-eighths to one and seven-eighths percent over Libor and a fee of three-eighths of one percent, include a mid-term two year grace period with repayment over five years, that was designed to help the SAG reduce an anticipated 1990-91 debt repayment hump. About \$5 billion of debt has been converted into these exit loans.⁸⁹

The second mechanism was a debt-equity conversion through which the banks could convert their funds into investments in South African enterprises. These investments can be liquidated and the funds taken out of the country through the sale of Financial Rands.⁹⁰ About \$600 million of debt has been converted through this mechanism.⁹¹

THE THIRD INTERIM ARRANGEMENT

In mid-1989 the anti-apartheid movement began to prepare for the negotiation of a Third Interim Arrangement that would be required when the Second Interim Arrangement terminated in June 1990. Its objective was to convince the banks to condition a Third Interim Arrangement on SAG agreement to dismantle apartheid and negotiate

85. See *Technical Memorandum*, *supra* note 84, § 8. The special restricted accounts are credited to the original creditor who is paid out according to the terms of the Interim Arrangement. As long as the funds were actually held in the accounts, they were available to the SAG, that could use the funds to finance public sector securities. See *Second Interim Arrangements Letter*, *supra* note 84, § 7.01(c).

86. See Public Investment Commissioner's Act, Stat. of S. Afr. No. 45 of 1984; The Department of Finance, *supra* note 71, at 109-16.

87. See *Technical Memorandum*, *supra* note 84, § 1. See also *id.*, Appendix A § 4.1.

88. See *id.*, § 12.

89. See Tommey, *Outlook for Foreign Funding Improving*, *The Star*, June 6, 1990; S. Fidler, *Lenders Take Up S. African Exit Option*, *The Financial Times*, May 16, 1989, at 4. In May 1989, only \$3.5 billion had been converted to exit loans.

90. *Technical Memorandum*, *supra* note 84, § 6. The financial rand which trades at a discount to the commercial rand, cannot be transferred out of South Africa. This means that any sale of financial rands represents merely a change in ownership and no net outflow of funds from South Africa. See *The Bank of Lisbon and South Africa Limited*, *supra* note 60, at 339-40.

91. See Tommey, *supra* note 89; Fidler, *supra* note 89, at 4.

with the democratic forces on the establishment of a nonracial democratic constitutional order in South Africa.⁹²

The timing seemed propitious. The democratic forces appeared to be regrouping from the blows they had suffered when the state of emergency was declared, and the South African economy was again in deep crisis.⁹³ The country was clearly suffering from the financial sanctions that had been imposed by the transnational commercial banks in 1985, that effectively denied South African borrowers access to international financial markets, and from the international sanctions campaign, that reduced South African access to traditional markets in the United States and Europe and raised its overall cost of doing business.⁹⁴ It was well known that South Africa could not repay the US\$8 billion that would fall due when the Second Interim Arrangement terminated.⁹⁵ In addition, the country had substantial obligations falling due in 1990-91 on debt outside the scope of the interim arrangement.⁹⁶

The SAG, therefore, urgently needed debt relief if it was to avoid a recurrence of the 1985 crisis. This appeared to give the banks great leverage over the SAG.⁹⁷ The anti-apartheid movement argued that the banks should use this leverage to help end apartheid. It contended that the banks could do this by denying the SAG debt relief unless the

92. In April 1989 four South African churchmen, Archbishop Desmond Tutu, Dr. Allen Boesak, Dr. Beyers Naude, and Reverend Frank Chikane, issued an appeal to fourteen creditor banks not to reschedule South Africa's debt unless five conditions were met. They were that the SAG must end the state of emergency, release all political prisoners and detainees, unban all political organizations, repeal all racist legislation, including the Group Areas Act, the Land Acts, the Separate Amenities Acts and the Population Registration Act, and establish a process for negotiating a new constitution for a non-racial, democratic, and unitary South Africa. These demands were taken up by the anti-apartheid movement. See COMMONWEALTH COMMITTEE OF FOREIGN MINISTERS ON SOUTH AFRICA, SOUTH AFRICA: THE SANCTIONS REPORT (1989) [hereinafter SANCTIONS REPORT]; *Rescheduling South Africa's Debt: Hearing before the Subcomm. on International Development, Finance, Trade, and Monetary Policy of the Comm. on Banking, Finance, and Urban Affairs*, 101st Cong., 1st Sess. 101-45 (1989) [hereinafter *Hearings*] (Statement of Terry Crawford-Browne and Additional Materials Submitted for the Record); *Divestment and Non-Equity Links by Transnational Corporations in South Africa, Report of the U.N. Centre on Transnational Corporations*, U.N. Doc. E/C.10/AC.4/1989/2 (1989) [hereinafter *Divestment Report*].

93. See Statement of John Lind in *Hearings*, *supra* note 92, at 76-77; Joffe, *Economics Not Faith Tell Churchmen Where To Apply Pressure*, *The Weekly Mail* (Johannesburg, South Africa), June 23-29, 1989, at 15.

94. See SANCTIONS REPORT, *supra* note 92, at 38-45. See also R. BETHLEHEM, *supra* note 28.

95. See sources cited *supra* note 93; *Divestment Report*, *supra* note 92, at 2, 13; K. OVENDEN & T. COLE, *supra* note 82, at 75-98.

96. The country's total repayment obligations for 1990-91 were estimated to be between \$1.5 and 2.0 billion per year. See *Divestment Report*, *supra* note 92, at 2, 13; Statement of John Lind in *Hearings*, *supra* note 92, at 77.

97. For a detailed discussion of commercial bank exposure to South Africa, see *Divestment Report*, *supra* note 92.

government made specific political concessions that in effect amounted to a commitment to dismantle apartheid.⁹⁸

Unfortunately, the anti-apartheid movement's strategy was based on an overly optimistic assessment of the bargaining position of the banks and an underestimation of the forces propelling them to reach an agreement with SAG. In 1989 the banks were facing serious problems with their outstanding debts to developing countries, which were accumulating substantial arrears.⁹⁹ Domestically, many banks were beginning to experience significant problems with other parts of their loan portfolios.¹⁰⁰ The banks were also concerned with raising capital to meet new capital adequacy requirements.¹⁰¹ Consequently, they were in no mood to create new problems with one of the few debtor countries that was meeting its renegotiated debt obligations in a timely fashion.

The strategy also ignored the banks' reluctance to attach policy-related conditions to debt renegotiations. Banks had tried this, with a notable lack of success, in Peru in the mid-1970s. In that case, the banks forced Peru to accept certain policy reforms as a condition for rescheduling its debt, but had been unable to enforce the conditions when the government failed to implement them.¹⁰² This experience persuaded the banks to rely on the IMF to promote policy reforms in troubled debtor countries.¹⁰³

98. See sources cited *supra* note 92.

99. In 1989 total arrears on developing country debt was \$79 billion, equal to 6.4% of total debt. About half of this was owed to private creditors. See THE WORLD BANK, WORLD DEBT TABLES, 1990-91, at 22 (1990).

100. For a discussion of the problem in the U.S. banking industry, see SUBCOMM. ON FINANCIAL INSTITUTIONS, SUPERVISION, REGULATION, AND INSURANCE OF THE HOUSE COMM. ON BANKING, FINANCE AND URBAN AFFAIRS, 101ST CONG., 2D SESS., THE BANKING INDUSTRY IN TURMOIL: A REPORT ON THE CONDITION OF THE U.S. BANKING INDUSTRY AND THE BANK INSURANCE FUND 81 (Comm. Print 1990).

101. See COMM. ON BANKING REGULATIONS AND SUPERVISORY PRACTICES, BANK FOR INTERNATIONAL SETTLEMENTS, PROPOSALS FOR INTERNATIONAL CONVERGENCE OF CAPITAL MEASUREMENT AND CAPITAL STANDARDS (Dec. 1987), *reprinted in* 27 I.L.M. 530, 547-49 (1988) [hereinafter PROPOSAL FOR CONVERGENCE]. These rules, which are implemented by national bank regulators, require banks by 1992 to have minimum capital levels equal to at least 8% of total risk-adjusted assets. Of this at least 4% must be core capital that consists of equity plus disclosed reserves. The banks were required to meet an intermediary standard of 7.25%, of which at least half should be core capital, by Dec. 31, 1990. *Id.* This meant that in 1989-90 most of South Africa's commercial bank creditors were concerned with raising capital at a time of falling income levels and rising levels of problem loans.

102. See R. PLAN, EXTERNAL DEBT RESCHEDULING 58-61 (Law, Economics, International Trade, Vol. 8, 1985). The banks had experienced similar problems in their attempts to renegotiate the obligations of the German government in the 1920s and '30s. See R. CHERNOW, THE HOUSE OF MORGAN: AN AMERICAN BANKING DYNASTY AND THE RISE OF MODERN FINANCE (1990) (material at 392-99 is particularly pertinent).

103. The IMF, for political and legal reasons, could not play such a role in South Africa. See sources cited *supra* notes 45-46 and accompanying text.

Even if the banks had been willing to impose tough political conditions on SAG, it is not clear how successful the strategy would have been. A South African debtor intent on evading its financial obligations knew when these obligations would mature and when the banks would be entitled to take legal action against it. Consequently, the debtor could easily protect itself against creditor action by moving its assets out of vulnerable jurisdictions prior to the maturation date of the debt obligations and by utilizing the country's substantial sanctions-busting experience to avoid future problems. Even if the creditors were able to locate attachable South African assets, their ability to attach these assets could be complicated by a mismatch between the identity of their obligor and of the legal owners of the attachable assets.¹⁰⁴ Under these circumstances, the banks would be unlikely to view judicial action against South Africa, which would be expensive and time-consuming, as desirable or cost-efficient.

Furthermore, by 1989, the SAG knew it could not expect new money from the banks and so had little incentive to accede to bank demands, including calls for political reforms, that it viewed as unreasonable.¹⁰⁵ While there are obvious costs associated with such a strategy, it would have enabled the SAG to both avoid troublesome demands and keep the foreign exchange it owed to the banks. The SAG could have further strengthened its position by rewarding those banks that were willing to be more accommodating.¹⁰⁶

The strategy was also based on an overestimation of the role played by the international sanctions campaign in South Africa's debt problems. Despite international pressure, banks had continued lending money to South African entities until late 1984. As discussed above, their refusal in August 1985 to roll-over their South African loans was primarily due to financial factors. The political forces that influenced their 1985 decision to stop lending to South Africa were largely generated within South Africa by the trade unions and the

104. See *Hercaire International, Inc. v. Argentina*, 821 F.2d 559 (11th Cir 1987) (Judgment against foreign sovereign could not be enforced against the assets of the State-owned airlines even though the foreign sovereign owned 100% of the airlines.)

105. See *Recent Developments in South Africa and H.R. 3458: Joint Hearing Before the Subcomm. on International Development, Finance, Trade and Monetary Policy of the House Comm. on Banking, Finance, and Urban Affairs and the Subcomm. on Africa of the House Comm. on Foreign Affairs*, 101st Cong., 2d Sess., 101-79 (1990) [hereinafter *Recent Developments*] (Statements of Rodney B. Wagner, Vice Chairman, Morgan Guaranty Trust Company, and John J. Simone, Executive Vice-President, Manufacturers Hanover Trust Company). Some South African commentators had begun to argue for a "unilateral rescheduling." See Ensor, *SA Should Withdraw From Onerous Debt Arrangements—Academics*, Business Day (Johannesburg, South Africa), Dec. 29, 1989, at 5.

106. On sovereign default strategies, see generally A. KALETSKY, *THE COSTS OF DEFAULT* (1985).

member organizations of the United Democratic Front.¹⁰⁷

The banks were able to use these weaknesses in the anti-apartheid movement's strategy to portray the strategy as financially naive and unworkable.¹⁰⁸ This enabled them to base the South African debt negotiations on their own profit-maximizing criteria and to justify the results as being the most "feasible" under the circumstances.

In fact, the banks' position was subject to significant challenge. They had originally loaned money to South African borrowers despite clear evidence of the economic irrationality of apartheid and of the profound political problems that it caused.¹⁰⁹ It was also apparent that these factors were the primary cause of the country's debt problems and that between the 1985 and the 1989 negotiations there had been no real changes in the political and economic structure of the country.¹¹⁰ The banks' outstanding South African credits, which by 1989 had been converted from short term into medium term credits, were as much at risk in 1989 as they were in 1985.

In reality, the government's major economic achievement up to that point was that it had managed to make timely payment of all its debt obligations. However, the impressiveness of this feat is substantially diminished when one remembers that Ceausescu's Romania managed a similar feat.¹¹¹

The anti-apartheid movement's failure to raise these issues allowed the banks to avoid justifying their treatment of South African debt in terms of their own prudence as bankers. The anti-apartheid movement also lost an opportunity to engage the banks in a discussion on how the debt, which was trapped in South Africa, could be used to promote appropriate socioeconomic development in South Africa.

The result was that in October 1989 the SAG and the banks announced that they had concluded a third interim arrangement that followed lines similar to that of the second agreement.¹¹² The arrange-

107. See sources cited *supra* note 52 and accompanying text.

108. See, e.g., Statements of Rodney B. Wagner and John J. Simone in *Recent Developments*, *supra* note 105.

109. See discussion of South Africa's political economy, *supra* notes 14-32 and accompanying text.

110. See sources cited *supra* notes 14-15. During this period President P. W. Botha remained in power and the country was still under a state of emergency.

111. For a discussion of Romania's debt, see Note, *U.S.-Romanian Trade: Foreign Debt, Trade Barriers, and Future Problems and Prospects*, 21 *LAW. & POL'Y. INT'L BUS.* 73 (1989).

112. The agreement was implemented through a bank acknowledgement of the receipt of a letter dated October 23, 1989 and the accompanying technical memorandum from the South African Minister of Finance. The 3½ year agreement, beginning in July 1990, covers U.S. \$8 billion in loans and continues the interest rates applicable under the second interim arrangement and provides for the same relending and exit loan options available under the Second Interim Arrangement. According to the arrangement, South Africa will repay about \$1.5 billion of the

ment significantly alleviated the financial pressure on the SAG and has led to new financing prospects for South Africa.¹¹³

The third arrangement was publicly announced on October 19 as the leaders of the Commonwealth Nations were meeting in Australia to discuss the question of strengthening sanctions against South Africa.¹¹⁴ The timing could hardly have been coincidental and is indicative of the strength of the SAG's bargaining position.¹¹⁵ While the banks clearly had their own reasons for wanting to reach an arrangement with the SAG, there was no compelling reason for the banks to conclude an agreement more than six months prior to the expiration of the Second Interim Arrangement.

SUBSEQUENT DEVELOPMENTS

Since the announcement of the Third Interim Arrangement, and in light of the recent developments in South Africa, the international anti-apartheid movement has adopted a "wait and see" policy that includes the maintenance of existing sanctions,¹¹⁶ and keeping the mechanisms for a future ratcheting up of the financial sanctions campaign in reserve.¹¹⁷

debt over the life of the arrangement. This means that South Africa could still owe \$6.5 billion when the agreement terminates on December 31, 1993. See the discussion of the Third Interim Arrangement, *supra* notes 92-115 and accompanying text. On the financial consequences of the Third Interim Arrangement, see J. LIND, *THE NEW INTERIM AGREEMENT BETWEEN THE BANKS AND SOUTH AFRICA AND ITS IMPLICATIONS* (CANICCOR Research 1989); Tommey, *supra* note 89.

113. See *Swiss Roll-overs*, Financial Mail, Nov. 16, 1990, at 37.

114. See Erlanger, *Group Seeks New Ways to Pressure South Africa*, N.Y. Times, Oct. 20, 1989, at D6; Wren, *Pretoria and Banks Reach Pact*, N.Y. Times, Oct. 20, 1989, at D1.

115. Fabricius & Heystek, *South Africa Wins Debt Rollover Battle*, The Star (Johannesburg, South Africa), Oct. 25, 1989, at 17.

116. At its Consultative Conference in December 1990, the ANC also called for the continuation of sanctions. See Van Niekerk, *Grim Ordeal—but ANC Emerges Stronger*, The Weekly Mail (Johannesburg, South Africa), Dec. 20, 1990-Jan. 10, 1991, at 7, 8. This approach was modified at the ANC's July 1991 conference. Reportedly, the ANC is now considering supporting the lifting of sanctions in phases linked to certain, as yet unspecified and presumably unmet, concessions by the SAG. See Wren, *South Africa: New Reality*, N.Y. Times, July 8, 1991, at A1.

A number of city councils in the United States are strengthening their sanctions. See, e.g., New York, N.Y., Dep't of Fin., Rules Relating to the Anti-Apartheid Classification of Banks, CITY RECORD, July 10, 1991, at 1207-08. It should be noted that these rules encourage banks to use their funds trapped in South Africa to support organizations promoting the transition to a democratic post-apartheid South Africa. See *id.* § 4(17-19).

117. The leaders of the Commonwealth could still implement the proposals made by its panel of independent experts if this newly begun South African negotiation process falters. This panel of experts proposed a five year strategy for increasing financial sanctions that will ultimately cut South Africa off from all trade credits and banking relationships and will, in effect, exclude the country from the international financial system if it does not dismantle apartheid and establish, through negotiation, a non-racial, democratic constitutional order for the country. See SANCTIONS REPORT, *supra* note 92, at 174-75. In the United States, a South African Financial Sanctions for Democracy Amendment Act designed to increase financial pressure on the SAG has been proposed. See South African Financial Sanctions Act of 1989, H.R. 3458, 101st Cong., 1st

The international anti-apartheid movement's failure to substantially influence the renegotiation of South Africa's debt has increased its frustration with South Africa's creditors. As a result, some elements of the movement would like to see the banks punished for lending to South Africa even if this results in neither additional pressure being imposed on the SAG nor in any discernible benefit to the people of South Africa.

This is most clearly seen in the Financial Sanctions for Democracy Amendment Act.¹¹⁸ Section 3 of the bill would require all U.S. nationals to sell their exit loans by December 31, 1992. The effect of this provision would be to force the holders to sell the loans at a steep discount to non-U.S. investors. Since South Africa has been reliably servicing its debt, these forced sales would give a windfall to the purchasers and impose costs on U.S. holders without imposing any additional costs on the South African debtors, whose debt service obligations would remain unchanged.

There are many possible purchasers of the South African exit loans, including speculators, investment banks, and other investors less sensitive than commercial banks to pressure from the anti-apartheid movement. In fact the purchaser could be acting for the SAG, so the forced sale could actually bestow an undeserved benefit on the SAG. Moreover, South Africa's non-U.S. creditors would feel no pressure to buy the loans because, as long as they intend on holding their credits to maturity, the value of their credits depends on the reliability of South Africa's debt service performance and not on the price of South African debt in the secondary market.¹¹⁹

A strategy which appears to punish South Africa's creditors is

Sess., 135 Cong. Rec. 7037-9 (1989). This bill was proposed in the 101st Congress by Rep. Fauntroy. It is similar to the Commonwealth proposals in that it provides for time-triggered financial sanctions that slowly exclude South Africa from the international financial system. *Recent Developments, supra* note 105, at 170-88 (text of H.R. 3458). It could be resubmitted to the 102d Congress.

118. *Recent Developments, supra* note 105, at 170-88 (text of H.R. 3458).

119. Similar considerations apply to Section 5 of H.R. 3458, which will prohibit U.S. banks and their foreign branches and subsidiaries from offering correspondent banking services to South African entities. *Id.* See GENERAL ACCOUNTING OFFICE, SOUTH AFRICA: RELATIONSHIP WITH WESTERN FINANCIAL INSTITUTIONS, GAO/NSIAD-90-189 (June 7, 1990) at 14-15 (discussing correspondent banking relations and trade credits); GENERAL ACCOUNTING OFFICE, DEBT RESCHEDULING AND POTENTIAL FOR FINANCIAL SANCTIONS, GAO/NSIAD-90-109BR (Feb. 1990) at 8-10.

The effect of these provisions would obviously be much greater if other countries would impose similar conditions on their banks. In that case South Africa would find it difficult to replace banking services lost as a result of this legislation and there would be a definite decrease in their access to the international financial system. Such a strategy was proposed to the Commonwealth but has not been adopted. See K. OVENDEN & T. COLE, *supra* note 82, at 187-205; SANCTIONS REPORT, *supra* note 92, at 111-13, 136-37, 174.

counterproductive.¹²⁰ Given the banks' public relations problem and their interest in developing links to the people and organizations that could be the leaders of a future non-racial democratic South Africa, they should be willing to consider creative proposals regarding the treatment of their South African debt. A creative anti-apartheid approach to the debt would seek to both maintain pressure on the SAG and to use the debt to promote structural transformation in the South African political economy. In this regard, one should not forget that the dynamics of the apartheid system ensure that it is the victims of apartheid who bear the burden of the debt, even though they have received no real benefits from it.¹²¹

The next section will discuss how an alternate sanctions strategy that creates opportunities for using debt for appropriate development purposes could have been designed. Even though the third interim arrangement has been concluded, elements of this strategy can still be implemented because the country's creditors have outstanding assets that are trapped in South Africa until at least December 1993.¹²²

AN ALTERNATE STRATEGY FOR SOUTH AFRICAN DEBT

An alternate sanctions strategy must be based on the recognition that sanctions will impose costs on South Africa that will continue to affect the country after the sanctions are lifted. Many of the creditors and investors who disinvested from South Africa will have developed new business connections and will be wary of reinvesting before a predictable and profitable business environment exists in the country. In addition, the country will need to devote resources to repairing the domestic and international costs of sanctions. This will constrain its development possibilities.¹²³

120. The strategy also can adversely influence the actions of creditor governments. In December 1990, the European Community agreed to lift the prohibition on new investment in South Africa despite a plea from Nelson Mandela, the ANC deputy-president, to maintain sanctions. See *European Statement on South Africa*, N.Y. Times, Dec. 16, 1990, at I24. See also Wren, *DeKlerk's Surprise*, N.Y. Times, Feb. 4, 1991, at A1; Riding, *Europeans Move to Lift Pretoria Curbs*, N.Y. Times, Feb. 5, 1991, at A3. In April 1991, the European Community, ignoring the opposition of the ANC, agreed to lift its ban on the importation of South African iron, steel, and gold coins. See Buchan, *South Africa Steel and Gold Ban Lifted*, The Financial Times, Apr. 16, 1991, at 4, col. 4.

On July 10, 1991, President Bush terminated the sanctions imposed against South Africa by the CAAA, but left in place all other sanctions, including those related to the IMF. See Exec. Order No. 12,769 (July 10, 1991), and accompanying statement by President.

121. See sources cited *supra* note 8.

122. The debt covered by the Third Interim Arrangement is not expected to be fully repaid before the expiration of the Arrangement on Dec. 31, 1993. See sources cited *supra* note 112.

123. See generally SANCTIONS AGAINST APARTHEID (M. Orkin ed. 1989); R. BETHLEHEM, *supra* note 28; 1 INVESTOR RESPONSIBILITY RESEARCH CENTER, THE IMPACT OF SANCTIONS ON SOUTH AFRICA: THE ECONOMY (1990).

These costs could be minimized if the sanctions include a "development exception" that allows international financial and economic transactions that support appropriate development opportunities that may arise during the sanctions campaign.

Ensuring that these development efforts promote the structural transformation of the South African political economy and do not deteriorate into disguised "sanctions-busting" requires a method for identifying "appropriate development opportunities." Since the identification of "appropriate development" will itself influence socioeconomic activity after the sanctions campaign is over, the identification method should respect the sovereign right of the South African people to determine their own post-apartheid future. Consequently, the method must be based on those internationally recognized and accepted standards of conduct that a post-apartheid South Africa will be expected to observe. This would be consistent with the international legal justification for sanctions against South Africa which is that apartheid is a violation of international norms of conduct.¹²⁴

Since these development activities should result in an improvement in the socioeconomic condition of the victims of apartheid, the identification method must incorporate the principles of sustainable, equitable development.¹²⁵ It must also be equally applicable to charitable, community, and welfare projects and to commercial ventures that increase black participation in the South African economy.

A sanctions strategy with a development exception must include a development financing mechanism that does not undermine the punitive goal of the sanctions. This mechanism should contain incentives to encourage those who have financed the present apartheid political economy to contribute to appropriate development activities, and should be available to other public and private organizations interested in funding appropriate development activities. The mechanism could expand into a more comprehensive development assistance framework for a post-apartheid South Africa.

It is not unreasonable to expect South Africa's creditors to contrib-

124. The United Nations has resolved that apartheid is inconsistent with the principles of the United Nations Charter and the Universal Declaration of Human Rights. S.C. Res. 181, 18 U.N. SCOR (1056th mtg.) at 7, U.N. Doc S/5386 (1963); S.C. Res. 182, 18 U.N. SCOR (1078th mtg.) at 8, U.N. Doc. S/5471 (1963); S.C. Res. 191, 19 U.N. SCOR (1135th mtg.) at 13, U.N. Doc. S/5773 (1964); S.C. Res. 418, 32 U.N. SCOR (2046th mtg.) at 5, U.N. Doc. S/12436 (1977). The General Assembly also adopted the International Convention on the Suppression and Punishment of the Crime of Apartheid on November 30, 1973. G.A. Res. 3068, 28 U.N. GAOR Supp. (No. 30) at 3, U.N. Doc. A/9030 (1973), *opened for signature* Nov. 30, 1973, 1015 U.N.T.S. 244, *entered into force* July 18, 1976. In total, the United Nations has adopted more than 320 resolutions concerning apartheid. See K. TOMASEVSKI, *supra* note 5, at 84.

125. These principles are discussed in more detail *infra* notes 129-51 and accompanying text.

ute to these development efforts. When the banks loaned money to South African borrowers, they knew or should have known about the structural weaknesses in the country's political economy and about the need for structural adjustment in the economy.¹²⁶ In addition, at the time they loaned the money they knew or should have known that South Africa, in fact, was unable to obtain IMF financing.¹²⁷ Consequently, the banks should have anticipated that in the event of the country being unable to meet its debt obligations, they could be compelled to support structural adjustment in the country's political economy financially or risk losing their outstanding credits.

These elements of an alternate sanctions strategy can be implemented with or without creditor government participation. If creditor governments are involved, they could require banks to disclose to the relevant regulatory agencies how they are using their outstanding South African credits. Alternatively, banking regulators could require banks to either establish loss reserves against their South African credits, or finance appropriate development in South Africa. Such a reserve requirement can be justified on the grounds that bank exposure to a debtor country, like South Africa, that has consistently failed to adopt the adjustment policies needed to correct its socioeconomic problems is a threat to the safety and soundness of the banks. The best way for the banks to protect themselves against the risk of default by such a borrower may be to use some of their outstanding credits to fund development activities that promote appropriate socioeconomic changes in the debtor country.¹²⁸

In the event that creditor governments do not participate in the strategy, the anti-apartheid movement could establish a monitoring committee which would collect information, serve as an information clearing house, and help development projects and their sponsors locate sources of funds. The anti-apartheid movement could also use shareholder resolutions and local consumer action to encourage banks to cooperate with the strategy.

Each of the novel elements of this strategy—a method for identifying “appropriate development” that includes developmental and human rights guidelines, a development financing mechanism, and the

126. See discussion of South Africa's political economy *supra* notes 14-32 and accompanying text.

127. See sources cited *supra* note 47.

128. In this regard it is important to remember that timely payment of debt obligations by sovereign debtors with flawed political economies may not mean that bank assets are adequately protected. It was purely fortuitous that banks were repaid their Romanian debt prior to the overthrow of the Ceausescu dictatorship. See Note, *supra* note 111, at 71.

means of encouraging creditor participation in this strategy—are discussed in more detail below.

IDENTIFYING “APPROPRIATE DEVELOPMENT”

The purpose of the method for identifying appropriate development is to help creditors and other interested parties identify projects and project sponsors that will promote the socioeconomic development of the people of South Africa and that will help create a democratic order in the country. Qualifying projects must both promote sustainable development and must meet international human rights standards.

Since the SAG is part of the problem, the development criteria must be based on the experiences of countries where development has occurred without and even despite the efforts of government.¹²⁹ It must also be based on the development experience of non-governmental organizations (NGOs).¹³⁰ While specific lessons will vary depending on the type of development project being considered,¹³¹ it appears that successful projects share at least two characteristics.¹³²

The first is the importance of participation by the project beneficiaries in the design, implementation, and management of the projects.¹³³ This means that project sponsors must work with the project beneficiaries during the design phase of the project, that the project structure must include channels for communication between

129. There are numerous examples of successful development projects that have occurred without government support and even with its active opposition. See, e.g., A. HIRSCHMAN, *GETTING AHEAD COLLECTIVELY: GRASSROOTS EXPERIENCES IN LATIN AMERICA* (1984); H. DE SOTO, *supra* note 14; S. Paul, *Governments and Grass Roots Organizations: From Co-Existence to Collaboration*, in *STRENGTHENING THE POOR: WHAT HAVE WE LEARNED* 61 (J. Lewis ed. 1988). For examples of such projects in South Africa, see F. WILSON & M. RAMPHELE, *supra* note 15, at 279-92.

130. The term “non-governmental organization” includes all organizations that are privately organized, managed, and financed. It includes commercial enterprises, trade unions, charitable, welfare, educational, environmental, community, youth, consumer, and cultural organizations. For discussion of the role of such organizations in development, see Durning, *People Power and Development*, 76 *FOREIGN POL’Y* 66 (1989); M. CERNEA, *NON-GOVERNMENTAL ORGANIZATIONS AND LOCAL DEVELOPMENT* (World Bank Discussion Paper No. 40, 1988); G. GRAN, *DEVELOPMENT FOR PEOPLE* (1983).

131. For a useful discussion of the lessons to be learned in social, economic, agriculture, and health projects, see *THE FIELD DIRECTORS’ HANDBOOK: AN OXFAM MANUAL FOR DEVELOPMENT WORKERS* (B. Pratt & J. Boyden eds. 1988) [hereinafter *OXFAM MANUAL*]; F. MOORE LAPPE, J. COLLINS, & D. KINLEY, *AID AS OBSTACLE* (1980).

132. See generally S. HELLINGER, D. HELLINGER & F. O’REGAN, *AID FOR JUST DEVELOPMENT* (1988). See also sources cited *supra* note 129.

133. For a discussion of the meaning of the right to participation, see Paul, *International Development Agencies, Human Rights and Humane Development Projects*, 17 *DEN. J. INT’L LAW. & POL’Y* 67, 108-13 (1988). See also *AFRICAN CHARTER FOR POPULAR PARTICIPATION IN DEVELOPMENT* (International Conference on Popular Participation in the Recovery and Development Process in Africa 1990).

project managers and project beneficiaries, and that the project beneficiaries must be able to hold the project managers accountable for their actions. The organizational structures created by such projects will benefit not only future development activities in South Africa but also the anti-apartheid movement's efforts to end apartheid and create a democratic political order in the country.

The second is that successful development projects are environmentally and managerially sustainable. Environmental sustainability means, at a minimum, that the project does not lead to long term environmental degradation and that, where appropriate, the project design includes a plan for assessing the environmental impact of the project and for managing any environmental problems created by the project.¹³⁴ Managerial sustainability means that the project design must include plans for developing the financial and managerial capacity to sustain the project once the initial support ends.¹³⁵ Sustainability also requires that the project design include an evaluation procedure. This will ensure that the lessons learned from each project are available to others and that the country develops a repository of development know-how.¹³⁶

Furthermore, appropriate development projects must help create a South Africa that conforms to internationally recognized standards of conduct. While international human rights standards are applicable to all societies and are not specifically designed to promote development, there is a growing recognition of the connection between human rights and development and of the need to ensure that development strategies do not involve an abrogation of human rights.¹³⁷ Therefore,

134. For a discussion of the importance of environmental sustainability to development, see OUR COMMON FUTURE, REPORT OF THE WORLD COMMISSION ON ENVIRONMENT AND DEVELOPMENT (1987). For a discussion of the environmental damage that apartheid has caused and of the need for environmentally sustainable development in South Africa, see A. DURNING, APARTHEID'S ENVIRONMENTAL TOLL (World Watch Paper No. 95, May 1990); B. HUNTLEY, R. SIEGFRIED, & C. SUNTER, SOUTH AFRICAN ENVIRONMENTALISTS INTO THE 21ST CENTURY 43-123 (1989).

135. See S. HELLINGER, D. HELLINGER, & F. O'REGAN, *supra* note 132, at 33-47, 181-95. See also sources cited *supra* notes 129-30. Foreign NGOs can play a useful role in helping develop local financial and managerial capacity. Appropriate development during the sanctions campaign could, therefore, have provided an opportunity to develop links between democratic organizations in South Africa and NGOs in both developing and industrialized countries. Such links would assist development planning in the democratic South Africa that sanctions are helping to create. S. HELLINGER, D. HELLINGER, & F. O'REGAN, *supra* note 132, at 99.

136. For a discussion of the importance of evaluation procedures, see S. HELLINGER, D. HELLINGER, & F. O'REGAN, *supra* note 132, at 143-44. See also OXFAM MANUAL, *supra* note 131, at 99-107, 127-33; F. MOORE LAPPE, J. COLLINS, & D. KINLEY, *supra* note 131, at 121.

137. There is an extensive literature on this subject. See generally HUMAN RIGHTS AND THIRD WORLD DEVELOPMENT (G. Shepard & V. Nanda eds. 1985); HUMAN RIGHTS AND DEVELOPMENT (D. Forsythe, ed. 1989); THE RIGHT TO FOOD (P. Alston & K. Tomasevski eds. 1984); Pronk, *Development and Human Rights*, in DIFFERENT DIMENSIONS IN DEVELOPMENT

the definition of appropriate development projects should be based on applicable international human rights instruments.¹³⁸ These are the Universal Declaration of Human Rights,¹³⁹ the International Covenant on Civil and Political Rights,¹⁴⁰ the International Covenant on Economic, Social and Cultural Rights,¹⁴¹ the International Convention on the Elimination of All Forms of Racial Discrimination,¹⁴² the Convention on the Elimination of All Forms of Discrimination Against Women,¹⁴³ the Declaration on the Elimination of All Forms of Intolerance and of Discrimination Based on Religion and Belief,¹⁴⁴ and the Banjul Charter on Human and Peoples' Rights.¹⁴⁵ The International Labor Organization's Conventions on the rights of industrial and rural workers, which provide for rights of association and for "humane" working conditions, are also relevant.¹⁴⁶

IN THE 1980's 1-24 (B. de Gaay Footman ed. 1981) (*reprinted in* United Nations Conference on Trade and Development Reprint Series No. 18, 1981); Stewart, *supra* note 5; K. TOMASEVSKI, *supra* note 5; *Symposium on International Development Agencies, Human Rights and Environmental Considerations*, 17 DEN. J. INT'L. LAW. & POL'Y 29 (1988); Paul, *Rural Development, Human Rights and Constitutional Orders in Sub-Saharan Africa*, 1989 THIRD WORLD LEGAL STUD. 57 (1989).

138. It should be noted that South Africa is not presently a signatory to any of the human rights conventions. However, based on the statements of the democratic movement inside South Africa, it is to be expected that a future democratic government will sign these Conventions, which are consistent with the policies of the largest anti-apartheid movement. See, e.g., *The Freedom Charter*, as adopted by the Congress of the People on June 26, 1955 which is the basic policy document of the ANC. R. SUTTNER AND J. CRONIN, 30 YEARS OF THE FREEDOM CHARTER 262 (1986). See also ANC Constitutional Guidelines for a Democratic South Africa, *reprinted in* A.N.C. DEPARTMENT OF POLITICAL EDUCATION, THE ROAD TO PEACE: RESOURCE MATERIALS ON NEGOTIATIONS 23-40 (June 1990) [hereinafter ROAD TO PEACE]; Declaration of the OAU Ad-hoc Committee on Southern Africa on the Question of South Africa, (The Harare Declaration), Harare, Zimbabwe, Aug. 21, 1989, *reprinted in* ROAD TO PEACE, *id.* at 34-41; Resolution on Negotiations and the Constituent Assembly (adopted at the Conference for a Democratic Future), *reprinted in* ROAD TO PEACE, *id.* at 72-73. While the SAG has not yet formally released its own constitutional proposals, statements by government ministers suggest that it will contain a bill of rights that incorporates universally recognized human rights. See Breier, *Two Bills of Rights Have Common Ground*, *The Star* (Johannesburg, South Africa), May 15, 1991, at 3; Johnson, *Viljoens Blueprint for New SA*, *The Star* (Johannesburg, South Africa), May 29, 1991, at 12.

139. G.A. Res. 217A(III), U.N. Doc. A/810, at 71 (1948).

140. G.A. Res. 2200, 21 GAOR Supp. 16, U.N. Doc. A/6316, at 52 (1966), *opened for signature* Dec. 19, 1966, 999 U.N.T.S. 171, 6 I.L.M. 368 (1967), *entered into force* Mar. 23, 1976.

141. G.A. Res. 2200, annex, 21 GAOR Supp. 16, U.N. Doc. A/6316, at 49 (1966), *opened for signature* Dec. 19, 1966, 993 U.N.T.S. 3, 6 I.L.M. 360 (1967), *entered into force* Jan. 3, 1976.

142. G.A. Res. 2106, annex, 21 GAOR Supp. 14, U.N. Doc. A/6014, at 47 (1965), *opened for signature* Dec. 21, 1965, 660 U.N.T.S. 195, 5 I.L.M. 352 (1966), *entered into force* Jan. 4, 1969.

143. G.A. Res. 180, U.N. Doc. A/RES/34/180 (1979), *opened for signature* Mar. 2, 1980, 1249 U.N.T.S. 14, *entered into force* Sept. 3, 1981.

144. G.A. Res. 55, U.N. Doc. A/RES/36/55 (1981), 21 I.L.M. 205 (1982), adopted without vote on November 25, 1981.

145. Organization of Africa Unity Document CAB/LEG/67/3/Rev.5 (1981) (from the OAU Ministerial Meeting on African Charter on Human and Peoples' Rights, Banjul, The Gambia), *reprinted in* 21 I.L.M. 58 (1982).

146. ILO Conventions 14 and 87 deal with the rights of industrial workers, and ILO Conven-

Based on these Conventions, appropriate development projects should be undertaken by organizations that are committed to the principle of nondiscrimination on the basis of race, color, sex, national or ethnic origin, religion, or political beliefs. Projects must also be designed to provide benefits (which could be housing, education, agricultural services, health or legal services, credit, jobs, or welfare services) on a similar nondiscriminatory basis. In addition, the development projects should be designed to ensure that all project beneficiaries have both access to the information necessary to ensure that project design and management is consistent with their needs, and the right to organize themselves to ensure that their concerns are addressed by project management.¹⁴⁷

In the specific context of a sanctions campaign, appropriate development projects must also be designed so as not to undercut the punitive aspects of the sanctions campaign. Sponsors of development activities must be able to demonstrate that the project will not translate into disguised support for the SAG. This means that development sponsors should not include SAG-affiliated organizations unless they can demonstrate that the project is able to meet the other elements of the definition of appropriate development.

Based on these considerations, it is possible to establish the following set of guidelines for identifying appropriate development projects and project sponsors:

- (a) the projects are undertaken by groups which can demonstrate that they do not discriminate on the basis of race, color, sex, religion, national or ethnic origin, or political beliefs;
- (b) the projects are intended primarily to benefit disenfranchised South Africans without regard to the gender, political or religious beliefs and affiliations, or national or ethnic origins of the beneficiaries;¹⁴⁸
- (c) neither the South African government nor organizations, including homeland and other authorities, that are financed or

tion 141 is concerned with the role of organizations of rural workers in economic and social development: Convention Concerning the Application of the Weekly Rest in Industrial Undertaking, *opened for signature* Nov. 17, 1921, 38 U.N.T.S. 3, *entered into force* May 28, 1947; Convention Concerning Freedom of Association and Protection of the Right to Organize, *opened for signature* July 9, 1948, 68 U.N.T.S. 17, *entered into force* July 4, 1950; Convention Concerning Organisations of Rural Workers and Their Role in Economic and Social Development (1975), *reprinted in* INTERNATIONAL LABOUR CONVENTION AND RECOMMENDATIONS 15 (1982). See also *Declaration of Principles and Programs of Action Adopted by the 1976 World Employment Conference*, World Employment Conference Doc. WEC/CW/E.1.

147. See Paul, *supra* note 133.

148. This criterion is designed to ensure that qualifying projects will seek to transform the racial bias of the South African political economy.

controlled by it, are involved in the design and management of the projects or in the management of the sponsoring organizations;

- (d) the project design includes mechanisms, such as channels of communication, disclosure requirements, or management structures, that will allow project beneficiaries to participate in the design and operation of the project, to remain informed about the operations of the project, and to hold the project's management accountable for their project-related activities;
- (e) the project sponsors are able to demonstrate that they either have the technical, managerial, and financial capacity to sustain the project after the initial funding is exhausted, or that they have a plan of action for developing this capacity. Where applicable, the plan must include a strategy for training local people to take over the responsibilities of outside experts;
- (f) the project design includes an evaluation procedure that will result in a project report that is available to project beneficiaries, funding agencies, and other non-governmental organizations; and
- (g) the project design includes an assessment of the project's environmental impact and a strategy for dealing with any damage caused by the project to the region's air, land, water, and wildlife.¹⁴⁹

In addition to satisfying the objectives of a development-oriented sanctions strategy, these guidelines are designed to be attractive to both South African NGOs and to potential funding sources. The criteria are sufficiently flexible that they can be used by South Africa's creditors who have funds covered by the Third Interim Arrangement of South African debt, corporations that have blocked assets in South Africa, and both commercial and grantmaking entities that are interested in getting involved in South Africa for the first time.

The generality of the definition means that it can be applied to a wide range of development projects including health, education, legal services, housing, rural development, small scale credit,¹⁵⁰ and job creation projects. The definition can also be applied to commercial ven-

149. Unlike the other criterion, the environmental criteria may not be applicable to all projects. Many projects, such as technical training and welfare projects, are in themselves "environmentally neutral."

150. Wilson and Ramphela have pointed to the urgent need for mechanisms that will provide credit to communities that historically have been denied access to credit. F. WILSON & M. RAMPHELE, *supra* note 15, at 281-83. For a more recent discussion of South Africa's developmental needs, see M. SINCLAIR, *supra* note 32.

tures, particularly those designed to promote black participation in the formal economy.¹⁵¹ Hopefully, this flexibility will facilitate South Africa's development learning process. If necessary, the guidelines can be refined as South Africa's development expertise grows.

One problem with these guidelines is that their generality raises the possibility of abuse of the development exception to the sanctions. This problem can be minimized by incorporating into the sanctions a transparent funding process that includes a mechanism for monitoring development financing activities.

A TRANSPARENT FUNDING PROCESS

Transnational bank creditors have gained experience in other debtor countries that they could apply to funding appropriate development projects in South Africa. In some countries they have worked with NGOs to convert debt into funding for environmental and development projects and for non-traditional exports.¹⁵² They have also had experience with "informal" debt conversions, in which private sector debt is converted into equity investments without the participation of the government, and in relending schemes in which debt repaid by the original borrower in local currency is reloaned to a new borrower in the debtor country.¹⁵³

These transactions usually take place in countries in which the banks have an established presence or involve NGOs that are able to convince the banks of their ability to successfully conclude sophisticated financial transactions. These conditions are not easily satisfied in South Africa. Most of South Africa's creditors do not have an established presence there and do not have well-developed links to South African NGOs or their supporters in the creditor countries. Consequently, they do not have the means to identify appropriate project sponsors or development projects.¹⁵⁴ In addition, their history in South Africa does not demonstrate a clear understanding of its developmental needs.

This suggests that a successful development-oriented sanctions strategy must incorporate a mechanism for linking South Africa's

151. See Sethi, *Economic Rights for the Disenfranchised Citizens of South Africa: A New Approach to Black Economic Empowerment*, 7 DEV. S. AFR. 17 (Feb. 1990).

152. See sources cited *supra* note 6.

153. See generally INTER-AMERICAN DEVELOPMENT BANK, *supra* note 3; UNITED NATIONS CENTRE ON TRANSNATIONAL CORPORATIONS, DEBT EQUITY CONVERSION: A GUIDE FOR DECISIONMAKERS, U.N. Doc. ST/CTC/104, U.N. Sales No. E.90.II.A.22 (1990).

154. This situation may be slowly changing as attention in South Africa begins to focus on socioeconomic issues. See, e.g., Kifner, *Planning is Begun on South African Aid Bank*, N.Y. Times, July 5, 1990, at A3.

creditors and qualifying development projects. The mechanism could be either a formal institutional structure, or an informal network of contacts between interested parties.¹⁵⁵

A formal mechanism would require the creation of institutional structures through which funds would flow from the banks to qualifying projects. For example, a coalition of NGOs in South Africa and their counterpart organizations around the world could establish a "Fund for Democratic Development in South Africa" (Fund).¹⁵⁶ To ensure that the organization promotes the types of activities that the people of South Africa desire, its board of directors, staff, and advisors should be drawn from both South African and non-South African NGOs active in development and human rights work.

The Fund or a subsidiary should be incorporated in a creditor country so that it can take advantage of any tax benefits available in the creditor country. This would enable the banks to treat any extensions of credit to the Fund or its subsidiary as a domestic rather than a South African credit. Without a specific exemption, the latter would be subject to all reserve and other regulatory requirement applicable to international and, particularly, South African credits.

The Fund would be authorized to arrange financing for qualified development projects from sources both inside and outside South Africa. Consequently, it would be able to raise funds from South Africa's creditors and corporations with blocked assets in South Africa. The Fund should be authorized to act as a direct supplier of financial

155. Both types of arrangements have been used in other debtor countries. Most debt for nature or development conversions have arisen out of *ad hoc* arrangements between NGOs, banks, and creditor governments. See, e.g., sources cited *supra* note 6. However, a number of NGOs have formed a Debt for Development Coalition and Foundation to promote such conversions. The Coalition and Foundation receives support from U.S.A.I.D.

156. A number of entities that could serve this function have been proposed. The South African Development Bank has been proposed by Peter Goldmark of the Rockefeller Foundation and is supported by the ANC. See Kifner, *supra* note 154. The U.S. Commission on Southern Africa, proposed by Congressman Dymally, would be an independent entity with a board appointed partially by the President and partially by Congress and would be mandated to raise funds for human resource development in South Africa. See H.R. 721, 102d Congr., 1st Sess., 137 CONG. REC. H823 (daily ed. Jan. 30, 1991). For the text of the bill, see House Comm. on Foreign Affairs, 101st Cong., 1st Sess., Report on H.R.2655: International Co-operation Act of 1989, at 165-67 (Comm. Print 1989) (text of bill is reprinted as Title XIII §§ 1301-1310). Ambassador Herman Nickel has proposed that Congress create an "American Foundation for a Democratic South Africa" that would seek to raise funds for a range of development activities. See *U.S. Policy Toward South Africa*, in POLICY CONSENSUS REPORTS (Johns Hopkins Foreign Policy Institute, Jan. 1990). The European Community's Kagiso Trust, which presently relies on official sources to fund human rights activities in South Africa, could be encouraged to tap private sources as well. The EC is considering broadening the mandate of the Kagiso Trust to include funding development activities. See *European Commission Proposes New Guidelines of the Special Programme in Favour of Apartheid Victims*, EUROPE (LUXEMBOURG), June 14, 1990 at 6bis (formerly EUROPE: DAILY BULLETIN). There are also a number of efforts presently underway that are designed to create such an entity inside South Africa.

assets to and a guarantor for sponsors of qualifying development projects. Further, it should be empowered to act as a merchant banker that arranges for creditors and donors to directly fund qualifying projects. The Fund could also coordinate technical assistance and development information for South African NGOs.¹⁵⁷

In order to ensure that the financing mechanism's operations conform to other elements of the sanctions strategy, the Fund and any other participating funding organizations should be required to give public reports on their activities. These reports could then be used by anti-apartheid organizations and other interested parties to monitor the activities of all participants in the process.¹⁵⁸

Informal mechanisms, which could coexist with a formal mechanism, would rely on the existing network of NGOs in South Africa and other countries to link banks with individual qualifying projects and project sponsors. These organizations would have to play the role of monitor of the system and facilitator of the financing arrangements. This places a much greater burden on NGOs, which would be responsible for both identifying the qualifying projects and helping to arrange financing packages.

ENCOURAGING BANK CONTRIBUTIONS TO APPROPRIATE DEVELOPMENT

The history of bank lending in South Africa does not demonstrate that banks have an interest in promoting appropriate development here.¹⁵⁹ It is, therefore, realistic to assume that a successful development exception to a sanctions strategy would need to both monitor bank compliance with the strategy and give banks an incentive to contribute funds to appropriate development projects.

The choice of a particular compliance mechanism depends on the role creditor governments play in the sanctions strategy. If they are active participants, the compliance mechanism should focus on regula-

157. South Africa's creditors could be a useful source of technical assistance to certain qualifying projects. They could provide business and financial skills training for project managers and beneficiaries. One benefit of such assistance would be to develop links between NGOs in South Africa and the banking community that could have spill-over political benefits for the democratic movement in the country.

158. Such reports may be legally required by the place of incorporation of the organizations. For example, in the United States, most U.S. tax-exempt, non-profit corporations are required to make annual reports to the Internal Revenue Service. I.R.C. § 501(c)(3) (1990). For implementing regulations, see 26 C.F.R. § 1.501(c)(3)(1) (1990).

159. International capital, including bank loans, was used to finance the development of South Africa's mining and industrial sectors and to support the public sector, particularly in the 1970s. See, e.g., S. LEWIS, *supra* note 14, at 62-72. The costs of this development process have been discussed *supra* notes 14-32 and accompanying text.

tory measures, particularly bank reserve and disclosure requirements. The justification for these requirements is that they are designed to protect the safety and soundness of the banks from the risks arising from their outstanding South African credits. If creditor governments do not participate, the mechanism should involve careful monitoring by NGOs of bank action, voluntary bank disclosure requirements, and shareholder and consumer action.

Compliance mechanisms can operate independently of other elements of the sanctions. If sanctions are dismantled while creditor funds remain blocked in South Africa, the compliance mechanism can still be used to encourage creditors to contribute funds towards appropriate development activities in South Africa. The various compliance mechanisms are discussed below.

RESERVE CRITERIA

It is now well understood that the apartheid system is the primary cause of South Africa's financial predicament.¹⁶⁰ Consequently, until apartheid is replaced by a more equitable and sustainable political and economic system, regulators in creditor countries cannot have complete confidence in South Africa's ability to meet all of its financial obligations in a timely fashion. Banking regulators should, therefore, require banks to protect themselves against the risk of nonpayment by either maintaining loss reserves against their South African credits or by helping to finance appropriate development projects that will help create such order in South Africa.

Since reserves are charged against a bank's income and adversely affect its income statements, a reserve requirement could act as a significant incentive for the banks to contribute funds to qualifying development projects.¹⁶¹ This incentive would be enhanced if the banks' reserves were not tax deductible.¹⁶²

160. For the background on the South African debt crisis, see *supra* notes 33-67 and accompanying text.

161. The accounting and tax treatment of reserves varies from country to country, but in all cases, reserve requirements are viewed negatively by banks. For a general discussion of the tax and accounting treatment of bank reserves in creditor countries, see J. HAY & M. BOUCHET, *THE TAX, ACCOUNTING AND REGULATORY TREATMENT OF SOVEREIGN DEBT* (Cofinancing and Financial Services Dept of the World Bank, Sept. 1989). Until December of 1990 the full amount of the general reserves could be included in regulatory capital. However, under the *PROPOSAL FOR CONVERGENCE*, *supra* note 101, at 537-38, general reserves will constitute a declining portion of regulatory capital. Since the end of 1990, general reserves in excess of 1.5% of risk-weighted assets are excluded from capital and by the end of 1992 this should be reduced to 1.25% of risk-weighted assets. *Id.* at 538-46.

162. In the United States, most bank loss reserves are not tax deductible but Allocated Transfer Risk Reserves, which are special reserves banks are required to establish against value-impaired country debt, are tax deductible. 12 U.S.C. § 3904 (1990); 12 C.F.R. § 211.43 (1990).

A reserve requirement designed to encourage specific bank actions is not unprecedented. In the United States, section 905A of the "Foreign Debt Reserving Act of 1989"¹⁶³ seeks to have additional general reserve requirements imposed on banks that do not participate in debt reduction arrangements for troubled debtor countries.¹⁶⁴

Furthermore, two countries already require their banks to maintain reserves against their South African credits. The Bank of England, under its matrix system for treatment of sovereign debt,¹⁶⁵ and the German Federal Banking Supervisory Office¹⁶⁶ require banks to maintain reserves against South African debt. In addition, the banking supervisors in Canada and France require their banks to maintain reserves against their exposure to a number of sovereign debtors which in both cases includes South Africa.¹⁶⁷

There are a number of factors that are relevant to determining the appropriate size of the reserves that the banks should maintain against their South African assets. The most important is that the purpose of the reserves is to give the banks an incentive both to fund appropriate development activity and to ensure that they get full and timely debt service from South African debtors. Therefore, the reserve requirement should not be so high as to cause the banks to lose interest in South Africa so that they sell their debts at a substantial discount or to demand such onerous terms from their South African debtors that they are likely to default. Other relevant factors are the total amount of the exposure to South Africa of all banks in the relevant country, the amount that regulators would like to see banks contribute to appropriate development projects,¹⁶⁸ and the steps South Africa is taking to correct the labor and capital supply rigidities that have effectively rendered it ineligible for IMF financial support.¹⁶⁹

163. 12 U.S.C. §§ 3901-3912 (1990); Pub. L. No. 101-240, 103 Stat. 2501 (Dec. 19, 1989).

164. For general discussion of the regulatory issues raised by debt reduction arrangements, see J. HAY & M. BOUCHET, *supra* note 161 (particularly pertinent are pp.19-21, 39-40, 51-53 and 72-73). See also INTER-AMERICAN DEVELOPMENT BANK, *supra* note 3.

165. See K. OVENDEN & T. COLE, *supra* note 82, at 129. In 1989 this reserve was equal to 5-15% of outstanding credits. For a discussion of the matrix system, see J. HAY & M. BOUCHET, *supra* note 161, at 77-86.

166. The Federal Banking Supervisory Office requires the banks to maintain special reserves against their loans outstanding to certain debtor countries, but leaves it to the banks to determine the level of the reserves. In 1989, the German banks had established reserves equal to 25-40% of their South African credits. See J. HAY & M. BOUCHET, *supra* note 161, at 59-65; K. OVENDEN & T. COLE, *supra* note 82, at 132.

167. See J. HAY & M. BOUCHET, *supra* note 161, at 35-45 (for information on Canada); *id.* at 47-56 (for information on France).

168. In order to give the banks an incentive to make the contribution, the size of the required contribution should be smaller than the size of the reserve requirement.

169. This factor is based on 22 U.S.C. § 286aa (1988) and on the assumption that the reliabil-

DISCLOSURE REQUIREMENTS

An alternative or supplementary approach to the reserve requirements is to require the banks to disclose specifically to the relevant banking regulators how they are using their outstanding South African credits to support structural adjustment in South Africa. This information should be publicly available so that organizations in South Africa and their international supporters can use it to identify possible sources of funds for appropriate development projects.

A disclosure requirement would not cause significant regulatory change in the United States. Most of South Africa's creditors already disclose significant amounts of information to banking regulators and, as publically traded companies, to the Securities Exchange Commission.¹⁷⁰ However, banks are required to disclose very little specific information about their South African credits.¹⁷¹ They do not include such information as the size of the bank's special restricted accounts with the Permanent Investment Commissions.¹⁷² These disclosures, therefore, do not provide sufficient information for anti-apartheid organizations interested in identifying possible sources of appropriate development financing.

For the disclosures to be useful to organizations that sponsor appropriate development in South Africa, each bank should provide the following information:

- (a) the level of its financial exposure to South Africa;
- (b) whether that exposure is debt covered by the Third Interim Debt Rescheduling Arrangement and its predecessor agreements and, if so, whether it is still debt outstanding to the original debtor, a new corporate debtor, or is maintained in the Special Restricted Accounts with the Permanent Investment Commissioners, or is ten year exit loans;
- (c) whether credits not covered by the Rescheduling Arrange-

ity of South Africa as a debtor must improve when it becomes eligible for IMF support. See also Morell, *supra* note 47, at 4-7.

170. For a general discussion of bank disclosure requirements, see Coombe & Lopic, *Problem Loans, Foreign Outstandings and Other Developments in Bank Disclosure*, 40 BUS. LAW. 485 (1985).

171. See, e.g., 17 C.F.R. §§ 210.9-01 through § 210.9-07 (dealing with bank holding company disclosure requirements). See also J. P. MORGAN & CO., 1989 ANNUAL REPORT 27 (1990); CITICORP, 1989 ANNUAL REPORT 29 (1990). These disclosures give information on the amount of the banks' exposure in South Africa but not on how the bank is using these assets. Also, Citicorp's 10-Q Form does not discuss any details about the Third Interim Arrangement. CITICORP, FORM 10-Q (1990). The FEDERAL FINANCIAL INSTITUTIONS EXAMINATION COUNCIL, STATISTICAL RELEASE (Jan. 9, 1991) only gives aggregated bank information.

172. For information on the PIC and the special restricted accounts, see *supra* note 73 and accompanying text.

ment have been extended to the South African public or private sector;

- (d) whether it has any other blocked assets in South Africa;
- (e) whether the bank has provided funding to any appropriate development projects in South Africa and, if so, the amount of such credits, the nature of the funded activity, and information demonstrating that the recipients of the funds satisfy the requirements for certification as an appropriate development project;¹⁷³ and
- (f) what other steps it is taking to support appropriate development projects.

For these purposes, "financial exposure" should be defined to mean any loan, as defined in section 5001(3) of the Comprehensive Anti-Apartheid Act,¹⁷⁴ plus any blocked assets. "Blocked assets" should be defined as (a) royalties, dividends, and capital repayments that are due to persons not residents of South Africa but that cannot or have not been taken out of South Africa because of the operation of South African exchange control regulations, and (b) any other payments due to persons not residents of South Africa that are presently on deposit with a bank in South Africa or an agency or instrumentality of the SAG.

This definition of "financial exposure" covers non-financial transnational corporations with blocked assets in South Africa. There is no reason that such corporations should not be encouraged to contribute some of their assets to appropriate development projects. Thus, publicly traded corporations should also be required to include the above disclosures in their annual reports.

If creditor governments do not participate and the compliance program has to be privately "imposed," anti-apartheid organizations should establish a set of disclosure requirements, based on many of the above requirements, that banks could voluntarily adopt.¹⁷⁵ An independent monitoring group could then compile a public report that development-oriented anti-apartheid groups could use to identify possible sources of funds for appropriate development.¹⁷⁶

173. This disclosure could be structured to ensure that the confidentiality of fund recipients and business proprietary information is respected.

174. 22 U.S.C. § 5001(3) (1990).

175. Many banks already have voluntary disclosure codes that can easily be amended by concerned banks to include increased disclosure on South Africa. See Coombe & Lopic, *supra* note 170, at 488.

176. There are already numerous organizations that monitor and publish information on compliance with sanctions. They could perform this service with relative ease. For some information on the activities of these organizations, see J. HANLON AND R. OMOND, *supra* note 44, at 300-65 (1987). Last year, a Panel of Experts recommended to the Commonwealth that a small

Both voluntary and involuntary disclosures are not unprecedented. U.S. banks and corporations engaged in any act or transaction subject to the terms of the Comprehensive Anti-Apartheid Act are required to keep complete records on the transactions and to furnish them on demand to the Office of Foreign Assets Control. They are also required to register any contributions to their controlled South African entities and any investments in firms owned by black South Africans.¹⁷⁷

The signatories of the Sullivan Code have regularly disclosed the actions they are taking to meet the standards of the Code to a private firm. Each year the private firm publishes an annual "report card" on the signatories' performance.¹⁷⁸

Finally, if the banks refuse to make voluntary disclosures, information can be obtained through questions at shareholder meetings and through consumer actions against particularly recalcitrant banks.¹⁷⁹ Such activities could involve not only anti-apartheid groups, but development organizations, foundations that fund development in South Africa, and investors who are concerned about the safety and soundness of banks with exposure to South Africa.

AMOUNT OF FUNDS AVAILABLE FOR APPROPRIATE DEVELOPMENT PROJECTS

It is clear that successful use of the development exception to the sanctions strategy requires a significant degree of coordination and agreement among a wide range of organizations and entities. Determining whether or not it is a worthwhile effort depends on the amount of funding it will generate and on its potential for contributing to appropriate development in a post-apartheid South Africa. There are two things that affect an estimation of the amount of money that could be made available for appropriate development during the period of sanctions.

The first is that, since the development financing aspects of sanctions must be consistent with the goal of maintaining financial pressure on the South African government, the proposed creditors' contribution to appropriate development should not be so onerous that it would reduce the banks' incentive to take appropriate actions, in-

secretariat should be established to monitor compliance with sanctions. See SANCTIONS REPORT, *supra* note 92, at 173.

177. 31 C.F.R. §§ 545.601-545.604 (1990).

178. See INDUSTRY SUPPORT UNIT INC., 14TH REPORT ON THE SIGNATORY COMPANIES TO THE STATEMENT OF PRINCIPLES FOR SOUTH AFRICA (1990).

179. See Coombe & Lopic, *supra* note 170, at 487-88. This article suggests that information can be obtained from a number of other sources including testimony and discovery incident to litigation and unauthorized disclosures by employees.

cluding judicial action, to fully enforce their rights against their South African debtors. If banks perceive the contribution as unduly burdensome, there is a real risk that they could use it as an excuse to be less vigilant in their oversight of their South African debts. This could result in a *de facto* reduction in the foreign exchange obligations of the South African government. Alternatively, it could result in the banks' selling off their South African debt, even at steep discounts, to investors who may be less susceptible to anti-apartheid pressure or may even be acting as agents of the South African government.

The second consideration is that any new funds brought into the country will ultimately contribute to its foreign exchange reserves and will therefore enhance the SAG's access to foreign exchange.¹⁸⁰ Consequently, any support for development should be generated from funds presently inside the country or should be in the form of "in-kind" support. Based on these considerations, special restricted accounts with the Permanent Investment Commissioners are the major source of potential funds.¹⁸¹

A second useful source could be the blocked assets of foreign investors.¹⁸² However, tapping into this source is much more difficult because, unlike rescheduled debt, these assets are not subject to public discussion and scrutiny. Their availability for appropriate development, therefore, depends on the goodwill of the individual asset holders.

Using the special restricted accounts to fund appropriate development will have one positive and one negative consequence on the operation of the sanctions campaign. First, it will deprive the SAG of funds that it has been using for certain public sector activities.¹⁸³ Second, the transfer of funds out of these accounts will reduce the SAG's foreign exchange repayment obligations unless funds extended for de-

180. Under South Africa's foreign exchange control regulations only "authorized dealers," primarily banks, are allowed to buy or borrow foreign exchange without special permission. See Du Plessis, *supra* note 59, at 24-27.

181. According to the March 1990 report of the Reserve Bank, there was R3869 million held from unaccounted sources in PIC accounts. S. AFR. RESERVE BANK Q. BULL., *supra* note 28, at S-44. It is reasonable to assume that the special restricted accounts constitute a significant portion of this. For information on these accounts, see sources cited *supra* note 64 and accompanying text. One commentator estimates that \$386 million (about R1 billion) of this is debt-related. See *Swiss Roll-Over*, *supra* note 113, at 37.

182. The operation of the financial rand system and the foreign exchange regulations of South Africa means that many corporations are unable to take all of their assets out of the country as quickly as they would like. The result is that they have to maintain these assets in the country until they are able to dispose of their Financial Rands to a willing foreign purchaser. See *The Bank of Lisbon and South Africa Limited*, *supra* note 60; Du Plessis, *supra* note 52, at 34. The SAG gives no information on the amount of blocked assets.

183. See sources cited *supra* note 71.

velopment are repaid into these accounts.¹⁸⁴

With the above considerations as background, some estimate of the amount of funds that could be available for development can be made. The total payments due from South Africa to all creditors during the term of the third interim arrangement, including payments on the ten year exit loans, are expected to be between \$1.1 and \$1.7 billion per year, of which U.S. banks will receive between \$50 and \$244 million per year.¹⁸⁵ Thus, if all creditors used only one percent of the annual payments due to them to fund development projects in South Africa, it would generate more than \$10 million per year.¹⁸⁶ This estimate does not include possible contributions from holders of blocked assets. Also, commercial ventures can qualify as appropriate development projects. Consequently, banks may be persuaded by profit-making possibilities to contribute a considerably higher portion of their funds to appropriate development projects.

The size of the bank contributions could be increased by enabling them to take advantage of any tax or other benefits that may be available under their domestic law.¹⁸⁷ They could receive some reward for making particularly generous contributions. For example, they could take a deduction in their contribution requirement if the grant element in their financing exceeds a stipulated percentage.¹⁸⁸ This could help ensure that at least some funds are made available on better than commercial terms.

While the amount of funding may be small relative to South Af-

184. *Id.*

185. J. LIND, *supra* note 112, at 4. Lind estimates that total annual debt payments due from South Africa will equal \$2.2 billion in 1990, and \$1.5 billion in 1991, 1992, and 1993, and that total payments to U.S. banks will equal \$50 million in 1990, \$89 million in 1991, \$138 million in 1992, and \$244 million in 1993. Another commentator, Edward Osborn, chief economist of Nedbank, estimates total payments at \$1.7 billion in 1990, \$2.1 billion in 1991, \$1.1 billion in 1992, and \$2.6 billion in 1993. See *Swiss Roll-Overs*, *supra* note 113, at 37.

186. This is equal to about R36 million at present exchange rates.

187. For example, in the United States, banks may be able to claim a tax deduction for any funds that they donate to qualifying development projects. Whether or not this is possible will depend on whether the recipient is registered as a charitable, educational, or religious organization under Section 501(c)(3) of the Internal Revenue Code. See I.R.C. § 501(c)(3)(1990). This means that qualifying recipient organizations will have to operate through a U.S. counterpart even though the funds are used in South Africa. See I.R.C. § 170(c)(1990); INTERNAL REVENUE BULL., Rev. Rule 63-252, 1963-2, C.B.101 (interpreting the language of I.R.S. § 170(c), and noting situations where a charity organized in the United States can deduct contributions to foreign charitable organizations). See also B. HOPKINS, *THE LAW OF TAX-EXEMPT ORGANIZATIONS* 815-19 (5th ed. 1987).

188. One possible method for doing this would be to calculate the grant element according to the formula used by the Development Assistance Committee of the O.E.C.D. This formula compares the present value of the future payments due on the financing with the face value of the funds being provided. DEVELOPMENT ASSISTANCE COMMITTEE OF THE ORGANIZATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, *TWENTY-FIVE YEARS OF DEVELOPMENT CO-OPERATION: A REVIEW* 171-73 (1985).

rica's total development needs, it is significant to NGOs that are operating in a hostile political and economic environment. They can use the funds to support projects that provide goods and services to the victims of apartheid and that improve their development know-how and organizational capacities. These projects will not only provide some development assistance during sanctions, but will also help South Africans prepare for a post-apartheid future. In this sense, the resources can make a significant contribution to the structural adjustments required to create a democratic post-apartheid South Africa.

CONCLUSION

The above analysis demonstrates that South Africa's debt problems have a lot in common with those of the debtor countries of Latin America and Eastern Europe. Its debt problem, like theirs, was caused by a flawed development strategy, mismanagement of the domestic economy, and unfavorable international economic and financial developments. Similarly, the solution to South Africa's debt problem depends on correcting those structural elements in the country's political economy that caused the debt problems and that inhibit sustainable development.

Viewed from this perspective, it is clear that financial sanctions should have been perceived as part of a structural adjustment program designed to promote the democratic, political, and socioeconomic transformation of South Africa. Measured against this standard, the financial sanctions campaign cannot be considered a success. While it may have contributed to recent political changes in the country, the campaign missed an opportunity to support appropriate development activities in South Africa.

The sanctions campaign's failure was primarily caused by the anti-apartheid movement's single-minded focus on the punitive potential of the debt crisis.¹⁸⁹ This led to an inaccurate assessment of the SAG's and the banks' relative bargaining strengths. As a result, the sanctions campaign failed to pay adequate attention to either the developmental potential of sanctions or the role that support for appropriate development could play in the process of defeating apartheid.

This paper demonstrates that the anti-apartheid movement could have corrected this failure, without any real sacrifice in the financial pressure imposed on the SAG, by incorporating into the sanctions an

189. In this sense, the failure of the anti-apartheid's financial sanctions campaign bears some resemblance to those IMF structural adjustment policies that have been criticized for an over-emphasis on macroeconomic factors at the expense of the distributional and social aspects of economic development. See sources cited *supra* note 1.

appropriate development exception. This development exception could have been structured to only generate financial support for development and commercial activities that are consistent with the principles of sustainable, efficient development, and with international human rights standards.

Two interesting conclusions can be derived from this analysis of the South African case. The first is that the proposed development-oriented financial sanctions technique can be used against any country that violates any of its citizens' human rights and in which foreign enterprises, particularly banks and other creditors, have blocked assets. The use of this technique will ensure that sanctions can both help modify the behavior of the offending government and strengthen the ability of its victims to promote their own human rights and developmental interests.

The second lesson is that the key elements of the proposed appropriate development criteria are not necessarily dependent on the peculiar characteristics of South Africa or of a human rights-related sanctions campaign. These criteria can also be used by development and human-rights NGOs to test the developmental appropriateness of any proposed development project and to promote dialogue on the linkages between human rights and sustainable development. It would indeed be a fitting tribute to the participants in the anti-apartheid struggle if its successes and failures could be used by those concerned with human rights and development to devise more effective ways of promoting human rights and sustainable development.