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DEBT-FOR-NATURE SWAPS: ASSESSING THE FUTURE

Stimulating conservation while ameliorating debt would encourage progress on both fronts.¹

Environmental action adds a new dimension to the fight against global poverty. It recognizes that sound ecology is good economics. Indeed the objectives of sustainable economic growth, poverty alleviation and environmental protection are often mutually reinforcing.²

INTRODUCTION

In recent years, approaches to solving the mounting debt problems of the developing countries (DCs) have primarily focused on the relationships between industrial country performance and the opportunities for DCs to increase exports to achieve economic growth.³ Environmental and conservation organizations (ECOs) have, however, forcefully argued that economic growth, without regard for environmental well-being and natural resource conservation, will ultimately undermine the potential for long-term sustainable growth and “increas[e] the future costs of correcting the environmental destruction inflicted now.”⁴ In seeking solutions to their debt problems within the conventional framework of export-led growth, DCs are often encouraged to emphasize cash crop monocultures and intense exploitation of their natural resources for short-term gain.⁵ These myopic schemes

³. THE WORLD BANK, 1989 ANNUAL REPORT 26. The total external indebtedness of the developing countries was $993.2 billion as of the end of June 1989. Id. at 30. It is currently estimated at approximately $1.3 trillion. WORLD RESOURCES INSTITUTE, NATURAL ENDOWMENTS: FINANCING RESOURCE CONSERVATION FOR DEVELOPMENT 8 (Sept. 1989) [hereinafter NATURAL ENDOWMENTS] (available from World Resources Institute, Washington, D.C.).
⁵. Debt Crisis, supra note 4, at 192. A recent article notes that “[m]any Third World
are often carried out to the detriment of existing and sometimes fragile ecosystems, including tropical rainforests, wetlands, watersheds, and grasslands.6

The debt crisis has presented opportunities for encouraging better environmental management of these ecosystems and for further bolstering the relationship between economic well-being and the environment.7 As the market value of such debt has declined, a number of debtor DCs, especially in Latin America, have exchanged certain amounts of debt with creditors for equity holdings in local commercial and industrial enterprises in the debtor DCs.8 These transactions, known as "debt-for-equity" swaps, allow creditors to sell foreign-denominated debt at a discounted amount of the original face value to purchasers in the international secondary debt markets, who in turn convert it to equity holdings in the debtor DC.9 One type of debt-for-equity swap is that pioneered by the ECOs known as "debt-for-nature" swaps.° Unlike debt-for-equity swaps, purchasers in debt-for-nature swaps do not take title to an asset. These transactions involve private banks selling amounts of debt owed to them by DCs to private ECOs. The ECOs then forgive the debt in return for specific environmental commitments, such as conserving a particular tropical rainforest or wetlands area and providing for

countries depend greatly for their development prospects on the natural resource base . . . that sustains much of their economic activity. For instance, in Central America about one-fourth of gross domestic product is based on natural resources; these resources also account for more than one-half of all employment and for most export earnings." Meyers, Environment and Security, 74 FOREIGN POL'T 23, 24 (Spr. 1989) (emphasis added). See also Auferheide & Rich, Environmental Reform and the Multilateral Banks, 5 WORLD POL'T J. 301, 302 (Spr. 1988) [hereinafter Auferheide & Rich].
6. Debt Crisis, supra note 4, at 192.
8. THE WORLD BANK, 1988 ANNUAL REPORT 27.
9. Id. In a debt-for-equity transaction, a foreign company, usually working through an intermediary bank, proposes a debt-for-equity transaction with the debtor country's government. Once officially approved, the company purchases portions of the country's debt through the intermediary bank in the international secondary debt market at a substantial discount. The company subsequently presents the debt instrument to the debtor country's central bank for redemption in local currency (greater than the amount paid for the original debt instrument, sometimes as much as face value) at the official exchange rate. The debt is officially retired and the company uses the local currency to make an equity investment in the debtor country. Note, International Debt: Debt-to-Equity Swaps, 28 HARV. INT'L L.J. 507 (1987). See also Blackwell & Nocera, The Impact of Debt to Equity Conversion, 25 FIN. & DEV. 15 (June 1988) (available from the World Bank, Washington, D.C.). The international secondary debt market developed "so that banks could swap loans among themselves, thereby avoiding overexposure to any single troubled economy," but came increasingly to be used for swapping debt for equity by commercial investors. Debt for Trees, supra note 4, at 2. See also Weinert, Swapping Third World Debt, 65 FOREIGN AFF. 85 (Winter 1986-87).
10. Debt for Trees, supra note 4, at 3.
its maintenance with local currencies made available by the debt forgiveness.\(^1\)

This Comment focuses on two aspects of this type of environmental initiative. First, this Comment will examine debt-for-equity transactions known as "debt-for-nature" swaps to see what is involved in carrying out such a transaction and what such swaps have accomplished to date. Second, the Comment will assess what future, if any, such transactions may have in reducing the overall debt of the DCs and in enhancing their environments. The purpose is to discern what measure of viability such debt-for-nature transactions have achieved as debt relief mechanisms and what success they have had in establishing linkages between conservation of natural resources and achieving long-term sustainable development in DCs.

In order to fully assess the viability of debt-for-nature swaps, the Comment will first examine the general nature of this complex transaction to see how debt is exchanged for nature. Second, it will provide a brief overview of the debt-for-nature swaps that have been arranged to date, identifying the parties involved in the transaction and describing what was accomplished. Finally, this Comment will explore the future of such swaps and their role in debt relief and in enhancing sustainable growth.

I. WHAT IS A DEBT-FOR-NATURE SWAP

A. Overview

Arranging a debt-for-nature swap is a complicated and technical financial transaction involving a number of variables. Although each debt-for-nature swap arranged to date differs in certain respects, there are common characteristics. Generally, the typical debt-for-nature swap involves a five-step process. The first step involves the sponsoring ECO (located in the United States or Europe) obtaining approval from the debtor country. Specifically this entails gaining the approval of the three main actors involved: the government, the central bank, and perhaps most important, a private ECO. The debtor country ECO will receive the funds and manage the resulting conservation program. Arguably, the sponsoring ECO is in the most difficult position, as it must not only relinquish effective control over the funds in order to avoid "sovereignty" questions,\(^2\) but also must act as guarantor for the continued responsible use of such funds to domestic donors and tax authorities.\(^3\)

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12. See *infra* notes 119-22 and accompanying text.

A wide range of issues may be raised in negotiations with the debtor country's government, including setting the exchange rate used in converting the debt into local currency and designating a local agent to control the funds and dispense the proceeds. In addition, the agreed upon conservation program is designed to address local priorities, and therefore may include specific projects or more general environmental and conservation objectives.

The second step in the transaction involves identifying and acquiring the debt instrument. The sponsoring ECO literally shops for the best available denomination debt notes that are acceptable to the debtor country. Typically, an ECO either buys or receives as a donation the external debt of a DC. The debt may be purchased in the international secondary debt market where prices range from a few cents on the dollar to parity. The price serves as an indicator of risk — the closer to parity the less risk involved. The money needed to acquire the debt can be raised either through traditional fundraising techniques or may be donated outright. Outright donation of the debt presents a new and otherwise inaccessible source of funds to the sponsoring ECO. Other options include "sale at a preferential price or donation of cash" for purchase of the debt on the market; the choice is often dictated by the tax status of the parties.

The third step, transfer of the title to the debt, is often the most complex. Three principal methods of debt transfer have arisen out of debt-for-nature transactions negotiated to date. The method chosen has usually been dictated by financial and tax-related factors, and in some instances accounting considerations. Methods of debt transfer include: (1) the acquisition of the debt by the sponsoring ECO in the creditor country, which in turn donates it to its partner ECO in the debtor DC; (2) the donation of the necessary resources to the partner ECO allowing direct acquisition of the debt; and (3)

15. 1 WORLD WILDLIFE FUND LETTER, supra note 14, at 8.
16. The debtor country retains effective control over approval of such transactions because the debt cannot be freely disposed of in these markets by the bank due to covenants entered with debtor countries in the course of debt rescheduling negotiations. von Moltke, supra note 13, at 1-2. The price of the debt depends on the buyer's and the seller's opinion of its value, which, in turn, depends on a number of variables, including its likelihood of repayment and its value in any debt-equity swap. U.S. Accounting: A Summary, in NATIONAL WILDLIFE FEDERATION/WORLD WILDLIFE FUND, DEBT FOR NATURE: AN OPPORTUNITY (1989) (available from either National Wildlife Federation, Washington, D.C. or World Wildlife Fund, Washington, D.C.).
17. von Moltke, supra note 13, at 2.
18. Id.
finally, donation of the debt directly to the partner ECO, which acts as the creditor country's agent. The fourth step entails the actual conversion by the debtor DC's central bank of the acquired debt into a local currency instrument, i.e., local currency bonds, measures to protect designated areas, cash payment of local currency, or some combination of the above. The fifth and final step — the actual objective of the swap — is the implementation of the conservation program. Again, the creditor country or sponsoring ECO may have the most at stake, since it is required to not only relinquish effective control of the funds, thereby placing them at risk, but must also assure donors and tax authorities that these funds will be used properly and in accordance with the agreement.

B. Debt-for-Nature Swaps Negotiated to Date

Several factors combined in late 1986 and in 1987 to provide a conducive atmosphere for the first debt-for-nature swaps. One major factor was that a growing number of commercial banks began to conclude that large portions of their debt portfolios, especially in Latin America, were uncollectible. This conclusion led the banks to "write-down" or sell high-risk debts at considerable discounts, thereby increasing activity in the international secondary debt market. In addition, many DCs undertook debt-for-equity transactions, redeeming portions of their debt in local currency by allowing debt-holders to take equity interests in commercial and industrial enterprises. Indeed, the initial "debt-for-nature" opportunities emerged from the debt-for-equity concept as debtor countries and private lenders became frustrated by the failure of conventional mechanisms to alleviate the mounting debt crisis, and, as a result, began to consider unconventional solutions.

The United States Treasury Department provided further impetus for undertaking such transactions in issuing a favorable revenue ruling in November 1987. The ruling essentially clarified the tax treatment of possible

19. Id. Hansen notes that at least four different debt-for-nature swap schemes have been proposed: (1) conversion of debt by the Central Bank into local currency or local debt bonds to be held by the local ECO; (2) donation of debt to a local ECO for investment in environmental projects; (3) purchase of debt by an ECO and discounted sale to a multinational corporation to support environmentally sound investments; and (4) official debt relief tied to supporting environmental management. Hansen, supra note 11, at 78.

20. von Moltke, supra note 13, at 2.

21. Id.


25. Rev. Rul. 87-124, 1987-2 C.B. 205. See also Banks Are Offered Way to Write Off
gains and losses arising from conversion of debt to equity, as well as donations of debt instruments to charitable organizations for environmental or other social purposes in DCs. The ruling permits lenders that donate debt to ECOs to take a tax deduction equal to their cost basis in the debt. Prior to issuance of the ruling, tax laws limited the charitable deduction to the mar-

Third World Loans, Wall St. J., Nov. 19, 1987, at 44, col. 3. Prior to the issuance of this ruling, the ECOs had been pursuing legislative solutions. The ECOs welcomed this ruling, but were concerned as to whether the ruling would apply in particular debt transactions or countries then under consideration. The Treasury Department effectively addressed these issues in an April 1988 interpretive ruling, enhancing debt-for-nature transaction possibilities and eliminating the need for specific legislation. See 1 WORLD WILDLIFE FUND LETTER supra note 14, at 8. See also Fuller & Williamson, supra note 24, at 303.

With regard to legislation concerning debt-for-nature swaps, to date three measures have been passed into law. The first of these was the 1987 Continuing Resolution, Pub. L. No. 100-202 § 537, 1987 U.S. CODE CONG. & ADMIN. NEWS (101 Stat.) 1329 which contained language directing the Treasury Department to promote environmentally sustainable economic growth through the multilateral development banks and to report to Congress on debt reduction initiatives involving conservation activities. An April 1988 Treasury report stated that debt-for-nature swaps directly involving these institutions could not be a part of the “menu” of options because loans from these institutions were not “saleable in the secondary markets, cannot be converted to grants for environmental purposes, and are not reschedulable.” The report did, however, recommend a number of initiatives, including a debt-for-nature pilot project to increase the World Bank’s technical assistance and support role in debt-for-nature transactions and conservation programs in general. The second piece of legislation was the Foreign Operations Export Financing, and Related Programs Appropriation Act 1989 (Pub. L. No. 100-461, 1988 U.S. CODE CONG. & ADMIN. NEWS (102 Stat.) 2268), which referenced language exhorting the World Bank and the African Development Bank to expand their advisory roles and encourage debt-for-development swaps for “human welfare and environmental conservation.” See Cody, Debt-for-Nature Swaps in Developing Countries: An Overview of Recent Conservation Efforts, Congressional Research Service, Library of Congress, Rept. No. 88-647, 24-26 (Sept. 26, 1988). The third piece of legislation was the International Development and Finance Act of 1989 (Pub. L. No. 101-240, 1989 U.S. CODE CONG. & ADMIN. NEWS (103 Stat.) 2492) which, inter alia, (1) authorized the Agency for International Development to make grants to non-governmental organizations for use in debt-for-nature swaps in DCs, (2) established a pilot program of debt-for-nature exchanges focusing on sustainable agriculture for sub-Saharan Africa, (3) encourages the Secretaries of State and Treasury to make global warming and other environmental factors a priority in U.S. bilateral and multilateral assistance programs, and (4) requires the Secretary of Treasury to include support for conservation and sustainable development in debt reduction programs. Id.

Market value of the loan when such value was below the cost basis of the loan, as is the case with many of the loans to the DCs. Thus, if a lender donated such debt to an ECO, it would be unable to recover its entire basis through the charitable deduction. Doing so would place the lender in a worse position than if it sold the debt and donated the proceeds to charity. The ruling rectified this situation by placing the lender in the same position regardless of whether the debt is donated, or sold and the proceeds donated.

While the ruling alleviated certain problems associated with these transactions, questions of how to value both the loan loss and the charitable contribution deductions were left unanswered. This situation, combined with the general lack of financial incentives and banks' traditional reluctance to donate assets, has produced a marked lack of response by the banks. To date only two banks have donated portions of their debt to U.S. ECOs.

Despite the general skepticism of the banking community regarding debt-for-nature swaps, nine such swaps have taken place to date in six countries: Bolivia, Ecuador, Costa Rica, the Philippines, Madagascar and Zambia. A summary of these transactions follows.

27. Generally, the amount of the deduction for a charitable contribution of property to a § 501(c) (3) organization is the fair market value of the property at the time of the contribution. Treas. Reg. § 1.170A-1(c) (1988). In the case of a sale of ordinary income producing property, such as DC debt held by a commercial bank, the amount of deduction is reduced by the amount of ordinary income realized, thus limiting the deduction to the donor's adjusted cost basis. I.R.C. § 170(e) (1988).

28. See DfN Exchange, supra note 26, at 25 & n.14. The related question of whether such deductions are to be counted against foreign source or domestic source income was addressed in late April, 1989. The IRS issued a notice which provided that charitable contributions may generally be taken against domestic source income, while loan loss deductions are to be apportioned between domestic source and foreign source income. I.R.S. Notice 89-58, 1989-1 C.B. 699.


30. It was earlier believed that Fleet National Bank had used this revenue ruling to donate its debt to The Nature Conservancy in its debt-for-nature transaction with Costa Rica. Cody, Debt-for-Nature Swaps: A Brief Overview, Congressional Research Service, Library of Congress, Rep. No. 88-489, 4 (July 12, 1988). However, in a later report, Cody notes that according to William Penn, senior vice president for Fleet, uncertainty surrounding the IRS ruling led Fleet to write the donation off as a loss, instead of treating it as a charitable donation. Cody, Debt-for-Nature Swaps in Developing Countries: An Overview of Recent Conservation Efforts, Congressional Research Service, Library of Congress, Rep. No. 88-647, 15 n.25 (Sept. 26, 1988); see also DfN Exchange, supra note 26, at 25-26. In December 1988, an affiliate of Chase Manhattan Bank donated approximately $400,000 of Bolivian debt to Conservation International, but again, tax benefits did not appear to be the primary motivation behind the donation. Id. Also in December of 1988, Midland Bank, PLC, in the first donation of debt by a British bank, donated $800,000 of Sudanese debt to UNICEF, which exchanged the debt for an undisclosed amount of local currency to finance a rural water purification project. Id. at 25 n.16 (citing Thirst Quencher, ECONOMIST, Dec. 24, 1988, at 87.).
I. Bolivia / Conservation International

In the first negotiated debt-for-nature swap, Conservation International, a Washington, D.C. ECO, purchased $650,000 of Bolivia's commercial bank debt to finance and ensure protective management of over four million acres of tropical forests and grasslands. Citicorp Investment Bank acted as Conservation International's agent in the international secondary debt market. The debt was purchased at approximately an eighty-five percent discount of its face value. In addition, the Frank Weeden Foundation provided a $100,000 grant to finance this transaction.

The terms of the agreement, signed July 13, 1987, provided that in return for cancellation of Bolivia's obligation to pay the $650,000 debt, Bolivia would give maximum legal protection to the Beni Biosphere Reserve and increase to 3.7 million acres the protected areas abutting the reserve. Bolivia also agreed to establish a local currency operating fund totaling $250,000 to manage the reserve and the protected areas. The reserve, located in northeastern Bolivia, supports thirteen endangered species, five hundred species of birds, and the nomadic Chimane Indians. Management of the reserve will emphasize using the forests and grasslands in a sustainable manner to benefit all regional peoples, thus protecting the ecosystem and preserving the traditional lifestyle of the Chimane.  

32. Bolivia Agreement, supra note 31, at cl. 3; Bolivia Sets Precedent, supra note 31, at 1.
33. The Bolivia Case, supra note 31.
34. Id.
35. Id. See also Bolivia Sets Precedent, supra note 31, at 2.
38. But see Collett, Bolivia Blazes Trail . . . to Where?, Christian Sci. Monitor, July 10, 1989, at 4. Chimane and Moxo Indian leaders claim that conservation measures are being subordinated to commercial logging interests. Under the terms of the debt swap, Conservation International agreed to assist the government of Costa Rica in supervising logging efforts in the Chimanes Permanent Forest, the largest of three areas comprising a buffer zone around the Beni Biosphere Reserve. These logging efforts, and additional logging concessions granted by the government just prior to implementing the debt-for-nature swap, were implemented without consulting the Indian tribes. These concessions conflict with existing uses of the forest area
remained under the control of the Bolivian government, "sovereignty" issues and accusations of foreign intervention were essentially avoided.\(^3\)

Responsibility for carrying out these environmental programs rests with a national commission composed of local officials of the Beni region, scientists from the Ecology Institute and the Beni Biological Station, and a representative from the environmental coalition Liga de Defensa del Medio Ambiente (LIDEMA).\(^4\) Administration of the operating fund rests jointly with the Bolivian Ministry of Agriculture and the national commission.\(^4\)

2. Ecuador

   a. World Wildlife Fund

In an agreement signed December 14, 1987, World Wildlife Fund arranged to purchase one million dollars in debt from the Central Bank of Ecuador for $354,000 to be converted to nine-year local currency bonds.\(^4\) The bonds will finance a broad range of conservation activities in Ecuador's national parks by Fundacion Natura, a leading Ecuadorian conservation group.\(^4\)

The Ecuadorian government issued the bonds at the full amount of the debt note which were converted to the local currency, sucres, at the official exchange rate.\(^4\) The principal will become an endowment for Fundacion Natura, while the interest generated by the bonds will pay for a variety of programs, including management plans for protected areas, development of park infrastructure, acquisition of small nature reserves, training of park personnel, and environmental education activities.\(^4\) In addition, Fundacion Natura will act as a conduit to support the efforts of other private conserva-

by the semi-nomadic tribes, who also fear further encroachment by settlers via the roads built by the logging concerns. Conservation International has apparently been the recipient of funds from the logging interests, in particular the International Timber Trade Organization, a Japanese-based organization, and has sided with the government of Costa Rica in opposing the tribes' desires to establish integrated tribal areas in the region. \(\text{Id.}\)

40. Id.
41. Id. Bolivia Agreement, supra note 31, at cl. 11.
43. Ecuador Agreement, supra note 42, at §§ 1 & 2; The Ecuadoran Case, supra note 42; Fuller & Williamson, supra note 24, at 302.
44. Ecuador Agreement, supra note 42, at § 1; The Ecuadoran Case, supra note 42.
45. Ecuador Agreement, supra note 42, at §§ 1 & 2; The Ecuadoran Case, supra note 42; see also Fuller & Williamson, supra note 24, at 302.
tion groups.46


In the second debt-for-nature swap with Ecuador, World Wildlife Fund, The Nature Conservancy and Missouri Botanical Garden collaborated to purchase a total of nine million dollars of debt from American Express Bank and Morgan Guaranty Trust Company.47 The debt will be converted on a one-to-one basis into nine million dollars worth of eight-year local currency bonds. This transaction was initiated by Fundacion Natura, the lead conservation organization in Ecuador's first debt-for-nature transaction.48

Using the interest generated by the bonds, Fundacion Natura will fund park acquisition and management projects in the Andes, the Ecuadorian Amazon region, and the Galapagos Islands.49 In addition, the interest will also fund local training of conservation professionals and the creation of a conservation data base for the collection and storage of information concerning Ecuador's biological diversity that will allow for more scientifically accurate conservation and development planning.50

World Wildlife Fund will purchase $5.4 million of the debt package from Morgan Guaranty Trust Company, and The Nature Conservancy will purchase $3.6 million of the debt from American Express Bank, including $400,000 purchased on behalf of the Missouri Botanical Garden. The entire debt package cost $1.069 million.51

3. Costa Rica

a. The Nature Conservancy & World Wildlife Fund

In the second largest of the debt-for-nature swaps to date, the Costa Rican government agreed to a debt exchange program allowing the pooling of

46. Ecuador Agreement, supra note 42, at §§ 2(b) & 3; Ecuadoran Case, supra note 42.
49. Ecuador, supra note 47, at § 2. See also TNC News, supra note 47, at 2.
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funds from debt donors to finance a broad spectrum of environmental programs. The agreement, signed March 4, 1988, permitted the purchase of up to $5.4 million (the government has recently agreed to allow possibly as much as $55.4 million) in Costa Rican external debt for $891,000 from the American Express Bank and Bankers Trust. The debt will be exchanged for local currency bonds, the proceeds of which will be used to establish a Costa Rican National Resources Conservation Fund. Fundacion de Parques Nacionales, a leading Costa Rican conservation organization, will administer the fund.

Many lending institutions provided the debt notes for the swap, including Fleet National Bank of Rhode Island (part of the Fleet/Norstar Financial Group, Inc.), which donated $254,000 of Costa Rican debt to The Nature Conservancy. This donation made Fleet the first U.S. financial institution to donate outright a portion of the foreign debt it holds for charitable purposes. Pooled funds to purchase the debt were provided by a number of ECOs and charitable foundations.

The Costa Rican debt was purchased at approximately an eighty percent discount and was exchanged for bonds offered at seventy-five percent of face value.

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55. Costa Rica Agreement, supra note 54, at Preliminary Statement ¶ 4 & ¶ 1; *The Costa Rican Case*, supra note 54.

56. *The Costa Rican Case*, supra note 54; Sun, Costa Rica’s Campaign for Conservation, 239 SCIENCE 1366, 1367 (Mar. 18, 1988); see also supra note 30 and accompanying text.

57. These included The Nature Conservancy, World Wildlife Fund, Asociacion Ecologica La Pacifica, the Pew Charitable Trust, the MacArthur Foundation, the J.S. Noyes Foundation, the Swedish Society for the Conservation of Nature, the W. Alton Jones Foundation, the Organization for Tropical Studies, and Conservation International. ECOs entering into debt swap agreements with Costa Rica may specify particular projects they wish to fund. *The Costa Rican Case*, supra note 54; *DfN Exchange*, supra note 26, at 15.
value carrying an average of twenty-five percent interest.\textsuperscript{58} Because the bonds cannot be immediately sold under the arrangement, only the interest payments are immediately available for environmental projects.

The National Resources Conservation Fund will be used to acquire additional property for "wildlands" protection, as well as to manage and protect existing parklands.\textsuperscript{59} In addition, the Fund will finance environmental education and conservation training programs and other activities related to developing the sustainable use of natural resources, including reforestation, and innovative work with local populations to prevent deforestation. One of the most important recipients of these funds will be the Guanacaste National Park Project, which involves the purchase of land located between existing parks and reserves to allow the restoration of a dry tropical forest.\textsuperscript{60}

\subsection*{b. Conservation International}

In a second debt-for-nature transaction with Costa Rica, Conservation International transferred \$50,000 to the Fundacion de Parques Nacionales.\textsuperscript{61} These funds will be used to purchase \$215,000 of Costa Rican debt.\textsuperscript{62} This \$215,000 will be paid in monetary stabilization bonds, which in turn will be placed in the National Resources Conservation Fund.\textsuperscript{63} Interest generated by these bonds will be earmarked to finance resource conservation and development in Costa Rica's La Amistad Biosphere Reserve.\textsuperscript{64}

The La Amistad Biosphere Reserve, designated in 1982, contains two national parks, two biological reserves and five indigenous reserves occupied by two distinct cultures, the Bribri and the Cabecar. The 612,000 hectare (approx. 1.5 million acres) reserve encompasses a variety of plant communities, ranging from premontane rainforest up through cloud forest and temperate oak woods to alpine meadow scrub.\textsuperscript{65} Animal life is diverse; rare and endangered mammals inhabiting the reserve include all six tropical cat species, the giant anteater, and the tapir, as well as over four hundred species of birds.\textsuperscript{66}

\begin{itemize}
\item \textsuperscript{58} The Costa Rican Case, supra note 54.
\item \textsuperscript{59} Costa Rica Agreement, supra note 54, at Attachment.
\item \textsuperscript{60} Costa Rica Agreement, supra note 54, at Attachment & § 2.
\item \textsuperscript{62} The transaction takes into account the rate at which Costa Rican debt was then selling (17 cents/$1) and a twenty-five percent redemption fee being charged by the Central Bank of Costa Rica. Costa Rica News Release, supra note 61, at 2.
\item \textsuperscript{63} Id.
\item \textsuperscript{64} Id. at 1-2.
\item \textsuperscript{66} Id.
\end{itemize}
c. The Nature Conservancy

On January 12, 1989, The Nature Conservancy announced that it had concluded the largest private debt-for-nature swap to date with the government of Costa Rica. The transaction involved the purchase of $5.6 million of discounted Costa Rican debt for $784,000 from American Express Bank, a subsidiary of American Express Company. The debt, totaling over $1.7 million under the renegotiated terms, will be converted to Costa Rican currency bonds which, at an average annual interest of twenty-five percent over five years, are expected to generate over $3 million for vital conservation projects. Projects to be funded include park protection, conservation training, educational programs, biological inventories, and land acquisition at nine parks or reserves in Costa Rica encompassing over 355,000 acres.

The transaction was initiated by the Fundacion de Parques Nacionales and authorized by the Costa Rican Natural Resources Ministry and the Central Bank. The American Express Bank provided valuable technical assistance and has agreed to assist and advise The Nature Conservancy on future debt-for-nature transactions. The Nature Conservancy received additional assistance in this transaction from the Stroud Foundation; the MacArthur Foundation; the J.S. Noyes Foundation; the W. Alton Jones Foundation; The World Wildlife Fund; the government of the Netherlands; the Swedish Society for the Conservation of Nature; and the People’s Trust for Endangered Species based in the United Kingdom.

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69. *Id.*

70. *Id.* at 2.

71. *Id.* at 1.

72. *Id.* at 2.

73. Although not much is known concerning the details of the transactions, Costa Rica has recently entered into debt-for-nature swaps with the governments of The Netherlands and Sweden. *DfN Exchange, supra* note 26, at 16. Within the context of its bilateral aid program with Costa Rica, the government of The Netherlands will exchange over $30 million of commercial bank debt for local currency bonds equalling 33% of the principal amount of the debt. Proceeds generated by the bonds will finance various reforestation projects in Costa Rica. *Id.* The government of Sweden has also negotiated a debt-for-nature swap, purchasing approximately $25 million of commercial bank debt, also to be exchanged for local currency bonds equalling 70% of the principal amount of the exchanged debt. Proceeds will fund the completion and endowment of the Guanacaste National Park. *Id.* n.8.

4. Philippines / World Wildlife Fund

In the first example of a debt-for-nature swap in Asia, World Wildlife Fund signed an agreement with the Philippine government on June 24, 1988, allowing it to acquire up to two million dollars in Philippine debt. Initially, World Wildlife Fund will acquire debt worth $390,000 at a discount of fifty-five percent of face value, which will be converted by the central bank to a local currency account managed by the Haribon Foundation, a leading Philippine ECO. The participation of other ECO or donor agencies is encouraged by the agreement.

Initial funds made available by this transaction will benefit two parks on Palawan Island, the St. Paul Subterranean River National Park, which includes an underground river and caverns as well as mountain forests and coastal areas, and El Nido National Marine Park, which encompasses reefs surrounding smaller islands off the northwest tip of Palawan. Projects to be funded include management plans, buffer zone acquisitions, research and environmental education activities, training for local community resource managers, and fellowships for graduate students in conservation-related areas. Funds will also be used to aid the government's efforts to halt illegal trading and exploitation of wildlife resources, survey critical areas, and plan for an integrated system of protected areas. Use of the funds is restricted only in that they cannot be used to pay non-Philippine consultants and must be devoted to national projects.

5. Madagascar / World Wildlife Fund

World Wildlife Fund announced August 3, 1989, that it had signed a debt-for-nature agreement with the Central Bank of Madagascar, the first in Africa, which would allow for an exchange of up to three million dollars of


76. WWF News Release, supra note 75, at 3; The Philippines Case, supra note 75.
77. Philippines Agreement, supra note 75, at § 3.
78. WWF News Release, supra note 75, at 2; The Philippines Case, supra note 75.
79. Philippines Agreement, supra note 75, at § 2(a); The Philippines Case, supra note 75.
80. The Philippines Case, supra note 75.
81. Philippines Agreement, supra note 75, at § 2(b).
Malagasy debt at one hundred percent of its principal amount over the next two years.\textsuperscript{82} World Wildlife Fund has actively supported conservation efforts in Madagascar for over twenty-four years.\textsuperscript{83} Even more importantly, the U.S. Government, through the Agency for International Development (AID), will provide substantial financial support, possibly as much as one million dollars of the transaction's total funding costs.\textsuperscript{84} Bankers Trust Company, which had previously assisted World Wildlife Fund in its debt-for-nature swaps in Ecuador and the Philippines, arranged a European syndicate of seven commercial banks to participate in the transaction.\textsuperscript{85}

World Wildlife Fund will initially use $950,000 to redeem approximately $2.1 million in Malagasy debt, at a rate of 45 cents on the dollar.\textsuperscript{86} World Wildlife Fund currently has plans to convert the remaining $900,000 (under the $3 million ceiling) over the next two years.\textsuperscript{87} AID will cover hard currency expenditures in the amount of $300,000 associated with the transaction.\textsuperscript{88}

Proceeds from this transaction will fund conservation projects over a three-year period in Madagascar's high priority protected areas and to train,
equip and support four hundred park rangers. A recent study of the island's protected areas (home to a vast array of unique plant and animal species) revealed that all were threatened by rapid deforestation due to slash-and-burn cultivation, illegal logging, poaching, drainage of wetlands or over-grazing by cattle and goats.

6. Zambia / World Wildlife Fund

On August 15, 1989, Dr. Henner Ehringhaus, Deputy Director of World Wildlife Fund International, announced the signing of a $2.27 million debt-for-nature swap with the Central Bank of Zambia, the second in Africa. World Wildlife Fund has been active in Zambia since 1962. In addition, this swap is the first transaction involving European funds and arranged by a European bank — NMB Bank of The Netherlands.

World Wildlife Fund is purchasing the total debt for approximately $470,000, a discount of eighty percent. Over half the purchase price came from an anonymous Swiss donor who had specifically requested that the money be used for debt-for-nature swaps in Africa.

II. Whither Debt-for Nature Swaps?

A recent article, co-authored by attorney Bruce Rich of the Environmental Defense Fund, states that "[c]learly, debt-for-nature swaps, no matter how successful, are not an answer to international debt," noting that Conservation International's debt swap "reduced Bolivia's $4.1 billion external debt by only $650,000." Rich further stated, however, that such transactions offer a unique opportunity to induce DCs to "shift priorities" and emphasize resource management and conservation. Obviously, therein lies the crux of debt-for-nature transactions. Will the unique opportunity these transactions offer in terms of resource conservation accompanied by only minimal debt relief be enough of an inducement for DCs to use such transactions at a time of growing international tension due to the mounting debt crisis which

89. WWF News Release Madagascar, supra note 82, at 3; DfN Exchange, supra note 26, at 17.
92. Id. at 2.
93. Id. at 1.
94. Id.
95. Id.
97. Id.
they face? It is a question that is not easy to answer. Examining the salient advantages and disadvantages and limits of debt-for-nature transactions will shed some light on possible answers.

Assuming that an appropriate debt instrument can be obtained and that the various interests of the parties, (i.e., the ECOs, the banks, and the debtor DC) involved in a debt-for-nature swap can be reconciled, one of the most important limitations in concluding a successful transaction would seem to be the presence of an effective partner ECO in the debtor DC. The successful agreements concluded to date have taken place in DCs where there were longstanding relations between the initiating or sponsoring ECO, such as The Nature Conservancy or World Wildlife Fund, and the debtor DC partner ECO. Indeed, one expert has warned that debt donations for DCs "where no effective conservation organizations exist need to be viewed with extreme caution," as the primary issue is ensuring proper use of the funds once relinquished.

Ensuring proper use is complicated in transactions involving agreements with a sovereign government. On the one hand, without enforcement mechanisms, continued adherence to the agreement appears to rest on the DC's perception of how damaging failure to implement the agreement would be to its economic and political status. On the other hand, the agreements are the product of mutual negotiations, the "swap" concerns control of local currency not land, and the funds remain wholly in the DC for use by local ECOs for the conservation and sustainable development of "national" natural resources, such as parks, forests or wetlands. Such an agreement would seemingly provide a large measure of security, trust and accountability, given the DC's vested interest in the implementation of the agreement.

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98. For a more in depth analysis of the various interests of the actors at stake in a debt-for-nature swap see von Moltke, supra note 13; see also Hansen, supra note 11.
99. See Debt-for-Nature Agreement, supra notes 31, 33, 35, 38, 39, 41, 42, and 44.
100. von Moltke, supra note 13, at 2.
101. Id. at 5.
102. Hansen, supra note 11, at 83.
103. Id. Hansen suggests that a debt-for-nature swap take the form of compensation that can be stopped if the agreement is not strictly adhered to, e.g., annual or periodic compensation payments to force the country to abide by rather than breach the agreement. It has also been suggested that bilateral and multilateral governmental institutions be required to consider the DC's observance of its debt-for-nature transactions prior to granting foreign aid. DfN Exchange, supra note 26, at 28.
104. Debt for Trees, supra note 4, at 3-4.
105. Id. See also DfN Exchange, supra note 26, at 29 (concludes that such "transactions are neither less nor more inherently vulnerable... than any other conservation investment in a foreign country, unless the... exchange requires a long-term financial commitment on the
A more difficult question is "whether debt-for-nature swaps contribute significantly to the stabilization" of DC external debt. In those DCs where such transactions have taken place to date, the total volume of debt-for-nature swaps is relatively small in comparison to the principal amount of debt. One expert has argued that such transactions relative to annual interest payments on the principal appear more important. Even more significant, the expert contends, is the comparison of such transactions as against the effective annual rise in principal attributable to a country's inability to service its debt. Most DCs are in fact making partial interest payments, the balance in practice being added to the principal. Since virtually no new real loans are being made, a DC's debt situation could be considered stabilized when interest payments are not causing an increase in indebtedness. Thus, when measured against this standard, debt-for-nature swaps "indeed make a noticeable contribution towards a more viable [DC] debt situation." Debt-for-nature swaps have, however, taken place only in those DCs labeled by the World Bank as "heavily indebted" and/or only in those DCs whose debts are heavily discounted in the international secondary debt market. Obviously, such countries are attractive to ECOs because of their limited budgets.

DCs must also resolve the question of whether debt-for-nature transactions and their resulting programs represent an unnecessary intrusion on their sovereign rights, a form of "eco-imperialism." Critics of these debt-for-nature transactions have charged that these swaps "undermine the sovereignty of the government," and then it becomes subject to the vicissitudes of political change.

106. von Moltke, supra note 13, at 3-4; see also Auferheide & Rich, supra note 5, at 320.
107. von Moltke, supra note 13, at 3.
108. Id. at 3-4.
109. Id. at 4.
110. THE WORLD BANK, 1989 ANNUAL REPORT 25 (Table 2-3). The "heavily indebted" countries include Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Cote d'Ivoire, Ecuador, Jamaica, Mexico, Morocco, Nigeria, Peru, Philippines, Uruguay, Venezuela, and Yugoslavia. Id.
111. "As of December 1987, Bolivian debt was selling at between 8 and 10% of face value, Peru between 5 and 7%, Costa Rica 20 to 22%, Zambia 17 to 19%, and Nigeria 25 to 27%. The major economies of Brazil and Mexico . . . are not perceived to be such bad risks, as their debt is selling at around 42% and 52% respectively." Debt for Trees, supra note 4, at 2.
112. ECOs, because of limited budgets, are drawn to DCs "whose debt sells at large discounts in order to make the most of their contributions." Trouble in Paradise, 2 SWAPS 9 (Nov. 1988). Michael Sweatman of the World Resources Institute, has stated that ECOs "tend to concentrate on countries where there is more leverage and more value for your dollar." Id.
The sovereignty question is likely to continue to be a barrier to overcome in DCs, such as Brazil, despite the fact that ECOs do not seek to conserve capital as a goal per se, but seek to give away money for conservation. Many DCs, in fact, do not allow significant levels of capital formation in ECOs and other nonprofit groups, placing them in an advantageous position to transact debt-for-nature swaps, since the threat of losing capital is not as likely as in the case of debt-for-equity swaps by commercial investors. Moreover, the debt-for-nature swap mechanism requires the debtor DC and the local beneficiaries "to agree upon the purpose to which the proceeds of the exchange are being put, therefore ensuring that the investment being financed is responsive to both national and local interests." This amounts to a "litmus test" of sorts; presumably those transactions that do not comport with these interests will not be authorized.

One other key question is whether banks can be induced to participate more actively in debt-for-nature swaps. Despite the tax ruling explained earlier, to date only banks holding limited amounts of DC debt are seeking to dispose of these assets because they find that the uncertainties of valuation and the complexities of future participation in renegotiating and reschedul-
ing such debt outweigh the residual economic benefits of holding the debt.\textsuperscript{123} Because their debt holdings are small, these banks can dispose of them without undermining their overall financial strength.\textsuperscript{124} Thus, donation of the debt may prove the most efficient way of disposal by "avoiding the uncertainties of the international secondary debt market and generating some publicity and goodwill."\textsuperscript{125} However, to date, only two banks have donated debt.\textsuperscript{126} Others have yet to follow.

With regard to tropical deforestation, it has long been recognized that large-scale deforestation can contribute to regional and global environmental change and thus affect vital interests of the industrialized countries.\textsuperscript{127} In fact, tropical rainforests are seen as one of the primary beneficiaries of debt-for-nature swaps because such transactions can provide vital assistance to debtor countries who have been forced to cut back on conservation programs in order to service their debts while simultaneously reducing emissions of greenhouse gases and thereby benefiting all countries.\textsuperscript{128} ECOs have also been pursuing alternatives which have achieved a modicum of success,\textsuperscript{129} such as adding environmental conditions to aid and loans provided by the World Bank, the International Monetary Fund, and other multilateral development banks. Few mechanisms, however, have been discovered that allow creditor countries to protect important natural ecosystems and to contribute to sustainable management of forest and other natural resources in debtor DCs.\textsuperscript{130} Under the right circumstances, debt-for-nature swaps may prove the most effective means of achieving such ends.

One fear is that debt-for-nature swaps may be a response to a specific economic situation that may not continue for much longer.\textsuperscript{131} To date, almost all such transactions have been consummated by U.S. ECOs,\textsuperscript{132} the

\begin{itemize}
  \item \textsuperscript{123} von Moltke, \textit{supra} note 13, at 3.
  \item \textsuperscript{124} Id.
  \item \textsuperscript{125} Id. One Nature Conservancy official believes that the debt restructuring process may provide a means of raising donations. As part of the negotiations, participating banks would be asked to donate, as a gesture of good will, a small percentage of the debt for a special "debt-for-development fund." \textit{Trouble in Paradise}, 2 SWAPS 10 (Nov. 1988).
  \item \textsuperscript{126} See \textit{supra} note 30; see also Fuller & Williamson, \textit{supra} note 24, at 303.
  \item \textsuperscript{127} von Moltke, \textit{supra} note 13, at 4.
  \item \textsuperscript{128} Wirth, \textit{supra} note 7, at 17-20; see also Gradwohl & Greenberg, \textit{Saving the Tropical Forests} 23-53 (1988). One author argues that indeed "the dominating rationale for concentrating debt swaps to equity in the form of natural reserves/tropical habitat is the rich countries' demand for habitat preservation and their concern for the global commons." Hansen, \textit{supra} note 11, at 88.
  \item \textsuperscript{129} See Aufderheide & Rich, \textit{supra} note 5; \textit{Debt Crisis, supra} note 4.
  \item \textsuperscript{131} von Moltke, \textit{supra} note 13, at 5.
  \item \textsuperscript{132} But see \textit{supra} note 40.
\end{itemize}
majority with Latin American countries. Negotiations have been initiated with Peru, Jamaica and Brazil. Certain U.S. ECOs believe great potential exists for such swaps in Africa, beyond those concluded in Madagascar and Zambia. They concede, however, that they might have to be differently structured since most African debt, over seventy percent, is owed to governments and public lending institutions, such as the World Bank and other multilateral institutions, and the possibilities of debt swaps involving such public held debt is unknown. Certainly the multilateral development banks could potentially play a critical role in facilitating such exchanges either by allowing debt owed to them to be used, although critics have pointed out that such activity might jeopardize their credit ratings, or by providing transactional assistance to commercial bank debt-for-nature exchanges. A long term solution to the debt crisis negotiated by the banks with the DCs might eliminate the need for such countries to consider debt relief in the form of such swaps. On the other hand, if such a solution is not reached, most debt will be written down to a level that renders it worth-

133. Debt for Trees, supra note 4, at 4.
134. Id. Government lenders and the World Bank “are not in a legal or political position to redeem debt at a discount,” although there is ongoing consideration of debt-for-nature transaction possibilities using different financial mechanisms. European banks have also consulted World Wildlife Fund concerning the possibility of using outstanding loans in developing countries and Eastern Europe for conservation purposes. WORLD WILDLIFE FUND LETTER, supra note 14, at 7. There have also been numerous proposals for the creation of a new international debt reduction facility, affiliated or in some way associated with the World Bank. See Debt Reduction OK, But How Much?, 16 DEV. FORUM (July-Aug. 1989) (available from the World Bank, Washington, D.C.); Speth, Bargaining for the Future: Debt Relief and Climate Protection (Jan. 1989) (available from World Resources Institute, Washington, D.C.); Bramble & Millikan, External Debt, Democratization, and Natural Resources in Developing Countries: The Case of Brazil 6 (June 27, 1989) (available from National Wildlife Federation, Washington, D.C.).
135. For a further discussion of such possibilities see DfN Exchange, supra note 26, at 37-40; see also World Resources Institute, Natural Endowments: Financing Resource Conservation for Development (Sept. 1989) (available from World Resources Institute, Washington, D.C.).
136. On July 24, 1989, the Mexican government announced that it had reached an agreement with its commercial bank creditors on a comprehensive debt reduction package. If implemented, the agreement would reduce by 35% the face value of the banks’ $54 billion worth of loans to Mexico, a strategy long advocated by U.S. Treasury Secretary Nicholas Brady under his so-called “Brady Plan.” Debt Reduction Agreement Is Reached With Mexico, Wash. Post, July 24, 1989, at A1, col. 1. For further information on the Brady Plan, see The Brady Plan, INT’L. ECON. 39-61 (May/June 1989). African countries were offered just such large scale relief when the Paris Club rescheduled debt of the sub-Saharan countries providing “essential breathing space.” WORLD BANK, 1988 ANNUAL REPORT 27. Moreover, the G7 countries at their July, 1989 summit recommended that “banks should increasingly focus on voluntary, market-based debt and debt service reduction operations, as a complement to new lending.” Summit of the Arch, Economic Declaration, 10 (July 16, 1989) (available from the International Monetary Fund, Washington, D.C.); see also Rowen, Leaders at Summit Warn Bankers on Third World Debt, Wash. Post, July 17, 1989, at A1, col. 4.
less for the purposes of a debt-for-nature swap.137

CONCLUSION

It is clear that there are many factors working against debt-for-nature transactions as either long-term solutions to the DC debt crisis or as a mechanism to achieve significant conservation of resources or sustainable development in a large number of the DCs.138 They are products of complex negotiations requiring a confluence of factors that has occurred in only a few countries. Those countries are unique to some extent in that they are either members of the "heavily indebted" group or possess not only longstanding political ties with the U.S. but also longstanding ties between U.S. and debtor DC ECOs. Moreover, much of the debt of these countries is held by private lending institutions and despite the presence of a favorable tax ruling in the U.S., only two banks have donated debt so far. Thus, additional "new source" dollars for conservation have not been realized.

If these transactions are viewed modestly, however, as augmenting currently insufficient debtor DC investments in natural resource conservation and sustainable development, they are achieving what had heretofore been deemed impossible to achieve. In addition, debt-for-nature swaps have focused attention on the steadily depleting resource base of the debtor DCs, in particular tropical rainforest resources, which have been, in recent years, the focus of increasing global concern. At the same time, such transactions have strengthened ties between ECOs in the respective countries and provided these organizations with new leverage and expertise in political and economic venues which they previously did not possess.139 Likewise, debt-for-nature swaps have played an important role in involving the business and banking communities in conservation. Moreover, these transactions have affected the lives of local communities and indigenous peoples within the debtor DCs, providing them with new jobs, a market for new products, in

137. von Moltke, supra note 13, at 5.
139. Indeed, Barbara Bramble of the National Wildlife Federation has stated that:
   one of the chief goals of debt-for-nature swaps is to fortify local conservation groups:
   "The local groups learn how to talk to their government in financial terms and if it is
   a debt-for-nature-bonds arrangement, the local money ends up in accounts which
   benefit these local groups, giving them stability, financial security, and experience
   managing projects."
   nonprofit organizations should be minimal. They can act as a conduit of funds donated by
   banks, they can provide assistance to local groups in negotiating with the central banks, and
   they can help develop conservation projects and . . . accounting standards." Id.
some cases land rights, and with income that will work to sustain these achievements. Perhaps most importantly, they have provided a model for financial institutions and ECOs to emulate in finding even more innovative solutions in addressing positively and fairly the problems of debt and resource depletion in order to achieve the admirable objective of sustainable development.

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