Overview of the Legal Framework for Public Debt Management

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1. Introduction

The legal framework outlines the rules and steps that establish ways through which decisions should be made regarding public debt. A robust legal framework is critical for effective Public Debt Management (PDM) as it helps to promote accountability and transparency as well as order and discipline, while safeguarding debt managers from political influence. All of which are critical to achieving sustainable public debt.

Internationally, the PDM framework consists of a maze of laws at various levels, spanning from supranational, national and sub-national legal frameworks. Zambia's legal framework is in alignment with the international frame as demonstrated below.

Sources of PDM Legal Framework

Supranational

• Treaties of SADC, COMESA and international bodies: Several Acts authorise the application of international law in Zambia including the: International Development Association, Cap. 361; Bretton Woods Agreements Act, Cap. 367; and International Finance Corporation, Cap. 368. These Acts enable Zambia to be a member of, and therefore eligible to borrow from the respective institutions.

The Constitution (Amendment) Act No. 2 of 2016 - Zambia

• Remains the primary source of the Law. It distributes political structures and powers, allocates fiscal powers including taxing authority and sets basic institutional arrangements including the authority to borrow and pay for debt related costs and expenses. It also sets the requirements for audit and reporting.

Primary Legislation

• Dedicated debt legislation - The Loans and Guarantee's (Authorisation) Act No. 13 of 1994, contains the prescribed public debt management laws, Government loan laws, treasury securities laws, and other prescriptions, which provide more specifically for mandates, institutional, and operational matters relating to public debt management;

• Public Financial Management (PFM) legislation - Includes budget laws, PFM or administration laws, and fiscal responsibility laws. The current operational PFM law in Zambia is the Public Finance Management Act No. 1 of 2018. Once enacted, the National Planning and Budgeting Bill of 2019 will establish the framework for budget preparation and execution, cash management, public debt, accounting, auditing, and reporting. Additionally, it will enshrine debt objectives in the primary legislation with the aim to build a culture of transparency and accountability. However, Zambia is currently basing its planning and budgeting decisions on the National Budgeting and Planning Policy approved by Cabinet

in 2018. There are no dedicated fiscal responsibility laws in Zambia, they are nonetheless encompassed in the PFM Act; and

• Others - Include other relevant laws such as Central Bank laws, Public Procurement Laws, etc. Central Bank laws typically provide for Government borrowing (if any) from Central Banks, and the Central Bank's role as fiscal agent to Government.

Secondary Legislation

• Regulations, rules and guidelines. For instance, those set by fiscal agents in governing the market for Government securities.

Adapted from Awadzi, A. E. (2015) Designing Legal Frameworks for Public Debt Management

Aside from the international laws, Zambia is also party to regional agreements. One regional PDM example is the requirement under the Fiscal Convergence Programme in the Common Market for Eastern and Southern Africa (COMESA), where the standard for government budget deficit (excluding grants) is set to 3% of Gross Domestic Product (GDP). Additionally, COMESA prohibits the Central Bank from financing the budget deficit and requires that "total debt as a ratio of GDP is reduced to sustainable levels" . This provision prescribes a regional constraint on public debt and overall fiscal policy by which Zambia should abide.

Zambia's PDM legal framework is correspondingly embodied in other levels of legislation. At the supreme level of the Constitution, Part XVI broadly guides PDM. Specific provisions are laid out in subsidiary legislation dedicated to PDM in various Acts of Parliament, while secondary legislation is contained in different sets of regulations, "ministerial orders" or statutory instruments and rules.

2 Legal Framework guiding the mandate to borrow and issue new debt

Zambia's PDM legal framework gives the authority to borrow both domestically and externally. The Constitution gives general broad provisions while specific provisions for loans are given in the subsidiary legislation.

2.1 The Constitution (Amendment) Act No. 2 of 2016

The Constitution of Zambia Act No. 2 of 2016 is the Supreme Law of the Republic of Zambia. According to Article 1, it requires that all laws i.e. written law or customary law be consistent with it and it further states that any law which is inconsistent with its provisions is void to the extent of its inconsistency. It is on this basis that it is the main and primary source of law in Zambia. Within the Constitution, there are established across-the-board public finance requirements including the authority to borrow and pay for debt related costs and expenses, the scope of debt, as well as other procedures. In accordance with Article 65 of Act No. 2 of 2016, the Government may, among other things, raise or guarantee a loan or grant on behalf of itself or other state organs, as well as undertake repayment of the loans by introducing in the National Assembly, the Money Bills.

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Part XVI – covering Articles 198 - 212 of the Amended Constitution of 2016, stipulates the governance of public finances and the budget. Article (198) (c) lays down the guiding principle of sustainable borrowing to ensure inter-generation equity while Article 200 requires the establishment of a Consolidated Fund. The purposes of the fund include to be credited with all monies received in respect of a loan or grant approved and for the defraying of interest payments.

The powers to borrow and lend are enunciated in Article 207 Sub Article 1 (a) and (b) of the Amended Constitution. The Government may raise and/ or guarantee loans or grants on the State's behalf as well as on behalf of other State organs and other institutions. Article 207 Sub Article (2) provides that legislation enacted for borrowing and lending – (the Loans and Guarantees Authorisation Act (LGAA) in this case) shall provide for the category, nature and other terms and conditions of a loan, grant or guarantee.

Within the Constitution also under Article 207 (2)(a), there is a requirement that before a loan, grant or guarantee is executed, approval by the National Assembly is required. Loans to be contracted by the State and guarantees on loans contracted by State institutions or other institutions are to be submitted by Cabinet to the National Assembly for approval. Thus, assigning parliamentary oversight on the contraction of public debt by the Executive. Further, the words used in this provision of law make the approval by the National Assembly mandatory before the loan, grant or guarantee is executed.

For the Constitution, the general PDM provisions are sufficient. However, these specifications need to be further prescribed in subsidiary legislation for them to be effectively implemented.

2.2 The Loans and Guarantees (Authorisation) Act No. 13 of 1994

The Loans and Guarantees (Authorisation) Act No. 13 of 1994 is the primary legislation used for public debt in Zambia and it is the Act through which the broad pronouncements of the Constitution are to be prescribed. This is also stipulated in the Constitution (Amendment) Act No.2 of 2016 in Article 207 (2). The Act, authorises general borrowing, and grants power for the raising and granting of loans, guarantees and indemnities; specifies methods of raising loans; provides for the establishment of a sinking fund; and other supplemental debt related matters.

According to provisions of this Act in Part II, particularly in Section 3, the Minister of Finance is empowered to borrow and raise loans on behalf of the Government as he may deem desirable and should not exceed at any one time the amount/ ceiling he is authorised by the National Assembly. Under this particular provision, the only authorisation required from the National Assembly that is referred to is for the prescription of the amount/ceiling of the loan and such authorisation is from time to time. The methods by which a loan may be raised include, the issuing of bonds or stock, treasury bills or by agreement in writing. The only other party recognised in the finalisation of the loan contraction process is Cabinet, of which the Minister of Finance is party to. Further, Section 7 provides that any loan raised under this Act shall be raised in accordance with such conditions and terms as the Minister shall direct.

2.3. Other Legislation

In Zambia, PDM is also regulated by other legislations that provide additional legal support to the primary legal framework (Text Box 2). One salient Act with significance to the PDM framework is the Public Finance Management (PFM) Act No.1 of 2018.

Primary and Secondary Legislation Guiding Public Debt Acquisition in Zambia

- The Loans and Guarantees (Authorisation) Act No. 13 of 1994
- The Public Finance Management Act No. 1 of 2018
- The Treasury Bills Act No. 161 of 1965
- The Bank of Zambia Act No. 43 of 1996
- Local Loans (Registered Stock and Securities) Act No. of 1994
- The Development Bond Act No. 13 of 1994
- The Loans and Guarantees (Maximum Amounts) Order No. 25 of 2014
- The Loans (Local Registered Stock) (No. 3 and No. 4) Regulations
- The Loans (Stock, Bonds and Treasury Bills) Regulations
- The Development Bond Regulations

Adapted from Banda-Muleya. F. & Nalishebo. S. (2018) 'Reversing Zambia's High Risk of Debt Distress'

2.4 The Public Finance Management (PFM) Act No. 1 of 2018

The PFM Act in Zambia is limited to authorising the setup of institutions to manage and control PFM, and it also includes a section on financial misconduct which, however, only legislates on disciplinary procedures, but misconducts are not deemed to be criminal. The Act also grants the mandate for external audit to the Auditor General. The objective of this Act is to provide for oversight and accountability by detailing an institutional and regulatory framework for the management of public funds. The Act therefore, focuses on the use of public funds including debt after its contraction and hence its appropriation.

Part II Section 4 establishes the Treasury, with the Minister as its head, to make policy and decisions on behalf of the Government, which is explained in Section 5. Efficiency, effectiveness, transparency and accountability in the generation of revenue of the Republic is a requirement provided in Part III Section 20 of the Act. According to Section 27, all repayments of monies borrowed by the Minister, interest payable and costs, charges and expenses of managing the debt shall be charged against the Consolidated Fund and this is in line with the Constitution. Government's tool for consolidating and managing public finances or the Consolidated Fund was operationalised in 2016 and called the Treasury Single Account (TSA). All revenues and proceeds of debt are deposited into this account and before appropriations are undertaken, they require Parliament's approval. However, there is granted within the PFM Act discretion to the Secretary to the Treasury to open other working accounts which do not require Parliamentary approval before expenditure.

Interestingly, in other jurisdictions for instance Kenya and South Africa , PFM Acts play a clear-cut fundamental role in the management of public debt. The PFM Acts in these jurisdictions are comprehensive, restrictive and all-encompassing to include directions on national planning and budgeting, loans and guarantees, and general treasury matters including the determination of disciplinary and criminal procedures on misconduct. More specifically for the case of South Africa, according to their PFM Act No.1 of 1999 the Minister of Finance may, among other things, borrow to finance any purpose approved by the National Assembly by special resolution.

2.5 Secondary Legislation

Within Zambia's secondary legislation various guidelines are given for the enhancement of PDM. For instance, the Development Bond Regulations set a limit to the maximum holding of bonds and the incumbent amounts. However, while the setting of a specified ceiling is appreciated it presents some flaws. Specific bounds face the risk of becoming impractical when the country's economic growth performance is low. Besides, it is not clearly stated whether the country's ability to pay back is taken into consideration when coming up with these ceilings or not. It would have been more prudent if the ceiling figures were stipulated in line with the country's GDP.

3. Shortcomings identified in the LGAA

In light of the legislation that has been outlined, discordance arises on the final authorisation function on debt contraction between the LGAA whose final authority is Cabinet and the Amended Constitution which calls for debt to be approved by the National Assembly before contraction. Indeed, provisions in the LGAA remain contrary to virtues of good governance practice. Separation of roles and responsibilities and thus power in the management of a country is a necessity and should be extended to public debt as well, to promote unbiased decision-making and promote checks and balances in the management of debt.

The process that is followed when contracting loans is vague, hence there is no standard procedure to guide loan negotiators. For instance, for public external debt acquisition, a request for financing for a particular project will be submitted to the Investment and Debt Management Office (IDM) of the MoF. The IDM will then approach potential funders for the project or the line Ministries can specify the funders. If the terms of financing are in line with the set benchmark at MoF, a draft agreement is then prepared which is approved by the Attorney General. Then the negotiated terms of the loan are presented to Cabinet for final approval and then executed by the Minister in Charge of Finance.

More often than not, the clauses, terms and conditions are set by the lenders and investors as can be seen with the external agreements, as well as the financial agreements of the Eurobonds and the domestic Bonds bided competitively. Of importance should be the financial implications of the agreements. However, the Government does not have a lawyer who is well abreast with such issues to advise the negotiators, but they request for advice from the treasury counsel.

On another note, the legal framework calls for revenues generated from loans with periods of less than 1 year to be paid into the Special Deposit Account; and for periods exceeding 1 year, into General Revenues of the public. So, while the Constitution calls for only one fund which is the Consolidated Fund or the General Revenues fund, an additional account for loans raised for a period of not more than 1 year is also maintained, another provision that requires revision in the revised LGAA.

Majorly, the vehicle through which loans are to be redeemed or paid off as envisaged by the Act is through the creation of a Sinking Fund, for loans raised for a period of more than 10 years. From this fund, both interest and principal loans are to be paid out. Despite this, the Act does not stipulate the amounts that are to be contributed to the fund or in what frequency. But it is clear that the intent is for the Fund to be sufficiently serviced with funding that provides for redemption of loans, upon the expiry of the period of such loan, of not less than 75% of the principal. Without the rider on the periodic funding, the Sinking Fund provision falls short of a distinct yardstick and creates room for non-compliance to it. Nonconformity to the requirements of the provision in the Act are observed with Zambia's current Sinking Fund .

Additionally, transparency and accountability are is not encouraged as there are no provisions for sanctions on debt managers for mismanagement for not following procedure. There are no requirements for audits, transparency and accountability, nor any penalties stipulated for abrogating the LGAA. This makes it difficult to put on the right track those responsible for debt management and help stakeholders audit, assess and measure the effectiveness of the debt, policies the management and their implementation.

Lacking in the LGAA are the purposes for borrowing. The non-description of situations in which the Government can obtain borrowed funds has probably been one of the major reasons why borrowing has been undertaken to majorly finance budget deficits and not investments.

Within the LGAA, prescription of the scope of the Government's debt includes guarantees and indemnities of other State organs and institutions. But what is not clear is whether this extends to debts arising from the privatisation of State-Owned Enterprise's (SoEs) or funds used for solving problems of bankruptcy of credit institutions like Development Bank of Zambia and the Credit Guarantee Scheme, or the expenses for environmental remediation, etc. otherwise known as contingent liabilities.

The Act is also silent on whether subnational entities can undertake borrowing on their own behalf. For instance, India in 2011 had an alarming rate for its subnational debt recorded at 25% of its GDP because of this ambiguity. The absence of stipulated actions on such incidences lead to potential risks for public debt sustainability. Without which, it is difficult to know the true reflection of the country's total contingent and public debt alluded to in the 2013 Auditor General's report concerning Zambia's MoF.

Contrary to the belief that debt ceilings are austere and restrictive, most governments actually use them to make borrowing easier. The larger an endorsed ceiling, the more debt a country can accrue. Statutory instrument (SI) 53 of 1998, introduced the debt ceiling at K20 billion (or K20 trillion at the time) until 2014 when it was raised to K35 billion within the Loans and Guarantees (Maximum Amounts) Order No. 25 of 2014. The ceiling was increased further to K60 billion in 2015 and by over 100% to K160 billion in 2016. There is need to strategically set debt ceilings to ensure that they allow for sufficient borrowing during robust economic times and curtail borrowing during harsh economic periods.

4. Recommendations to Strengthen The Public Debt Management Legal Framework

Following the analysis above, below are the key recommendations:

Recommendation	Explanation
1. Amend the Loans and Guarantee's Authorisation Act	The legislation in its current form leaves room for discretion for the responsible authorities. In the current LGAA, the National Assembly role remains limited to approving the debt ceilings and the Money Bills even though the Constitution requires the National Assembly to approve all contracted debt. Therefore, there is need to align the LGAA to the Constitution as it the Supreme Law of the Land, as it will provide for step by step procedures on the requirement that final loan authorisation be passed by the National Assembly. This will facilitate that terms and conditions of the loans are also debated in Parliament as is with case in South Africa. The amended LGAA should also make it a requirement that the Treasury Counsel or the Attorney General is involved in the negotiations of debt contracts and not just to give comments, which in turn should also be debated in Parliament. By making it mandatory for legal personnel to be involved in the negotiations, this will also encourage that all loan agreements are agreed upon under local laws and jurisdictions. This will enhance redemption, conversion and or the consolidation of loans. Agreements should include Collective Agreement Clauses (CACs) as the use of CACs has become the norm under English Law. The presence of CACs in the loan agreement can facilitate creditor-debtor negotiations in a restructuring situation. Apart from only having the Sinking Fund as the means of redemption, whose presence in the law is not backed by a requirement of consistent periodic funding, the Sinking Fund provision should prescribe how often and when the funds should be credited and clear guidance given on the percentages required. The LGAA should also be amended so as to specify what borrowed monies should be used for. This will help to safeguard against borrowing for speculative investments and borrowing to finance expenditures that have not been included in the annual budget or approved by the legislature.

2. Expand the definition of public debt clarify this from a legal perspective, because this has varying policy implications for the types of public instruments and institutions that are governed by the requirements of the PDM legal framework.	The scope of government debt needs to be widened. Contingent liabilities to be covered in the central government borrowing should be explicitly stated and adjusted and those contingent debts not covered should be given clear constraints (e.g. the case of South Africa). The framework can also be enhanced by restricting amounts that the government can guarantee (e.g in Kenya) to allow for accurate, adequate and consistent calculations of the nation's public debt.
3. Strategically set the debt ceilings as a percentage of GDP in the PDM legal framework.	Ceilings expressed as ratios allow for debt to move in line with the performance of the economy, such that in harsh economic times borrowing may be curtailed and encouraged in robust economic times.
4. Debt management should ensure consistency between fiscal and monetary policy.	In other jurisdictions such as Kenya, the legal framework mandates the Central Bank to assess the possibility of crowding out effects on the private sector, arising from Government borrowing whenever raising Government securities. A similar provision should be made in Zambia and could be achieved through requiring the undertaking of annual debt sustainability analysis in the law. The results of the analysis would help with the formation of strategies that would protect economic growth in the domestic economy.
5. Allow for audit, accountability, transparency and sanctions	The Government should move towards full disclosure of information and data related to public debt. Openness should cover information on borrowing plans and what they intend to achieve, the sources and uses of public debt, the interest rates and amounts to be paid on the debt as well as effects of the exchange rates and how often and when the principle will fall due. Information of this nature will additionally give auditors a basis to take part in the management of public debt thus, within the law, there should be provided clarified audit tasks and responsibilities. Auditors should be responsible for examining and certifying data of all kinds of public debt and debt indicators, clarifying the purpose of debts, evaluating the effectiveness of the used debts, examining the debt payment, and defining the security and sustainability of public debt and should be conducted annually. Additionally, an enforcement mechanism should be provided for that will address non-compliance to procedures governing the utilisation of borrowed funds such as failure to provide regular reports as provided for by the law and failure to account for the utilisation of such funds.
6. Include Civil Society Organisations as distribution channels of information on debt.	The laws should also outline the role of Civil Society Organisations in the contraction and utilisation of public debt. CSO are also key in the sensitisation and dissemination of information to the general public regarding public debt.

Endnotes

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