

MEMORANDUM

TO: Officials of the United States Government

DATE: February 22, 2002

RE: Default by China of Full Faith and Credit Bonds: 40% of Proceeds to Benefit U. S. Government and Many American Communities

Summary of Plan to Donate Bonds or Proceeds to U. S. Treasury

The People's Republic of China owes American bondholders billions of dollars for defaulted gold denominated bonds that it refuses to pay. These U.S. bondholders respectfully seek the assistance of the United States government in obtaining payment from China of these lawful full faith and credit obligations. The bondholders¹ have formed the American Bondholders Foundation to pursue their claims against China and, in cooperation with the United States Government, to donate 10% of the bonds (or proceeds) -- in **addition** to applicable capital gains income tax liability payable to the U.S. Government -- directly to the United States Treasury and contribute another 30% of the proceeds to designated humanitarian, charitable and public interest organizations and projects in all 50 states.²

¹ Over 343 bondholders from more than 24 states.

² The ABF is a limited liability company organized under Delaware law. A companion not-for-profit corporation of the same name has been created to collect and donate the humanitarian, charitable and public interest distributions from Bond proceeds. The corporation will seek status as a 501(c)(3) charity under the Federal Internal Revenue Code.

The value of the defaulted Chinese Government bonds presently held by bondholders affiliated with the American Bondholders Foundation is over \$89,000,000,000³. Collection of the debt owed by China on these bonds would result in a donation by the ABF of nearly \$ 9 billion directly to the United States Treasury⁴ and additional donations by the ABF to a broad number of humanitarian and public interest projects within the United States totaling in excess of \$ 27 billion (30%).

Congress can promote the proposal by signing the Petition to President Bush supporting action by the Administration to hold the Chinese Government accountable to American citizens for a fair resolution of their claims.

The Bonds

The ABF bondholders own more than 18,261 Chinese Government Bearer Bonds issued between 1913 and 1942, the most predominate being the 5% Reorganization Gold Loan of 1913 Bearer Bonds.⁵ The 5% Gold Loan bonds were issued in 1913. All the Chinese Government Bonds held by the ABF affiliated bondholders were issued as full faith and credit obligations of the established and recognized government of China. They were sold in Europe and the United States by the Hong Kong & Shanghai Banking Corporation, Deutsche Bank and other prominent international banks. (Both the Hong Kong & Shanghai Banking Corporation and Deutsche Bank remain large and powerful financial institutions that have substantial U. S. operations today through their subsidiaries Marine Midland/HSBC Bank and Bankers' Trust.) The 5% Gold Loan Bonds were denominated as "gold loans" and were payable in British pound sterling and three other European currencies in semi-annual interest payments with the principal due and payable in 1960. Other of the Bonds were issued payable in U. S. Dollars. The Chinese Government secured payment of the 5% Gold Loan Bonds by pledging revenues from salt mines owned by the Chinese Government.

The Chinese Government paid the semi-annual interest on the 5% Gold Loan Bonds until 1939. However, the Chinese Government defaulted on the Bonds in 1939 based on the financial

³ Includes principal and years of accrued and unpaid interest on the approximately 18,261 "gold loan" Chinese Government bonds held by bondholders affiliated with the American Bondholders Foundation. Including U.S. Dollar denominated bonds issued between 1925 – 1940, 16,795 £20 "gold loan" bonds (issued in 1913 and denominated in British pound sterling and other currencies) valued at \$3,806,754 per bond and 1,466 £100 "gold loan" bonds (issued in 1913 and denominated in British pound sterling) is valued at \$19,033,770 per bond. The calculation, prepared by an expert of gold denominated government bond instruments, is based on historic gold values and current British pound/American dollar exchange rates.

⁴ The bondholders are willing, at the option of the U.S. Government, to either immediately donate 10% of the Bonds they own directly to the U. S. Treasury prior to collection of any payments from China or donate 10% of the cash proceeds to the U. S. Treasury at the time such funds are collected from China.

⁵ ABF affiliated bondholders also own other defaulted Chinese Government bonds issued up through 1942.

difficulties of World War II. When the Communist Party took control of the Chinese Government in 1949 (renaming it the People's Republic of China), it renounced any obligations to pay the Bonds⁶, despite its assumption of the ownership of the assets pledged to secure the Bonds.

The position of the current Government of China disclaiming the obligations of an established and widely recognized predecessor government of the same nation flagrantly violates international law. (See *the Restatement (Third) of the Foreign Relations Law of the United States*, Section 712(2) and *Creditors Claims in International Law*, The International Lawyer, Vol. 34, page 235, Spring, 2000) In fact, in 1987 the People's Republic of China entered into a treaty with Great Britain that recognized the obligation of the PRC for Chinese Government bonds issued prior to the 1949 change of governments.⁷ This treaty provided compensation to British citizens and businesses who were holders of Chinese Government bonds issued prior to 1949, including the 5% Gold Loan Bonds. A Yale University study estimates that approximately 10% of the then outstanding pre 1949 Chinese government bonds were submitted for payment to a British claims commission administering the settlement. Unfortunately, only British citizens and British companies, and no American bondholders or other non-British nationals, were eligible to submit claims.⁸

U.S. Judicial Remedy Not Available to American Bondholders

The American holders of the Bonds are dependent upon the assistance and participation of Congress and the Executive Branch of the United States Government in order to pursue the bondholders' rightful claim for fair compensation for the Bonds from the Chinese Government.

A U. S. federal court ruled in 1984 that American bondholders were not eligible to sue the Chinese Government in a United States court to collect Chinese Government bonds because of the doctrine of "foreign sovereign immunity". The court ruled that the United States had recognized prior to 1952 a broad immunity for foreign governments against being sued in an American court. The court held that, although American law changed in 1952, a creditor of a

⁶ The People's Republic of China continued to assert this position for many years. In 1983 it provided an *Aide Memoire* to the United States Department of State stating that the PRC recognized no obligation to pay external debts incurred by earlier Chinese governments.

⁷ According to the *New York Times* of June 8, 1987, Britain reached a settlement with the Chinese Government pursuant to which China paid £23.5 million to Britain in early 1988 for distribution to British bondholders. "China was previously barred from issuing bonds on the London market because of its refusal to honor debts incurred by governments before the 1949 Communist Revolution." The settlement did not provide full value to the British bondholders, but it does provide official evidence of the Chinese government's willingness, however reluctantly, to recognize its obligation to honor bonds like those held by the American bondholders affiliated with the American Bondholders Foundation. According to a July 12, 2001 letter of HSBC Group Company Secretary R G Barber bondholders who submitted claims to the British commission "received approximately 8% of the face value of their claim."

⁸ See Part IV of the Foreign Compensation (People's Republic of China) Order 1987 of Her Majesty's Government.

foreign government could not retroactively apply the newer 1952 law to obtain a U. S. judgment against a foreign government for debt issued prior to 1952. Since the Chinese bonds in question in the case were issued in 1911, the Chinese Government was not subject to American court jurisdiction.⁹ The court did not rule on the merits of the bondholders' claims that the Chinese Government is liable for payment of the bonds. It held only that American courts lacked the power to hear the case.

American law changed in 1952 to strip foreign governments of sovereign immunity for their commercial activities after 1952 (e.g., sale of governmental debt) within the United States.

American holders of Chinese bonds were also excluded from participation in the 1979 settlement between the United States and the People's Republic of China related to claims for property expropriated and nationalized by the Chinese Government in 1949 upon the communist assumption of governmental control. The May 11, 1979 agreement, entered into as part of the diplomatic arrangements whereby the United States recognized the People's Republic as the established government of China, settled all claims of nationals of the United States against the Chinese Government for losses of property occurring after October 1, 1949 because of nationalization or expropriation or "other taking" of property of U.S. nationals. The People's Republic of China paid \$80 million to the United States in full settlement of such claims. However, the U. S. Foreign Claims Settlement Commission¹⁰ ruled in October 1979 that Chinese Government bonds that had been in default prior to October 1, 1949 (e.g., the 5% Reorganization Gold Loan of 1913 Bearer Bonds which went into default in 1939) were not property that had been "taken" between October 1, 1949 and May 1979 and were thus outside the scope of the 1979 compensation agreement between the United States and the People's Republic of China.¹¹ Accordingly, American bondholders were not eligible to receive any proceeds of the 1979 settlement.¹²

⁹ Jackson v. The People's Republic of China, 596 F. Supp. 386 (N.D. Al. 1984), affirmed 11th Circuit U.S. Court of Appeals, 794 F. 2d. 1490 (1986).

¹⁰ The Commission was authorized by Congress in 1966 to receive and determine the validity of claims "against the Chinese Communist regime ...for losses resulting from the nationalization, expropriation, intervention, or other taking of, or special measures directed against, property ...owned ... by nationals of the United States..." 22 United States Code Sec. 1643.

¹¹ In the Matter of the Claim of Catherine E. Olive, Foreign Claims Settlement Commission of the United States, Decided October 17, 1979, declaring: "The Commission has consistently held that ... a bondholder's right is "taken" by the debtor foreign government on the day when it refuses to pay the obligation for the first time; in other words when the foreign government first defaults upon its obligations" Because of the finding of default in 1939 and non-payment thereafter, the Commission held that the Chinese government bonds had not been "taken" by the People's Republic of China.

¹² Significantly, the People's Republic of China at the time of the 1983 bondholders litigation in U. S. federal court did not claim that the earlier 1979 settlement agreement with the United States precluded or estopped the American bondholders claims. Rather, the Chinese Government insisted in the Aide Memoire to the United States Department of State that it did not recognize the validity of any debts of prior Chinese governments. See Note number 3.

Because of the continued resistance of the Chinese Government to pay pre-1949 full faith and credit bond obligations and the lack of an independent judiciary in China, the bondholders do not have access to any fair judicial or court hearing within China.

China Continues to Stonewall

In June 2001 this law firm submitted a claim to the People's Republic of China's Embassy in Washington, D.C. and to the Ministry of Finance in Beijing, China (both English and Mandarin Chinese versions) on behalf of several American bondholder clients now affiliated with the American Bondholders Foundation seeking a fair settlement for payment of the Bonds. This law firm again in February 2002 submitted an additional claim to the People's Republic of China's Minister of Finance in Beijing and to their Embassy in Washington, D.C. To date, the Chinese Government has not even acknowledged receipt of the claim.¹³

The willingness of China to negotiate a fair settlement of its lawful obligations to pay the Bonds will be a reliable test of whether it is accepting its responsibility as a major global economic power and honorable trading partner with the United States. China has received numerous and lucrative economic benefits from its open access to American commercial, consumer and financial markets. It is appropriate for China to demonstrate that it fully recognizes the obligations of its growing economic prosperity and power by abiding by established international commercial law norms and practices.¹⁴

Resolutely encouraging China to accept its financial responsibilities for payment of the defaulted Bonds will enable the United States to engage China in an arena unrelated to military or national security concerns – and financially benefit the American government and public in the process.

Foreign Bondholders Protective Council To Negotiate with China

In seeking the assistance of the American government to obtain fair compensation for the defaulted Chinese Government Bonds, some of the American bondholders sought to activate the Corporation of Foreign Security Holders that was authorized by Congress in legislation enacted

¹³ This law firm has also filed a notice of claim with the Taiwan Government (the Republic of China) in Taipei and the Taiwanese quasi-official office in Washington, D.C. Although we have received no response from the Taiwanese government, one of the bondholders affiliated with the ABF was notified by the International Commercial Bank of China on Taiwan in January 2000 of the position of the Republic of China/Taiwan Government that a determination of liability for pre 1949 Chinese bonds is “not appropriate...prior to the unification of the country...” Letter of Wang Zhu Shung, General Manager, International Commercial Bank of China, January 14, 2000.

¹⁴ See “Beijing’s Broken Promises”, Wall Street Journal, August 20, 2001, for the important role that the United States can and must play in guiding China’s conduct as a world economic and military power: “Mr. Bush and Congress should search constructively for policies that work to persuade China to behave in a manner consistent with international norms on nonproliferation, arms control and international trade. Relying on any more promises from Beijing would be a mistake.” _____

in 1933. The Corporation of Foreign Security Holders¹⁵ was intended by Congress to be a vehicle to facilitate the collection of defaulted foreign government bonds owned by Americans. Congress made activation of the Corporation dependent upon a Presidential Proclamation. Based on discussions between the Roosevelt Administration and Congressional leaders it was decided in 1933 not to activate the governmental Corporation of Foreign Security Holders, but, instead, to create a non-governmental not-for-profit organization called the Foreign Bondholders Protective Council¹⁶ to assist Americans seeking the collection of defaulted foreign government bonds. The FBP Council still operates today and is headed by a respected veteran of Wall Street, John Petty. Mr. Petty maintains a business office in a Virginia suburb of Washington, D.C. The Foreign Bondholders Protective Council has facilitated the settlement of claims of American holders of defaulted bonds of several Eastern European governments over the last half century.

U. S. Government officials contacted in the first half of 2001 at the United States Department of State, the White House Counsel's Office and the Securities and Exchange Commission directed the American bondholders to pursue their claims on the defaulted Chinese Bonds through the Foreign Bondholders Protective Council.¹⁷

The Foreign Bondholders Protective Council and its President John Petty have agreed to seek a fair settlement with China on behalf of the American owners of the defaulted Chinese Government Bonds. The FBP Council has encouraged the American holders of the defaulted Chinese Government Bonds to act collectively through the American Bondholders Foundation and to provide information to appropriate U.S. government officials within Congress and the Executive Branch. The FBP Council will seek the cooperation of Executive Branch officials in the relevant U. S. diplomatic and government finance agencies and departments and will provide to Congress and the Executive Branch any requested information.

Need for Congressional Support and Direction to U.S. Treasury To Accept Donation of Chinese Bonds

Working together, the U.S. Government, the Foreign Bondholders Protective Council and the bondholders affiliated with the American Bondholders Foundation have the potential, at no cost to the United States Government, to generate billions of U.S. dollars payable to the United States Treasury for use to stimulate the American economy, to support our military's war on

¹⁵ The Corporation, if activated by Presidential order, would be a federal government controlled entity operated under the auspices of the Securities and Exchange Commission. See the Corporation of Foreign Bondholders Act. 15 United States Code Sec. 77bb.

¹⁶ The FBPC was created in 1933 and has remained in operation at varying levels of activity.

¹⁷ Correspondence of Assistant General Counsel Arthur B. Laby of the U. S. Securities and Exchange Commission, dated June 13, 2001 copied to legal advisors at the U.S. State Department and the Counsel to the President's Office.

international terrorism **and to provide relief to the injured and grieving families and damaged communities suffering from the September 11 atrocities.**

The bondholders affiliated with the American Bondholders Foundation propose to immediately donate 10% of the defaulted Chinese Bonds that they own to the U. S. Treasury. The United States Government would then obtain payment from the Chinese Government for the Bonds. Under international law, the Peoples Republic of China is obligated to pay these full faith and credit obligations of the Chinese Government since the Bonds were lawfully issued by the then established and recognized government of the nation of China. The current Chinese Government acknowledged and accepted this principle of its obligations by entering into a 1987 Agreement with Great Britain requiring China to make a payment to settle British bondholders' claims for pre-1949 Chinese Government Bonds.

In lieu of negotiating a direct payment from China, the U.S. Government could, if the Chinese Government refuses to pay the Bonds or otherwise fails to negotiate a settlement in good faith, exercise a customary legal right of set-off by applying the amount owed by the Chinese Government on the Bonds received by the United States Government from American bondholders against a similar amount of debt obligations payable by the United States on U. S. Treasury notes and bonds owned by the Chinese Government¹⁸.

If the owners of the Chinese Bonds affiliated with the American Bondholders Foundation receive payment from the Chinese Government they will donate, through the ABF, 30% of the proceeds to a large number of charitable, humanitarian and public interest projects.¹⁹ The American Bondholders Foundation and the bondholders affiliated with it are prepared to immediately transfer ownership and deliver to the United States Treasury 10% of the Bonds they hold and further to enter into a binding agreement with the United States Treasury Department to donate all the proceeds from 30% of the Bonds that they hold to the charitable, humanitarian and public interest causes and organizations that they have identified.²⁰

The American Bondholders Foundation requests the assistance of Congress and the Executive Branch in supporting this proposal for the United States to, first, accept the donation of Chinese Bonds offered by the American Bondholders Foundation and then, second, in cooperation with the Foreign Bondholders Protective Council, to initiate negotiations with the

¹⁸ The Government of China is the fifth or sixth largest owner of U.S. Treasury bonds and notes according to a recent Congressional Record transcript of remarks by Sen. Byrd of West Virginia.

¹⁹ The American Bondholders Foundation has prepared a report that designates recipients of these funds by dividing the disbursements into four allocation categories: Humanitarian, Native American, Energy and Agricultural. Copies of the report are available from the Website of the ABF at www.americanbondholdersfoundation.com or from the President of the ABF, Jonna Z. Bianco, at 931-359-8781, abfinfo@americanbondholdersfoundation.com or by mail at 2840 Glasscock Road, Lewisburg, TN 37091.

²⁰ Of course, the American Bondholders Foundation and its affiliated bondholders invite representatives of Congress and the Executive Branch to review the list of proposed recipients and to propose alternative beneficiaries that would benefit the American public.

People's Republic of China for the purpose of requiring China to honor its legal obligations to pay defaulted Chinese Government full faith and credit Bond obligations.

Congress can promote the proposal by signing the Petition to President Bush supporting action by the Administration to hold the Chinese Government accountable to American citizens for a fair resolution; and by urging the United States Treasury to defer 50% of each payment made to China (derived from U.S. taxpayers dollars) off of the Government issued U.S. Treasuries that China holds and to direct the 50% deferred funds to the American Bondholders Foundation to begin paying down the defaulted Chinese Government full faith and credit bonds held by United States citizens. (The American Bondholders Foundation welcomes and encourages United States Government oversight of the disbursement of payments to the U.S. bondholders.) Additionally, Congress can assist by urging the United States Treasury to accept the donation of Bonds offered by the American Bondholders Foundation. Alternatively, Congress can enact legislation authorizing the United States Treasury to accept the donation of Bonds and mandating it to take all lawful measures reasonably necessary to negotiate a fair settlement with China for payments due and payable on the Bonds. The bondholders also seek support in obtaining a ruling from the Internal Revenue Service that the 10% of the Bonds to be donated to the United States Government and the proceeds from the 30% of the Bonds that will be donated to humanitarian, charitable and public interest causes and projects will not be treated as taxable income to the donating bondholders.²¹

The American Bondholders Foundation and its affiliated bondholders thank officials and representatives of the United States Government for their assistance in this matter.

B. Riney Green

²¹ Any proceeds from the remaining 60% of the bonds received by bondholders would, of course, be taxable to the bondholders in accordance with applicable federal and state laws.