

# Investment in America



American Bondholders Foundation

# Debt Relief for the Nation of Iraq

## International Setoff on Iraq Debt to China

### Information Summary

**Transfer and Exchange of Bonds Held by U.S. Citizens to the Nation of Iraq and Subsequent Cancellation of Equivalent Value of External Sovereign Debt Owed by Iraq to China by Right of Setoff**

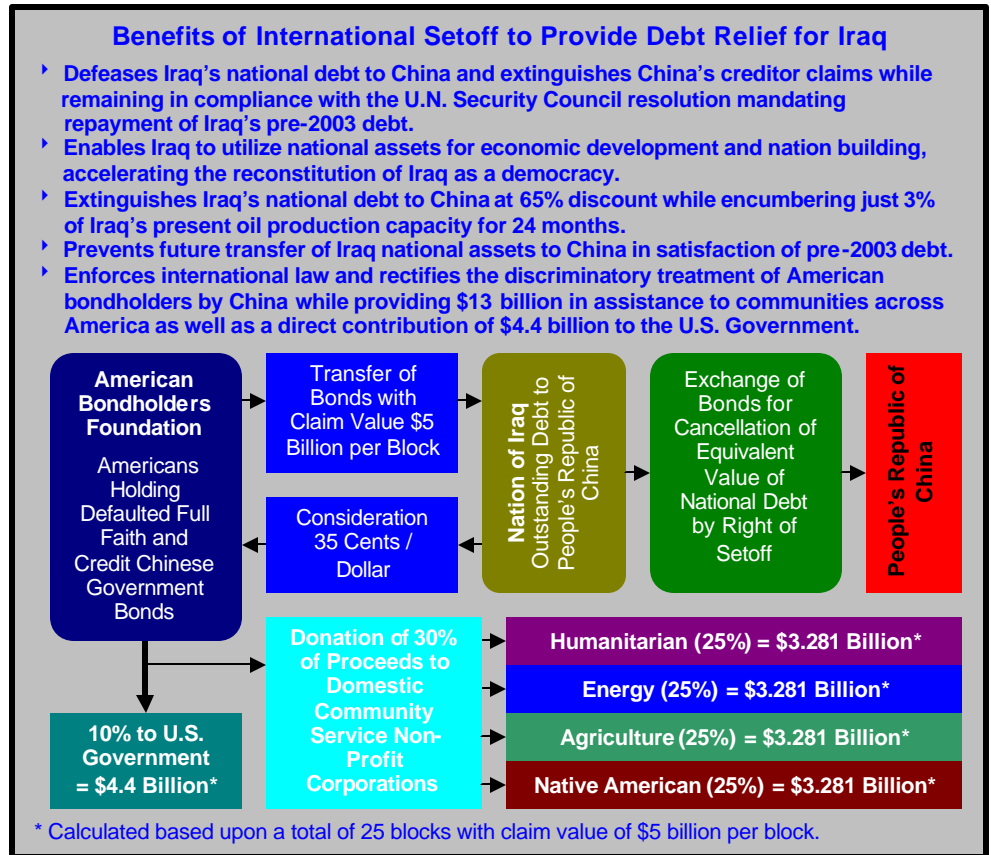
**Defeasance of Iraq Debt to China and Extinguishment of China's Creditor Claims**

#### AMERICAN BONDHOLDERS FOUNDATION

The American Bondholders Foundation (the "ABF") is the incorporated national organization representing the consolidated claims of thousands of United States citizens located across America who are holders of full faith and credit sovereign bonds issued by the government of China and on which that government has defaulted and continues to evade payment. The ABF is duly incorporated under the laws of the state of Delaware. The ABF and its members have retained the law firm of Stites & Harbison to act as counsel in the matter of collecting on the defaulted Chinese government debt.<sup>1</sup> On June 13, 2001, at the direction of the White House Counsel, the United States Department of State and the Securities and Exchange Commission, the ABF contacted the Foreign Bondholders Protective Council (the "FBPC") to initiate collection proceedings on these defaulted obligations. The FBPC was created by Presidential Executive Order to assist U.S. citizens in collecting on foreign defaulted debts. The FBPC has successfully completed collection of 47 previous defaulted bond settlements. The ABF has been featured extensively by the international print and broadcast media, including the British Broadcast Corporation ("BBC"), Financial Times, Wall Street Journal, Associated Press, Bloomberg, USA Today, Voice of America, Business Week and Barron's. The American Bondholders Foundation maintains a website ([www.americanbondholdersfoundation.com](http://www.americanbondholdersfoundation.com)).

Numerous members of the 107<sup>th</sup> United States Congress, including the House Majority Leader and the Chairman of the House Financial Services Committee, signed a letter to President George W. Bush expressing their desire that the Administration take action to compel the Chinese Government to honor its debt. In response to the efforts of the ABF and its many Congressional supporters, the 108<sup>th</sup> Congress held a hearing in the House on this issue preparatory to a vote on H.Con.Res.60,

<sup>1</sup> Refer to Stites & Harbison Memorandum addressed to Members of the United States Congress (February 22, 2002) for a comprehensive analysis of legal issues. The Memorandum affirms the rights of American citizens to collect payment on their legally valid outstanding claims. Refer to Stites & Harbison Memorandum to Members of the United States Congress (May 30, 2003) for a discussion of issues involving the Foreign Claims Settlement Commission. See also, Choate Legal Opinion (June 8, 2003).



stating the desire of the United States Congress that China honor its debts to American taxpayers.<sup>2</sup>

#### NATURE OF THE DEFAULTED OBLIGATIONS

The most prevalent obligation for which payment is sought by the ABF is the Chinese Government 5% Reorganization Gold Loan. This class of obligations was issued by a global syndicate of international banks and was sold to investors in the United States and Europe. The bonds were scheduled to mature in 1960. The language of the bond certificates, as well as the language of the loan agreement authorizing the bond issue, mandated that the obligations were to be considered as binding upon the Government of China and its successors. The obligations which are the subject of the ABF collection action have been appraised by a recognized specialist in bond valuation.<sup>3</sup> The value of the obligations has been determined in accordance with the provisions specified in the language of the loan agreement. All such bonds which have been tendered for collection are presently held in trust by the ABF.

<sup>2</sup> Refer to H.Con.Res.60, introduced into Congress on February 27, 2003. Transcripts available of testimony presented at hearing conducted by the House International Relations Committee on October 21, 2003.

<sup>3</sup> For an analysis of the valuation of the affiliated bondholder claims, refer to Choate Valuation (May 27, 2003).

#### PRECEDENT FOR PAYMENT OF CLAIMS

In addition to general principles of international law, there exist several recent precedents that are applicable in the immediate instance.

1. In 1987, the British government compelled the People's Republic of China to settle the claims of British citizens who were holders of an identical series of defaulted Chinese government obligations.
2. In 1996, the French government compelled Russia to settle the claims of French citizens who were holders of defaulted pre-1917 Russian government bonds.
3. In 1986, the British government compelled the Soviet Union to settle the claims of British citizens who were holders of defaulted pre-1917 Russian government bonds.

Despite the obligation of the People's Republic of China to honor the claims of U.S. bondholders under international law, the PRC continues to blatantly disregard the claims of American bondholders and continues its discriminatory treatment of United States citizens in an attempt to evade payment of these claims.

#### SETOFF ON IRAQ DEBT TO CHINA

The defaulted full faith and credit Chinese government bonds are, under established international commercial law, bearer bonds in transferable form. Whomever is the lawful holder of the bonds has the right to receive payment from the obligor. In the event that the

new government of Iraq acquires bearer Chinese government bonds from current ABF bondholders, it will have valid standing as the lawful holder to receive payment from the obligor (i.e., the government of China). It is also a standard international commercial law practice for two parties who are obligors and obligees of each other to apply a setoff of their respective claims. To the extent that Iraq is a debtor that owes money to China (based on Saddam / Baathist-era transactions between Iraq and China), Iraq is certainly entitled, once it becomes the lawful holder of Chinese government bonds (via purchase from ABF bondholders) to apply the value of those Chinese government bonds against the value of the financial claim that the Chinese government may have against Iraq (i.e., the offset mechanism). The offset mechanism will defeat Iraq's debt to China and extinguish China's claims as a creditor nation of Iraq, thereby acting to prevent the possible future transfer of Iraqi national assets to foreign creditor nations (e.g., to preemptively block any future transfer of state assets to China as satisfaction of claims arising from pre-2003 indebtedness). The setoff will provide debt relief for the people of Iraq at a substantial multiple of the cash cost, and is multiplied even further by the ABF's immediate \$250 million contribution to the country, while providing American bondholders with a twenty cents on the dollar bond settlement. The international offset mechanism enables the Nation of Iraq to tender satisfaction, at a substantial discount, of the claims of the People's Republic of China as a creditor nation while simultaneously providing a source of finance for the economic revitalization of Iraq, all while remaining in compliance with the provisions of the United Nations Security Council resolution governing post-conflict administration of Iraq and mandating payment of pre-2003 claims. The offset mechanism also eliminates any potential adverse ramifications from the possible characterization of Iraq's pre-2003 creditors as odious. The implementation of a setoff will provide for the economic adjustment and stabilization necessary for reconstituting the Nation of Iraq as a stable democracy, and enable the release of national assets to nation building as a precursor to self-determination.

### BENEFITS OF IRAQ DEBT RELIEF PROGRAM

The Iraqi Regime which entered into the borrowing arrangement with the People's Republic of China was not representative of the will of the Iraqi people. The debt proceeds derived from this arrangement were utilized for purposes which acted to destabilize the region and undermine global stability. The borrowing arrangement between Iraq and the People's Republic of China was by its very nature a gross misappropriation of national resources from the Iraqi people for the express purpose of furthering an oppressive agenda of private ambitions benefiting the privileged few. The tender of valid full faith and credit sovereign obligations of the Chinese government, which the People's Republic of China is obligated to accept under international law as cancellation of Iraq's existing external sovereign debt to the PRC, will reinforce accepted conventions of international trade and commerce as well as free Iraq from an oppressive debt burden. The Iraq debt relief program described herein will

### NATIONAL SECURITY THREAT ASSESSMENT

A creditor nation of Iraq may be expected to assert a valid claim for repayment of debt based upon the provisions of the United Nations Security Council resolution governing the post-conflict administration of Iraq, which mandates that a successor Iraq government remain liable for repayment of the Iraq's pre-2003 external sovereign debt. Without a setoff, if Iraq should ever default on its debt to China, or if such debt ever goes into default, especially after the American presence is withdrawn from governance of the country, then there is a risk that China might either begin privatization negotiations with the Iraqi Government as a means of canceling the outstanding debt, or sell some or all of its Iraq paper in the secondary market. In the first instance, the risk to the United States is that a subsequent Iraqi Government may elect to extinguish its outstanding debt to China by allowing or even encouraging a debt-swap privatization program. Under such a program,

#### China's Skyrocketing Dependence on Foreign Oil Producers\*

- ▶ China surpassed Japan in 2002 as world's second largest oil consumer.
- ▶ China accounted for 100% of 2002 global oil demand increase.
- ▶ China's oil imports doubled in 2000 over previous year.
- ▶ China's domestic oil production has plateaued.
- ▶ China's emerging automobile industry will substantially increase domestic oil consumption.

#### U.S. National Security Threat Parameters

- ▶ China's rapidly escalating oil consumption and increasing dependence on petroleum imports.
- ▶ China's announced intent to acquire foreign oil assets.
- ▶ Iraq national debt owed to China and existence in force of a U.N. Security Council resolution mandating repayment of Iraq's pre-2003 debt.
- ▶ Iraq Petroleum Minister's stated intent to privatize the country's national oil assets.

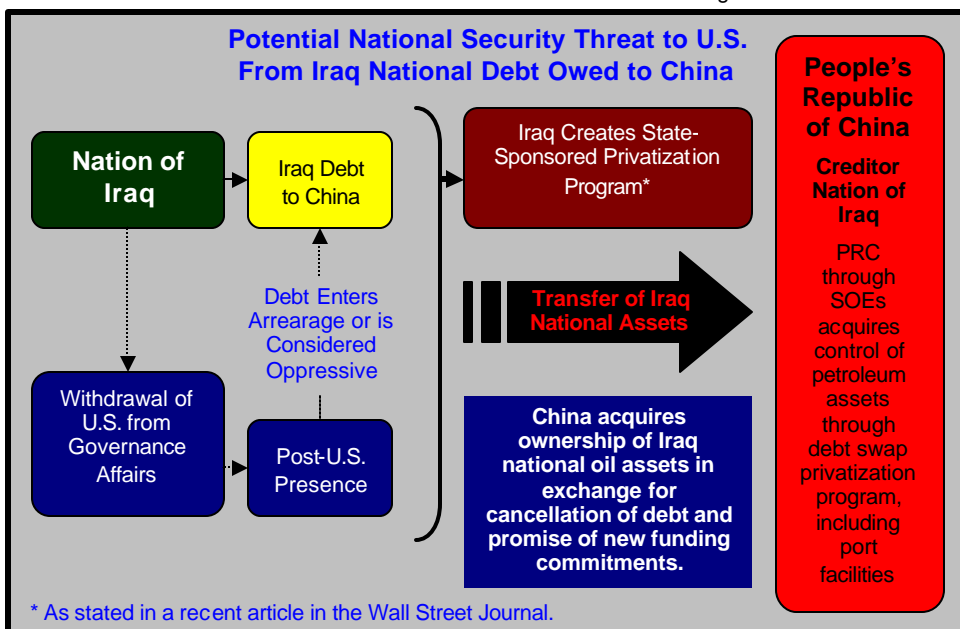
\* Sources: Wall Street Journal; Statistical Review of World Energy (2003); Alexander's Oil & Gas Connections (Vol. 8, No. 14).

enable the Nation of Iraq to conserve its resources for economic development and nation building while remaining in compliance with the provisions of the United Nations Security Council Resolution governing post-conflict administration of the affairs of the country. The program will thus enable Iraq to achieve sustainable prosperity and serve as a viable model for the region.

China (perhaps acting through its state-owned enterprises) could acquire ownership (i.e., control) of Iraqi national assets, such as oil refineries and shipping terminals or port facilities. This would cause a significant shift in strategic balance in the region. The magnitude of risk increases significantly as Iraq transitions towards autonomous governance. In the second instance, China could sell its Iraq debt to a nation (e.g., Libya, North Korea, Syria), or to a state-owned company, which is unfriendly to the U.S., and the same scenario as described in the first instance could occur. The advantage of imposing a setoff, from a national security perspective, is the ability to block such a scenario as described above from happening, and so protect America's interests in the region, before the Chinese have an opportunity to acquire control of strategic regional assets. The risk of not imposing a setoff is the loss of strategic regional assets to other creditor nations, including the Chinese. Through imposition of a setoff, the U.S. Government has an opportunity to mitigate the risk of allowing Iraq's external sovereign debt to enter the secondary distressed debt markets and possibly fall into the hands of a hostile nation seeking to acquire control of strategic assets in the region.

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## American Bondholders Foundation



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