



Vulture Funds — Spotlight on Zambia

Vulture Funds Prey on Africa

Africa Action has become involved in work to protect countries in Africa from “vulture funds”. Vulture funds are companies that attempt to make exorbitant profits at the expense of impoverished nations — many in Africa. Vulture funds identify countries that are on the brink of a major debt restructuring or debt relief deal and buy the debt from the creditors at a huge discount before it is

restructured or relieved. Then the company sues the debtor for the original amount of the debt, often with interest and penalty fees added on top, making a tremendous profit.

The creditor countries win in this scenario because they get paid millions for debt that is about to be written off since it has not been or cannot be serviced by the impoverished debtor

country. The vulture fund profits because they spend a small amount to buy a large debt and then can sue for the full amount owed. **The debtor country loses entirely**, being forced to pour debt relief savings into corporate lawsuits and, in many cases, then being required to use these debt savings to pay off the full amount of the old loans. **The case of Zambia is a perfect example.**

Zambia's Vulture Fund Challenge

In 1979, Romania loaned \$15 million to Zambia to buy tractors and other forms of agricultural machinery. Unfortunately, the machinery and the tractors did not work well. This was compounded by the fact that European agricultural subsidies undercut Zambia's ability to compete in the global marketplace. Zambia was not able to produce enough, or get a high enough price for their products, which meant that the country did not raise enough from its exports to be able to repay the loan.

In 1999, Romania and Zambia negotiated to liquidate the debt for \$3 million. A private company, **Donegal International (DI) swooped in at the last moment and bought the debt from Romania for \$3.3 million.** At that time, the total value of the debt was \$30 million. This

transaction happened when notoriously corrupt Chiluba was president of Zambia.

In 2003, amidst many accusations of corruption and bribing of civil servants, **Zambia signed a settlement deal with DI to pay off the debt at the reduced price of \$15 million**, even though the total value of the debt had risen to \$44 million at that time. Zambia agreed to penal rates of interest if it defaulted on its payments and that any disputes would be settled under English law.

Shortly thereafter, **Zambia stopped paying, arguing that the deal was made under corrupt circumstances.** Donegal International did not sue right away, but instead waited until one month before Zambia qualified for debt relief under the Heavily Indebted Poor Countries

(HIPC) initiative and only a few months before the historic 2005 Group of Eight (G-8) wealthy nation agreement to provide 100% debt cancellation for a handful of countries, Zambia included. The Donegal International debt was not included in the G-8 deal since the creditor is a private corporation, not a country or one of the eligible International Financial Institutions. **DI saw the opportunity to profit off the savings Zambia was awarded by the G-8 and sued Zambia for \$55 million, which includes the full value of the debt plus interest and penalties.**

The case was taken to a British court. The initial ruling was that \$55 million was too much, but Zambia should pay DI some amount. The final ruling was that Zambia would pay \$15.5 million, almost 40%

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Zambia's Vulture Fund Challenge Continued



of Zambia's expected debt cancellation savings for 2007.

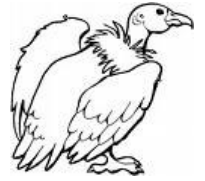
Zambia has already done remarkable things

with the savings from the 2005 debt cancellation. An incredibly impoverished nation where the majority of the population lives on less than \$1 a day and the

average life expectancy is only 38, **Zambia has managed to efficiently channel the savings into abolishing "user fees" for primary health care and providing hundreds of thousands of people living with HIV/AIDS with life-saving anti-retroviral drugs.**

Zambia has been counting on the \$40 million annual savings from debt cancellation to address poverty and continue these critical health initiatives.

As a result of the Donegal International victory in British courts, **Zambia has been forced to siphon these desperately needed resources from providing health care to its impoverished citizens to pay off a wealthy corporation.**



Who is Donegal International?



Donegal International is a company that is incorporated in the British Virgin Islands but run by U.S.-based businessman, Michael Sheehan. Donegal International is part owned and managed day to day by Debt Advisory International, which was also founded by Michael Sheehan. Mr. Sheehan works out of DAI in downtown Washington, DC.



"Ultimately, Donegal was awarded \$15 million in the suit. For Zambia, \$15 million translates to over 60 million Zambian Kwacha, which would be enough to facilitate three private manufacturers of animal-drawn plows and other equipment appropriate to and affordable for small-scale farmers (to complement the tractors for which Zambia originally got the 1979 loan from Romania)."

~ Muvatwa Sitali, Zambia

How Are "Vulture Funds" Legal?

It seems improbable that it is legal for a corporation to buy a debt that is on the brink of default and then be able to sue the debtor for as much as ten times the amount when the debtor finally has debt cancellation on the horizon.

There are a couple elements that make this process legal, though the case can be made that countries should do more to crack down on these funds and pass legislation and court decisions that would make these practices illegal.

Since the vulture fund buys the loan from the creditor, not the debtor, the vulture fund can technically claim payment of the full amount, even if it paid only a fraction



of the value. When the vulture fund negotiates with the debtor, the corporation is careful to ensure that the contract enables the company to have the flexibility to sue for the full amount, plus interest and penalties, in the case of non-payment or any other deviation from the contract.

Why Would Zambia Agree to the DI Deal?

In light of the fact that vulture funds operate in the public sphere, one might wonder why Zambia would agree to such a risky prospect. In 2003, when Zambia signed an agreement with DI, Zambia appeared to be getting a good deal. Zambia was committing to pay only \$15 million of a \$44 million debt. In court testi-

mony DI argued that they entered into the agreement with Zambia anticipating to engage in a debt and development swap, with no intent to sue. It is likely that this was the way that the debt deal was presented to Zambia initially. Debt and development swaps are common ways for impoverished countries to avoid paying

the debt and in return give incentives and open up opportunities for corporations interested in doing business in the impoverished nation. Bribery, corruption and fraud ensued during the process of drawing up the contracts, which included the agreement that Zambia was open to suit in the case of non-payment.

Zambia is Not Alone

Zambia is not the only country that has fallen victim to vulture funds. There are over 40 cases of companies suing heavily indebted countries that are eligible for debt relief. More than half of these cases are in Africa. In light of the recent progress towards debt cancellation for Liberia, we expect Liberia will be the next target for vulture funds.

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Next Steps

“These odious practices must be abolished along with the odious debt itself.”
~ Jubilee South

In recent months, vulture funds have come under increasing criticism, but much more needs to be done to address this corporate abuse of impoverished people. Jubilee South, the umbrella for the debt cancellation campaigns in Africa, Asia and Latin America has released a statement condemning vulture funds as a ***“despicable manipulation of an already unjust financial economic system.”***

Jubilee South challenges the U.S. and other G-8 governments to crack down on the corporations, making illegal the practice of buying “bad” debts cheaply and then using wealthy country courts to demand full payment illegal. Jubilee South invites governments of impoverished countries to dismiss vulture fund claims or legal rulings on the ground that the entire debt is illegitimate.



Jubilee South encourages popular movements and campaigns world wide to, ***“...fight to end both vulture firms and the vulture system that continues to uphold debt as an instrument of colonial bondage, exploitation and subservience.”***

It might not be surprising to learn of criticism among social movements, but even leaders in the International Financial Institutions have begun to speak out against the vulture funds. World Bank president, Paul Wolfowitz described the case against Zambia as

“appalling” and said, ***“I’m hoping that...increased attention on this issue may enable the international community to come up with some effective legal remedies that protect countries like Zambia from that kind of unfair dealing and in time sustain an effective credit system for poor countries.”***

Members of Congress and even White House aides have expressed openness to finding ways to crack down on vulture funds when they try to seize assets of impoverished countries in U.S. courts.

Africa Action, TransAfrica Forum, Jubilee USA Network and other allies in the U.S. will be following vulture funds more closely in coming months and will invite activists to engage with us as we search for legal and legislative strategies to



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Africa Action has a Campaign to Cancel Africa's Debt. Africa's over \$200 billion debt burden is the single biggest obstacle to the continent's development.

Most of this debt is illegitimate, having been incurred by despotic and unrepresentative regimes. African countries spend almost \$14 billion annually on debt service, diverting resources from HIV/AIDS programs, education and other important needs. The U.S. and other rich countries have resisted calls to cancel this debt, instead proposing partial solutions that are inadequate and impose harsh economic policies on indebted countries. Africa Action's Campaign to Cancel Africa's Debt mobilizes pressure on the U.S. government to push for 100% debt cancellation for all impoverished African countries without harmful conditions.



Next Steps Continued

address this problem at its core.

Public interest is critical to ensuring that vulture funds stay on the radar of concerned policymakers as debt experts work together to develop specific solutions.

Possibilities exist to stop vulture funds from taking advantage of poor countries like Zambia at both the national and international level. Internationally, institutions like the World Bank or informal groupings of wealthy countries such as the G-8 or the so-called "Paris Club" could work together to develop and implement universal "Codes of Conduct" that ensure responsible creditor behavior. They could also develop an international bankruptcy mechanism so that poor countries who default on their debt face a structured process to help them navigate that challenge without being exposed to predatory vultures. Such a framework would be technical and complex, however, and could take years to develop.

In the meantime, wealthy countries need to work together to develop comprehensive sets of national laws that prevent firms from engaging in

vulture activities within each of their borders. These laws could outlaw the profiteering practices that makes snatching up the debt of poor countries so attractive. They could also force any private companies interested in purchasing distressed national debt to disclose the records of their transactions and activities. This would both make it easier for activists and analysts



to take early action on each new case, but it would also discourage hedge funds, who tend to guard all their information very secretively, from pursuing a vulture strategy in the first place.

Early this year, the Belgian Senate set an important precedent by unanimously passing both a law and a resolution against vultures designed to safeguard development assistance and savings from debt cancellation against vulture funds. Other countries should build on

this victory by developing their own legal frameworks to discourage or prohibit vulture behavior.

In order for legislative or legal remedies to the vulture problem to be successful, policymakers need to hear public pressure so that this important issue stays on their radar. To build momentum, we encourage you to raise the issue with your elected officials or in your community whenever you discuss the problem of international debt or global poverty.

In addition to working with our allies to develop and promote policy solutions, Africa Action is also exploring possibilities for how individuals and organizations can make a direct difference on this issue as investors. We'll keep you updated with our latest research on exactly who the firms making big profits through this malicious practice are, and how you can ensure that you or your community aren't supporting the vultures through your investment dollars.

Together, we can work to protect African nations from continued economic abuse at the hands of wealthy countries and corporations.