SUPPORTING ARGENTINE SAVERS IN THE COURTS OF NEW YORK

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The Argentine government submitted at the end of December 2003 a memorandum in support for its motion to have the United States courts discriminating among unsecured creditors. Specifically, the Argentine government asked U.S. courts to allow prejudice the property rights of those Argentine savers that do not want to accept the big losses included in the repayment proposal (losses of up to 92%). This article argues against the government motion and it is aim at defending the rights of those Argentine investors that want to protect their savings and in doing so have filed legal actions before the courts of New York.

NO MORE DILATORY TACTICS

Why do the courts exist? They mainly exist to protect the rights of those affected persons by the actions of third parties. In this case, the government of Argentina is infringing the rights of Argentine investors holding payment promises (bonds) issued by the Republic several years ago. The infringement has now lasted more than two years as the government defaulted on its payment obligations under the payment promises at the end of 2001. Under New York law the contracts must be honored. The Republic is not honoring the contracts executed with Argentine investors holding those claims. The affected investors have accessed the courts of New York (competent tribunal according to the contractual provision of the claims) to obtain justice.

When the bonds were issued (some years ago), and even today, there are no formal bankruptcy proceedings for countries. Therefore, when a country defaults or is about to default, it can't rush to courts and ask for protection against litigation. Moreover, a hold-out investor (such as the more than 200 Argentine savers claiming in New York) has the right to collect on the original terms by suing the sovereign if it defaults. And the hold-outs may attach assets that are "attachable" given the immunities and waivers of immunity applicable. Argentina for example has waived any kind of immunity it may have. This is a consequence of the breaching, and the keeping of such breach, of the contracts by the sovereigns, in this case the government of Argentina. Otherwise, bond contracts would only be a "piece of paper" with no execution force.

As we will see below, this is the understanding of the financial community, which understands that if there is a default, the restructuring of the defaulted debt is quite difficult, because, among other things, the actions of the hold-outs, which are generally-accepted in the bond markets. Moreover, in the Argentine case, there is an important number of hold-outs that are purely retail investors, savers, that resist to lose their investments. "The question of how to handle situations of unsustainable sovereign debt acquired increased urgency in the 1980's, when private capital flows-mostly lending from private banks to sovereigns- had grown enormously relative to official flows. Then, in the 1990s, private flows-bonds as well as bank-lending-exploded. As I will later, this diversity in debt instruments has added to the challenge of how to tackle situations where sovereign debt has become unsustainable... This is because bondholders

can be even more difficult to coordinate than bank creditors. Unlike bankers, bondholders also have greater incentives to sue delinquent creditors, because unlike banks they do not have to share the proceeds of litigation. The situation is further complicated by the growing variety of debt instruments and derivatives in play. Because of all these factors, it is difficult to get everybody in the same room and hammer out an agreement that everyone accepts as a fair solution," explains Anne Krueger, deputy managing director of the International Monetary Fund.[1] Krueger has proposed the implementation of an international bankruptcy for courts given the total absence of such a tribunal today.

The financial community is vividly discussing how to solve the hold-out problems in future issuances of bonds. And there are basically two proposals about it. Krueger proposes an international bankruptcy courts for countries (Sovereign Debt Restructuring Mechanism or SDRM). The U.S. Secretary of the Treasury and other representative countries propose to include the so-called collective action clauses (CACs) that, among other things, permit the modification of the payment terms (nominal amount, interest rate, payment dates, currency, etc.) by a determined supermajority of bondholders instead of unanimous consent as it is required now. "The two proposals -CACs and SDRM- would help bring about faster and more orderly restructuring. Let me try and describe briefly how each would work. CACs apply to individual bond issues. They would permit a specified super-majority of holders of the bond issue to agree to a restructuring that would be binding on all holders of that issue -that's what the clause does.

[1] International Monetary Fund, Sovereign Debt Restructuring Mechanism-One Year Later, By Anne O. Krueger, First Deputy Managing Director, IMF, Presented at the European Commission, Brussels, Belgium, December 10, 2002.

That would then prevent hold-outs in individual bond issues, thereby facilitating any needed restructuring. A registry of holders, or trustee arrangements, could accelerate the process. The use of such CACs would be an improvement over the current system and the IMF is committed to promoting their use among its member countries. The SDRM proposal goes further than CACs and could complement it nicely. It provides a mechanism which, when activated, would enable creditors and debtors to negotiate a restructuring, aggregating across instruments, and ratifying an agreement binding on all by a specified super-majority. As with a domestic insolvency law, it would aggregate claims for voting purposes and could apply to all existing claims. An independent and centralized dispute resolution forum would be established to verify claims, insure the integrity of the voting process, and adjudicate disputes that might arise. By providing the locus and secretariat for these activities, this forum would enable a smoother and quicker than now seems feasible. Both approaches were endorsed at the Annual Meetings of the World Bank and the IMF by the International Monetary and Financial Committee, the EVIFC."[2]

The U.S. government then dropped its support for the SDRM; it now only backs the inclusion of collective action clauses in the new issuances of bonds. This is an indication that there is no enough support for the establishment of bankruptcy court for countries.[3] Further, it is unimaginable that a U.S. federal

[2] International Monetary Fund, Sovereign Debt Restructuring Mechanism-One Year Later, By Anne O. Krueger, First Deputy Managing Director, IMF, Presented at the European Commission, Brussels, Belgium, December 10, 2002.
[3] U.S. Secretary of the Treasury, John B. Snow.

court ends up being acting as a bankruptcy court for countries without any modification of the current U.S. and international laws.

In any event, the official financial community understands that currently the problem really exists and may not be solved unless a formal change in the international laws is implemented. "There is a growing consensus that the present process for restructuring the debts of a sovereign is more prolonged, more unpredictable and more damaging to the country and its creditors than would be desirable... The risk that some creditors will be able to hold-out for full payment may prolong the restructuring process, and even inhibit agreement on a needed restructuring."[4] Therefore, it does not make any sense the heart-breaking allegations from the Republic of the type: "To conclude that a single plaintiff has the unprecedented ability to prevent the Republic or any other distressed borrower from restructuring debt held by other creditors would lead to just an absurd result, by effectively precluding the Republic from making payments to any of its creditors unless it was able to satisfy in full all of its obligations to all of its creditors... Creditors who wish to restructure would be held hostage to those who do not, creditors who are willing to accept the financial sacrifices necessary to restructure would be blocked from receiving payment even on the new debt reflecting that sacrifice, and debt restructuring would become impossible." Krueger says "currently a creditor who holds out can scuttle an agreement acceptable to the majority and quite possibly obtain better terms for himself. That also serves as a disincentive for other creditors to organize. In short, there is a lack

[4] Anne O. Krueger, A New Approach To Sovereign Debt Restructuring, International Monetary Fund, 2002.

of incentives to resolve the collective action problem."[5] The whole world of the international finance is making proposals to "change" this. Unless that changes occur, if they do and in accordance with their eventual extent, the situation that so alarms the Argentine government is the current legal "status quo." Therefore, there is no point in showing themselves alarmed before this situation as an implicit asking to the U.S. courts for these courts not to apply the law.

The bonds hold by the Argentine savers were issued under the laws and jurisdiction of New York because, among other things, the creditors trusted, and still do, that their rights would have enough protection to be operative; not a mere declaration of interest or a sort of moral obligation whose payment only depends on the unilateral will of the debtor. The sovereign markets understand that the New York and U.S. Federal courts enforce those contracts. When a party (in this case the debtor) breaches the contracts, the other party (the Argentine savers) has remedies. This is why the sovereign bonds issued under New York (along those issued under British jurisdiction) account for the vast majority of the entire issuance of this type of debt instruments. Additionally, as we mentioned before, under New York law the so-called payment terms of the bonds may only be modified by unanimous consent which means that a bondholder may hold-out from the new repayment proposal and if the debtor defaults with it, try to collect on the original terms.

Putting these three concepts together (the lack of formal bankruptcy proceedings for countries, the traditional enforcement of contracts subject to the

[5] International Monetary Fund, Sovereign Debt Restructuring Mechanism-One Year Later, By Anne O. Krueger, First Deputy Managing Director, IMF, Presented at the European Commission, Brussels, Belgium, December 10, 2002.

New York law and jurisdiction and the ability of a bondholder not to accept the new terms offered and claims the original terms, one may conclude that there is no authority to regulate these summary judgment proceedings as bankruptcy proceedings. The general authority that the U.S. courts have to defer for a short and limited period of time the execution of the judgments already granted (almost a year ago) may not be used to alter the nature of the proceedings (summary), unless not at a risk (and a fact) of violating the rights of the parties affected by the breach of the bond contracts. Effectively, one thing is to give the Argentine officials and politicians some time to put together an exchange proposal, but other very different is to go along with the whole restructuring process as if the proceedings were not of the type of summary judgment but of the type of bankruptcy proceedings. For example, it was said that the Argentine government would make a formal offer on January. But this kind of exchange offers sometimes are extended and may even last for months. It is unacceptable that said process enjoys court protection. The stay then should no question be lifted on January 31, 2004 or the day the Republic makes an offer, if before.

After the Republic has attempted all kind of dilatory tactics, it is time for the dilatory tactics to cease. It is time for the Justice to prevail. It is time for the court to apply what the New York contemplates for these cases of default under plain vanilla bonds: execution of the judgments already granted.

THE "SACRIFICES" OF THE GOVERNMENT PROPOSAL

The Republic's counsel has mentioned in some occasions that the Argentine savers will need to make some concessions on their original claims. These concessions are also described as "sacrifices." According to the payment terms that were announced by the Republic in Dubai and confirmed later on, the "sacrifices" would account for losses up to 92% of the original claims the investors have. No question they are sacrifices. Moreover, they are short of being sacrifices; they are a decapitation.

Both the Argentine saver organizations *(Asociacion de Damnificados por la Pesificacion y el Default, ADAPD, and Asociacion de Ahorristas Argentines, AARA)* as well as individual Argentine investors and the international creditor associations have totally rejected those payment terms on the basis that they are considered confiscatory of the property rights.

The government, on the other hand, continues spending money on different domestic projects. On December 26, 2003 one of the leading Argentine financial newspapers put on its cover as the main news the following: "The Government Challenges the IMF and Bondholders: It Will Spend USD 500 Million Of The Budget Surplus."[6] This money is over the already contemplated amount that the government is expected to use to re-repay foreign debt. By the way, among the moneys so contemplated there is nothing to repay the defaulting debt. And the government spends any extra-money that it collects. Without paying not even a penny to the defaulting bondholders whether they have judgments or not.

[6] Ambito Financiero.

In addition, the economy grew on 2003 more than 8% (the highest growth in the world after China) and it is expected that it will grow again this year on very high marks (at least 6%, according to the majority of the analysts). Argentine politicians and public officials, including the President, has said a number of times that it will not better, in any way, the terms already announced, the so called "sacrifices." And the Argentine politicians and officials now want the protection of the U.S. courts so that they go along the government lines preventing any Argentine saver that do not agree with the "sacrifices" to exercise its legal right to collect on the terms of the judgments, not on the terms offered. The governments recur to the U.S. courts to coerce those non-accepting bondholders to accept the proposal, whether they want to or not. This is totally illegal.

THE DOCTRINE OF PRAVIN: PARTICIPATION IN RESTRUCTURINGS IS VOLUNTARY

Judge Griesa based the judgments already granted against Argentina on certain New York cases involving sovereign defaults. One of those precedents was Pravin v. Peru. Judge Griesa wrote in the judgment against the Argentine government: "The Second Circuit has dealt with similar circumstances and similar issues in Pravin Banker Assoc. v. Banco Popular del Peru, 109 F.3d 850 (2d Cir. 1997). There the plaintiff had invested in the debt of a bank owned by the Republic of Peru. The Republic guaranteed the debt. During a national economic crisis, the bank stopped making interest payments. The plaintiff demanded

payment of the principal and unpaid interest. Peru's central bank appointed a committee of liquidators for the bank. Negotiations were also undertaken to resolve the overall debt of Peru. The plaintiff refused to take part in the liquidation proceedings or the other debt negotiations, and brought suit in the Southern District of New York against the bank and the Republic. The plaintiff moved for summary judgment. The defendants opposed the motion and cross-moved to dismiss or stay the action, arguing that international comity should be extended to Peru so that it could resolve the debt problems of the bank and the Republic. The district court granted a six-month stay to allow the completion of the bank's liquidation proceedings. Apparently there was no resolution, and, after the six-month stay expired, the plaintiff renewed the motion for summary judgment. The district court granted an additional two/month stay to obtain more information about the course of events in Peru. At the conclusion of the second stay, the plaintiff again renewed the motion for summary judgment, which was granted by the district court. The defendants moved to stay the judgment and this motion was denied. The defendants appealed. The Court of Appeals, agreeing with the reasoning and the actions of the district court, stated that extending comity to Peruus debt negotiations was only appropriate if it was consistent with United States government policy. They recognized two United States policies as being implicated by the lawsuit. The first policy was that the United States encourages participation in foreign debt resolution procedures. Second, the United States has a strong interest in ensuring the enforceability of foreign debts owed to United States lenders. The Court stated that the second interest limits the first, and

went on to say that creditor participation in foreign debt negotiations 'should be on a strictly voluntary basis.' The Court of Appeals expressed approval of the limited stays granted by the district court, but agreed with the district court that an indefinite stay to allow Peru to renegotiate its foreign debt 'would prejudice the United States interests.' The Court further reasoned that, if the plaintiff's rights were made conditional upon the debt restructuring process (which had no obvious termination date), this would have converted voluntary negotiations into a "judicially-enforced bankruptcy proceeding, for it would, in effect, have prohibited the exercise of legal rights outside of the negotiations. The Court of Appeals thus ruled that the district court was correct in granting summary judgment to the plaintiff and denying a further stay."

Under New York law a hold-out investor has always the right to hold-out. Under New York law, the payment terms may not be modified without the consent of all and each one of the affected creditors. If a bondholder doesn't like the proposal (with the "sacrifices"), it has the total and absolute right to stay away from the offer and claim to try to collect on the original terms of the bonds. According to the Argentine government tactics (having a "shielded channel" to exclude the non-accepting bondholders from the flow of payments, which means coercing them to accept the "sacrifices"), the contents of the New York laws regarding the necessity for the issuer to have unanimous consent among the bondholders in order to change the payment terms would fall and be replaced by a new legal concept: if an issuer obtains for example 75% of approval to an

exchange of bonds offered then the non-accepting 25% of bondholders would have no option but accept the proposed terms because otherwise they would never have the chance to collect, unless the issuer, at its exclusive and discretionary will decides to pay whatever amount and in whenever dates it wishes. As we will expand below, this outcome is so because the bondholder that, exercising an absolute right that it has, decides not to accept the offer would not be able to collect from the main assets that the sovereigns have: the flow of payments to international creditors, including both official creditors (such as the IMF, the World Bank, the Inter-American Development Bank) or private creditors (bondholders, trade creditors, banks, etc...). Therefore, if they want to collect something, they must enter into the restructuring. This is against New York law and the Pravin doctrine.

The Republic has accepted that this is the whole objective of the motion I am attacking. The memorandum in support for the motion says: "Creditors who wish to restructure would be held hostage to those who do not, creditors who are willing to accept the financial sacrifices necessary to restructure would be blocked from receiving payment on the new debt reflecting that sacrifice, and debt restructuring would become impossible." This declaration is an express recognition that they want to create a security in favor of certain (originally unsecured) creditors which means that those originally unsecured creditors would now be "secured" creditors because the revenue stream generated by the Republic to pay them would not be attachable by other creditors. If a creditor wants to hold-

out and claim the original term, it would not get paid for years. This is coercion and this is unacceptable and against the New York law.

The Republic also says that Judge Griesa should preclude plaintiff judgment creditors from interfering with payments by the Republic to other creditors on the purported ground that such payments would violate the Pari Passu clause. The word "interference" is extremely funny. Its use is absolutely without sense. The Argentine plaintiffs will not "interfere" with anything. They will attempt to attach any possible asset that may be attachable in order to collect what it is owed to them. The use of such word is wrong by itself. It gives the indication that the government has the right to preclude any creditor, that in the exercise of its right has brought legal action, from getting paid. And any such legitimate action would be labeled "an interference" with the (perverse) tactic carried on by the Argentine officials. Neither the government nor any other creditor has the right to leave the non-accepting bondholders with the hands empty just because they can't accept the "sacrifices."

The point here is that the government is in default and New York law condemns defaults under bond contracts. All the Argentine savers want is to get paid. The government must pay them. This discussion is aim at finding a tactic to pay only the creditors that for whatever reasons accept the big losses. Therefore, the unanimous consent clause to modify the payment terms would turn meaningless.

WHY DID ELLIOT AND LEUCADIA (THE TWO MOST RECENT CASES AGAINST SOVEREIGNS) EXIST?: THE IMPORTANCE OF THE PAYMENT FLOWS IN THE CASE OF SOVEREIGN DEFAULTS

Due to the fact that defaulting sovereigns do not have a great number of assets abroad, the financial flows involving international payments have a great deal of importance. Defaulting sovereigns usually remove assets from the court jurisdictions back to their territories. Further, defaulting countries that do not have state-owned enterprises operating internationally (as the case of Argentina) do not have significant assets to be attached. But defaulting sovereign sovereigns keep paying certain debts to certain unsecured creditors. For example, in the Elliot case Peru kept paying the Brady-Plan creditors while it was in default with Pre-Brady-Plan creditors. By the same token, Nicaragua decided to default with holders of certain debt with foreign banks and investors but resolved to maintain itself current with bonds issued to indemnify victims of the Sandinista regime (the latter traded internationally through Euroclear). Even though Peru and Nicaragua were required for years to pay the defaulting debt they never paid attention to those claims. And investors and the courts finally got tired and attached money from those countries that was intended to be used to pay non-defaulting creditors. Those assets were attached while they still were under the property of the debtors; they were not attached from the pockets of the non-defaulting creditors. Without attaching this type of assets (payment flows), there is a risk that the judgment creditors may go years without collecting. As we mentioned, the Republic now

wants to isolate those payment flows so that the Argentine savers (that do not want to accept the "sacrifices" and recur to the protection of the New York laws and courts to exercise their well-recognized rights not to participate in the restructuring) go years without having the possibility to collect. The Argentine officials and politicians want the protection of the U.S. courts to do this. This can't be done without rendering the provisions of the bond contracts, the New York law on restructuring participation and the vast jurisprudence on the voluntary nature of the participation in restructurings totally meaningless.

PAYMENT FLOWS TO OTHER CREDITORS ARE "ATTACHABLE" ASSETS

The question should be: "can the payments to said unsecured creditor be attached by creditors that hold New York judgments granted due to a default with them? If, as I believe, the answer is yes, then the quote from the Republic's memorandum is a political and/or economic consideration whit no legal fundamental.

Until any payment that the Republic intends to direct to third parties is actually deposited with an account from such parties, it does not belong to said parties, but to the Republic. Therefore, those payments are assets of the debtor (this was exactly the decision in the Elliot case).

In this case, until any money is deposited with an account of the IMF and other unsecured creditors, such as the World Bank and the Inter-American

Development Bank, it belongs to the debtor and hence fully attachable under the lack of immunity those flows enjoy and in any event, under the waiver of immunity granted by the Republic in the contractual provisions that regulate the bonds.

In addition, the argument may be considered to support the following: "We care about defaulting with some (unsecured) creditors but not with you. We will use money that we may otherwise use to pay other creditors. And with that money we want to pay exclusively such other (unsecured) creditors and we don't want you to ever attempt to collect a piece of it (the use the funny "interference"). All for other (unsecured) creditors, nothing for you. Unless you accept the 'sacrifices.'" In Annex A hereby we include the applicable provisions of the U.S. Foreign Immunity Act. Argentina waived all protections under it.

WHY THE DISCUSSION OVER THE PARIPASSU CLAUSE IS ABSURD?

In reality, the discussion of the application of the pari passu clause to these proceedings allows the government to hide the money of it (their own assets) that is used to pay something (in this case, invoices with other unsecured creditors) and that is attachable in its entirety because it is not protected by immunity.

Therefore, those moneys should not, in the first place, even fall under the pari passu clause. They are assets that are still the property of the government and

as such should be attached integrally before they pass on to the property of other unsecured creditors.

The pari passu debate should be of no existence.

But, if your Honor still considers that the clause applies to these proceedings, we believe that the interpretation about the application still favors the Argentine savers that have obtained attachments.

DISCUSSING THE PARI PASSU CLAUSE IN ANY EVENT

Although we believe the discussion over the application of the pari passu is meritless (because all payments attached should go first to the account to the Argentine investors that hold judgments), we will, in any event, discuss this clause in the, we believe, remote case that the U.S. court accepts this discussion.

The legal representatives of the Republic start the memorandum by saying: "no treatise on banking law or legal opinion writing has ever suggested that the pari passu clause requires each creditor to be paid pro rata, prohibits payment to one creditor because another creditor has an outstanding judgment, or permits a judgment holder to enjoin payments to other creditors." False. Says Professor Philip R. Wood: "In the state context, the meaning of the clause is uncertain because there is no hierarchy of payment which is legally enforced under a bankruptcy regime. Probably the clause means that on a de facto inability to pay external debt as it falls due, one creditor will not be preferred by a method going beyond contract; and (perhaps) that there will be no discrimination against the

same class in the event of insolvency."[7] And he also says: "In government loans, the clause is probably to be construed as a general non-discrimination clause prohibiting, e.g., the allocation of insufficient assets to one creditor if the state is effectively bankrupt."[8] English commentator William Tudor said: "the pari passu clause is primarily intended to prevent the earmarking of revenues of the government towards a single creditor, the allocation of foreign currency reserves and generally against legal measures which have the effect of preferring one set of creditors against the others or discriminate between creditors."[9] University of California Professor Vinok Aggarwal wrote: "as a direct effect of the pari passu provision and in connection with external debt only, the lender shall not be discriminated in the matter of availability of assets."[10] Mr. Brian Semkow says that in the context of sovereign borrowing, the pari passu provision "will prevent sovereign borrowers from discrimination against the lending banks in the payment of creditors out of general revenues or foreign currency reserves."[11]

Interestingly, Lee Buccheit, from the law firm that represents Argentina and an article of whom we will describe below, wrote: "A lender who remains unpaid at a time when other creditors are current on their loans may articulate his grievance in terms of liberty, equality or fraternity, but he should not invoke his pari passu covenant as the legal basis for his disappointment. This provision

[7] Philip R. Wood, PROJECT FINANCE, SUBORDINATED DEBT AND STATE LOANS (Law and Practice of International Finance 1995.
[8] Philip R. Wood, INTERNATIONAL LOANS, BONDS AND SECURITIES REGULATION 41 (Law and Practice of International Finance 1995.
[9] Sovereign Risk and Immunity minder English Law and Practice, in Robert S. Rendell, ed. International Financial Law, Vol 1, p 71 at 95 (2ed. 1983.
[10] Vinod K. Aggarwal, Negotiation of Specific Clauses of Loan Agreements.
[11] Brian W. Semkow, Sindicating and Rescheduling International Financial Transactions: A Survey of the Legal Issues Encountered by Commercial Banks, 18 Int'l Law. 869, 899 (1984).

assures the creditor that its loan will not be subordinated to the claims of other creditors in the event of the borrower's bankruptcy, but it does not force the solvent borrower to make pro rata payments to all its creditors."[12] At *contrarius sensu,* it forces the insolvent borrower to make pro rata payments to all its creditors.

As it is world-wide recognized by the markets, the official financial community (IMF, the U.S. Treasury, the Group of 7, etc.) and the legal community Argentina is insolvent as it can't honor its debt. Therefore, it should be forced to make pro rata payments to all its creditors.

The fact that there are no legal insolvency proceedings for countries does not mean that countries can go insolvent. Again, the fact that countries may be insolvent is internationally recognized with no opposition to it.

The Republic also says that never before a creditor has attempted to give the clause the interpretation that it requires equal treatment. This has explanation however. At the corporate world, the creditors have the right to attach any and all assets of the debtor (with the exception of certain limitations that may apply) and use them to satisfy their claims (this is what your Honor should do in these proceedings as we explained before), without sharing it with any other creditor, unless creditors having judgments and attachments. And, if the judgments and attachments threat the whole business or existence of debtors, then they file for bankruptcy. What does the bankruptcy court do on bankruptcy proceedings

[12] Lee C. Buccheit, How to Negotiate Eurocurrency Loans (2nd ed. 2000), at 83.

regarding unsecured debt? In general, it applies pari passu clauses, sharing payments among creditors of the same category. Therefore, at the corporate world, there was no necessity to apply the pari passu clause to pre-bankruptcy proceedings, and the clause is fully applied at the bankruptcy proceeding stage. For example, Judge Martin of the Southern District of New York ruled that the pari passu provision's only effect in terms of legal remedies was to ensure that in the event of Tribasa's bankruptcy, all of Tribasa's noteholders would share equally in the distribution of the company's unencumbered accounts. Citing the Elliot v. Peru decision in Brussels Judge Martin speculated that the pari passu covenant "may ... have given the Smith Parties (the discriminated plaintiffs) the right to obtain an injunction to bar Tribasa (the defendant) from making preferential payments to some of its note holders and that another note holder with notice of that injunction could be liable ... if it thereafter accepted preferential payments."[13]

At the sovereign arena, on the other hand, there have been only a handful of default cases, and in at leats three of the few existing cases, the equal treatment issue was present and in fact, constituted the central aspect of the collection stage of the litigation. These three cases are Elliot (decided on the New York courts), Leucadia (in Belgium) and Red Mountain (in California courts)[14], which are three of the most recent litigations on the sovereign area. In all these three cases the

[13] National Financiera, SON v. Chase Manhattan Bank, NA, No 00 Civ. 1571 (JSM), 2003 WL 1878415, at 2 (SDNY, Apr. 14, 2003).
[14] Red Mountain Fin., Inc v. Democratic Republic of Congo and Nat'l Bank of Congo, Case No. CV 00-0164 R (C.D. Cal. May 29, 2001). The judge expressly enjoined Congo from making any payments in respect of its External Indebtedness (as defined in the loan instruments defaulted) without making a "proportionate payment" to Red Mountain.

courts favoured the creditors that suffered discriminatory acts from defaulting governments which were trying to pay only some unsecured creditors while not paying other unsecured creditors.

The Republic then indicates that the application of the pari passu clause would nullify some other clauses. No serious and developed fundamentals were presented to back such a general and mistaken phrase.

The Republic says first that such application would nullify the cross-default clause. Under this general and unexplained statement, the Republic seems to suggest that a non-accepting bondholder might use this clause instead of the pari passu. And if it uses the pari passu clause, then the cross-default would be left effectless. What is the point of using a clause (cross-default) that is useless and that directly does not apply to the collection part of the litigation?. Indeed, the cross-default clause is useless and it has no application at the collection stage and is supersedes by a direct payment default on the part of the debtor.

Second, the Republic indicates that the acceleration clause would also loss its effects. I ask why?. The acceleration clause permits to claim also the principal before the original maturity date. This clause still maintains its full force and effect, and in fact the Argentine investors are using it in connection with these proceedings.

Third, the Republic alleges that the application of the pari passu to these proceedings would render the negative pledge clause useless. In fact, the contrary is true. The negative pledge clause works together with the pari passu clause. As

an example of this statement, the negative pledge clause was expressly quoted by one of the courts in Belgium that resolved this issue. Such court affirmed that the payments to some creditors and the lack of payment to others constitute a violation of the negative pledge that provided that Nicaragua was prevented from implementing any preferential mechanism with the effect of using its assets to grant privilege to certain creditors.

Fourth, the Republic also asserts that the application of the pari passu clause to these proceedings would render the sharing clause useless. This clause, however, still fully applies and in fact strengthens the position of the Argentine investors. Under the sharing clause, no bondholder of a certain series of bonds may collect more than a bondholder of the same series, absence a judgment. Therefore, the government would be prohibited from doing what it wants to do: paying A and not B (if they are from the same series and absence a judgment). But, the sharing clause does not apply to credits that arise from different instruments.

The Republic also indicates that "for private borrowers, nullify the limits on involuntary bankruptcy petitions by allowing a single unpaid creditor to force a default on all its debtor's other obligations." In fact, a creditor may attach any asset of the debtor, including money that may, and/or is about to be used to pay any other creditor until that money is deposited with an account of said other creditor.

The Republic further reiterates that for sovereign borrower, the pari passu would prevent voluntary debt restructuring by giving any hold-out creditor a veto over payment to creditors who would otherwise agree to receive restructured debt and would create the absurd result of holding every creditor hostage to every other creditor, since no one could be paid except by unanimous consent. Again, the question should be: are those flows attachable under New York law? If they are, as we believe so, then they may be attachable. These are the rules under which the bonds were issued. What the Republic wants is changing the immunity laws and leaves the clause where it waived the immunity effectless. The Republic pretends to have immunity where it does not have it. Creditors have the right to participate in restructurings, what includes the option not to participate in them and instead bring legal action. The legal actions to have some concrete effects must give alternatives to collect what is owed, provided there are assets (including financial flows) that, as is this case, may be attached. If seven creditors agree to participate in the restructuring, fine. And if three creditors agree not to participate, fine too. The latter creditors have the right to attach "attachable" assets. If this situation leads the seven finally not to accept due to the fear of having the payments attached, then the debtor should better the terms of the offer. These are the rules under which the bonds were issued as in the sovereign financing although there are de facto insolvencies, there are no formal bankruptcy proceedings. See Krueger above.

The Republic's lawyers says: "The Republic must be permitted to pay the new restructured debt as well as its debt to multilateral lenders like the IMF, and holders of other debt incurred by the Republic in solving its financial crisis." This is again an asking to legalize the following: "I care only about the IMF and the creditors that accept the "sacrifices."

Further, the Republic says "If this process is to succeed...." There is no New York case on the sovereign defaults (or any other authority) that indicates that a debt restructuring, to "succeed", must be based on destroying the rights of those bondholders that decide not to participate in the restructuring.

The pari passu clause says: "The Securities will constitute (except as provided in Section 11 below) direct, unconditional, unsecured, and unsubordinated obligations of the Republic and shall at all times rank pari passu and without any preference among themselves. The payment obligations of the Republic under the Securities shall at all time rank at least equally with all its other present and future unsecured and unsubordinated External Indebtedness (as defined in this Agreement)." (Argentine Fiscal Agency Agreement, dated October 19, 1994.)

One of the core parts of the pari passu clause is the two words "without preference." If having the right to get paid over other creditors is not a preference, then what is a preference?. The Republic's strategy (discriminating among unsecured creditors) constitutes a payment priority (in favour of the IMF and the

creditors that accept the big losses contemplated under the exchange offer) that violates the rights of holders of other unsecured debt.

Other important part is the word "rank." This word rank means "particular order or position." For example the following order or position: A B C D

A is before B, C and D. B is before C and D and C is before D, which is last in the order. Under the Republic's proposal, there would be a well defined and shielded "rank" whose members would not rank pari passu at all:

A, would be the International Monetary Fund (an unsecured creditor)
B, would be other international organizations (unsecured creditors)
C, would be the creditors that accept the "sacrifices" (unsecured creditors)
D and last, would be the creditors that do not accept the "sacrifices" (unsecured creditors).

This is a proposed "order or position". This is "to classify". This is illegal because it is detrimental to D since it creates a "payment priority" which is prohibited by the clause. When D acquired the bonds, there was no rank where A, B and C ranked first.

Then the Republic says: "The correct adjectives to be used with 'rank' are therefore those such as 'senior' and 'subordinate', not earlier, simultaneous or later. Likewise, although Black's Law Dictionary does not define 'rank' per se, it defines 'priority' as 'the status of being earlier in time or higher in degree or rank.'"

As the Argentine counsel says, "priority" means, indeed, "earlier in time." Therefore, a debt being earlier in time has priority. Gets paid first. As the Republic says, a creditor with priority is senior to a creditor that has no priority ("later in time"). A creditor with a payment priority ("earlier in time") does not rank pari passu with others. It ranks higher. Aren't A, B and C earlier in time (of payments) than D?. Yes, they would be under the Argentine proposal because the Republic indicated that it will only pay the IMF and those bondholders that accept the exchange offer. As the Republic said, the non-accepting bondholders won't be paid by the Republic. Therefore, it is more than a priority: it is almost about the existence of the claim where the bondholders that hold out would have seen their claims disappeared.

The prohibition against subordination is that there will be no "order" or "position" regarding the legal effects of the instruments subject to the ranks. What is the point of saying that the rank is the same (as the Republic alleges) but the order or situation regarding what we all care, the legal effects (the payment priority), are not the same?. "Senior" means a debt that is paid first that other debts. When the senior debt is fully paid, the debtor will pay the subordinated debt. The legal effects (the legal reality) of a structure like this are that some

creditors collect first and others collect second, or third or fourth, or never collects. Again, what are the legal effects of the government strategy which is putting in place a "legal" structure that allows it to safely pay "some" creditors while forgetting other by sending them to the last places in the "rank" (order or position)?. Put in place a senior-junior debt structure. As we said, the President and the Ministry of Economy from the Republic have expressed many times that the bondholders that do not accept the new bonds won't be paid. So there is the possibility that if the unreasonable petition of the Republic is approved by the U.S. courts, then the subordinated creditors (the non-accepting Argentine savers for example) won't even collect a penny.

Some commentators quoted by the Republic such as Mr. Gulati and Mr. Klee are academically associated to the leading partner in the sovereign field of the firm representing the Republic, Mr. Buccheit. Their opinions therefore may not be considered impartial. See for example how they explained how the pari passu "works in practice" as they said, forgetting to add "according to them":

"The pari passu works as a covenant by the borrower that it will not bestow a legally senior priority status on certain lenders. This protects against the temptation for the sovereign to enact laws affecting the legal ranking of creditors. 'Ranking' pari passu therefore is about insolvency payouts (in the corporate

context) or about alteration of payment priorities by law (in the sovereign context). It is an equal ranking, but it applies to specific contexts." [15]

But see other opinions quoted by the Republic, either in the Republic's petition or in an article written by Mr Buccheit about this topic:

Philip R. Wood wrote: "In the case of a sovereign state, ... the clause is primarily intended to prevent the earmarking of revenues of the government or the allocation of its foreign currency reserves to a single creditor and generally is directed against legal measures which have the effect of preferring one set of creditors over the other or discriminating between creditors."[16]

K. Venkatachari wrote in his famous The Eurocurrency Loan: Role and Content of the Contract: "In the case of the sovereign borrower the [pari passu] clause is intended to prevent the borrower giving preference to certain creditors by, say, giving them first bite at its foreign currency reserves or its revenues... This kind of clause catches arrangements which merely give a right of priority of payment."[17]

Thomas A. Duvall HI, Chief Counsel to the World Bank wrote: "With loans to a sovereign state which are not subject to domestic bankruptcy laws and whose assets cannot be liquidated by judicial proceedings... it is generally believed that a pari passu covenant prevents the sovereign from discriminating between lenders by law or governmental decrees which prefers some unsecured

[15] Gulati and Klee, Sovereign Piracy, 56 The Bus. Law. (Authorities, tab G) 635, at 636 (ABA Publ'ns Feb. 2001).
[16] Philip R. Wood, LAW AND PRACTICE OF INTERNATIONAL FINANCE 156 (1980).
[17] The Eurocurrency Loan: Role and Content of the Contract.

creditors over others - for example, allocating reserves for the benefit of some creditors or devoting some government revenues to servicing specific debts."[18]

The point here is that the violation occurs generally but not exclusively by legal measures that have the effect of preferring one creditor over other or discriminating between them. So, the violation may not necessary occur from legal measures and second, the arrangement of giving preferences on revenues, reserves, assets, etc... may be formal or informal. The Republic here will approve the offer, the exchange and related acts through legal measures. These legal measures are either a law from the Legislative, a decree from the Executive or(/and) a resolution from the Ministry of Economy. These legal measures would be complemented by and eventual judicial arrangements involving U.S. courts to create a legal "shielded channel" through which revenue stream from the government would flow toward the creditors that accept the offers and which would have the legal effect of preventing non-accepting bondholder any access to those revenue stream, which would be "earmarked" through legal measures. In all event, the government will at least establish a *de facto* priority (paying some creditors while not others) therefore doing what the pari passu seeks to prevent: the violation of the rights of the creditors of the same category. Otherwise, why would any government take legal measures to establish formal senior-junior debt structures if it could do something with the same effects without considered to be breaking the law or the contracts?. Governments would just resolve to pay certain

[18] Thomas A. Duvall III, Chief Counsel to the World Bank, Legal Aspects of Sovereign Lending, in External Debt Management: An Introduction 35, 45 (June 1994).

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debts (the senior ones) and not pay others (the junior ones). It is not serious arguing that to be illegal, the discrimination requires legal measures establishing formal subordinations. What is the difference between doing the same thing (discriminating among pari passu unsecured creditors) *de facto* or through the law?.

The literal meaning of the term pari passu comes from the Latin noun "passus" which means "step, pace, stride" and from the Latin adjective "par" meaning "equal or like". The term is defined in the Webster's New International Dictionary: "By an equal progress; equably, ratably; without preference. Used specially by creditors who, in marshalling assets, are entitled to receive out of the same fund without any precedence over each other."

New York University Professor Andreas Lowenfeld was invited to opine on the Elliot case about he application of the pari passu clause to that litigation. He concluded that the pari passu clause does really mean what it says: "a given debt will rank equally with other debt of the borrower, whether that borrower is an individual, a company or a sovereign state."

Lowenfeld opined in line with what was written by the well-known Profesor Philip R. Wood: if the government is insolvent, the pari passu orders to distribute any asset pari passu among unsecured creditors.

Lowenfeld then added that the Court of Appeals of the Federal Courts in New York have already decided on the issue under analysis in the case Alliance Bond Fund, Inc. v. Grupo Mexicano de Desarrollo S.A. (143 F3.d 688 (2d Cir.

1998)). In this case, the Mexican borrower and its guarantor (Grupo Mexicano) were enjoined from making payments to some creditors while plaintiffs, who were the beneficiaries of a pari passu clause, were going to be left out.

Lowenfeld concluded in the right direction saying that the pari passu clause "creates a binding and continuing obligation to treat all covered borrowers equally without discrimination."

The Republic says it is impossible to pay all debts the same date because they have different maturity dates. There is no discrimination paying one debt that matures on January 2003 while not paying a debt that is due on January 2005. The discrimination appears when a debtor pays an unsecured debt that is due on January 2003 and does not pay an unsecured debt that is due the same day or before. The unpaid creditor should be able to sue and attach those payments. There would be no question that it should be able to attach these assets (the payments) while they are property of the debtor. If your Honor applies the pari passu clause those payments would be shared with the other creditors; if the court decides not to apply such clause, those assets would then be used to pay first the suing creditors and if there are assets left, to the other creditors.

In an interesting academic article,[19] two partners of the law firm that defenses Argentina (what is an indication of their lack of impartiality and what turns the article more into a memorandum in support of the Republic position)

[19] The Pari Passu Clause in Sovereign Debt Instruments, Lee C. Buccheit and Jeremiah S. Pam, Working Paper, Harvard Law School, December 2003.

explain, in any event, how worried sovereign creditors were about being discriminated by the sovereign in the service of the debt. One of the authors is Mr. Buccheit. The lawyers of the firm representing the Republic[20] indicate in the article that the pari passu clause (along with the negative pledge clause -we have always understood that the two clauses work together) had always in mind protecting creditors from discriminatory measures, either formal or informal, taken by the debtor governments to breach the equal treatment among bondholders. The authors indicated that the pari passu was not focused only on one type of action, but on three: (i) earmarking of assets by the sovereign; (ii) decrees or laws from the governments breaking the equal rank among unsecured creditors; and (iii) involuntary subordination among creditors produced by certain practices common in civil law countries.

This means that the discrimination can't come from one individual source but from more than one. Further the sources are not considered to reduced to the existing ones. If discrimination occurs (either with formal mechanisms used or not) and there is a clause that usually was aim at fighting against discrimination (through different measures), then this clause should apply. How can be defendable an argument saying that discriminating through a determined mechanism, let's say mechanism A, is illegal while discrimination using mechanism B is not. The concern underlying the pari passu clause (in some cases along with the negative pledge clause) has always been the same: being subject to a mechanism (either formal or informal and whether A, B or C) of being left set

[20] The article says that Mr. Buccheit is not involved in the representation of Argentina. Some partners of Mr. Buccheit are involved.

aside from the payment flows. This is exactly what the Republic wants to accomplish: discriminate through mechanisms that involve: (i) an exchange offer; (ii) acts or decrees from the Argentine powers approving the exchange and all related acts; (iii) assuming the obligation to keep current (pay) on the new bonds, what includes generating and disposing of certain revenue stream contemplated in the Annual Budgets of the government in favor of that debt (a sort of earmarking); (iv) express and permanent declarations from the Ministry of Economy and the President that the bondholders that don't accept won't be paid; and (v) protection of the U.S. courts to "isolate" those revenue stream destined to pay the accepting bondholders.

Regarding the IMF and other international organizations, the Republic will also include in the Annual Budgets revenue stream to pay them and similarly require the U.S. courts a "shielded channel" so that the non-accepting holders can't get paid. This means that there would be no revenue streams contemplated for them until all other creditor (the accepting bondholders and the IMF) gets paid. All the Republic wants if to "legally" escape the enforcement of the bond contracts and have immunity where it has no it.

CONCLUSION

The U.S. court should reject the petition of the Argentine politicians and officials and enforce the bond contracts. As part of such enforcement, the assets of the debtor that is intended to be used as money to repay certain unsecured

creditors should be fully attached, for the benefit of the Argentine savers that have obtained judgment and attachments. The attached assets should be used first to pay those savers. If the court applies the pari passu clause those assets (payments) should be distributed on a pro rata basis among the IMF, the accepting bondholders and the judgment creditors.

ANNEX **A: Relevant Sections of the U.S. Foreign Sovereign Immunity Act**

§ 1602. Findings and declaration of purpose

The Congress finds that the determination by United States courts of the claims of foreign states to immunity from the jurisdiction of such courts would serve the interests of justice and would protect the rights of both foreign states and litigants in United States courts. Under international law, states are not immune from the jurisdiction of foreign courts insofar as their commercial activities are concerned, and their commercial property may be levied upon for the satisfaction of judgments rendered against them in connection with their commercial activities. Claims of foreign states to immunity should henceforth be decided by courts of the United States and of the States in conformity with the principles set forth in this chapter.

§ 1605. General exceptions to the jurisdictional immunity of a foreign state

(a) A foreign state shall not be immune from the jurisdiction of courts of the United States or of the States in any case --

(1) in which the foreign state has waived its immunity either explicitly or by implication, notwithstanding any withdrawal of the waiver which the foreign state may purport to effect except in accordance with the terms of the waiver;
(2) in which the action is based upon a commercial activity carried on in the United States by the foreign state; or upon an act performed in the United States in connection with a commercial activity of the foreign state elsewhere; or upon an act outside the territory of the United States in connection with a commercial activity of the foreign state elsewhere and that act causes a direct effect in the United States;
(3) in which rights in property taken in violation of international law are in issue and that property or any property exchanged for such property is present in the United States in connection with a commercial activity carried on in the United States by the foreign state; or that property or any property exchanged for such property is owned or operated by an agency or instrumentality of the foreign state and that agency or instrumentality is engaged in a commercial activity in the United States;
(4) in which rights in property in the United States acquired by succession or gift or rights in immovable property situated in the United States are in issue;
(5) not otherwise encompassed in paragraph (2) above, in which money damages are sought against a foreign state for personal injury or death, or damage to or loss of property, occurring in the United States and caused by the tortious act or omission of that foreign state or of any official or

employee of that foreign state while acting within the scope of his office or employment; except this paragraph shall not apply to --

(A) any claim based upon the exercise or performance or the failure to exercise or perform a discretionary function regardless of whether the discretion be abused, or
(B) any claim arising out of malicious prosecution, abuse of process, libel, slander, misrepresentation, deceit, or interference with contract rights; or

(6) in which the action is brought, either to enforce an agreement made by the foreign state with or for the benefit of a private party to submit to arbitration all or any differences which have arisen or which may arise between the parties with respect to a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration under the laws of the United States, or to confirm an award made pursuant to such an agreement to arbitrate, if (A) the arbitration takes place or is intended to take place in the United States, (B) the agreement or award is or may be governed by a treaty or other international agreement in force for the United States calling for the recognition and enforcement of arbitral awards, (C) the underlying claim, save for the agreement to arbitrate, could have been brought in a United States court under this section or section 1607, or (D) paragraph (1) of this subsection is otherwise applicable.

§ 1609. Immunity from attachment and execution of property of a foreign state

Subject to existing international agreements to which the United States is a party at the time of enactment of this Act the property in the United States of a foreign state shall be immune from attachment arrest and execution except as provided in sections 1610 and 1611 of this chapter.

§ 1610. Exceptions to the immunity from attachment or execution

(a) The property in the United States of a foreign state, as defined in section 1603 (a) of this chapter, used for a commercial activity in the United States, shall not be immune from attachment in aid of execution, or from execution, upon a judgment entered by a court of the United States or of a State after the effective date of this Act, if --

(1) the foreign state has waived its immunity from attachment in aid of execution or from execution either explicitly or by implication, notwithstanding any withdrawal of the waiver the foreign state may purport to effect except in accordance with the terms of the waiver, or
(2) the property is or was used for the commercial activity upon which the claim is based, or

(3) the execution relates to a judgment establishing rights in property which has been taken in violation of international law or which has been exchanged for property taken in violation of international law, or
(4) the execution relates to a judgment establishing rights in property —

(A) which is acquired by succession or gift, or
(B) which is immovable and situated in the United States: Provided, That such property is not used for purposes of maintaining a diplomatic or consular mission or the residence of the Chief of such mission, or

(5) the property consists of any contractual obligation or any proceeds from such a contractual obligation to indemnify or hold harmless the foreign state or its employees under a policy of automobile or other liability or casualty insurance covering the claim which merged into the judgment, or
(6) the judgment is based on an order confirming an arbitral award rendered against the foreign state, provided that attachment in aid of execution, or execution, would not be inconsistent with any provision in the arbitral agreement.

§ 1611. Certain types of property immune from execution

(a) Notwithstanding the provisions of section 1610 of this chapter, the property of those organizations designated by the President as being entitled to enjoy the privileges, exemptions, and immunities provided by the International Organizations Immunities Act shall not be subject to attachment or any other judicial process impeding the disbursement of funds to, or on the order of, a foreign state as the result of an action brought in the courts of the United States or of the States.