SHEARMAN & STERLING LLP

LITIGATION CLIENT PUBLICATION

January 7, 2013

Don't Cry for Me Argentine Bondholders: Update of Second Circuit Briefing

If you wish to receive more information on the topics covered in this publication, you may contact your regular Shearman & Sterling contact person or any of the following:

Contacts

Henry Weisburg
New York
+1.212.848.4193
hweisburg@shearman.com

Antonia E. Stolper
New York
+1.212.848.5009
astolper@shearman.com

Stephen J. Marzen
Washington, DC
+1.202.508.8174
smarzen@shearman.com

Patrick Clancy
London
+44.20.7655.5878
patrick.clancy@shearman.com

SHEARMAN.COM

An update on the many recent appellate filings in the *NML v. Argentina* matter.

As provided in the schedule adopted by the Second Circuit for hearing the appeal from Judge Griesa's November 21 Injunction, the principal appellate brief for the Republic of Argentina, as well as the briefs of various entities granted "non-party appellant" and "intervenor" status, and briefs of *amici* supporting both sides, have all been filed.

The plaintiffs' briefs are due to be filed on January 25, 2013; replies by the appellants are due on February 1 (at which point briefing should be concluded); oral argument is scheduled for February 27. We will issue a further update following receipt of these additional briefs.

We summarize below the main arguments running through these many pleadings. Copies of all of the filings with the Second Circuit discussed below, as well as Judge Griesa's November 21 Injunctions and our prior notes on this topic, can all be found on our Argentine Sovereign Debt webpage, at http://www.shearman.com/argentine-sovereign-debt/.

Summary of Briefs Filed to Date

Brief for The Republic of Argentina

The brief filed on behalf of Argentina advances multiple arguments, roughly divisible into four categories:

- **The Injunction violates the Foreign Sovereign Immunities Act**: Section 1609 of the FSIA provides (subject to certain exceptions set forth in Section 1610) that "*the property in the United States of a foreign state shall be immune from attachment arrest and execution . . . .*" Citing that provision, Argentina argues that the injunction "*clearly violate[s] the FSIA by compelling the Republic to bring immune assets into the country*

to satisfy the balance of plaintiffs' contract claims for money damages" and that it "is the functional equivalent of a . . . 'turnover' order, which would clearly be barred by the FSIA." (Argentina Brief at 21.) Argentina goes on to say, "*the Amended Injunctions violate the principles behind it by essentially invading the Treasury of a foreign sovereign, and commandeering its Legislative and Executive branches - based on an unprecedented reading of a boilerplate clause—to appropriate funds for a specific purpose while forbidding their appropriation for another purpose unless the first appropriation is made*." (Argentina Brief at 22–23.) This argument has added significance because it is the argument that most plausibly could be the basis for a successful certiorari petition to the Supreme Court (even if still an extreme long shot).

- **The Injunction is inequitable**: Argentina next argues that the Injunction puts the plaintiffs "*in a far better position than other creditors*" and is therefore "the antithesis of equity." (Argentina Brief at 2.) It goes on to argue the injunction would:

  > *treat plaintiffs better than the exchange bondholders, because plaintiffs would get 100% of all debt while the exchange bondholders (representing 92% of the old debt) would get only a single installment of interest on a lower amount. And it would put plaintiffs ahead of other holdouts, who would presumably have claims based on their own "pari passu rights." Both groups would have the right to demand in the name of "equality" what plaintiffs get, and as a result would trigger claims by all Argentine debt holders, thus threatening to undo Argentina's debt restructuring.* (Argentina Brief at 29.)

- **The Injunction impairs the rights of holders of the Exchange Bonds**: Argentina also argues that the Injunction "*unreasonably burdens*" the Exchange Bondholders, who are "*innocent third parties*" as to whom the plaintiffs "*assert no rights*." (Argentina Brief at 31–32.) Argentina does not address this argument at length, clearly leaving it to the Exchange Bondholders and others to address more completely.

- **The Injunction improperly enjoins participants in the international payments system**: Argentina next argues that the Injunction improperly extends to financial institutions in the worldwide payments system, such as the "*hundreds of third parties located throughout the world, 'including' BNYM, DTC, the European 'clearing systems' Euroclear and Clearstream, and other entities that are neither the 'agent' of, nor acting in 'concert' with, the Republic*." (Argentina Brief at 33.) Argentina argues this overbreadth violates both Article 4A of the Uniform Commercial Code (see UCC §503) and provisions of the Federal Rules of Civil Procedure governing injunctions (see F.R.Civ.P. 65(d)(2)(C)).

More generally, Argentina advances throughout its brief a "public policy" argument, repeatedly suggesting that the Injunction poses a fatal threat to debt restructurings generally. "*If the Amended Injunctions are allowed to stand, we may very well see the end of such restructurings and enter an era where debt crises are unresolvable." (Argentina Brief at 26.) "The district court's pari passu clause interpretation and related remedy will encourage commercial parties to avoid New York law, and as a consequence to move their financing business outside the realm of New York and the New York financial services industry*." (Argentina Brief at 51.)

Further, Argentina announces in its brief that it is willing to offer plaintiffs the same economic deal that it offered to those bondholders who accepted Argentina's prior exchange offers (an offer that the plaintiffs will certainly reject and the Court will most likely ignore).

Finally, Argentina suggests that the Circuit Court should certify to the New York State Court of Appeals the question as to the appropriate remedy for breach of a *pari passu* clause. (*See* discussion below as to certification to the New York Court of Appeals.)

Briefs for Non-Party Appellants and Intervenors

Three different entities have been granted leave by the Second Circuit to participate in the *NML* appeal as "non-party appellants." (This designation is significant, because it may leave some or all of those participants free of the Injunctions if the Second Circuit holds that they are not in "active concert or participation" with a person properly subject to the Injunctions. The "non-party" designation may also be important for subsequent proceedings because only a "party" may petition for rehearing by the panel (Fed. R. App. P. 40(a)(1); 2d Cir. Local R. 40.1(d)), rehearing by the Second Circuit *en banc* (Fed. R. App. Pr. 35(b); 2d Cir. Local R. 35.1(a)), and review by the US Supreme Court by writ of certiorari (28 U.S.C. § 1254(1).) In addition, two entities have been given leave to participate as "intervenors." All have filed briefs.

Brief for Non-Party Appellant Exchange Bondholder Group

A group of significant holders of Exchange Bonds, constituting themselves as the Exchange Bondholder Group ("EBG"), has also filed a brief, advancing three basic arguments:

- **The Injunction is inequitable**: The EBG brief argues that the Injunction is a "judicial mousetrap" in which their property rights are unfairly used as "bait." (EBG brief at 25.)

  > *[T]he express purpose of the Injunction is to coerce the Republic into paying NML by forcing it to choose between the loss of market standing and paying NML. This imposes conditions on the Exchange Bondholders' otherwise unconditional rights to payment, leaving them at the mercy of the Republic's decision whether to pay NML*. (EBG Brief at 23.)
  >
  > *The Injunction inequitably prioritizes the interests of NML—a group of private litigants holding a tiny fraction of the Republic's total debt—over those of innumerable other bondholders*. (EBG Brief at 2.)

- **The Injunction violates the Fifth Amendment**: The EBG has also makes the argument that the operation of the Injunction violates the Due Process and Takings clauses of the Constitution. "*The Injunction thus constitutes a deprivation of private property for* ***private****, not public, purposes—a result forbidden by the Constitution as 'arbitrary and irrational' under long-standing due process principles." (EBG Brief at 34, emphasis in original.) "Although the Exchange Bondholders' property is not being seized outright by the government, the practical outcome of the Injunction will inevitably be, at a minimum, a 'significant restriction...placed upon [the Exchange Bondholders'] use of [their] property – clearly a 'taking.'*" (EBG Brief at 34; citation omitted.)

- **The Injunction was issued in breach of the EBG's right to procedural Due Process**: Finally, the EBG argues that the Injunction puts important rights of the EBG members at risk, but was issued without notice to them or an opportunity to be heard, and without joining them as necessary parties to the case. (EBG Brief at 36–44; see Fed .R. Civ. P. 19 & 60.)

Brief for Non-Party Appellant The Bank of New York Mellon

A brief has also been filed by the Bank of New York Mellon, the Indenture Trustee for the Exchange Bonds. It sets forth three central arguments:

- **The Injunction violates Due Process**: Noting that it is not a party to the case and has not been subjected to the District Court's jurisdiction, BNY Mellon argues that "*[t]he District Court . . . ran roughshod over the principles of proof, process and jurisdiction that implement the Constitution's promise of due process*." (BNY Mellon Brief at 19.) The Injunctions are alleged to offend due process for the additional reason that "*the Due Process Clause also prohibits punishment for 'lawful' conduct*," and "*[t]here is nothing unlawful in BNY Mellon's receipt or distribution of funds from Argentina to the Exchange Holders*." (BNY Mellon Brief at 20, 22.)
- **The Injunction cannot be justified under an "agency" theory**: BNY Mellon also attacks the District Court's determination that the injunction could be extended to the trustee on the basis that the trustee was in "*active concert*" with Argentina, as provided in the Federal Rule of Civil Procedure 65(d)(2). BNY Mellon first argued that "*no statute or rule of civil procedure can displace or negate in any way the safeguards provided by the Constitution concerning injunctions against non-parties . . . .*" (BNY Mellon Brief at 23.) Second, "*there is no proof that BNY Mellon can aid or abet the purportedly wrongful conduct – Argentina's refusal to make a Ratable Payment to Plaintiffs whenever it pays the Exchange Holders . . . . Argentina, alone, makes the decision on whether a Ratable Payment should be made and it does so without acting through or with BNY Mellon*." (BNY Mellon Brief at 2.)
- **The Injunction is contrary to the public interest**: BNY Mellon also argues that "*[c]ourts cannot exercise their injunctive power where it would disserve the public interest*," and that the Injunction does so by endangering the rights of non-parties, undermining the position of indenture trustees, unsettling commercial and creditor-debtor relationships, and threatening to trigger additional litigation. (BNY Mellon Brief at 32.)

The brief concludes by noting that, if the injunction is upheld, BNY Mellon "*will face a potential conflict between its obligations to the Exchange Holders under the Indenture and its obligations to the Court*"; it therefore "*respectfully requests that this Court clarify that BNY Mellon's compliance with the Injunctions will not result in any liability to BNY Mellon*." (BNY Mellon Brief at 41.) Notably, BNY Mellon does not address the UCC Article 4A issue.

Brief for Non-Party Appellant Fintech Advisory, Inc.

Fintech Advisory, a significant Exchange Bond holder, filed a brief asserting that the Injunction violates "*basic laws of trusts and property . . . and any conceivable principle of equity*" (Fintech Brief at 12), Fintech's brief makes three more specific arguments:

- **The analysis supporting the Injunctions is flawed and incomplete**: Fintech asserts that the District Court's orders lack support because it "*did not give any reasonable consideration to the impact [of the Injunctions] on third parties and their interests*." (Fintech Brief at 12, 15.) Fintech's brief also disputes the District Court's conclusion that the indenture trustee and other financial intermediaries are in "active concert or participation" with Argentina. "*[T]he Trustee, DTC, and other non-parties are independent actors which do not act on behalf of the Republic . . . The conduct of these third parties is not active concert or participation in the Republic's wholly separate and independent decision to pay or refrain from paying the Original Bondholders*." (Fintech Brief at 22, 25.)

- **The Injunctions constitute a "tak[ing]" in violation of the Fifth Amendment**: "The beneficial owners of the Exchange Bonds, such as Fintech, hold equitable title to the Trust assets and are the 'real owners' of the Trust property." (Fintech Brief at 26.) Any restraint upon the distribution of payments made into the trust by Argentina would therefore constitute "a taking of Fintech's property without Due Process." (Fintech Brief at 12–13.) Moreover, not only the payments themselves but "Fintech's rights and expectations under its valid contracts with the Republic are 'property' protected by the Fifth Amendment." (Fintech Brief at 29.)
- **The Injunctions violate the UCC**: Fintech also asserts that the Injunctions contravene Article 4A of the UCC, which prohibits injunctive relief against intermediary banks.

Brief for Intervenor ICE Canyon LLC

ICE Canyon, a holder of Euro-denominated GDP-linked paper issued by Argentina, was given leave by the Second Circuit to appear as an "*intervenor*." ICE Canyon has filed a brief contending that the GDP-linked paper is not "*indebtedness*" for purposes of the *pari passu* clause, and that the Court of Appeals should clarify that these securities are not subject to the Injunctions. ICE Canyon further argues that the Injunctions have an impermissible extra-territorial impact, as the payment stream for the GDP warrants does not run through the US, and that the GDP warrant holders have been denied due process.

Brief for Intervenor Euro Bondholders

The Second Circuit also granted leave to appear as an intervenor to the Euro Bondholders, representing holders of Exchange Bonds issued in Euros. They filed a brief arguing that, since the payment stream for the Euro-denominated Exchange Bonds does not run through the United States, the Injunctions are excessively broad, and that the Injunctions "*threaten[] to spur a flood of foreign litigation and increase uncertainty in financial markets worldwide*." (Euro Bondholders' Brief at 2.)

Briefs for *Amici*

Eleven briefs on behalf of *amici* have been filed. Five amici support reversal and six amici support affirmance. These briefs are summarized below. Significantly, no *amicus* brief was filed by the United States Government with respect to Argentina's appeal from the November 21 Injunction.

Amicus Brief for The Clearing House Association L.L.C. (supporting reversal)

The Clearing House brief primarily advances the argument that the extension of the Injunctions to non-parties engaged in the payment stream with respect to the Exchange Bonds—who are simply carrying out "*ordinary business activities*" or "*acting pursuant to a pre-existing duty*"—are not subject to injunction under Federal Rule of Civil Procedure 65(d), as they are not properly categorized as "*persons in active concert or participation*" with defendant. More broadly, the Clearing House argues that the Injunctions improperly "*commandeer[]*" third parties in the service of one creditor to enforce the defendant's obligation to a different creditor.

Amicus Brief of The American Bankers Association (supporting reversal)

The American Bankers Association makes the point that indenture trustees play a critical role in the US banking system, and that it would be detrimental to the operation of US capital markets to expose such trustees to injunctions and similar litigation risks. More pointedly, the Association argues that the trustee on the Exchange Bonds, BNY Mellon, is not acting "*in active concert or participation*" with Argentina, and therefore cannot be within the permitted scope of an injunction under Federal Rule of Civil Procedure 65(d).

Amicus Brief for Euroclear Bank SA/NV (supporting reversal)

Euroclear Bank has filed a short letter brief with the Court of Appeals asserting that the Injunctions breach both UCC 4A and Federal Rule 65(d), have an improper extraterritorial impact, and would require Euroclear to breach the laws of Belgium (where Euroclear is based).

Amicus Brief for Anne Krueger (supporting reversal)

Professor Anne Krueger of Johns Hopkins, and formerly a senior officer at the IMF, has filed a brief that opens with the comment that it is "*written by an economist*," not a lawyer. Professor Krueger argues that affirmance of the Injunctions would have significant adverse economic consequences worldwide, because they would render sovereign restructurings more difficult and increase the cost of borrowing for sovereign debtors. She also comments that experience with collective action clauses is insufficient to conclude that they have mitigated issues created by "holdouts."

Amicus Brief for Puente Hnos. Sociedad de Bolsa A.A. (supporting reversal)

Puente Hermanos, an Argentine securities broker and active trader in Argentine securities, has filed a brief which disputes the District Court's (and Second Circuit's) interpretation of the *pari passu* clause, and argues that the Injunctions provide disproportionately favorable and not "equal" treatment to the plaintiffs. Puente also argues that the Injunctions improperly seek to enjoin non-US entities that are not within the jurisdiction of the courts of the United States, who did not receive adequate notice of the proceedings in this case.

Amicus Brief for Duane Morris Individual Plaintiffs (supporting affirmance)

A group of individual plaintiffs represented by the law firm Duane Morris filed a brief disputing the characterization of the plaintiffs in this case as "*vulture funds*," noting that some of the plaintiffs are individuals and others who purchased FAA Bonds at full price upon their initial offering. They ask that the Court of Appeals, in any balancing of the equities, consider that the Exchange Bondholders are "*no more 'innocent' than the holdout bondholders who were duped by Argentina*." (Individual Plaintiffs' Brief at 7.)

Amicus Brief for Italian Bondholders (supporting affirmance)

A brief filed on behalf of Italian holders of repudiated Argentine debt (a group that is pursuing a bilateral investment treaty claim against Argentina in an ICSID arbitration) asserts that extraordinary relief is justified in this case as the result of Argentina's "*uniquely egregious conduct . . . .*" (Italian Bondholders' Brief at 15.)

Amicus Brief for Ronald Mann and EM Ltd. (supporting affirmance)

Professor Ronald Mann of Colombia Law School, an expert in the law of funds transfer, and EM Ltd., a judgment creditor of Argentina, have filed a brief that analyzes UCC Article 4A in detail, arguing that the Injunctions do not contravene it.

Amicus Brief Montreux Partners, L.P. and Wilton Capital (supporting affirmance)

Sovereign debt investors Montreux Partners and Wilton Capital have filed a brief that seeks to refute the arguments advanced by BNY Mellon, contending that the indenture trustee's due process concerns are misplaced and that the District Court was correct in finding that it was in a position to act in "*active concert or participation*" with Argentina to thwart the Injunctions.

Amicus Brief for Kenneth W. Dam (supporting affirmance)

The brief of Professor Kenneth W. Dam of the University of Chicago Law School takes issue with Argentina's claim that affirming the Injunctions would inhibit the orderly restructuring of sovereign debts, arguing that the collective action clauses now commonly included in bond issues can effectively check the risk that "holdouts" will frustrate future restructurings.

Amicus Brief for the Washington Legal Foundation (supporting affirmance)

The Washington Legal Foundation has filed a brief in which it argues that the Fifth Amendment and due process arguments made by the Exchange Bondholders and Fintech are without merit, and that the Court of Appeals should disregard these arguments as untimely.

Significant Motions Pending Before the Second Circuit

In addition, two significant motions relating to this appeal are pending before the Second Circuit.

Petition for Panel Rehearing and Rehearing *En Banc*

As we previously reported, Argentina petitioned for panel rehearing and rehearing en banc with respect to the October 26, 2012 decision of the Second Circuit construing the *pari passu* clause. (See our prior note of November 14, 2012.) That petition is pending and undecided; as discussed in our November 14 note, such petitions are very rarely granted. However, on December 28, 2012, the US Government filed an *amicus* brief with the Second Circuit supporting Argentina's application for rehearing, arguing that the Court's October 26 interpretation of the *pari passu* clause was wrong and the Injunctions authorized by the Second Circuit breached the FSIA. In addition, Argentine Congressman, and former Central Bank Governor, Alfonso Prat-Gay filed a brief in support of rehearing, arguing that the true value of the Exchange Bonds was misapprehended by the Second Circuit.

The US *amicus* brief is significant because it was signed by the Department of Treasury and the Department of State, but it may prove to be of limited assistance to Argentina because it largely repeats the views that the United States presented—unsuccessfully—in its *amicus* brief and at oral argument to the Second Circuit panel.

Point II of the US *amicus* brief contends that the Injunctions violate Section 1609 of the Foreign Sovereign Immunities Act. That question of the proper construction of a federal statute represents Argentina's best hope of obtaining review in the

Supreme Court if the Second Circuit affirms Judge Griesa's orders. Supreme Court review, in turn, typically turns largely on whether federal appellate courts have disagreed on the legal question. The federal government lawyers plainly searched for and did not find any circuit court decisions that conflict with the Second Circuit panel's conclusion that a condition on a foreign state's use of funds violates the FSIA. The best the US *amicus* brief offers besides the Second Circuit's decision in S&S Machinery Co. are three garnishment cases involving the Democratic Republic of the Congo, two from the Fifth Circuit and one from the Ninth Circuit. All four cases concern efforts to take a foreign state's property and thus do not speak to the question whether a condition on immune property violates the FSIA. The prohibition on the "arrest" of immune property in Section 1609 of the FSIA might be argued to extend to restraints on its use. But the US *amicus* brief does not develop that argument, and it would seem to be an issue of first impression in the circuit courts.

Point I of the US *amicus* brief repeats the federal government's representation to the panel that the *pari passu* clause has (in the words of the government) a "settled market understanding" (p. 2) before the panel's decision. The panel rejected that representation as inaccurate in its October 26, 2012 decision because the meaning of the *pari passu* clause was in fact not settled. If the panel is correct, the government's argument for rehearing lacks a factual foundation. In addition, although the government offers an alternate construction of the *pari passu* clause, it does not explain why the panel's construction is wrong (other than the market's settled understanding).

Lastly, no attorneys from the Solicitor General's Office appear on the *amicus* brief. Although the Solicitor General was not required to appear on the brief (he was required to authorize its filing), his absence from the cover plainly reserves his option not to support Argentina in seeking Supreme Court review or a stay of the Second Circuit's mandate if that becomes necessary for Argentina.

Motion for Certification to the New York Court of Appeals

On December 27, 2102, the Exchange Bondholder Group filed a motion for certification to the New York Court of Appeals. (The certification mechanism permits the Second Circuit to request that New York's highest state court provide the Circuit Court with its views as to issues of New York state law.) The question that the Exchange Bondholders Group suggests should be certified is:

> *[should a pari passu clause] be interpreted to require the issuer to make payments to the bondholders concurrently and proportionally to any payments it makes to third-party holders of separate and distinct bonds issued subsequently as part of an internationally sponsored post-default restructuring of the sovereign issuer's debt, and if so, how that proportion should be calculated.* (Motion for Certification at 2.)

In its brief filed the next day, Argentina includes a similar application. (*See* Argentina Brief at 55–57.) While we could envision the Court certifying questions with respect to the *pari passu* clause if it were to grant the reconsideration application, we would find it surprising for it to deny reconsideration but grant certification, in view of the fact that it has already released its definitive decision as to the meaning of the *pari passu* clause.

* * *

As mentioned above, we will issue a further update following receipt of the plaintiffs' briefs and Argentina's reply.

599 LEXINGTON AVENUE | NEW YORK | NY | 10022-6069