



# **SOVEREIGN DEBT: LEGAL ISSUES RELATING TO COLLECTIVE ACTION**

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# LITIGATION AFTER ARGENTINA'S RESTRUCTURING

*NML Capital Ltd v Republic of Argentina* 699 F 3d 246 (Second Circuit, 2012)

*NML Capital Ltd v Republic of Argentina* 727 F 3d 230 (Second Circuit, 2013)

In the UK *NML Capital Ltd v Republic of Argentina* [2011] 2 AC 495 contains (in the judgment of Lord Collins at paras 100-108) an erudite and entertaining account of the surprisingly long history of default on sovereign debt.

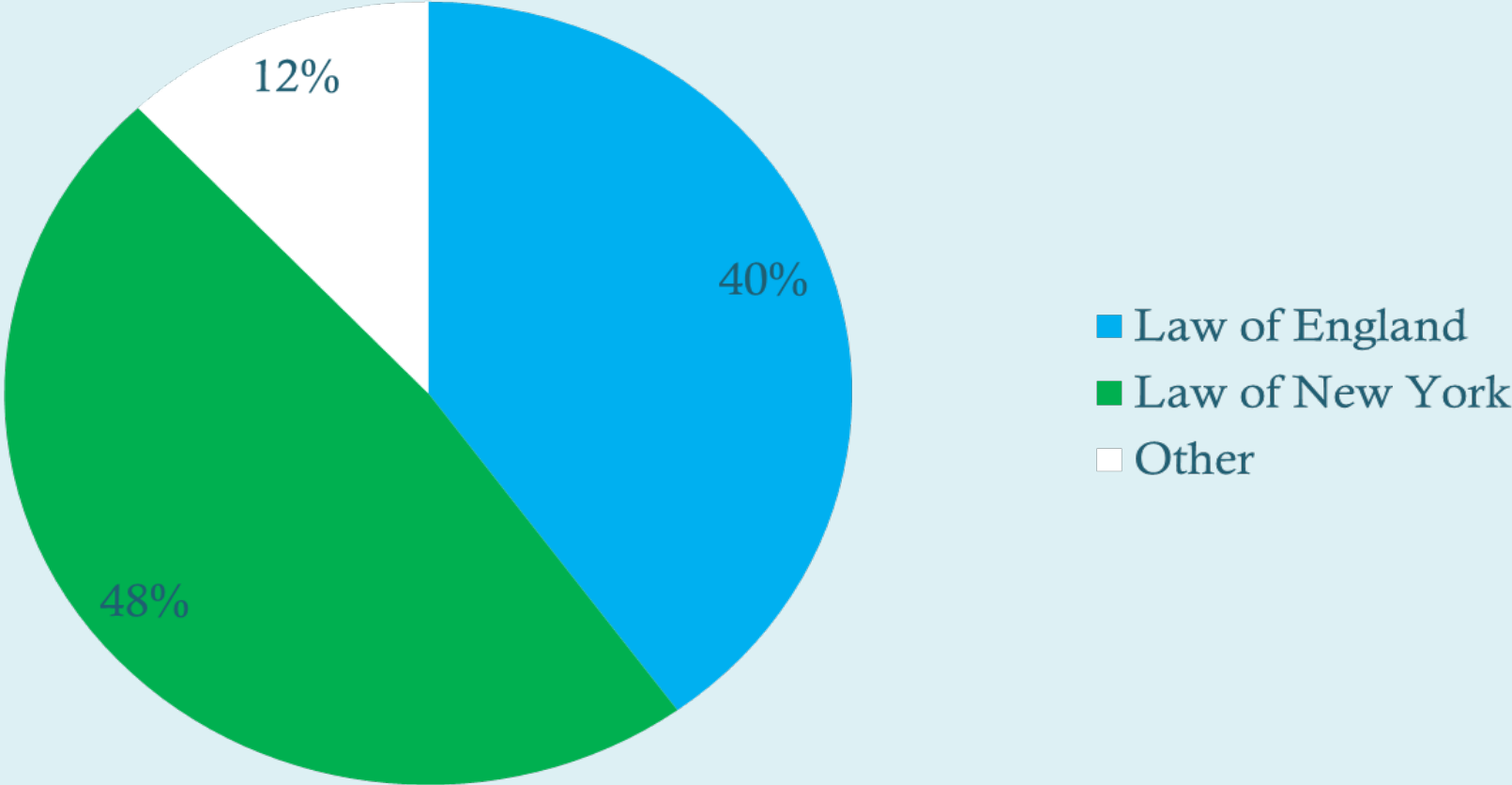
# THREE MAIN ISSUES

1. The interpretation of *pari passu* clauses;

2. The appropriate remedy for enforcement;

3. Strengthened collective action clauses.

# THE GOVERNING LAW OF SOVEREIGN BONDS



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# SOVEREIGN IMMUNITY

- In the United States and in England the scope of sovereign immunity is defined in a statutory code.
  - In the United States the relevant statute is the Foreign Sovereign Immunities Act (“FSIA”).
  - In England it is the State Immunity Act 1987.
- The 2004 United Nations Convention on Jurisdictional Immunities of States and their Property will come into force when ratified by 30 member states. In 2013 it had been signed by 28 states (not including the USA or the UK) but ratified by only 14.
- Most legal systems now accept that sovereign immunity should be limited to activities and assets which a sovereign state undertakes or holds *jure imperii* (that is, in its capacity as a sovereign power) and should not extend to activities or assets undertaken or held *jure negotii* (that is, for the purposes of trade).

# *PARI PASSU*

- The expression “*pari passu*” (“in equal step”) finds its natural context in national systems of insolvency law.
- A sovereign can be insolvent, but cannot be made bankrupt.
- In a sovereign bond is *pari passu* concerned with equality of **rank** or of **payment**?

# EXAMPLES OF *PARI PASSU* CLAUSES

- Two example *pari passu* clauses drafted by the Republic of Estonia (in June 2002) and the Republic of Croatia (in February 2001):
  - Republic of Estonia:
    - “The Notes and Coupons rank and . . . will rank *pari passu*, without any preference among themselves, with all other outstanding unsecured and unsubordinated obligations of the Issuer, present and future.”
  - Republic of Croatia:
    - “The Notes and Coupons rank *pari passu*, without any preference among themselves, and at least *pari passu* in right of payment with all other present and future unsecured obligations of the Republic, save only for such obligations as may be preferred by mandatory provisions of applicable law.”

# COLLECTIVE ACTION CLAUSES

- Historically, ineffective because hold-out creditors achieved a blocking position in certain bonds.
- Now, however, they are generally viewed as the best way forward due to the introduction of single-limb voting mechanism across several series of bonds.
- August 2014, ICMA published a standard model CAC with certain variant forums.
- *Redwood Master Fund, Ltd and Others v TD Bank Europe Limited and Others* upheld the validity of CACs:
  - “By signing up at the outset, each lender submits to the decision of the majority of lenders at important forks in the road”



# WHAT DOES THE FUTURE HOLD?

*Stronger Collective action clauses may be a long-term solution; but it will take at least a decade until the results are seen.*