

INCORPORATING ENHANCED COLLECTIVE ACTION AND *PARI PASSU* CLAUSES IN SOVEREIGN DEBT



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INTRODUCTION TO THE WORK OF THE FMLC ON SOVEREIGN DEBT

In 2005 the FMLC produced a paper on the interpretation of *pari passu* clauses which examined the English law position in relation to these clauses. The paper concluded that the ranking interpretation was the correct construction of the clause.

In 2012, the Eurozone crisis prompted a review of the possible responses to sovereign debt restructuring including the use of collective action clauses. The FMLC hosted a seminar on this topic, drawing together legal and market experts to examine these issues.

The renewed impetus for reviewing the possible responses to sovereign debt restructuring under English law became more urgent in the of light of the decisions in *NML Capital Ltd., v Republic of Argentina* in the US courts. The IMF, subsequently, invited the FMLC to consider the question of enforceability of single-limb aggregated CACs in sovereign debt and the interpretation of *pari passu* clauses.

The FMLC produced memoranda on both topics setting out its interim views and published two subsequent papers on these issues this year.

CACS: THE FMLC'S CONCLUSIONS ON ENFORCEABILITY

The memorandum summarised the FMLC's view that single-limb CACs would be enforceable under English law.

The FMLC published a paper with comprehensive legal analysis expanding on this interim view. The paper stipulated:

- single-limb CACs, subject to certain caveats, are enforceable under English law;
- single-limb CACs significantly reinforce legal certainty by eliminating some of the problems which can occur in respect of hold-out creditors by promoting swift resolution of disputes arising in the context of sovereign debt restructuring; and
- oppression, bad faith or insufficient disclosure in the exercise of powers will lead to vulnerability with all types of CACs, including single-limb, but these situations will tend to be rare.

PARI PASSU: THE FMLC'S CONCLUSIONS ON INTERPRETING THESE CLAUSES

The FMLC published a separate memorandum in 2014 which affirmed that the findings in its 2005 paper on *pari passu* clauses hold good today.

This was prompted, in particular, by the judgment of the US Court of Appeals, Second Circuit in the Argentina litigation. This judgment was made final in 2014 when the US Supreme Court refused an application for a *writ of certiorari* filed by the Republic of Argentina.

The FMLC's paper confirms:

- the views set out in the 2014 memorandum that the conclusions expressed in the FMLC's 2005 paper hold good today; and
- that the English courts would likely take a different approach in relation to remedies from the approach taken in the US Courts of Appeals in the Argentina case and, in particular, would be unlikely to order the remedy of specific performance.

IMF-FMLC USER SURVEY RESULTS



Survey Questions:

1. Are you aware of new single-limb aggregated collective action clauses e.g. as published by the International Capital Market Association?
2. If so, are you incorporating these into your, or your client's, new issuances?
3. Has the inclusion or exclusion of these modified clauses affected the pricing or rating of your bonds?
4. Are you planning to undertake liability management operations, such as bond buybacks or swaps, on your outstanding bonds in order to issue new bonds containing the modified collective action clause and *pari passu* provision?