

Did Argentina ‘Default’?

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A us court ruling has warped the otherwise precise meanings of three key words – “republic”, “sovereign”, and “default” – leading to absurdities like a New York district court holding the Republic of Argentina in “contempt of court”! The entire understanding of sovereign debt and its restructuring is being read through private “contract law” that cannot address the complex questions that are inherently public in nature, à la questions around restructuring Argentina’s debt. It appeared that a misreading of key words could benefit some vulture funds, but so far no one has seen as much as a penny! Maybe they never will.

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The Setting

As lawyers know all too well, semantics does matter, and Argentina’s case is no exception. Accordingly, terms such as “republic”, “sovereign”, and “default” take centre stage.

Ever since the mess the United States (us) Judge Thomas Griesa created (Öncü 2014b), the word “default” has been misused hundreds of times regarding Argentina’s 2014 sovereign debt payments.

So, let us start with “default”. Financial default means “failure to meet financial obligations”.

So, did Argentina “default”?

This should be of the utmost legal, financial, and political interest worldwide, in view of recent headlines – think Europe, think Greece, think PIGS (Portugal, Italy, Ireland, Greece and Spain) (Pope 2014).

The Mess

Due to the glaring lack of (and badly needed) international framework for sovereign debt restructuring, Argentina’s New York Law bonds today are basically in the hands of (a) the us judiciary with its non-performing “default” rulings, and (b) the International Swaps and Derivatives Association (ISDA), under direct oversight of the Federal Reserve Bank of New York, for credit default swap (CDS) settlement purposes

where (beyond belief!) Elliot Management Corporation – the parent company of plaintiff NML Capital – is a voting member (Hayakawa 2014).

Logically and geographically, (a) and (b) should not be applicable to Argentine bonds issued under other jurisdictions such as London or Tokyo. Unfortunately, in this case, logic is rarely the rule. Judge Griesa leads the lot, including his sophomoric judgments declaring the sovereign Republic of Argentina in “contempt of court” or that its payments are “illegal”.

After six turbulent months, neither Argentina’s legitimately restructured bondholders nor the Cayman Islands’ vulture funds have collected a penny. Possibly they never will, unless Judge Griesa’s rulings are revoked or something to that extent, as was proposed in a piece in *The New York Times* (Norris 2014b).

The us judiciary, including its Supreme Court of Justice (SCOTUS), has been clearly ineffective regarding the Argentine case (Vilches 2014). Indeed, us Supreme Court Justice Ruth B Ginsburg has openly dissented with the “exorbitant” 16 June 2014 decision taken by her SCOTUS colleagues whereby financial service providers – clearinghouses, banks, trustees, fiscal agents worldwide – are now sovereign debt enforcement agents.

Default Check

The us judiciary authorities have ruled that despite timely and proper disbursement of restructured due payments, Argentina has supposedly defaulted by

failing to meet an unprecedented interpretation of its financial obligations towards 1% of its restructured bond exchange holdouts (Öncü 2014a).

Furthermore, terms such as “technical default” and/or “selective default” and/or “partial default” have been artificially and hurriedly coined by third parties in their attempt to capture the essence of the resulting confusion.

Insisting again on proper semantics, we doubt the value of this widely-used “ex-post-facto” terminology. Being in default “somewhat” is like being “somewhat” pregnant.

Be it as it may, not so fast.

For example, the ISDA is the only authority entitled and empowered to enforce the settlement of Argentina’s CDS obligations. Interestingly, the ISDA does not even attempt to invoke the term “default” or any of its respective flavoured variations in the case of Argentina. Instead, the ISDA declared that Argentina has incurred in a “failure to pay credit event”.

The Federal Reserve Bank of New York was actively involved in establishing

timelines for dispute resolution and auction hardwiring of CDSs, while supporting “the permanent incorporation of the auction-based mechanism in order to increase the certainty, transparency and orderliness of settling CDS transactions following a credit event” (FRBNY 2009: 6).

Once again, interestingly, the New York Fed also does not deal with any type, shape or form of “defaults” (Duffie, Li and Lubke 2010).

The Good, the Bad and the Ugly

We argue that the inconsistency of terminology used throughout the financial community and the lack of common definitions may not be all that innocent.

One explanation is that the entire financial world has not been able to get its act together on some fundamental matters, thus making the whole system inconsistent and, thus, ineffective.

Another possibility is that the above confusion was allowed and perpetuated on purpose so as to have all possible options open, as with Argentina’s case today, making it fully discretionary rather

than “certain, transparent and orderly” as the New York Fed and ISDA say it is supposed to be.

Or maybe it is just another glaring case of international financial incompetence.

Jurisdiction and Applicable Legislation

True enough, the Republic of Argentina did issue New York Law restructured bonds. But such bonds are not within the legal scope of parochial “contract law”. Semantics again. The Latin etymology of the term “Republic” is “*res publica*” meaning “public thing, matter or affair”. So public law rules here, not private law.

Georgetown University academic Adam Levitin has described Argentina’s case as “a high-stakes game of chicken with a sovereign state...that us courts cannot and should not win... abstention would have been the right approach” (Levitin 2014). This case involves a sovereign state with 45 million people and their futures are at stake. This is not a family gourmet restaurant in Upper Manhattan under a run-of-the-mill Chapter 11 bankruptcy

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process whereby creditors jockey for anything up for grabs, refrigerators included.

“Sovereign” means “supreme independent authority not subject to any other power or state”. It is not called “sovereign debt” for nothing. In the case of a sovereign state such as the Republic of Argentina, local legislation is an acknowledged part of its bonds wherever they are issued, New York or elsewhere. The Republic of Argentina has specific legislation regarding its sovereign debt payments, which it necessarily has to abide by. Otherwise, Argentina would be violating its own laws while simultaneously ceasing to be a sovereign republic.

In case of a disagreement with what was accepted by 92.4% of the original creditors, the 1% of the remaining creditors should sue before Argentine Courts of Law, not before the Wall Street tribunals. In turn, the us judiciary should abstain from getting involved in a case completely outside its scope as it will not solve, nor help to solve, sovereign debt restructuring processes such as the many that are threatening to hard land upon the world’s economy these days.

Effective Payment

The trustee banks’ “Trust Indenture and Prospectuses” of Argentine restructured exchange bonds foresaw two different payment mechanisms. The first one was through intermediary trustee banks. The second one was direct payment to bondholders who wished to get paid without intermediation.

In the first case Argentina’s responsibility ended as soon as trustee banks received the funds. In the latter case, it was Argentina’s specific responsibility to ensure that bondholders received the payment.

Argentina has regularly paid 92.4% of the original creditors who agreed to the restructuring through its intermediary trustee banks as allowed by the Trust Indenture and Prospectuses, thus making trustee banks responsible for delivering payment to bondholders, not the Republic of Argentina.

But then Judge Griesa surprised the whole jurisprudential world yet again by deciding to “freeze” Argentine payments

as an additional unprecedented nuclear option of an “exorbitant” us court system.

Accordingly, bondholders (including George Soros and Kyle Bass) have already sued trustee banks thus contributing to the relentless confusion and non-performance. Adding insult to injury, the above “freeze” includes the British and Japanese Law bonds also, not only the New York Law bonds. Top-tier sovereign debt international authority Anna Gelpern is on record saying, “It’s scary” (Norris 2014b); “The world of sovereign debt is deeply dysfunctional” (Gelpern 2014).

The jurisprudential impact of this transnational overreach is unfathomable. Let us just imagine a Chinese judge saying: “If you don’t pay us you are violating the Chinese law”.

Argentina continues to insist on paying the remaining holdouts including the vulture funds exactly the same it has always paid the other 92.4% of creditors at a 300% profit for vulture funds (Herman 2014). Common sense indicates that this should be good enough for any bankruptcy situation. Otherwise a 99.99% creditor’s agreement would also mean “default” (sorry, “credit event”). Think Detroit (Davey and Walsh 2014).

A Quick Quiz

Q: Did Argentina “default”?

A: No, because it did not “fail to meet its financial obligations” as Argentina did pay 100% of its restructured bondholders duly and fully through its trustee banks as foreseen in the restructured bond Trust Indentures and Prospectuses.

Q: Did Argentina incur in a “failure to pay credit event”?

A: No, because Argentina’s officially registered trustee banks duly received 100% of the restructured sovereign debt payments in full compliance with the bond Prospectuses.

Q: Did Argentina fail to comply with the “pari passu” clause specified in its bond Prospectuses?

A: No, because Argentina has repeatedly and emphatically proposed to pay every single original sovereign debt creditor exactly the same that was agreed with 92.4% of its creditors.

Q: Has Argentina been victim of judicial extortion?

A: Yes, among other things, because the us judiciary has (a) illegally “frozen” Argentine payments that belong to their rightful owners, namely, the restructured bondholders, and (b) because it has allowed vulture funds direct access to us listings of Argentina’s seizable assets worldwide.

Q: Should the restructured bondholders make any claims on Argentina?

A: No, because Argentina opted to pay them through the officially registered trustee banks, not directly. It is Judge Griesa and the trustee banks they should go after.

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