

January 31, 2005

## **POSITION PAPER:**

### **“Most Favored Creditors Clause”**

On January 14, 2005, the Republic of Argentina (“Argentina”) filed a Prospectus Supplement (the “Prospectus Supplement”) with the United States Securities and Exchange Commission launching an exchange offer (the “Offer”) in which holders of Argentina’s defaulted debt are being offered the opportunity to exchange defaulted debt for new Argentine securities (“New Securities”). In an effort to encourage participation in the Offer, the Prospectus Supplement contains a provision on page S-60 (the “Most Favored Creditors Clause” or “MFC Clause”), which purportedly is intended to protect participants in the event that Argentina gives more favorable terms to other creditors at a later date. The MFC Clause states:

“Argentina reserves the right, in its absolute discretion, to purchase, exchange, offer to purchase or exchange, or enter into a settlement in respect of any Eligible Securities that are not exchanged pursuant to the Offer (in accordance with their respective terms) and, to the extent permitted by applicable law, purchase or offer to purchase Eligible Securities in the open market, in privately negotiated transactions or otherwise. Any such purchase, exchange, offer to purchase or exchange or settlement will be made in accordance with applicable law. The terms of any such purchases, exchanges, offers or settlements could differ from the terms of the Offer. Holders of New Securities will be entitled to participate in any **voluntary** purchase, exchange, offer to purchase or exchange extended to or agreed with holders of Eligible Securities not exchanged pursuant to the Offer as described below...” (emphasis added).

### **A Mixed Message**

Notwithstanding Argentina’s public statements that the Offer is final and that there will be no others, the first sentence of the MFC Clause specifically reserves for Argentina the possibility of cutting side deals with holdouts at any time on different, even better, terms. Such side deals can take many different forms including settlements and privately negotiated transactions. If Argentina truly believed that the Offer is final, there would be no need for a clause that provides otherwise.

### **Loopholes in the MFC Clause**

Argentina alleges that the MFC Clause adds value to its Offer because it protects holders of New Securities from being left out of any future deal or deals with better terms. However, creditors should be careful about relying on the MFC Clause. There are ambiguities and practical challenges in the MFC Clause that may make it much less valuable than Argentina asserts.

There are two important ambiguities to point out with respect to the language used in the MFC Clause. First, Argentina has deliberately left out the word “settlement” in the final sentence of the paragraph although the word appeared in a prior draft of the Prospectus Supplement. Argentina could make a strong argument that any “settlement” would not have to be extended to holders of New

Securities. Given the significant amount of litigation and arbitration against Argentina, this loophole is considerable. A “settlement” would certainly include agreements reached in the context of litigation or arbitration, but Argentina also could argue for a much broader interpretation. For example, Argentina could assert that a privately negotiated exchange or purchase on more favorable terms that is labeled a “settlement” would not trigger the MFC Clause.

Second, the inclusion of the word “voluntary” in the last sentence allows Argentina broad discretion to argue that any requirement by the official sector, such as by the International Monetary Fund that Argentina enter into a subsequent exchange or purchase on terms that are more favorable than the Offer would not trigger the MFC Clause. Argentina could claim that the arrangement with the official sector is not “voluntary” and, therefore, any exchange required by the official sector - even on better terms than the Offer - is not subject to the MFC Clause.

Finally, there are practical problems with relying on the MFC Clause. There is a serious question as to how creditors will ever know of side deals. If creditors do learn of side deals, the issue arises as to whether they will have access to enough information to demonstrate that the MFC Clause should apply notwithstanding the ambiguities described above.

These ambiguities and practical challenges give Argentina the ability to enter into a wide variety of side deals without necessarily triggering the MFC Clause.

### **Enforcement Issues**

Even if holders of the New Securities believe that the MFC Clause has been triggered, enforceability of the MFC Clause will be very difficult and onerous. According to the Prospectus Supplement, if Argentina breaches the MFC Clause and does not cure the breach within 90 days after it receives written notice thereof, the holders of New Securities can declare an event of default. To declare an event of default, holders of at least 25% of the aggregate principal amount of the debt securities of that series may, by written notice, declare the debt securities of that series to be immediately due and payable and such amounts will become immediately due and payable provided that the event of default is materially prejudicial to the interests of the holders of the debt securities of that series. Even if holders of the New Securities organize the requisite 25% threshold, actually stating a claim may be extremely difficult because of the ambiguity of the MFC Clause. In addition, due to the difficulties in organizing holders representing at least 25% of the aggregate principal amount of the debt securities, declaring an event of default under the New Securities will be a challenging process. Furthermore, even if an event of default is declared and the New Securities are accelerated, there is no guarantee that Argentina will actually pay. Finally, even if holders of New Securities organize and can prove a violation of the MFC Clause, Argentina has already shown its willingness to render itself immune from the enforcement of judgments in all major financial jurisdictions. As a result, if Argentina refuses to pay, then the holders that participate in the Offer will end up in the same position as they are today.

### **Conclusion**

For the reasons set forth above, holders of Argentina’s defaulted debt should place very little value on the MFC Clause. An analysis of the MFC Clause reveals that Argentina will be able to settle with individual holders at a later date on better terms without necessarily triggering the MFC Clause. Furthermore, if the holders of New Securities believe that Argentina has breached the MFC Clause, it will be difficult and onerous for such holders to enforce the MFC Clause and, even if they can enforce it, there is no guarantee that Argentina will pay if the New Securities are accelerated.

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