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Investors in Argentine Bonds Entitled to Millions in Additional Interest

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The New York Court of Appeals held that, under the terms of bond documents requiring biannual interest payments "until the principal…is paid," Argentina was contractually obligated to make biannual interest payments to bondholders even after the bonds' scheduled maturity date in 2005 and after certain bondholders accelerated the maturity date following Argentina's default in 2001. Because the bond documents required interest payments "until the principal…is paid," Argentina's obligation continued until it repaid the principal in full or until its obligation was "merged" into a final judgment.

In 1998, Argentina issued $200 million worth of Floating Rate Accrual Notes scheduled to mature in April 2005. Under the terms of the bond documents, Argentina assumed the obligation to pay bondholders interest-only payments twice a year until the principal was paid at a floating interest rate that would rise or fall based on changes in Argentina's financial condition. Bondholders were permitted to accelerate the due date of the principal in the event of a default.

During a 2001 financial crisis, Argentina defaulted on the bonds by announcing that it would no longer service its external debt and by ceasing to make the biannual payments on the Floating Rate Accrual Notes due to mature in April 2005. As a result of the defaults, the floating interest rate on the bonds soared to 50.5% per biannual period (from a normal range of 9% to 14%).

The bondholders sued in the U.S. District Court for the Southern District of New York to recover lost principal and interest. Argentina conceded its obligation to repay principal, but argued that its obligation to make biannual interest payments terminated when the bonds matured or when the bondholders accelerated the maturity date following Argentina's default. The bondholders argued that they were entitled to both the contract interest rate and an award of 9% statutory prejudgment interest under Civil Practice Laws and Rules Section 5001.

The case proceeded through the federal courts until the U.S. Court of Appeals for the Second Circuit certified the key issues to the New York Court of Appeals.

The New York Court of Appeals noted the general rule that, in the absence of express agreement on the issue, New York courts will apply the 9% statutory interest rate from the date of default. Where, however, the parties' contract expressly provides for payment of interest at a specified rate "until the principal shall be repaid," such a provision will be enforced. The Court of Appeals found that the plain text of the bond documents (which were negotiated by sophisticated parties) made clear that Argentina's obligation to pay interest did not cease at maturity or acceleration, but only at payment of principal.

The Court of Appeals also found that the bondholders were entitled to the 9% statutory interest rate. In rejecting Argentina's contention that such an award provided an unwarranted windfall or "interest on interest," the Court of Appeals found that the award of contract interest compensated the bondholders for Argentina's failure to repay principal, and the award of statutory interest compensated the bondholders for the separate injury cased by Argentina's failure to make the contractual biannual interest payments. (*NML Capital, et al. v. Republic of Argentina*, Civ. Action No. 128 (N.Y. June 30, 2011))

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