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Don't Cry for Me Argentine Bondholders: Important Argument in the Second Circuit

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The Second Circuit has heard extensive oral argument in the *NML v. Argentina* appeal.

The three-judge panel of the Second Circuit heard approximately two-and-a-half hours of vigorous oral argument in *NML v Argentina* yesterday. While no decision was announced, the judges gave strong suggestions as to their current views on many issues (all of which can, of course, change by the time the decision is finally issued).

The underlying appellate papers are on our Argentine Sovereign Debt webpage, at http://www.shearman.com/argentine-sovereign-debt/.

The Scene

This case clearly has generated massive interest, and the audience for the oral argument filled the courtroom, plus two large overflow rooms. (A courthouse security guard commented that the only other case he had seen that generated this much interest was the Martha Stewart trial.) The three-judge bench was "hot," deeply familiar with the record and the arguments of all the parties and *amici*. Further, the court allowed counsel to go way beyond their allotted time, which is unusual in the Second Circuit.

Those arguing were Jonathan Blackman for Argentina, David Boies for the Exchange Bondholders, James Martin for Bank of New York Mellon ("BNY Mellon"), and Ted Olson for the plaintiffs.

Rehearing of October 26 Order Denied

At the opening of the argument, the Court announced from the bench that Argentina's rehearing petition with respect to the Second Circuit's October 26 decision (in which the Solicitor General had joined) had been denied. While the Court was not specific as to whether this denial applied to both the panel and the *en banc* aspects of the rehearing petition, the court's order was subsequently released and shows that the denial only extended to the application for panel rehearing, and that the application for *en banc* rehearing therefore remains undecided.

The Arguments

While caution must be exercised in drawing definitive conclusions about the ultimate outcome of a case based on judicial comments during oral argument, the panel was very active and their comments suggest the following results:

- The Court showed little to no interest in the Foreign Sovereign Immunity Act arguments advanced by Argentina, the Constitutional arguments advanced by the Exchange Bondholders, or the UCC 4A arguments raised by some of the payment stream participants. Further, there was no meaningful discussion of potential distinctions between US dollar denominated Argentine Exchange debt and non-dollar denominated Exchange debt.
- The Court did not appear to be at all receptive to BNY Mellon's arguments that it was not a proper subject of the Injunction. It strongly suggested that it was ready to read the "*in active concert or participation*" language of Federal Rule of Civil Procedure 65(d)(2)(C) broadly, and capable of reaching an indenture trustee who forwarded payments on behalf of a party who is acting in violation of an injunction.
- The Court did express some interest in the question of whether there might be an alternative Ratable Payment formula – one that would provide for equitable payments to the plaintiffs over time but would not amount to a 100% one-time payment – that might be appropriate. However, proposals by counsel for both Argentina and the Exchange Bondholders as to what those alternatives might be were vague. (Should the Court wish to pursue that route, it would almost certainly require a further remand to Judge Griesa.)
- Argentina's counsel made it quite clear to the Court that in no circumstances would Argentina be making payment to the plaintiffs. On the basis of that declaration, both Argentina and the Exchange Bondholders argued that the Court should therefore vacate the Injunction, as its only effect would be to convert one default into two defaults. The Court appeared dismissive of this rationale.
- The Court gave no indication of when it would rule. However, one judge did ask the date of the next Exchange Bond payment date; the answer given was March 31. (Of course, no explanation was given by the judge for that question.)

In very brief summary, the main arguments were as follows:

Argentina: Argentina's argument was in large part an effort to revisit the Court's earlier construction of the *pari passu* clause, arguing the equal treatment for the plaintiffs should not mean full payment, and that payment of an amount equivalent to what has been paid to the Exchange Bondholders would be more appropriate. Counsel argued that the public policy the Court should adopt was that applicable in bankruptcy, of "*inter-creditor equity*" and "*haircuts all around*." The Court commented that Argentina had little right to argue an entitlement to equity, having paid nothing to holders of unexchanged debt for 11 years.

When asked directly by the Court whether Argentina would honor the Court's order if the Injunction is affirmed, Argentina's counsel replied that such order would not be "*voluntarily obeyed*." Counsel went on to say, while pointing to plaintiffs' counsel, Argentina "*will not pay him*."

Bank of New York Mellon: BNY Mellon argued principally that the Injunction deprived it of due process by essentially pre-judging that any payment it might make as an indenture trustee would constitute contempt. The Court disputed that reading, and suggested that BNY Mellon would not be held in contempt without a full hearing, and all that the Injunction did as to BNY Mellon was provide notice that it was potentially within the scope of persons that could be caught by Rule 65(d)(2)(C). The Court went on to suggest that the Injunction in fact provided BNY Mellon with notice to which it was not even entitled, as it would be subject to Rule 65 whether or not it had been named in the Injunction.

Further, in strikingly direct commentary, two judges suggested that any lawyer counseling BNY Mellon that it could make payment on behalf of Argentina at a time that Argentina was enjoined would be "*reckless*," and that an indenture trustee making a payment with the knowledge that such payment was being made in violation of an injunction was certainly acting "*in active concert or participation*" with the enjoined party.

Exchange Bondholders: On the basis of a concession by counsel for the plaintiffs that an Exchange Bondholder's receipt of payment from Argentina was not by itself a breach of the Injunction by that Exchange Bondholder, counsel for the Exchange Bondholders made the argument that BNY Mellon should not be subject to the Injunction, as payment to the indenture trustee was legally equivalent to payment to the Exchange Bondholders. Accordingly, it was argued that BNY Mellon should share an exemption from the Injunction to the same extent that the Exchange Bondholders do.

Counsel also argued that the Exchange Bondholders are "*innocents*," whose right to be paid is uncontested. Counsel stressed that in applying equity, the Court should fashion a practical remedy and should consider the result of its order, even if the result flows from another party's contempt. Counsel stressed that it is clear that the Court's order will not bring about payment to the plaintiffs, and would only produce huge losses for the Exchange Bondholders.

Plaintiffs: Counsel emphasized the necessity of the Injunction, in view of repeated statements by Argentine officials (including its President) that the plaintiffs would never be paid, plus Argentina's many years in default. As to the issue of the inclusion of BNY Mellon in the Injunction, counsel argued that the indenture trustee has been aware of the risk of this litigation since the Exchange Bonds were issued, as that risk is was described in the prospectus. Accordingly, BNY Mellon took on the role well aware of the litigation risk, and cannot be sheltered from that risk now. As to the argument that BNY Mellon should enjoy the same protected status as the Exchange Bondholders, counsel argued that BNY Mellon has multiple roles for which it is paid by Argentina, and is not the same as the widely dispersed holders.

The plaintiff's counsel was asked whether it was true that plaintiff NML had purchased CDS contracts pursuant to which it would make money were there to be a default on the Exchange Bonds. Counsel responded that he did not know the facts and that in any event the only issue here is enforcement of the defaulted bonds. (Counsel for the Exchange Bondholders later argued that this issue went directly to the plaintiff's entitlement to equitable relief from the Court and should be the basis for a remand to Judge Griesa for fact finding. The court made no response.)

Timing and Next Steps

As mentioned above, the Court gave no indication when it would hand down its decision. However, the prior decision in this case by this same panel came three months after argument. We expect this decision will be quicker.

The appellate rules generally provide 21 days before the mandate (appellate judgment) issues and becomes effective. (The 21 days is the sum of the 14 days provided to file petitions for panel rehearing and rehearing *en banc* plus the 7 days for the mandate to issue.) The same rules, however, also authorize the panel to alter the 21-day default timing and issue the mandate at the same time that it hands down its opinion. The panel here is well aware of that authority because it issued its mandate on the same day of its October 26, 2012 decision. What is more, the existing stay of the Injunction, issued by the panel on November 28, 2012, is in place only "*pending further order of this Court*."

The March 31 interest payment is much smaller than last December's payment. As a result, the panel may take several weeks to issue its decision and not disturb the March 31 payment. At the same time, however, it is not difficult to think that the panel could hand down its decision within the month of March and issue the mandate and lift the November 28 stay simultaneously. The panel might well take such action on the view that the main *pari passu* and FSIA issues have been decided and rehearing petitions denied; the objections to the Ratable Payment formula and Injunction scope issues

are not serious (in the panel's view based on the questions at oral argument); and Argentina and its *amici* have received ample opportunity to be heard and no just reason exists to delay enforcement of the Injunction.

Whether in March or by June, if the Injunction is affirmed, then Argentina's options become very narrow. Although the appellate and Supreme Court rules expressly authorize stays pending petitions for a writ of certiorari to the Supreme Court, such stays require the petitioner (here, Argentina, which would appear to be the only "party" entitled to seek Supreme Court review) to establish a substantial likelihood that four Justices would grant the petition. With no genuine conflict on a federal question, both a stay and petition would be a challenge to obtain – at least without the active support of the Solicitor General.

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