4-1-1988

Argentina

LEGAL MEMORANDA

ARGENTINA

The following is a review of recent legal and economic developments in Argentina.

Capitalization of Foreign Debt

By means of Communication "A" 1109, the Central Bank provided the general guidelines governing the conversion of foreign liabilities into investments in the private sector. According to this Communication, all private and public sector debts (other than short-term trade credits, debts owed to foreign government agencies and debts which are guaranteed or insured by non-Argentine government agencies) are eligible for conversion. They are known as the "eligible debt." With regard to convertible private sector debts, the original debtor and the company receiving the investment must be one and the same. The conversion of the debt requires the consent of the creditor and of the Argentine Central Bank. The public sector debts which are eligible include bonds registered in U.S. currency, government liabilities in U.S. currency (promissory notes), external bonds, Central Bank liabilities in U.S. currency, foreign borrowings of the Argentine government, medium term loans granted to the Central Bank, liabilities in U.S. currency, and other external liabilities of the Central Bank.

Applications for conversion are submitted to the Central Bank for approval by the Undersecretariat of Economic Policy. They are submitted through a local intermediary bank, and they must be accompanied by a performance guarantee issued by a local intermediary bank in the amount of one percent of the debt to be converted or by evidence of a deposit of that amount made in the account of the Central Bank. Conversion is made through presentation of the "eligible debt" to the Central Bank by the local bank. The australs (local currency) received in exchange for such

debt remain on deposit with a local bank until such time as they must be disbursed in connection with the investment. The investor receives accrued interest on the "eligible debt" until the date of conversion. After conversion, australs on deposit bear interest or, at the option of the investor, are indexed at the rate of exchange to the U.S. dollar and bear interest at a rate equal to LIBOR (London Interbank Offered Rate).

The first round of bids for the conversion of foreign debt within the framework of the present capitalization program took place on January 11, 1988. According to the Undersecretariat of Economic Policy, the highest bid that may be made is seventy-five percent (i.e., a minimum discount of twenty-five percent). The quota for bidding will be fifty million dollars. There is an amount of five million dollars earmarked for small and medium sized companies with the proviso that no project may exceed one million dollars.

Debt to Equity Conversion (Central Bank Communication "A" 1056)

Communication "A" 1056 of the Central Bank sets forth specific guidelines for the capitalization of outstanding private sector external debt as of April 30, 1987, excluding debt owed by financial institutions. For the purposes of the regulation these liabilities have been dealt with under three headings: liabilities without exchange insurance, liabilities with exchange insurance, and swap transactions.

These debts may be prepaid if, at the same time, an equivalent amount in foreign currency is brought into Argentina as a capital contribution to the debtor. If required, the foreign investor must obtain prior approval under the foreign investment law and comply with the additional requirements of the particular liability. The additional requirements depend on whether the liabilities are without exchange insurance, with exchange insurance, or represent swap transactions. Additional rules determine how the assignment of the rights and the transfer of obligations with respect to the debt being capitalized are effected.

In principle, the assignment of rights and the transfer of obligations with respect to any debt being capitalized are only subject to the requirements explained in the Communication. However, in the case of on-lending debt, if the assignee is a party to the 1985

Term Credit Agreement, the assignment is also subject to the relevant provisions of that Agreement. If the assignee is not party to the Agreement, the assignment requires the prior approval of the Central Bank.

Transfers of liability on debt without exchange insurance require the prior approval of the Central Bank. The transfer of liability with respect to on-lending debt also requires such approval, and the repayment or return of the matching funds associated with the on-lending capitalizations will not be authorized until the original maturity of the capitalized on-lending debt.

Debt to Equity Conversion: The First Argentine Call for Bids

On January 20, 1988, all offers filed in connection with the first Argentine call for bids under the debt to equity conversion program were opened at the Central Bank. Positive interest was exhibited. Fifteen different offers competed for the first US$ 50,000,000 tranche. (The annual aggregate conversion quota determined by the Executive is US$ 300,000,000.)

Domestic companies confronted multinationals (such as Coca Cola, Saab-Scania, Pioneer, etc.) with projects in areas as diversified as breweries, meat packing plants, auto part manufacturing, agro-industry and soft drink production. The size of the individual projects varied from small (US$ 300,000) to large (US$ 70,000,000). With a required minimum discount of 25%, only those offering at least 35.25% are to be awarded. The maximum offered discount was 40.20%; the mimimum was 28%.

Assuming that a foreign investor uses this particular capitalization mechanism to buy Argentine foreign debt instruments in the market at 40% of their nominal value, the investor may obtain an effective exchange rate 29.27% higher than the free exchange rate. Assuming the above mentioned discount, through the recent debt to equity conversion call for bids, investors received Austral 7.11 for each U.S. dollar. The free exchange rate, otherwise applicable, was approximately Austral 5.50 per U.S. dollar. These statistics show that there is a good market for debt to equity conversion based on investments in Argentina.

Demonopolization of Public Utilities

Decree 1842/87 promotes the general principle that the production and supply of goods and the provision of services should freely compete in the private sector. Historically, they were carried out by state-owned corporations dependent on the Ministry of Public Works.

The Decree cancels all regulations that granted or recognized privileges or exclusive rights of any kind, the purpose or effect of which was the exclusion of the private sector from providing goods and services to the public. The Decree establishes simple and speedy procedures aimed at eliminating the bureaucratic formalities required to obtain the approval of projects submitted by private parties. Projects relating to the oil and gas industry are not included in this ruling because these industries are regulated by the Houston Plan (Decree 1443/86 - 623/87) and the Olivos Plan (Decree 1812/87).

Petroleum: Olivos Plan

Decree 1812/87 approves one course of action of the Olivos Plan. The contracting companies are offered the opportunity to draw up plans for secondary or assisted recovery and thereby obtain a price for the additional or increased production at substantially higher rates than those agreed to in the contracts. The Decree also envisions a better price for increased production of natural gas.

The Houston Plan: Opening of Envelope "B"

Envelope "B," containing offers corresponding to the third round of the Houston Plan, was opened on December 9, 1987. The following bidding groups presented the best offers: Cuenca Neuquina: Area Payun Notre, Perez Companc (only bidder); Area Huantraico, San Jorge-Cabeen; Area Chihuidos, Trend-Asamera-Nomeco-Santa Fe-C.G.C.; Area Las Lajas, Cadipsa; Area Lago Pellegrini Este, Perez Companc-Petroquimica Rivadavia-Benito Roggio. Cuenca Noreste: Area Oeste Rio Bermejo, Bridas-Trend; Area Anatuya, Bridas; Area Tostado, Esso-Chevron-Capsa (only bidder). Cuenca Cuyana y Bolsones: Area Nancunan, Pluspetrol (only bidder); Area Rio Desaguadero, Tecnicagua.

RATIFICATION OF INTERNATIONAL CONVENTIONS

Law 23.502 and Decree 816/87 ratified the Convention on Civil Procedure adopted by the Hague Conference on Private International Law. Law 23.503 and Decree 815/87 ratified the Inter-american Convention on Letters Rogatory and the Additional Protocol, adopted by the First and Second Inter-American Conference of Private International Law in Panama City and Montevideo, respectively. Law 23.506 and Decree 812/87 also ratified the Inter-american Convention on Proof and Information in Foreign Law, adopted by the Second Inter-American Conference of Private International Law.

FREEDOM OF THE PRESS

On September 2, 1987, the Argentine Supreme Court issued a decision directly connected with the guarantee of freedom of the press. The case involved a traditional Argentine newspaper, La Prensa. On the issue of whether a daily newspaper is part of a nation's culture, the Argentine Supreme Court replied in the negative. The vote was three to two. The unusual decision arose as follows.

In June of 1985, the Argentine government launched the Austral Plan. The Plan was an attempt to combat extreme inflation. The Plan involved minting a new currency known as the "Austral," freezing wages and controling prices. The government could set maximum prices for the sale of "products and services destined for the public health, nourishment, dress, hygiene, housing, sports, culture, transportation, heating, refrigeration, and entertainment, as well as whatever other product or service satisfies directly or indirectly, the common necessities of the population." These broad delegated powers were granted to the Executive by Law 20.680. Still in effect, this controversial law was enacted in 1974 by the government of Isabel Peron. The law provided that newspaper prices fall within the price freeze.

On January 5, 1986, La Prensa alleged that it could not be forced to sell at a loss, and raised its newsstand prices by fifty percent. The government of Dr. Raul Alfonsin immediately fined La Prensa. The newspaper appealed the penalty on the ground that it violated its constitutional freedom of expression by making it economically impossible to publish. The trial judge affirmed the fine.

On October 30, 1987, the Supreme Court reversed. Each of the three majority justices filed an individual opinion. Although the three varied on different minor issues, they agreed on the basic conflict and how it should be resolved. They shared the view that the principal goal of the press is to provide a free flow of information, not to enrich a nation's culture. Relying on a strict interpretation of the law, the Supreme Court held that Law 20.680 (and the regulations issued under it) does not apply to La Prensa.

Skeptics argue that the Court's interpretation is so strict that it virtually rewrites the statute to fit its holding. And, they argue, the reasoning deviates from Law 20.680 in both letter and spirit.

The words' primary goal or ultimate objective or any other similar expression are not found in the text. Ignoring this language, it still does not follow that a newspaper transmits no culture to its daily readers. Newspapers are indisputably intertwined with the culture of the society where they are published. Furthermore, if newspapers do not fall into the category of culture, then they do fall into the category of satisfying a common or daily necessity of the population, under Law 20.680. The Supreme Court conveniently ignored this nearly all-encompassing phrase. With an important freedom at stake, this side-step was wise.

The majority made an effort not to deal with the underlying conflict between economic regulation of the press and the consitutional rights guaranteeing freedom of the press contained in articles 14 and 32 of the Argentine Constitution. Despite the above, there is an appealing efficiency in the Court's decision; Law 20.680 was not declared unconstitutional, and more importantly, freedom of the press was not narrowed.

The outcome of the La Prensa case is positive. However, because of the importance of freedom of the press, the Court's reasoning in defense of this liberty is circumspect. Freedom of the press deserves to be defended with clear and precise words. To play fast and loose with the meaning of the language in this case will affect any other questions regarding its interpretation.

Licensing Software in Argentina: An Important Decision

On August 25, 1987 the National Contentious Administrative Chamber (Room I) handed down a remarkable decision in "American Express Argentina S.A., appeal of Resolution 35 of the Secretary of Industry and Foreign Trade (S.I.F.T.)." The decision stated

that (i) the supply of software is licensable under the provisions of Law 22.426 on the transfer of technology and its regulations; and (ii) a five percent royalty calculated on the net sales agreed upon between the parties is perfectly valid, notwithstanding the fact that similar services in other deals may have been supplied against a lower fee.

The following is a brief summary on the above-mentioned decision.

Background

American Express Argentina S.A. appealed the decision of the S.I.F.T. which confirmed the previous ruling of the Instituto Nacional de Technologia Industrial (I.N.T.L.) denying the renewal of an agreement between the appellant and American Express Limited, its parent company. I.N.T.L. stated that the supply of software is not within the scope of the Law on the grounds that the software is already incorporated into a physical good, and therefore is not "an autonomous transmission of technology" as required by Article 1 of Decree No. 80/81 (the "Decree") which regulated the Law.

Defining "Licensable Technology"

The provisions of Article 1, paragraph (c) of the Decree, which define technology as "any technical knowledge for the manufacturing of a product or for the rendering of a service," were deemed applicable to the licensing of software. Moreover, the Court pointed out that the plaintiff might not be able to continue rendering its services of an international nature, without the mother company supplying the necessary foreign-made software. The Chamber referred to a report by a private university (Universidad Argentina de la Empresa) which expressed that "software applied to the solution of special problems, made according to the rules, guidelines and required quality, fits into the concept of technology and . . . if such elements are moved to a place where they are not available they amount to a form of transfer of technology." Taking this into account, the Chamber decided that the supply of software is within the scope of Article 1 of the Decree which defines technology as "any technical knowledge for the manufacture or service of a product."

Royalties

The Court also considered S.I.F.T.'s contention that a five percent royalty imposed upon the net sales to be paid by the licensee to its mother company was extremely onerous. Article 5 of the Law establishes:

> Legal acts considered in Article 2 (those entered into between a local company of foreign capital and the company that directly or indirectly controls it, or any branch of the latter), shall be approved, provided that a study shows that: (i) the obligations and conditions it establishes are in line with normal market practices among independent parties; (ii) the agreed compensation is in line with the technology to be transferred. Approval of such legal acts will be denied if they contain provisions for payment to be made for the use of trademarks. Guidelines for the implementation of this Article shall be established by the regulations of this Law.

According to Article 3, the Decree states:

> For purposes of Article 5 of the law it shall be assumed that payments agreed upon are in line with the transferred technology, when they do not exceed 5% (five percent) of the net sales value of the products manufactured or services rendered with the use of the transferred technology.

The Court, after construing the applicable rules, ruled that the royalty rate agreed upon between licensor and licensee had not violated any provisions of the Law or the Decree. The Chamber determined that the defendant's contention about lower rate agreements in other transactions governing similar services between third parties was completely irrelevant. The Chamber concluded that Article 3 establishes only a ceiling of five percent on the net sales value of the products manufactured or the services rendered with the transferred technology, which is independent of the normal market practices. Thus, as long as the five percent limit is not

violated, any agreement is lawful and well within the provisions of the Law.

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