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# Argentina

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# LEGAL MEMORANDA

## ARGENTINA

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

### I. CUSTOMS NEWS

On January 1, 1988, the Agreement for Implementation of Article VII of (GATT) will become effective in Argentina. Argentina's Tariff Law will be modified by replacing the at-normal-value approach to customs with a value-at-customs approach. The later approach, which has necessitated the adoption of a uniform international standard of goods valuation for customs purposes, requires that the price to be paid as of January 1 be determined by the new international standard rather than by the former competitive free-market price.

### II. CENTRAL BANK

#### *Communication "A" 918 (9-1-86)*

The maturity of a private domestic or foreign commercial debt shall be automatically extended for at least one year if such debt is not included in the foreign debt rescheduling program and is not cancelled at its maturity.

#### *Communication "A" 980*

As an incentive to foreign investors, the Central Bank has devised a special foreign exchange financing system. In the interest of promoting exports, this system now permits investors to be reimbursed directly in their respective countries with funds generated by the additional export of goods and services.

As of March 1, 1987, banks and finance companies may engage

in loan or deposit swap operations with Federal Government securities. The Central Bank's authorization also includes other intermediaries' transactions involving public instruments such as deposits, loans and collateral.

### *Government Bonds*

Executive Order No. 256 authorized the Central Bank to issue three new government austral bonds for an aggregate face value amount not to exceed a billion australs.

The first National Government Austral Bonds (BAGON) will have a four-year life span and will earn interest at a rate equal to that prevailing at the outset of each interest-accruing period for the external bond series used as a reference point for adjustment of service payments.

Assured Real Yield Adjustable Bonds (BARRA), yielding two percent interest per annum computed on the adjusted amount of principal, will have a three-year life span. Their retirement is to be made in six successive semi-annual installments, the first five of which will be equal to sixteen percent of the amount issued and the last at twenty percent of the amount.

Finally, Exchange Rate-Adjusted National Government Bonds (TACAM), will have a lifetime ranging from one to five years and will yield the interest rate prevailing on the London Interbank Market (LIBOR) for 180-day Eurodollar time deposits on the third working day prior to the date at which each interest-accruing period begins.

### III. CONSTITUTIONAL REFORM

On October 27, 1986, the Ad Hoc Committee on Constitutional Reform recommended the following amendments to the National Constitution of 1853:

(1) provisions affecting fundamental individual rights would be amended solely for clarification purposes and would incorporate certain procedural due process guarantees. New language would guarantee freedom of religion and establish the separation of church and state;

(2) provisions affecting the function of the Executive would be amended to provide for decentralization through the institution of

a prime minister system. Such an office would be held by a presidential appointee and would exist in lieu of the vice presidency. In the event of the president's permanent absence, the President of the Senate would assume the national presidency and convoke the electors;

(3) the President would be elected through direct, non-compulsory universal suffrage by the second ballot system. No president could serve for more than two four-year terms;

(4) the Committee advocated the introduction of free elections and popular referenda;

(5) efforts would be made on behalf of strengthening federalism, and natural resources would be explicitly allocated to the provinces.

#### IV. CASE LAW

In the area of products liability, an Argentine appellate court determined the extent of a manufacturer's liability pursuant to Civil Code regulations. In *Rincon de Avils S.C.A. v. Cooper Argentina S.A.*, despite the lack of privity of contract, the contract held a manufacturer of a hoof-and-mouth vaccine liable to the owner of ninety-six calves which died of the disease after vaccination. The owner had bought the vaccine from a veterinarian. The court reasoned that a manufacturer engaged in commerce owed certain contractual duties to his consumers, and this contract afforded the consumers protections *vis-a-vis* third parties. The court further held that state approval of a product would not relieve a manufacturer from liability where his product had caused injury due to a manufacturing defect.

This decision is significant because the insertion of manufacturer's liability into the contractual or extracontractual (tort) sphere affects the awarding of damages in Argentine law. Extracontractual liability allows for higher compensation because it includes injuries not proximately caused by defects and "moral harm," while contractual liability, as provided in Article 520 of the Civil Code, includes only "such injuries as shall be an immediate and necessary consequence of non-performance."

V. ARGENTINA'S DEBT TO EQUITY CONVERSION PROGRAM: AN  
OVERVIEW

On April 24, 1987, Argentina presented to the international banking community a finance plan which described the general principles for a new debt to equity conversion program. This program is designed to promote new productive investments by the private sector of approximately \$4 billion over a five-year period beginning July 1, 1987.

To induce investments the program will allow the conversion of \$2 billion of external debt owed by the public sector into local currency at face value. As this debt is currently traded on the international markets at a discount, the program makes it possible for prospective investors to obtain more local currency for the amount invested than they would obtain through usual investment procedures. An amount in foreign currency at least equal to the face value of the debt being converted, however, must be brought in from abroad and invested in the same project. Only funds brought in from May 1, 1987 are eligible for this purpose.

Regulations recently issued by the Minister of Economics (Resolution 520 of May 20, 1987) and the Central Bank (Communication "A" 1035 of June 1, 1987) contain the basic rules for the program. Investments made by non-residents will be subject not only to the above regulations but also to the general rules of the Foreign Investments Law. By and large, all outstanding external debt owed either by the Government or the Central Bank (other than short term trade credits and loans made or guaranteed by foreign government agencies) is eligible for conversion.

Conversion of any debt can be made in part or in full. However, when a portion of the debt is converted, the remainder of the balance not converted must be the same as the tenor of the whole debt before conversion. Debts not exceeding \$2.5 million at face value must be converted on a single date. Those over \$2.5 million may be converted up to three times, provided that at least \$2.5 million are converted the first time. The intervals between times must be no longer than one year.

The proceeds of conversion, as well as the additional funds being brought in by the investor, are required to be applied to the purchase of new equipment, the erection of a new plant, or the expansion of the productive capacity of an existing plant. A maximum of twenty percent of the additional funds may be used to

purchase real estate, if it is necessary. The proceeds of the conversion cannot be re-allocated to another investment within the country for three years. In the case of a foreign investor, the proceeds cannot be repatriated for ten years nor paid as profits abroad during the first four years.

All investment must be directed at increasing the net supply of goods in Argentina. However, investment proposals capable of increasing the net supply of services will be also considered by the government, particularly if they contribute to strengthening Argentina's balance of payments position.

A first group of funds that qualify as "additional funds" under the program includes:

(1) capital investment subject to the Foreign Investments Law, as in the case of a foreign investor;

(2) loans from a private source with a minimum tenor of six years and a minimum grace period of four years;

(3) purchase from the Central Bank of U.S. Dollar denominated external bonds of the Republic of Argentina, at ninety-six percent of par value.

A second group of funds may also qualify as "additional funds," provided that they do not exceed, in aggregate, fifty percent of the total amount of additional funds. This second group includes:

(1) project loans made by the International Finance Corporation and the International Investment Corporation;

(2) export financing with a tenor of no less than 18 months by multilateral or foreign government agencies;

(3) funds available from certain existing facilities (namely, the 1985 Term Credit Agreement and the 1987 Term Credit Agreement) by bringing into Argentina, on a one-to-one basis, other funds which are lent to the private sector with a tenor of at least six years and a grace period of at least four years. Funds counted as "other funds" cannot qualify as additional funds under the program. Of course, additional funds may be provided by a person other than the investor.

When the debt being converted does not exceed \$1 million, the additional funds must be brought in on or before the date of conversion. In converting a larger amount, the debt must be brought in according to an ad hoc schedule to be included in the investor's

proposal. This schedule must be such that the relation between the additional funds actually applied to the project and the amounts disbursed by the investor from the proceeds of the debt conversion, never be lower than the relation established by the investor in its conversion proposal.

If no additional funds have been brought in by the first (or only) date of conversion, the investor must furnish to the Central Bank a performance bond equivalent to three percent of such funds.

For monetary reasons, the Government has set quotas for debt to equity conversions of \$300 million for the first year and \$400 million for each of the following. There are also bi-monthly limits within each year, which are equal to one-sixth of the applicable annual quota and which will be carried forward to the next period. Conversions within each bi-monthly period will be awarded by the Central Bank through competitive bidding.

A prospective bidder must first have its investment project qualified as eligible by the *Subsecretaria de Politica Economica* of the Ministry of Economics. The bidder has 45 calendar days from the date on which all necessary information has been filed by the investor to issue to it a project qualification certificate.

The Central Bank will receive bids every two months at a specified date. Through any local banking institution holding a Class "C" license, each investor must submit a conversion proposal including the amount, at face value, of the debt that the investor wishes to convert, the amount of the additional funds that the investor undertakes, and a schedule of the additional fund payments. Each proposal must be accompanied by the relevant project qualification certificate and a cash or bank guarantee to secure that the proposed conversion, in the case of award, will be actually made. The amount of this guarantee will be equivalent to one percent of the face value of the debt to be converted.

To determine awards, each bid will be given a number of points equal to the result of dividing the amount of the additional funds undertaken by the amount of the debt to be converted. In cases of parity, preference will be given to the bid containing a higher percentage of the additional funds included in the first group above. If there is still a tie, preference will be given to the bid containing a higher percentage of additional funds in the form of a capital investment. The award or rejection of each bid will be

communicated by the Central Bank through the intermediary bank within four business days after the day set for the submission of bids.

Awards are always conditional upon the examination by the Central Bank of the debt instruments to be converted. For such purpose, the investor must deliver the relevant instruments to the Central Bank within 15 business days after being notified of the conditional award. Final awards will be notified by the Central Bank within six business days.

If any instrument proves not worthy of conversion, the Central Bank will notify the investor through the intermediary bank. The investor will have ten additional business days to correct it and to deliver other instruments in substitution. The Central Bank will finally accept or reject the proposal within the next six business days.

After final award, the Central Bank will announce the date of conversion to the intermediary bank. The investor will have three business days to furnish a cash or bank guarantee to secure that the additional funds undertaken and not yet brought in, if any, will actually be brought in. The amount of this guarantee will be equivalent to three percent of such funds. Once this requisite has been satisfied and, in the case of a foreign investor, there has been prior approval of the investment under the Foreign Investment Law, the relevant debt will be converted into local currency at the buying rate quoted by Banco de la Nacion in Argentina at the close of the business day preceding the date of conversion.

The proceeds of conversion will be deposited with the intermediary bank in the investor's name, and will be released if: (1) the relevant stage of the project has been completed; (2) the additional funds undertaken in the proposal have been brought in; and (3) the relation between the additional funds brought in and the amounts withdrawn from the deposit has not lowered with respect to the relation existing in the proposal. The relevant debt will be discharged upon the making of such deposit. The conversion guarantee will be released pro rata to the conversions made, and the additional funds guarantee will be released pro rata to the inflow to the country of the funds undertaken by the investor.

The following events, if not duly justified, will be regarded as events of default in respect of any conversion:

- (1) the investor fails to deliver, in time for examination, the

debt instruments to be converted;

(2) the substitute debt instruments delivered for examination after a first rejection are not appropriate for conversion either;

(3) the additional funds guarantee is not delivered in due course.

In any such case (and after sixty days if the conversion is not the first one), the conversion guarantee will be lost by way of penalty and the awarding will cease to have effect. If the additional funds are not brought in within the required time the conversion guarantee or the additional funds guarantee, as the case may be, will be lost by way of penalty, and sixty days thereafter the investor will lose, in addition, the right to make pending conversions. The unused proceeds of past conversions will be released to the investor according to conditions not yet established by the Central Bank. However, the amount to be released will be converted into US dollars at the exchange rate prevailing at the time of conversion, or, if lower, at the time of release.

## VI. ADDENDUM

New regulations, supplemental to the Conversion Program for Public External Debt recently implemented by the Minister of Economy Resolution 520 of May 29, 1987 and the Central Bank Communication "A" 1035 of June 1, 1987, have just been issued by Subsecretaría de Política Económica. The new resolutions are Resolutions 6, 7 and 8, dated July 30, 1987. Contemporaneously, the Central Bank issued Communication "A" 1056, implementing another program. Communication "A" 1056 addresses the conversion of *private* sector external debts into equity investments in the obligors of such debts.

Through the issuance of the above regulations, the implementation of the new Argentine debt to equity conversion scheme has been completed. The Central Bank, however, still regulates those capitalizations, the proceeds of which will be used to cancel long-term rediscounts by the Central Bank.

### *Additional Guidelines for Public Sector Debt Conversion*

Under Resolution 6, project loans made by the International Finance Corporation or the Inter-American Investments Corporation with a minimum tenor of six years have now been included in

the first group of "additional funds" defined in the program (that is, the group of funds that may be counted as additional funds without any limitation) with respect to any principal installment maturing after the fourth year of each disbursement.

Capital investments made out of profits paid abroad to registered foreign investors under the Foreign Investments Law with respect to any financial year ending after June 30, 1987 have been added to the second group of "additional funds" defined in the program (that is, the group of funds that may not be part of the additional funds in excess of 50% of the aggregate of such funds). In this connection, Resolution 710 of the Ministry of Economy has just renewed the right of registered foreign investors to remit profits abroad to the extent such profits are simultaneously brought back into Argentina as a capital investment.

Any investment made within the Conversion Program for Public External Debt, whether or not registered as a foreign investment under the Foreign Investments Law, must be registered with Subsecretaría de Política Económica in a special registry to be implemented for the program.

The proceeds of debt conversion must be capitalized in the local company receiving the investment which, at its option, may increase its capital either at the date the conversion is made or at each later date in which the proceeds of conversion are disbursed. Such date or dates will be the starting point for time restrictions applicable to profit remittances and investment repatriation.

The proceeds of conversion cannot be diverted from the original project even after the three year period required by Resolution 520 has elapsed. At such time the original investor will only be able to transfer ownership of the investment to another investor.

Resolution 7, in turn, approves the guidelines and forms for the submission of investment proposals to the Ministry of Economy in order to obtain both the qualification of the investment as "eligible" under the program and, when required, the approval of the investment under the Foreign Investments Law.

#### *Guidelines for the Private Sector Debt Conversion*

Communication "A" 1056 of the Central Bank sets forth specific guidelines for the capitalization of *private* sector external debt outstanding as of April 30, 1987, excluding debt owed by financial

institutions. For purposes of the regulation, these obligations have been dealt with under three different captions, namely: obligations without foreign exchange FX insurance, obligations with FX insurance, and swap transactions.

1. *Obligations Without FX Insurance*

These obligations can be prepaid if an equivalent amount in foreign currency is simultaneously brought into Argentina as a capital contribution to the debtor. The foreign investor must obtain, if required, prior approval under the Foreign Investment Law and comply with the additional requirements applicable to the particular obligation.

Additional requirements pertaining to obligations without FX insurance are divided into three groups, and each is subject to different conditions and restrictions.

The first group is composed of:

- (a) import obligations with an original tenor of one year or less;
- (b) import obligations with an original tenor of more than one year incurred from December 10, 1983;
- (c) loan obligations incurred within the framework of Communication "A" 558 of November 28, 1984, and regulations supplemental thereto;
- (d) other obligations incurred from December 10, 1983, except obligations derived from onlending (see below) and obligations to pay profits.

Capitalization of the above obligations does not require Central Bank authorization; it is subject only to reporting requirements. The foreign investor will not be entitled to repatriate its investment at any time earlier than original maturity of the prepaid obligation, regardless of whether its investment has or has not been registered under the Foreign Investments Law.

The second group is composed of:

- (a) import obligations with an original tenor of more than one year incurred before December 10, 1983;
- (b) loan obligations not within the framework of Communication "A" 558 of November 28, 1984, and regulations supplemental thereto;

(c) other obligations incurred up to December 9, 1983.

The requirements and conditions for the capitalization of these obligations are the same as above, except that: (1) repatriation of the investment cannot be made until after ten years of capitalization, if later than the original maturity of the pre-paid obligation; (2) no profits can be remitted abroad during the first four years; (3) profits accrued during the first four years must be remitted in at least eight equal semi-annual installments commencing four years and six months after capitalization and subject to the rules then applicable. In the case of any obligation guaranteed by the Treasury or any government bank, the creditor must notify the Central Bank of its intent to capitalize the debt prior to the effective date of the Guaranteed Refinancing Agreement of the guarantor or in any case not later than October 30, 1987.

The third group comprises government loan obligations transferred to the private sector up to April 30, 1987 under the onlending scheme provided for by the 1985 Term Credit Agreement.

Capitalization of these obligations is subject to prior approval by the Central Bank and to the same reporting requirements as the other groups. The restrictions applicable to the foreign investor are the same established for the second group. However, the capitalization is subject to the further condition that the debtor receives, in an amount equal to the amount of the capitalized onlending (i) a capital contribution subject to the above restrictions or, (ii) a Communication "A" 558 loan with a minimum tenor of ten years, or (iii) any combination of both.

If other funds have already been brought into Argentina (whether as a loan or as a capital contribution) in order to comply with the requirement of matching funds in connection with the capitalized onlending, such funds may qualify for the above purpose provided that: (i) if the funds are a loan, they are extended at the time such further condition is satisfied in such terms as necessary to meet the terms of the required loan; or, (ii) if the funds are a capital contribution, they comply from then on with the restrictions that the required capital contribution must otherwise comply with. Capitalization of onlending will reduce accordingly the onlending rights of the onlending bank under the onlending scheme.

## 2. *Obligations with FX Insurance*

External debt covered by FX insurance can be converted into local currency and applied to a capital investment under the Conversion Program for Public External Debt if, following compliance with all requirements of Communication "A" 1035 and prior to the conversion date, the FX insurance is cancelled under the provisions of Section A.I of Communication "A" 946 of November 12, 1986, by depositing with the Central Bank the amount in local currency necessary to pay the obligation at the FX insured rate. This capitalization alternative must be approved by the Central Bank before the prospective investor submits a bid to the Central Bank under Communication "A" 1035.

## 3. *Swap Transactions*

With prior approval by the Central Bank, external debts associated with swap transactions may be capitalized prior to conversion and after due compliance with all the requirements of Communications "A" 1035. The swap, paid in local currency, must include a premium equivalent to the premium charged in the case of acceleration of an FX insured debt under Communication "A" 946. Another alternative regards the debt as an obligation without FX insurance; the debtor waives his rights to the excess and the swap transaction is merely netted off for the sole purpose of its capitalization.

## 4. *Debt Assignments and Transfers*

Unless an assignee is a party to the 1985 Term Credit Agreement, the assignment of rights with respect to capitalizing onlending debts requires the prior approval of the Central Bank. Such assignment will reduce accordingly the onlending rights of the assignor. The Central Bank must also grant prior approval in cases of transfers of debt obligations without FX insurance or where such transfers involve onlending debts. The Bank's authorization to repay or return matching funds associated with the onlending, but not used for additional loan or capital contributions, is withheld until the onlending debt matures.

5. *Payment of Interest*

The regulations in force at the time of capitalized debt payment shall govern the manner in which interest accrued up to the date of capitalization shall be paid.

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