UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

ELLIOTT ASSOCIATES, L.P. Plaintiff, - against - BANCO DE LA NACION Defendant	96 Civ. 7916 (RWS)
ELLIOTT ASSOCIATES, L.P. Plaintiff, - against - THE REPUBLIC OF PERU Defendant	96 Civ. 7917 (RWS)

DECLARATION OF PROFESSOR ANDREAS F. LOWENFELD

1. I have been asked by Messrs. Dechert Price & Rhoads of New York to give my opinion as to the meaning and legal consequence of one of the provisions in a Guaranty dated as of May 31, 1983 issued by the Republic of Peru to lenders in a series of "Letter Agreements" of the same date. In particular, I have been asked to give my opinion on the rights and obligations flowing from Section 11(c) of said Guaranty, stating that the obligations of the Guarantor (i.e., the Republic of Peru) rank at least *pari passu* in priority

of payment with all other External Indebtedness of the Guarantor and interest thereon. I have no interest, direct or indirect, in the outcome of the litigation.

Qualifications

2. I am the Herbert and Rose Rubin Professor of International Law at the New York University School of Law. I have been a Professor at the New York University School of Law since the Fall of 1967, and from 1981 until 1994 I held the Charles L. Denison Chair at New York University School of Law. Prior to becoming a Professor of Law I was engaged for four years in the private practice of law in the City of New York, and served for more than five years in the Office of Legal Adviser in the United States Department of State, holding the position of Deputy Legal Adviser at the time I left government service. I am a member of the bar of the State of New York and the United States Supreme Court, as well as of the U.S. District Courts for the Southern and Eastern Districts of New York and of the Court of Appeals for the Second Circuit. I am a graduate of the Harvard College (M.c.L.) and of the Harvard Law School (M.c.L.).

3. My special fields are International Law, International Economic Transactions, Conflict of Laws, and International Litigation, and I have also taught Torts and Civil Procedure, as well as Aviation Law and Comparative Procedure. I have twice been a Lecturer at the Hague Academy on International Law, and I have taught as a Visiting Professor in London, Paris, Dublin, Moscow,

Warsaw and Sydney. I am a member of the American Law Institute, the American Bar Association, the Association of the Bar of the City of New York, and the American Society of International Law, and I am a frequent participant in international conferences for legal scholars and practitioners. In 1989 I was elected one of eight American members of the Institut de Droit International, and I have recently served as a Rapporteur for that institute on the subject of the obligations of multinational enterprises. In 1998 I was elected a member of the International Academy of Comparative Law.

4. Since becoming a full-time member of the faculty of Law of New York University, I have served as special consultant to several law firms both in the United States and abroad, and as expert witness before courts in the United States and various foreign countries. I have served as arbitrator in numerous cases brought under the rules of the American Arbitration Association, the International Chamber of Commerce, the United Nations Economic Commission for Europe, the Arbitration Institute of the Stockholm Chamber of Commerce, as well as a member of a Disputes Panel under the General Agreement on Tariffs and Trade. I have also acted as counsel in numerous cases before the United States Supreme Court dealing with conflict of laws, arbitration, and international controversies.

5. I am the author of twelve books dealing generally with the subject of international transactions -- public and private. My six-volume series on International Economic Law, now beginning its

third edition, includes volumes on International Private Trade, International Private Investment, Trade Controls for Political Ends, The International Monetary System, Tax Aspects of International Transactions (by D. Tillinghast), and Public Controls on International Trade. I have published more than 100 articles and reviews in the Harvard, Columbia, Chicago, and New York University Law Reviews, the American Journal of International Law, the American Journal of Comparative Law, the Journal of Maritime Law and Commerce, and comparable professional journals in the United States and Europe. I am or have been a member of the Board of Editors of the Journal of Air Law and Commerce, the Journal of Maritime Law and Commerce, the American Journal of International Law, and the American Journal of Comparative Law. I served for some eight years as Associate Reporter of the American Law Institute's Restatement (Third) of the Foreign Relations Law of the United States (1987), with principal responsibilities in that capacity for Part IV, Jurisdiction and Judgments, and Part VIII, International Economic Law. I am presently completing a comprehensive treatise on International Economic Law commissioned by the Oxford University Press.

6. Of particular relevance to the present controversy, I am the author of a case- and textbook on The International Monetary System (2d ed. 1984) and a number of law review articles on legal aspects of international finance. I have also advised several developing countries as well as a major public international financial institution with respect to rescheduling and restructur-

ing agreements, and I have served as arbitrator in a major controversy concerning international credit arrangements.

A copy of my *curriculum vitae* is attached and marked "A".

Background to the Question

7. As I understand the facts, Plaintiff is the holder of a judgment in the amount of US$ 55,660,832.56 against the Republic of Peru, issued by the U.S. District Court for the Southern District of New York dated June 22, 2000. The judgment arises from default by the borrowers and the Guarantor on the underlying Letter Agreements dated May 31, 1983. No portion of the said judgment has been paid. The Republic of Peru, as I have been informed, is scheduled to make a substantial payment to other creditors on September 7, 2000. As set out in more detail below, Plaintiff seeks an order that the Republic treat it equally with other external creditors in disbursing its funds, as called for by the *pari passu* clause, and therefore that the Republic not make a payment of principal or interest to other creditors while ignoring its obligation to Plaintiff.

8. Many of the lenders under the Letter Agreements of May 31, 1983 agreed in November 1996 to permit the Republic of Peru to redeem the obligations under the Letter Agreements in exchange for so-called "Brady Bonds" issued by the Republic. I am not familiar with that particular exchange, but in general the lenders under the Brady Plan had a choice whether to accept a lower interest rate than in the original loan while maintaining the principal amount or

to accept a lower face amount of principal while maintaining the original interest rate, in either case in return for greater security offered by the backing of U.S. zero coupon bonds.[1] At all events, the exchange under the Brady Plan was optional, and no creditor was required to choose either option. Elliott, which had previously purchased portions of the loans under the Letter Agreements from two European banks, elected to accept neither option, but to retain the original contract. Nothing in the Letter Agreements or the Guaranty of May 31, 1983 obligated Elliott to concur with other lenders in accepting the exchange offered under the Brady Plan, and it appears clear that Elliott remained a creditor under the 1983 Letter Agreements with all the rights granted under the said Agreements. This court so held in Elliott Associates, L.P. v. The Republic of Peru, 12 F. Supp. 328 at 344 (S.D.N.Y. 1998).

9. Plaintiff Elliott claims in this proceeding, inter alia, that it is entitled under Section 11(c) of the 1983 Guaranty, the "*pari passu* clause," to be treated with respect to payment of principal and interest at least on equal terms with all other External Indebtedness. Thus payment to the holders of Brady Bonds but not to Elliott -- whether of principal or of interest or both -- would constitute a preferential arrangement contrary to the

[1] See, Nicholas Brady, Remarks to Brookings Institute, reproduced in Edward R. Fried and Philip H. Trezise, eds., Third World Debt: The Next Phase (Brookings 1989); also e.g., Lee C. Buchheit, "Overview of Four Debt Reduction Programs: Mexico, Costa Rica, the Philippines and Venezuela," in Latin American Sovereign Debt Management p. 77 (Reisner, Cardenas, Mendes eds., 1990).

terms of Section 11(c). On this basis Plaintiff seeks an order enjoining the Republic of Peru from servicing its debt to the Brady Bondholders unless a payment is simultaneously made to it in an amount at least proportionate to the payment made to the holders of the Brady Bonds or other holders of External Indebtedness as defined in Section 1 of the Guaranty. It is in this context that I have been asked to give my opinion as to the rights and obligations derived from Section 11(c) of the 1983 Guaranty.

Summary Analysis

10. On the basis of the analysis set out hereafter, my conclusion is that the *pari passu* clause in the Guaranty entitles each Lender to share equally and ratably with any other holder of External Indebtedness as defined. I have no doubt that the Brady Bonds described above constitute External Indebtedness of the Republic of Peru. Accordingly, if the Republic pays principal or interest to holders of the Brady Bonds or some of them, it is obligated to make a payment of a proportionate amount to all holders of Affected Debt incurred in the Letter Agreements, including Plaintiff Elliott Associates, L.P., and that obligation is enforceable in this court -- if necessary by an injunction.

Analysis

11. Section 11 of the Guaranty dated as of May 31, 1983 reads in pertinent part as follows:

> Representations and Warranties. The Guarantor [i.e., the Republic of Peru] represents and

warrants as follows:

> . . .
>
> (b) This Guaranty is the legal, valid and binding obligation of the Guarantor, enforceable against the Guarantor in accordance with its terms.
>
> (c) The obligations of the Guarantor hereunder do rank and will rank at least pari passu in priority of payment with all other External Indebtedness of the Guarantor, and interest thereon.

There can be no doubt about the literal meaning of the clause.[2] There are to be no preferential arrangements with respect to External Indebtedness; every obligation subject to the Guaranty -- i.e., any portion of the debt issued under the Letter Agreements of May 31, 1983 -- is to have at least equal rank with all other External Indebtedness of the Republic. Based on the definition of

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[2] The expression comes from the Latin noun "*passus*" = step, pace, stride, as well as a Roman measure of length; and the Latin adjective "*par*" = equal or like.

Webster's New International Dictionary (2d ed., unabridged, 1951) defines "pari passu" as "with or at an equal pace; in or to an equal proportion, degree, place, rank, or title."

Black's Law Dictionary (6th ed. 1990) defines "pari passu" as "By an equal progress; equably, ratably; without preference. Used especially of creditors who, in marshalling assets, are entitled to receive out of the same fund without any precedence over each other."

The Oxford English Dictionary (unabridged ed., 1991, vol. XI) gives essentially the same definition, but adds several quotations, including the following:

> John Adams (1775): To...proceed with warlike measures and conciliatory measures *pari passu*.
>
> Gladstone (Speech in House of Commons 1890): The only method of describing *pari passu* was that adopted by Mr. John Bright..when he said that, when people were content with a *pari passu* progress, it was like driving six omnibuses abreast down Park Lane.

External Indebtedness contained in Section 1, it is clear that the *pari passu* clause covers any other portion of the debt issued under the Letter Agreements of May 31, 1983, as well as any bonds or other evidence of debt issued or guaranteed by the Republic, including the Brady Bonds issued some fourteen years later.[3]

12. A clause such as Section 11(c) is a standard clause included in virtually all loan or debt restructuring agreements, as well as sovereign guaranties of such agreements. Accord, e.g., Philip Wood, Law and Practice of International Finance, Vol. 2, §6.03 (1990); also id. §4.13 [7][g] ("Rescheduling of Commercial Bank Debt: Most Favored Debt Clauses"); Sandra Schnitzer Stern, Structuring Commercial Loan Agreements ¶4.16 (Rev. ed. 1999); Annotated Sample Loan Agreement Sections 9.1(h) and 9.2(g) in Daniel D. Bradlow, ed., International Borrowing: Negotiating and Structuring International Debt Transactions, pp. 332, 335 (2d. ed. 1986). I may add that all of the sovereign debt documents, including new loans, rescheduling/restructuring arrangements, and government guarantees that I have seen in the past twenty years in the course of my academic research as well as advice to governments, have contained a provision substantially identical to Section 11(c), in some instances in conjunction with so-called

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[3] In loans from private or corporate borrowers, there may be certain creditors with super-priority, for instance the tax authorities, employees, or in the case of a bank, depositors up to a certain amount. When the borrower (or guarantor) is a sovereign state, there are no super-priority unsecured creditors and the *pari passu* clause is a general non-discrimination clause. See, e.g., Philip R. Wood, International Loans, Bonds and Securities Regulation, §3-27 - §3-28 (1995).

negative pledge clauses, in others not. A negative pledge clause obligates the borrower not to give security to any other lender without protecting the interests of the lender in question; a *pari passu* clause records an affirmative obligation to ensure that the debt in question ranks equally with all other unsecured indebtedness of the borrower.

13. It is of course true that a *pari passu* clause in a loan to an individual or corporation may have direct effect in case of a winding up or bankruptcy, while sovereign countries do not go bankrupt and cannot be liquidated. And yet, as an English commentator has pointed out, "The clause which is commonly referred to as the *pari passu* clause is just as standard in a government loan agreement or bond issue as it is in loans to ordinary persons." William Tudor John, "Sovereign Risk and Immunity under English Law and Practice," in Robert S. Rendell, ed., International Financial Law, Vol. 1, p. 71 at 95 (2d ed. 1983) "Nevertheless," Mr. Tudor continues, "the *pari passu* clause is considered by lenders to be of the very greatest importance in a governmental loan agreement."

> [I]t is primarily intended to prevent the earmarking of revenues of the government towards a single creditor, the allocation of foreign currency reserves, and generally against legal measures which have the effect of preferring one set of creditors against the others or which discriminate between creditors.
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> Id. at 96.

The author goes on to describe a well known case of discrimination that came before the World Court, in which France contended that

Norway as borrower had given preference to Danish and Swedish bondholders over French bondholders. *The Norwegian Loans Case*, [1957] I.C.J. Rep. 37. The claim was dismissed on jurisdictional grounds, and so the contention by France that international law required *pari passu* treatment was not adjudicated. Mr. Tudor John, however, observes, "This is perhaps an example where a *pari passu* clause would have served a function and avoided academic arguments as to whether international law implied a *pari passu* obligation."

14. A number of articles have suggested that *pari passu* clauses, though very common in sovereign loan agreements, do not mean what they say, or cannot be relied on by lenders if they are disregarded or violated by borrowers. For instance, Lee C. Buchheit writes:

> The fact that no one seems quite sure what the [*pari passu*] clause really means, at least in a loan to a sovereign borrower, has not stunted its popularity among drafters of loan agreements and debt restructuring agreements.
>
> Lee C. Buchheit, "The *Pari Passu* Clause *sub specie aeternitatis*," 10 Int'l Financial L. Rev. No. 12, p. 11 (Dec. 1991).

I have no difficulty in understanding what the *pari passu* clause means: it means what it says -- a given debt will rank equally with other debt of the borrower, whether that borrower is an individual, a company, or a sovereign state.[4] A borrower from Tom,

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[4] The Securities and Exchange Commission, as part of its "Plain English Disclosure" Campaign, proposed the following change in debt offerings:

Before

After

Dick, and Harry can't say "I will pay Tom and Dick in full, and if there is anything left over I'll pay Harry." If there is not enough money to go around, the borrower faced with a *pari passu* provision must pay all three of them on the same basis:

> Suppose, for example, the total debt is $50,000 and the borrower has only $30,000 available. Tom lent $20,000 and Dick and Harry lent $15,000 each. The borrower must pay three fifths of the amount owed to each one -- i.e., $12,000 to Tom, and $9,000 each to Dick and Harry. Of course the remaining sums would remain as obligations of the borrower. But if the borrower proposed to pay Tom $20,000 in full satisfaction, Dick $10,000 and Harry nothing, a court could and should issue an injunction at the behest of Harry. The injunction would run in the first instance against the borrower, but I believe (putting jurisdictional considerations aside) to Tom and Dick as well.

15. A closely analogous case was recently decided in this court and the Court of Appeals, in which a Mexican borrower and guarantors of the financing arrangement were enjoined from making payments to some creditors while the plaintiffs, who were entitled to *pari passu* treatment, were going to be left out. Alliance Bond Fund, Inc., v. Grupo Mexicano de Desarrollo, S.A., 143 F.3d 688 (2d Cir. 1998). The District Court enjoined payment by the borrowers and/or guarantors to the Mexican creditors, and the Court of

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The new debt will rank pari passu with other senior debt of the company.	The new debt will rank equally with the other senior debt of the company.

Securities and Exchange Commission: Plain English Disclosure Proposed Rules, 62 Fed. Reg. 3152, at 3158 (Jan. 21, 1997).

Appeals affirmed. The U.S. Supreme Court reversed the decision of the Court of Appeals, on the ground that prejudgment injunctions preventing the payment of money were not authorized in the Federal Rules of Civil Procedure and were inconsistent with traditional equity jurisprudence. Grupo Mexicano de Desarrollo , S.A. v. Alliance Bond Fund, Inc., 527 U.S. 308 (1999). In contrast, in the present case plaintiffs have a judgment, so it would seem that the reason to refuse the injunction found by the Supreme Court in Grupo Mexicano is not present here.

16. Moreover, I point out that the Guaranty contains not only Section 11(c) but also Section 11(b),[5] which expressly states that the Guaranty is the legal, valid and binding obligation of the Guarantor, *enforceable against the Guarantor in accordance with its terms* (italics added). Coupled with the express choice of New York law clause (Section 16) and the express consent to the jurisdiction of this court (Section 10(a)), I believe that this court is not only entitled, but is expected to enforce the contract of guaranty. The *pari passu* clause is an express provision of the contract sued upon, and a court faced with a claim based on that clause should not shy away from applying it as written.

Conclusion

17. I conclude that Section 11(c) of the Guaranty as of May 31, 1983 creates a binding and continuing obligation to treat all covered borrowers equally and without discrimination, including

[5] See para. 11 supra.

Elliott Associates L.P., the plaintiff herein. This obligation is entitled to enforcement in this court, by injunction or otherwise.

Respectfully submitted,

Andreas F. Lowenfeld
Herbert and Rose Rubin
Professor of International Law

New York, N.Y.

August 31, 2000