THE ACQUISITION AND LEVERAGED FINANCE REVIEW

FOURTH EDITION

Editor
Christopher Kandel

THE LAWREVIEWS

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PREFACE

Acquisition and leveraged finance is a fascinating area for lawyers, both inherently and because of its potential for complexity arising out of the requirements of the acquisition process, cross-border issues, regulation and the like. It can also cut across legal disciplines, at times requiring the specialised expertise of merger and acquisition lawyers, bank finance lawyers, securities lawyers, tax lawyers, property lawyers, pension lawyers, intellectual property lawyers and environmental lawyers, among others. An additional area of complexity and interest at the moment comes out of market forces that are driving convergence in the large cap leveraged financings between loan and high-yield bond products generally, as well as between different markets (particularly pressure on markets outside the United States to conform to terms available in the US market but sometimes also vice versa), and increasingly the market is debating whether to adjust for differences in bankruptcy, guarantee or security regimes, and frequently deciding not to.

The Acquisition and Leveraged Finance Review is intended to serve as a starting point in considering structuring and other issues in acquisition and leveraged finance, both generally but also particularly in cases where more than just an understanding of the reader's own jurisdiction is necessary. The philosophy behind the sub-topics it covers has been to try to answer those questions that come up most commonly at the start of a finance transaction and, having read the contributions, I can say that I wish that I had had this book available to me at many times during my practice in the past, and that I will turn to it regularly in the future.

Many thanks go to the expert contributors who have given so much of their time and expertise to make this book a success: to Nick Barette, Gideon Roberton and Gavin Jordan at Law Business Research for their efficiency and good humour, and for making this book a reality; and to the partners, associates and staff at Latham & Watkins, present and past, with whom it is a privilege to work. I should also single out Sindhoo Vinod, Aymen Mahmoud, Angela Pierre and Oliver Browne for particular thanks – their reviews of my own draft chapters have been both merciless and useful.

Christopher Kandel
Latham & Watkins LLP
London
August 2017

Chapter 2

ARGENTINA

Tomas Allende and Francisco Lombardi[1]

I OVERVIEW

The M&A market has been fairly depressed over the past few years, mostly due to the business and legal environment created by the previous administration, which affected the overall economy and the rule of law. Throughout this period, capital has been scarce, and thus the few acquisitions were financed either through seller financing or with loans by local institutions, in small amounts. The presence of foreign lenders has been very limited, as high inflation and the implementation of strict foreign exchange controls, together with increased limitations to the purchase of foreign currency, acted as roadblocks to the inflow of foreign investments. Also, a *de facto* prohibition to the transfer of dividends out of the country and the uncertainty of future exit from investments, acted as another important deterrent in the industry. Furthermore, there were certain restrictions, caused by the characterisation of Argentina as a high-risk country by international rating agencies, that prevented some international funds and financial institutions from investing in Argentina.

Another issue that hindered the level of M&A activity, and clearly differs from more developed countries, is the lack of a deep local capital market, with little to no incidence in the use of securities to finance acquisitions. For example, even though financing for acquisitions could be theoretically obtained through the issuance of securities (such as convertible or negotiable bonds), this has not been the case in past years, as these types of structures are simply not utilised for acquisitions.

With the new administration taking office as of late 2015, many regulations affecting foreign investment were removed, which has helped to start to turn around a declining trend in M&A activity,[2] albeit at a slower rate than was expected by most in the business community. Recent activity has been focused mainly on energy and agro-industries,[3] but media and finance sectors were also relevant targets.

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1 Tomas Allende is a partner and Francisco Lombardi is a senior associate at Estudio Beccar Varela.

2 Orlando Ferreres & Asociados made a study that shows that M&A activity was US$869 million in 2015 and US$3,109 million in 2016.

3 Deals: Santander Río acquired Citibank's retail business; Macro (local bank) bought Deutsche Bank Argentina; Viacom bought one of the leading TV channels – Telefe; Vicentin acquired Sancor's yogurt and other retail businesses; Cablevision bought Nextel Argentina; BRF acquired local slaughterhouse company Campo Austral; and Pampa Energia acquired Petrobras Argentina.

With respect to providers of financing for M&A transactions, we have started to once again witness commercial banks and some private equity funds. Only a few acquirers have used international capital markets. Foreign players have increased their participation in transactions.[4]

II REGULATORY AND TAX MATTERS

i Regulatory matters

Anti-money laundering and corruption regulations

Anti-money laundering regulations always have an impact in acquisitions financing transactions. Argentina is one of the members of the Financial Action Task Force (FATF) and the FATF of Latin America, and has recently incorporated their recommendations into its legislation. In Argentine law, money laundering is a specific criminal offence that can be imputed both to legal entities as well as natural persons. The specific authority in charge of the investigation and the prevention of money laundering and terrorist financing is the Financial Information Unit, an agency responsible for issuing regulations and for monitoring compliance with money laundering, among other things. This has an impact on the financing of acquisition as, pursuant to local legislation, certain types of companies and individuals (which include financial entities, and certain government registries and agencies, among others) are required to report suspicious transactions to the Financial Information Unit, and carry out 'know-your customer' procedures.

These requirements are not different from those implemented by most countries, as they are very much in line with international guidelines. Thus, these do not affect debt financing any differently than what occurs in most countries, although of course the actual enforcement of these policies is always country-specific.

Also, the new administration has promised to make the fight against corruption one of the main political goals of its administration. Regarding new legislation, a set of anti-corruption bills was recently introduced to Congress. Among them, there is great expectation about the bill on corporate criminal liability for cases of corruption that originally provided for effective collaboration agreements, compliance programmes, joint and several liability of controlling companies, successor liability and fines of up to 20 per cent of the corporate gross income for the previous year, among others. This bill, which could have a massive impact on how business is currently done in Argentina, is, however, the subject of great debate and modifications due to its politically inflammatory nature. Given that Argentina will have a mid-term election in 2017, this proposed bill has been used by the different political parties to support their campaigns and attack companies or businesspersons that have some identification with a political party.

Other relevant bills under consideration are:

a the Asset Recovery Bill, which has already been sanctioned by one of the chambers of congress and, if enacted into law, would provide for an autonomous judicial action in order to confiscate any assets or proceeds that are a product directly or indirectly of illicit activity; and

4 Pursuant to a PwC study of 2016, foreign purchasers represented 47 per cent of the transactions while in the previous year they accounted for 33 per cent.

b the Lobby Bill, which would set forth the obligation to keep records of all hearings with public officers of all three branches of power.

Such records will be publicly available on the internet.

Foreign exchange regulations

A major regulatory concern in any type of foreign financing is the existence of foreign exchange controls that may somehow restrict the flow of funds in and out of the country. This has always been a hot topic in Argentina, with a long history of implementation of strict controls. In this regard, Argentine law requires, as a general rule, that all transfers of foreign currency to and from the country must be carried out through a licensed financial entity or foreign exchange business. Moreover, these transfers have been subject to numerous restrictions imposed gradually by the previous administration, although they were severely relaxed as of December 2015. Currently, however, the ability of Argentine residents to purchase foreign currency through the foreign exchange market was reinstated in December 2015. Likewise, transfer of funds in and out of the country has been normalised.

ii Tax matters

Most common tax issues: income and VAT tax

Tax matters are most commonly the main drivers in the structure of any type of transaction, and acquisition financing is no exception. With regards to Argentina, there are several issues affecting acquisition financing in this jurisdiction that tend to determine the viability of a transaction.

The acquisition of a company can be carried out as a stock purchase or an asset purchase, with the latter having a special procedure of transfer as an ongoing concern. Transfer of assets or transfer as an ongoing concern (the transfer of assets in bulk regulated by a special law) is taxed at 35 per cent of the value of the transferred assets, minus acquisition costs and expenses. Furthermore, VAT of 21 per cent is applied to the purchase of all moveable assets, whereas certain capital goods are taxed with VAT of 10.5 per cent.

The sale of stock is levied (1) for local legal entities, at a 35 per cent income tax rate over the difference between the purchase value and the acquisition cost; or (2) for foreign shareholders, 15 per cent over said amount or 13.5 per cent over the gross amount paid. It should be noted that the sale of stock is not subject to VAT or turnover tax.

Stamp tax

A major concern, that is very relevant in financed acquisitions, is stamp tax. Stamp tax is a local tax applied individually by each jurisdiction to instruments that have some sort of economic value and are either executed in Argentina or produce effects in Argentina. Since each local jurisdiction is in charge of the application in its own territory, this presents a challenge when a single transaction has effects in many jurisdictions, as the transaction may be taxed differently according to the jurisdiction at hand.

For example, in a transaction where funds are delivered to a company in jurisdiction X for the acquisition of assets in jurisdictions Y and Z, stamp tax may be applied by all these jurisdictions if, for example, the loan agreement is executed in X and there are pledges of

assets executed in Y & Z jurisdictions. The stamp tax rate varies per jurisdiction, but is usually between 1 and 1.5 per cent of the amount of the transaction that applies to said instrument – a very significant amount.

There are certain exemptions and ways to mitigate this tax, whether it is because there are special regulations that allow the consideration of payments (or exemptions) of stamp tax in other jurisdictions, or if the transaction is structured properly such as by executing an agreement through a reversal letter mechanism. The latter is a contractual mechanism in which one party sends a written offer and establishes that it will be considered to be accepted if the recipient performs a specific positive action (for example, payment or delivery of goods). This mechanism has been declared by courts as a legal contractual mechanism, and that stamp tax cannot be levied on it. However, there are certain limitations to this procedure as, for example, the mechanism for the registration of a pledge of assets in every jurisdictions sets forth the need to instrument the contract as a single agreement.

Withholding tax

With regard to withholding tax, interest paid by Argentine companies to foreign banks or financial entities (1) under the supervision of the relevant central bank or similar governmental authority, and (2) tax resident in a White List jurisdiction are subject to a 15.05 per cent withholding tax over gross payments (17.7163 per cent if the Argentine payer agrees to bear the withholding tax himself or herself).

Interest paid by Argentine companies for the import of moveable assets (except automobiles) if the loan was granted by the supplier is also subject to a 15.05 per cent withholding tax over gross payments (17.7163 per cent if the Argentine payer agrees to bear the withholding tax himself or herself).

In case of any other interest payment to foreign beneficiaries, a 35 per cent withholding tax rate applies over gross payments (53.8462 per cent if the Argentine payer agrees to bear the withholding tax himself or herself).

Notwithstanding, the applicable withholding tax rate can be reduced if the interest payment is made to tax residents of states that have a double tax treaty in force with Argentina (rates can be 10 to 12 per cent). Finally, no withholding tax applies on principal repayments.

Debit and credit tax

This tax is levied on debits and credits in bank accounts held at Argentine financial institutions. The tax is levied on the amount of each debit or credit and the triggering event is the occurrence of a debit or credit in a bank account. A rate of 0.6 per cent rate is applicable on each debit and credit. There are several exemptions applicable to finance transactions, including debits relating to time deposits, credits relating to loans granted by banks, and credits or debits relating to advances of discount operations. However, when structuring a transaction, this tax should be considered carefully, as it may increase transaction costs since it will affect the flow of funds to different accounts, and is usually the source of complex negotiation by the parties searching for the most efficient structure.

III SECURITY AND GUARANTEES

The most common types of security are mortgages, pledges of shares, pledges of assets and security trusts (over assets or over debtor's cash flow). A mortgage is pretty straightforward, with the underlying collateral usually being the real estate utilised by the acquired entity to

carry out its business, as this will compromise its activities in case of default and thus provides an incentive for the debtor to repay. The pledge of assets is very similar, with creditors usually requiring that the underlying collateral be the assets utilised for production. The re-sale value in case of foreclosure of the asset pledge can be tricky, as many assets can be hard to sell.

Another security used by lenders in certain transactions has been an assignment into a security trust of the target cash flows (i.e., assignment of receivables). Under the security trust, the fiduciary title of certain assets (which can be any type of assets) is transferred to a trustee (who is to be determined by contract) so that he or she can liquidate these assets in order to satisfy a credit, subject to the occurrence of certain conditions, most commonly a default of the debtor.

Even though security trusts have been utilised in Argentina for many years, they were not expressly regulated until the last reform of the Argentine Civil Code in August 2015. This lack of express regulation generated a lot of discussion in the legal community over the validity of the security trust and its scope, primarily under scenarios of insolvency. Discussions have involved whether:

a a creditor would have to participate or not in a hypothetical bankruptcy or reorganisation proceeding of the debtor (since the assets are held in trust); or

b the need for a creditor guaranteed by a security trust to verify the credit under the bankruptcy or reorganisation proceeding of a debtor (as a creditor).

In this sense, there is case law going both ways. There are precedents setting forth that a creditor under a security trust does not have to verify this credit under the bankruptcy proceeding, and jurisprudence setting forth that the creditor must verify his or her credit and also that the liquidation of the assets under the security trust is subject to control by the intervening judge. Finally, within the latter, there is a dispute regarding if the creditor (beneficiary of the security trust) must request a verification of his or her credit as:

a common;

b common eventual; or

c preferred or privileged.

This classification is relevant to define the priority of the claim against the estate.

Also, there is certain case law in which the effects of a security trust over the debtor's cash flow was terminated for the sole reason that without said flow the debtor will not be able to reorganise without this cash flow. This will not happen with a pledge or a mortgage.

One important guaranty that lenders should always try to get is personal guaranties from the owners. This is not easy to obtain, but generally in a stress scenario personal guaranties are a good leverage tool to renegotiate terms.

Finally, a *pagaré* (similar to a promissory note) issued by the borrower (or its shareholder) that allows lenders to request for bankruptcy on a summary procedure is a 'must' in every acquisition financing.

IV PRIORITY OF CLAIMS

Priorities in an insolvency procedure depend on the very nature of the existing debt. Privileges are ruled only by the Argentine Bankruptcy Law (ABL) and are detailed between Articles 239 and 250 of the ABL. Below is a chart describing priorities of claims.

Type of credit	Description	Scope	Detail of the assets over which the privilege can be exercised
Expenses reserve	Expenses necessary for the bidding process of the bankruptcy assets (Article 244 ABL)	Expenses	Over the assets of the bidding
Special privilege	Construction, improvement and conservation of a thing or asset (Article 241, Section 1)	Principal of credit (Article 242 ABL)	Over the thing, asset or subject of the improvement or construction (after paying 'expense reserve')
	Credits for remuneration owed to an employee for six months, and those coming from severance payments, accidents, years of service or dismissal, lack of prior notice and the unemployment fund (Article 241, Section 2)	Principal of credit plus interest for two years counting from the time of the due date (Article 242, Section 1 ABL)	Over merchandise, raw materials and machinery that are property of the insolvent and are located in the establishment where services were rendered (after paying an 'expense reserve')
	Taxes and fees applied over certain assets (Article 241, Section 3)	Principal of credit	Over certain assets (after paying an 'expense reserve')
	Mortgage, security interest (Article 241, Section 4)	Principal of credit plus costs and interests for two years prior to the bankruptcy and compensatory interests after the bankruptcy until effective payment (Article 242, Section 2 ABL)	Over the assets granted as subject matter of the relevant mortgage (after paying 'expense reserve')
	Debts owed to the withholder for withholding certain things (Article 241, Section 5)	Principal of credit	Over the retained thing (after paying an 'expense reserve')
	Others (Article 241, Section 6), in other words, the Navigation Law or the Customs Code	Principal of credit	After paying an 'expense reserve'
Justice and conservation expenses	All expenses derived from the conservation of the assets (i.e., fees of syndic, expenses carried out by Proteinsa, etc.) (Article 240 ABL)	Expense	Over all assets (after paying an 'expense reserve')
General labour privilege	Credits for payments and family subsidies owed to workers for six months and those coming from severance, work-related accidents, years of service or dismissal, lack of prior notice, vacations, 13th salary, unemployment fund, and any other credit related to the employee–worker relationship (Article 246, Section 1 ABL)	Principal of credit plus interests for two years from the due date and judicial expenses (if applicable)	Over all assets (after paying an 'expense reserve', 'special privilege' and 'conservation expenses')
General privilege	Payments owed to national, provincial or municipal social security organisms, family subsidies and unemployment fund (Article 246, Section 2)	Principal of credit	50% of all assets (after paying an 'expense reserve', 'special privilege', 'conservation expenses' and 'general labour privilege') (Article 247 ABL)
	Taxes and fees owed to national, provincial or municipal tax organisms (Article 246(4))	Principal of credit	50% of all assets (after paying an 'expense reserve', 'special privilege', 'conservation expenses' and 'general labour privilege') (Article 247 ABL)
Unsecured creditors	All credit without privilege	Capital and interests	50% of all assets (after paying an 'expense reserve', 'special privilege', 'conservation expenses' and 'general labour privilege') (Article 247 ABL) and Remaining assets (after paying the general privilege)

V JURISDICTION

i Choice of forum

The Civil and Commercial Code of Argentina allows the parties to an international agreement to select the jurisdiction of either an arbitration tribunal or a foreign court, for the settlement of disputes that arise under such agreement. Furthermore, the courts of Argentina have exclusive jurisdiction over insolvency procedures related to debtors who are domiciled in Argentina. With regards to the right to be heard in court, the Constitution of Argentina grants unlimited access to all people, foreign or nationals to have their disputes resolved by a court of law. Argentine courts also recognise procedures of Argentine debtors that have taken place abroad as long as the foreign country recognises reciprocity.

ii Enforcement of arbitration awards and foreign judgments

As a general principle, Argentine courts will recognise both arbitration rulings and foreign judgments. In the absence of a treaty for the enforcement of foreign judgments, the National Code of Civil and Commercial Procedure will be applied to the enforcement of foreign judgments if the matter at hand is decided before a federal court or if the defendant is domiciled in the City of Buenos Aires. In matters decided before provincial courts, provincial procedural rules will apply. Argentine courts will enforce foreign judgments and arbitration awards resolving disputes subject to the fulfilment of the following requirements:

a that the judgment was final and issued by a competent court of law, according to Argentine conflict of laws principles regarding jurisdiction;
b that the judgment was valid in the jurisdiction where it was given;
c that the defendant was granted due process, in accordance with Argentine legislation;
d the judgment must not be in conflict with a prior or simultaneous judgment of an Argentine court; and
e the judgment must not be contrary to any of the public policy principles of Argentine law.

Specifically with regards to arbitration awards, and subject to Section 1656 of the National Civil and Commercial Code, parties cannot waive their right to judicially challenge an arbitral award that breaches Argentinean law. However, courts have reasonably come to interpret that the extent of the waiver applies only to arbitration awards that are contrary to Argentine law in that they violate public policy or negate due process, as otherwise one could construe that any award could arguably be, in some way, in breach of Argentine law.

VI ACQUISITIONS OF PUBLIC COMPANIES

The main regulations applicable to public takeovers and mergers are:

a Securities Law No. 26,831;
b Decree No. 1023/13, Chapter II;
c Title III of the rules issued by the National Securities Commission (CNV) (CNV Rules) (General Resolution 622/2013); and
d Companies Law No. 19,550, as amended.

Public takeovers and mergers are regulated by the CNV. It may also be necessary to obtain approval from additional governmental entities (for example, the Argentine Central Bank and the Anti-trust Authority), depending on the circumstances and business activities of the company.

Before making a tender offer, it is common to obtain various agreements from the target's key shareholders (for example, management agreements). The terms of these agreements must comply with the target company's bye-laws and applicable regulations.

The parties must inform the CNV of the main terms of the agreement immediately after it is concluded (Section 99, Argentine Securities Law (ASL) (Law No. 26831) and Sections 2 and 3, Chapter I, Title XII, CNV Rules).

The CNV must consider the application within 15 business days of filing. This period can be extended if the CNV requires additional information. The authorisation is automatically granted if the CNV does not raise objections or ask for further information during this period.

The public offer must be open for not less than 20 and not more than 30 days from the date of the CNV's authorisation. Shareholders benefit from an additional term of at least five days and up to 10 days from the general closing date of the public offer, even where they have accepted the offer within the general term for acceptance. The same conditions will apply as during the original period.

Tender offers are also mandatory in some cases. Under the ASL and the CNV Rules, anyone seeking to obtain direct or indirect control of a public company by acquiring a 'significant interest' in the voting shares, pre-emptive rights, options, convertible notes or any similar securities that can give the right to own or buy, or can be turned into, shares, must file a public offering or a securities exchange addressed to the holders of these securities.

For indirect mergers or acquisitions (that is, a merger by incorporation or acquisition of a company which holds the shares of the target), if the company incorporated or acquired is a holding company or its principal assets are the shares of the target, the tender offer must be made in the same way as a direct acquisition of shares of the target. Otherwise, the mandatory tender offer is triggered only if the indirect merger or acquisition involves the acquisition of 51 per cent or more of the target company's shares, and is subject to specific provisions (Section 19, Chapter II, Title III, CNV Rules).

VII OUTLOOK

There are several drafts of bills that could affect leverage M&A activity, though we should note that, with mid-term elections happening this year, activity in Congress will be affected by political campaigns.

Among the various laws being discussed, we can mention the following:

a Capital markets reform. On 16 November 2016, the executive power presented a bill to Congress, proposing amendments to Capital Markets Law No. 26,831, Mutual Investment Funds Law No. 24,083 and Tax Relief for the Purchase of Private Securities Law No. 20,643, among others (the 'Bill'). The Bill states that its objective is to 'develop the national capital markets, looking to increase the number of investors and corporations that go to the markets for financing, particularly benefiting small businesses and to encourage the integration and federalisation of the different markets in the country'. The various proposals include amendments with respect to companies in the public offer regime of shares and the public offer regime of acquisitions:

- removal of first refusal and accretion rights in companies that make public offerings of their capital stock to facilitate the process of issuance of shares;
- prioritisation of existing shareholders in case of a capital increase for the allocation of new shares, provided that they comply with the placement procedure; and
- changes to criteria regarding, among other issues, the determination of the price and the moment to launch a public offer of acquisition that involves a change of control.

b The proposal for amending the Argentine Competition Act has two main changes that will affect M&A deals: the inclusion of *ex ante* merger control[5] and an increase in thresholds that trigger merger control.[6]

c Criminal liability of corporations, as described above.

5 Starting one year after the new Competition Agency starts functioning.

6 Local turnover of 150 million units and local price or value of 20 million units (inclusion of seller in calculation, which previously was restricted to purchasing group plus target).