



## Case & Project Experience

### International Arbitration Cases: Argentine Political Risk Insurance Litigation

#### Background

During the 1990s, Argentina privatized most of its state-owned infrastructure businesses in a broad movement that attracted the attention of investors worldwide. These privatizations, which attracted more than \$22 billion to the Argentine economy during the 1990s and early 2000s, were funded largely by debt from major international lenders. A key element in attracting such funds into an economy with a known history of some of the world's worst sustained currency instability were concession contracts that used the US dollar as the basis for all future regulated charges. Additionally, major international insurance underwriters offered coverage to the lenders for "political risk"—meaning expropriatory acts of the Government of Argentina that would impair repayments of principal and interest.

During that decade-plus of privatization, the utilities performed well, improving service reliability to consumers and expanding their coverage. But circumstances changed in January 2002, when the Government of Argentina passed Economic Emergency Law No. 25,561, which unilaterally removed the US dollar clause in concession contracts, devaluing the Argentine peso and instituting a peso-based tariff freeze. As a result, regulated charges were immediately and effectively reduced by two-thirds in US dollar terms. Most privatized utilities quickly defaulted on their debt payments as a direct consequence.

NERA provided evidence for consortiums of major international lenders in three prominent cases—two involving electric utilities and one involving Argentina's largest privatized toll-road concession. Two of the proceedings were before the London Court of International Arbitration (LCIA), while the third was before an ad-hoc arbiter. In all three cases, underwriters had claimed that the general business environment (a non-covered risk) had caused the defaults, not loss of the US dollar clause, as such.

NERA presented evidence showing that the defaults were a direct and inevitable result of politically-driven changes to concession contracts. The two electricity cases settled favorably for our clients. The decision in the toll-road case awarded the maximum payment to lenders (our clients).

#### Our Expert

##### Jeff D. Makholm, Senior Vice President

Dr. Makholm has directed an extensive number of projects in the utility and transportation businesses in 25 countries. These projects have involved work for more than 100 investor-owned and regulated businesses, as well as for governments, industry regulators, and the World Bank. He was directly involved in utility and transport infrastructure privatizations in Europe, South America, and Asia Pacific. He has provided expert evidence on more than 150 occasions before international arbitral panels, regulators, and courts in a number of countries.

## **NERA's Role**

### **Regulatory and Economic Advice to Counsel**

NERA supported the claimants' counsel, an international law firm, by providing advice based on expertise in regulatory and economic matters in the energy and transportation industries, as well as comprehensive, first hand knowledge of the privatization process implemented in Argentina in the 1990s—particularly with respect to the objectives of the reform and the effects of the Economic Emergency Law on regulated utilities.

### **Evaluation of Past Performance of the Three Utilities**

NERA analyzed the financial and operating performance of the regulated businesses. NERA also analyzed the opinion of independent credit rating agencies regarding the ability of these companies to repay their debt prior to the enactment of the Emergency Law, showing that the three utilities had acted with financial prudence and had achieved good performance prior to the de-dollarization/price freeze.

### **Financial Modeling, Scenario Analyses**

In each of the three cases, NERA developed a thorough financial model to examine the borrowers' capacities to repay their debt with and without the expropriatory elements of the Emergency Law. In each case, NERA determined that the borrowers would have been able to meet their debt payments if the Government of Argentina had not unilaterally altered concession contracts.

### **Company Valuations and Damages Estimations**

NERA valued the utilities under a range of different scenarios and estimated damages.

## **Outcome**

In the first case of its type to reach a decision, arbiters found in favor of NERA's client and awarded the maximum amount provided in the arbitration agreement. In the other two cases at the LCIA, NERA's clients settled favorably with insurers, employing NERA's work as a key piece of evidence to support their negotiations.

## **About NERA**

NERA Economic Consulting ([www.nera.com](http://www.nera.com)) is a global firm of experts dedicated to applying economic, finance, and quantitative principles to complex business and legal challenges. For over half a century, NERA's economists have been creating strategies, studies, reports, expert testimony, and policy recommendations for government authorities and the world's leading law firms and corporations. We bring academic rigor, objectivity, and real world industry experience to bear on issues arising from competition, regulation, public policy, strategy, finance, and litigation.

NERA's clients value our ability to apply and communicate state-of-the-art approaches clearly and convincingly, our commitment to deliver unbiased findings, and our reputation for quality and independence. Our clients rely on the integrity and skills of our unparalleled team of economists and other experts backed by the resources and reliability of one of the world's largest economic consultancies. With its main office in New York City, NERA serves clients from more than 25 offices across North America, Europe, and Asia Pacific.

## **Contact**

### **Dr. Jeff D. Makhholm**

Senior Vice President

+ 1 617 927 4540

[jeff.makhholm@nera.com](mailto:jeff.makhholm@nera.com)