

Mexico: Regulation of DIP Financing

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The Commercial Insolvency Law (*Ley de Concursos Mercantiles*) (LCM), which became effective on May 13, 2000, incorporated provisions allowing access to financing during the debtor's restructuring.² The Law on Bankruptcy and Suspension of Payments (*Ley de Quiebras y Suspensión de Pagos*), which was in effect during 1943-2000, did not contemplate this.



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A mediator (*conciliador*) must decide whether or not to terminate executory contracts and shall approve, with the prior opinion of the intervenor (*interventor*), the execution of new credit agreements.³ The mediator is appointed by the Federal Institute of Insolvency Specialists (*Instituto Federal de Especialistas de Concursos Mercantiles*) (IFECOM) upon commencement of the reorganization (*conciliación*) proceedings.⁴ The mediator must be appointed by IFECOM randomly from its list of registered estate fiduciaries, known as "insolvency specialists" in Mexico. However, the debtor and a group of creditors representing at least 50 percent of the value of the credits may agree on the appointment of a specific mediator from the list of IFECOM-registered specialists,⁵ or an independent mediator if the group of creditors represents at least 75 percent of the value of the credits.⁶ The mediator is mainly responsible for procuring an agreement between the creditors and the debtor.⁷ The intervenor represents the creditors' interests⁸

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and may be appointed by any class of creditors representing at least 10 percent of the value of the credits.⁹

Priority of Post-petition and Pre-petition Claims

DIP financing agreements are considered to be claims against the insolvency estate (*masa*).¹⁰ Certain labor claims for wages and other benefits have superpriority, and thus must be paid before any of the debtor's creditors.¹¹ The reorganization agreement¹² must include the payment terms for claims against the insolvency estate, including post-petition claims based on DIP financing agreements.¹³

Pre-petition claims will rank according to their category. The LCM,¹⁴ the Federal Labor Law (*Ley Federal del Trabajo*) (LFT)¹⁵ and the Fiscal Code of the Federation (*Código Fiscal de la Federación*) (CFF)¹⁶ establish five categories of creditor rankings. Other statutes also include their own set of rankings and priorities,¹⁷ although the provisions of the LCM, which is the statute

commenced after his death.¹⁹

Second, "secured creditors" (*acreedores con garantía real*) include creditors under mortgage (*hipoteca*), pledge (*prenda*) and purchase finance agreements (*créditos de habilitación o avío y créditos refaccionarios*) that can recover their debt from the proceeds of the secured property sale.²⁰ If there is more than one security interest in a property, creditors recover their debts according to the date on which their respective security was recorded.²¹ In practice, any excess amount of the sale proceeds shall become part of the debtor's assets and be made available for the unsecured creditors; if the sale proceeds are insufficient to satisfy a creditor's secured claim, the mortgagee or pledgee will be treated as an unsecured creditor for the deficiency.

Third, there is the federal tax authority (*fisco federal*). The Ministry of Finance and Public Credit (*Secretaría de Hacienda y Crédito Público*) via the Tax Administration Service (*Servicio de Administración Tributaria*) (SAT) acts as the creditor for so-called "social claims," namely, unpaid federal taxes.²² Certain labor claims rank *pari passu* with tax claims.²³

Fourth, "creditors with special privilege" (*acreedores con privilegio especial*) comprise all those creditors that, under the Commercial Code (*Código de Comercio*) (CoCom) or related statutes, have a special privilege or right of retention.²⁴ This category of creditors includes commission agents,²⁵ merchandise

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that applies to insolvency proceedings (whether reorganization or bankruptcy), prevail in case of a discrepancy.¹⁸ Under the LCM, the general rankings of claims are listed in descending order of preference.

First, "exclusively privileged creditors" (*acreedores singularmente privilegiados*) include, in connection with individuals, creditors for burial expenses of the debtor as well as expenses related to the disease that caused the death of the debtor where the insolvency proceedings have

vendors²⁶ and carriers.²⁷

Fifth are "common creditors" (*acreedores comunes*).²⁸ All other creditors holding claims not falling within the above categories are treated as nonpriority general unsecured creditors.²⁹

Creditor ranking (*graduación*) and creditor priority (*grados*) within each ranking (*prelación*), as provided by the law,

¹ This article was prepared following a presentation made during the International Insolvency Institute's Eighth Annual International Insolvency Conference held in Berlin, Germany during June 9-10, 2008. This article is not intended to be comprehensive or to provide specific legal advice. It only enunciates the main issues arising in connection with the subject matter hereof.

² See articles 75 and 224-II of the LCM. It is noteworthy that the LCM refers to the debtor as a "Merchant" (*Comerciante*).

³ *Id.*

⁴ *Id.* article 43-IV. The LCM created the IFECOM, an auxiliary agency of the Federal Judiciary Council (*Consejo de la Judicatura Federal*) with technical and operative autonomy. Its main role is to appoint, train and supervise the estate fiduciaries, such as examiners (*visitadores*), trustees (*síndicos*) and mediators, determine their compensation and evaluate their performance. See *id.*, article 311. See also Tesis Aislada. Registro No. 176,005. Novena Época. Tribunales Colegiados de Circuito. Semanario Judicial de la Federación y su Gaceta, Tomo XXIII, Febrero de 2006. pág. 1787. Tesis: I.3o.C.541 C. Materia: Civil, whereby the Circuit Court confirmed the managerial scope of IFECOM's activities as well as IFECOM's nature as an "auxiliary body of the court."

⁵ *Id.* article 147-I.

⁶ *Id.* article 147-II.

⁷ *Id.* article 148.

⁸ *Id.* article 62.

⁹ *Id.* article 63.

¹⁰ *Id.* article 224-II.

¹¹ See *id.* articles 224 and 225.

¹² *Id.* Title Fifth, Sole Chapter.

¹³ *Id.* article 153.

¹⁴ See *id.*, articles 217-222.

¹⁵ See articles 113-114 of the LFT.

¹⁶ See article 149 of the CFF.

¹⁷ See, e.g., article 288 of the Social Security Law (*Ley del Seguro Social*).

¹⁸ See Tesis Aislada. 227,087. Octava Época. Instancia: Tribunales Colegiados de Circuito. Fuente: Semanario Judicial de la Federación. IV, Julio a Diciembre de 1989. pág. 315. Materia(s): Penal. See also Tesis Aislada. 918,803. Séptima Época. Instancia: Tercera Sala. Fuente: Apéndice 2000. VII. pág. 262. Materia(s): Civil.

¹⁹ Article 218 of the LCM.

²⁰ *Id.* article 219; see also article 328 of the General Law of Negotiable Instruments and Credit Transactions (*Ley General de Títulos y Operaciones de Crédito*).

²¹ Article 219 of the LCM.

²² *Id.* article 221; see also articles 2, 4 and 149 of the CFF. It is noteworthy that amounts withheld, transferred or collected by the debtor for taxes can be separated from the estate under article 71-VI of the LCM. Also, under article 146-B of the CFF, a debtor may request from SAT a partial reduction of the amount of its social claims.

²³ Article 221 of the LCM.

²⁴ *Id.* article 220.

²⁵ See article 306 of the CoCom.

²⁶ See *id.* article 386.

²⁷ See articles 2662 of the Federal Civil Code (*Código Civil Federal*) and the Civil Code for the Federal District (*Código Civil para el Distrito Federal*), respectively.

²⁸ Article 222 of the LCM.

²⁹ *Id.*

determine payment order. Generally, creditors of the first through fourth priority categories have the highest probability of being paid in full. When assets are insufficient, first-priority creditors are paid in full before second-priority creditors and so forth. Fifth priority creditors are paid a *pro rata* reduced amount.³⁰ The fees of the insolvency examiner, mediator, trustee (*síndico*) and other specialists involved in the administration and preservation of the estate are payable as ordinary operating expenses.³¹

Liability of Estate Fiduciaries

There are no statutory provisions to shield insolvency specialists from liability in the event a new financing cannot be repaid, or if repayment affects the debtor's ability to pay the other creditors. However, the insolvency examiner, the mediator and the trustee shall be responsible vis-à-vis the debtor and the creditors for any losses or damages (unduly) caused by their actions (as well as those of their assistants').³² They shall also be responsible for any "breach of their duties" and for any "disclosure of confidential data that they may have obtained by virtue of their position."³³ In addition, the trustee, in managing the bankrupt company, must act "always as a diligent administrator" as if it were "his/her own enterprise," he/she being responsible for any losses or damages that the bankrupt company may suffer due to his/her "fault or negligence."³⁴

It is noteworthy that the LCM includes an entire section on the "Criminal Aspects of Commercial Insolvencies," namely Title Eleventh, Sole Chapter. This Title regulates insolvency-related crimes in seven articles.³⁵ Most of these provisions concern general

principles applicable to such crimes. They also contemplate sanctions for specific criminal behavior of debtors.

The foregoing notwithstanding, however, nothing precludes the application of criminal statutes such as the Federal Criminal Code (*Código Penal Federal*) to the estate fiduciaries where their actions so justify it.³⁶ Estate fiduciaries may be removed with or without cause.

The debtor, the District Attorney (*Ministerio Público*), any of the intervenors and any of the creditors may notify the district (bankruptcy) judge of illegal actions or omissions of the insolvency examiner, the mediator or the trustee.³⁷ The judge shall have broad authority to act upon such notification³⁸ and he/she may order IFECOM to replace the insolvency examiner, the mediator or the trustee "in order to prevent losses for the estate."³⁹

Thus, the LCM contemplates that failure to comply with certain specific duties may give rise to the judge issuing an order for IFECOM to remove an estate fiduciary.⁴⁰ The LCM also allows for a mediator to be replaced "without cause," *i.e.*, by agreement between the debtor and creditors representing a specified minimum percentage (75 percent) of the credits.⁴¹ Where creditors representing such credits and the debtor shall so agree, they shall be authorized to petition the court to appoint an outside mediator, namely one that is not IFECOM-registered.⁴² ■

³⁶ *Id.* article 329.

³⁷ *Id.* article 60.

³⁸ *See, e.g., id.* articles 269, 270.

³⁹ *Id.* article 60. In addition, IFECOM may cancel a specialist's registration in certain cases. *See id.* article 337.

⁴⁰ *Id.* article 60; *see also, e.g., id.* article 130. In the case of "special insolvencies," which are regulated by Title Eighth of the LCM, ad hoc rules apply. For example, in the case of public service companies operating under a concession (*concesión*), the concessioning agency (*concedente*) is authorized to petition the judge to appoint or remove the insolvency specialists. *Id.* articles 239-241. In the event of a commercial bank's bankruptcy, the Institute for the Protection of Bank Savings (*Instituto para la Protección del Ahorro Bancario*) is authorized to make such petition. *Id.* articles 249, 250. And in the event of an auxiliary credit institutions (*instituciones auxiliares de crédito*)'s insolvency, the National Banking and Securities Commission (*Comisión Nacional Bancaria y de Valores*) is authorized to make such petition. *Id.* article 259.

⁴¹ *See id.* article 147-I; *see also id.* article 174-I, which applies to trustees.

⁴² *See id.* article 147-II; *see also id.* article 174-II, which applies to trustees.

³⁰ *Id.*

³¹ *Id.* articles 333 and 75. Prior to the Dec. 27, 2007, amendments to the LCM that became effective the following day, said fees were treated as credits against the estate. The LCM seems to create a gray area concerning "normal expenses" relating to the "replacement, conservation and administration" of the estate's assets, which are treated as credits against the estate under article 224-III. Compare with the text of article 75, which refers to ordinary operations "including expenses that are essential" therefor.

³² *Id.* article 61.

³³ *Id.*

³⁴ *Id.* article 189.

³⁵ *See id.* articles 271-277.