Restructuring: Mexico

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Creel García-Cuéllar Aiza y Enriquez SC
By Thomas S Heather and Christian Dorantes

Introduction

Mexico is a jurisdiction that has seen a substantial number of major successful restructuring cases involving cross-border considerations in the past decades. Indeed, professionals engaged in restructuring and insolvency activities have achieved a high degree of sophistication and understanding of common issues arising in complex cross-border restructuring exercises and proceedings, including, notably, the need for greater efficiency in the process for in-court reorganisations. Although at less than optimum pace, the Mexican legal framework that is in place that supports the structuring of more effective insolvency proceedings has continued to evolve. This article focuses on describing the existing framework and identifying the principal issues and challenges that impact insolvency practice in Mexico today.

Year in review

Overview of restructuring and insolvency activity

Mexican restructuring cases regarding corporations with assets or liabilities, or a combination thereof, in significant amounts have continued to be successfully completed through consensual out-of-court negotiations. Mexican restructuring practice has undoubtedly created through decades, dating back to the early 1980s, a certain level of sophistication among bankers, investors, corporate officers and restructuring professionals, resulting in effective consensual restructurings, as a better alternative to any judicial proceeding. Indeed, Mexico continues to have a successful, proven track record in reaching acceptable and consented results, constructed even in the most complex of cases requiring a financial restructuring of a corporate entity.

Nevertheless, in recent years, since the creation of federal district courts specialised in insolvency proceedings known as *concurso mercantil* filings (as described below), a growing number of Mexican corporations have turned to the courts by filing *concurso mercantil*. Creditors have also turned to recovery through involuntary *concurso* filings. This has become an alternative, for example, where the company is an issuer of debt instruments through the Mexican securities market or the international markets (principally in the United States, further to Rule 144A or Regulation S facilities), or a combination of both.

Global economic and geopolitical factors such as continued high interest rates in the aftermath of the covid-19 pandemic, a slow (albeit steady) global economic recovery, supply chain disruptions, political and economic uncertainties affecting international trade and commerce, such as the growing Middle East conflict and the war in Ukraine, and a considerable surge in inflation leading to tight monetary policies,[1] coupled with local factors, have led a number of corporations to financial distress. Gaining the support of the majority of creditors, let alone unanimous consent, in cases involving debt issued in local or international financial markets, often proves to be a task of daunting proportions. Consequently, to preserve companies in such situations as ongoing concerns (which is one of the main purposes of the Concurso Law, the Mexican insolvency statute), and to address deteriorating financial conditions that could further jeopardise their viability, Mexico has experienced a growing number of *concurso mercantil* filings compared with prior years. However, the number of *concurso* filings remains modest. The annual average of *concurso mercantil* filings since the enactment of the Concurso Law in 2000 has not exceeded 40 procedures in total.

Concurso mercantil proceedings are often unreliable and unpredictable in their results, albeit with more recent notable and positive exceptions, which have increased in number. The Law of Commercial Insolvency enacted in May 2000 (as amended, referred to herein as the Concurso Law) was a welcome improvement from the

previous bankruptcy statute of 1943.

The process for acceptance of filings has often been a time-consuming exercise, although, since the recent creation of two specialised federal district courts with exclusive nationwide jurisdiction over all *concurso mercantil* filings, the acceptance process has improved. In many instances, however, stalling amid gargantuan formalities and creative delaying tactics in an unorthodox litigious environment, not to mention perplexing judicial interpretations and contradictions prior to the creation of these two courts (e.g., those based on perplexing expansions of the concept of violations of due process and human rights), have continued to be causes of considerable concern. Generally, those cases that have come to a successful conclusion have been voluntary filings made under a prearranged plan (*concurso mercantil con plan de reestructura previo*), pursuant to which the company and a majority of its creditors jointly agree to seek a court-protected reorganisation under pre-negotiated conditions.

While still an exception, a limited number of Mexican corporations have had to consider turning to the US bankruptcy courts for relief through Chapter 11 proceedings as an alternative to protect their viability. An added feature to this alternative is clearer access to debtor-in-possession (DIP) financing, which continues to be limited in Mexico. Although Chapter 11 may not be generally available as a viable instrument to reorganise a Mexican corporation, formal requirements are easier to address, and the outcomes are more foreseeable and transparent than those for a *concurso mercantil*. However, costs (legal and financial advisory fees) tend to be significant, labour must be kept current, and the company must be in tax compliance with its Mexican fiscal obligations (mainly with its withholding tax obligations, such as VAT remittances, payroll taxes and social security payments). Most filings made under Chapter 11 by Mexican companies have been efficiently concluded in a matter of months when a pre-pack plan has been included. On the other hand, involuntary filings attempted by creditors of Mexican companies through Chapter 11 have been unsuccessful to date.

Greater adherence to the time frames established in the Concurso Law and improving certainty in filings being accepted have become more of a general rule rather than an exception. Indeed, the new appointees to preside over the two federal courts have taken a marked approach to developing greater reliability that the provisions of the Concurso Law will be applied more consistently.

Nevertheless, substantial concerns remain, such as the continued use of *ex parte* proceedings filed through the local court system leading to excessive injunctive relief, which has caused considerable obstacles in situations of financial stress, sometimes delaying and impeding access to *concurso mercantil* as a viable tool to implement a comprehensive restructuring.

Furthermore, in a recent case admitted in a local tribunal, filed by an individual holding a minuscule percentage of stock of a major non-bank public company, alleging that further to four provisions of a corporate law statute dating back to 1934 the company had lost more than two-thirds of its equity and thus was under a cause of dissolution and its liquidation, a liquidator was originally appointed for the liquidation of its assets and to selectively apply the proceeds to the payment of debt. However, at the end of the day, the attempt to use the 1934 Law of Mercantile Corporations ended up in a prearranged plan (*concurso mercantil con plan de reestructura previo*), despite the disappointing initial ruling.[2] However, this 'creative alternative' is expected to be further resorted to as a procedural tactic, unfortunately resulting in an additional disruptive tool in insolvency practice.

Recent legal developments

In the recent past, no material amendments have been adopted. Nevertheless, it is relevant to point out that key material amendments to the Concurso Law were enacted by Congress in 2014. The principal objectives of the reform focused on the goals of a more expedient and efficient procedure, greater transparency and a reasoned intent to formally introduce DIP financing.

The most relevant provisions introduced by Congress included the following:

a. prohibiting the judge from extending the periods set forth in the Concurso Law;
b. the procedural consolidation of *concurso mercantil* proceedings of companies that are part of the same corporate group, the concept of which now includes companies that have the capability to make decisions in respect of another company, regardless of the actual shareholdings (substantive consolidation is not allowed);
c. the ability of a debtor to request the *concurso mercantil* status prior to being generally in default in respect of its payment obligations when such a situation is expected to occur inevitably within the following 90 days;
d. the possibility of requesting a *concurso mercantil* directly in the stage of bankruptcy (liquidation);
e. permitting common representatives to file credit recognition claims on behalf of a group of creditors and the addition of certain rules for the subscription of the debt restructuring agreement in the case of collective credits through their individualisation;
f. allowing for the use of standardised forms to voluntary request or involuntary demand *concurso mercantil*;
g. the prospect of filing petitions and other communications electronically;
h. an emphasis on transparency;
i. provisions permitting debtors to obtain DIP financing as necessary to maintain the ongoing business of the company and the essential liquidity during the *concurso*, the financing of which will be considered privileged in ranking (with a preference over all secured creditors) for purposes of the preference of the payment thereof in the event of a liquidation;

j. the recognition of subordinated creditors, including intercompany creditors in accordance with certain rules, which, among others, establish that such intercompany creditors will not be allowed to vote for the approval of the debt restructuring agreement when such intercompany creditors represent 25 per cent or more of the total amount of recognised credits, unless such creditors consent to the agreement adopted by the rest of the recognised creditors of the same class; and
k. the broadening of the retroactivity period applicable for the review of fraudulent conveyances in respect of transactions entered with intercompany or related creditors (to twice the statutory periods).

Liabilities of management and the board of directors

To avoid abuse in respect of an insolvent debtor, the amendments to the Concurso Law also included a set of provisions that refer to the potential liability of the debtor's management and relevant employees for damage caused to the debtor company if they are:

a. acting with a conflict of interest;
b. favouring one or more shareholders and causing damage to other shareholders;
c. obtaining economic benefits for themselves or for others;
d. knowingly making, providing, disseminating, publishing or ordering false information;
e. ordering or causing the accounting registries, related documentation or conditions in a contract to be altered, modified or destroyed;
f. failing to register transactions or causing false information to be registered, causing non-existent transactions or expenses to be registered, exaggerating real transactions or expenses, or otherwise carrying out any act or transaction that is illegal or prohibited by law, causing damage to the bankrupt debtor and obtaining an economic benefit, directly or indirectly; and
g. carrying out any wilful or illegal act or acting with bad faith pursuant to the Concurso Law or other laws.

Although the Concurso Law adopted the business judgement rule contained in the Securities Law applicable to the members of the board of publicly traded companies and allows such directors and relevant employees to obtain insurance, a guarantee or bonds to cover the amount of the indemnification for losses and damages caused, except for wilful misconduct or acts of bad faith, the Concurso Law expressly prohibits any agreement or provisions in the by-laws in respect of any type of consideration, benefit or exemption that may limit, release, substitute or redeem the liabilities of such members of the board and relevant employees of a bankrupt debtor in the event of wilful misconduct or bad faith.

As part of the 2014 amendments, a bank resolution regime was created and regulated in the Law of Credit Institutions. Such a regime is characterised by its celerity, pre-intervention corrective measures by the Institute for Banking Savings Protection and effectiveness in reaching an orderly liquidation if required, among other relevant features.

Finally, in August 2019, amendments were passed to clarify that corporations owned by the Mexican government may be eligible to file under the Concurso Law. In this respect, it is emphasised, however, that neither Petróleos Mexicanos (PEMEX) nor the Federal Electricity Commission (CFE) is a corporation. Both are productive state-owned enterprises, governed by their own comprehensive legal regimes, and they carry out specific constitutional mandates relating to oil and gas and electricity for the Mexican state. As a matter of Mexican law, neither may be declared bankrupt or insolvent or be subject to a *concurso*. Specific legislation enacted by the Mexican Congress would be required to judicially restructure or liquidate PEMEX or CFE.

Legal framework

The Concurso Law was published in May 2000 and amended in December 2007, with the introduction of the Mexican version of a pre-pack in January 2014 and, to a lesser extent, in August 2019 and in January 2020. Significant amendments are summarised in 'Recent legal developments'.

The following subsections present the principal aspects of the Concurso Law.

One proceeding

The Concurso Law provides for one sole insolvency proceeding (*concurso mercantil*), encompassing two successive phases: a conciliatory phase of mediation among creditors and debtor (known as the conciliation stage) and a second stage of bankruptcy or liquidation. There is, in fact, a complex preliminary stage: the preparation of the many formal documents to be attached to any petition and the filing thereof, with the objective of getting the case admitted, commencing the first conciliatory stage. In substantive filings, such a preliminary stage has proven to be challenging and has taken, on average, not weeks but months, adding to the uncertainties surrounding *concurso*.

The objective of the conciliatory phase is to conserve the business enterprise as an ongoing concern through a restructuring agreement. On the other hand, the stated purpose of bankruptcy is to liquidate the business. Prior to a debtor being placed in *concurso*, the process includes a preliminary examination proceeding to verify whether the debtor is generally in default. If a pre-pack is filed, such an examination is not required. Unfortunately, although the mandatory formats produced by the Federal Institute of Insolvency Specialist (IFECOM) (an agency of the federal judiciary) are quite simple in their structure, the examination proceeding seems to be misunderstood as being an audit of the company, leading to delays. The initial preliminary proceeding lacks transparency and the examination proceeding reports are not made public.

Procedural terms

An important part of the Concurso Law involves measures that were designed to expedite the handling of mechanical aspects of insolvency. Procedural terms in legal proceedings are relatively short, yet, with few exceptions, most courts fail to abide by them.

Provisions in the law as to procedural exceptions in legal proceedings were designed to avoid the automatic suspension of the conciliatory proceeding, as was the case under the prior 1943 Law, yet federal judges continue to apply measures that have, in fact, halted *concurso* proceedings.

The conciliatory stage is designed to be completed in 185 calendar days in the best of cases, although two 90-day extensions may be granted if a qualified majority of creditors so approves. The Concurso Law clearly underlines that in no event may the conciliatory stage be extended beyond 365 days, whereupon bankruptcy and liquidation of assets are, in theory, to begin immediately. In practice, this is not the case. In addition, the potential enforcement of the 365-day period in complex proceedings – with the threat of immediate liquidation – may lead to unwarranted results.

Petition for commercial insolvency

A business enterprise that is generally in default in respect of its payment obligations will be declared commercially insolvent. The debtor, any creditor or, exceptionally, the Office of the Attorney General or the tax authorities may file for insolvency.

The Concurso Law establishes precise rules that determine when a debtor is 'generally in default'. The principal indications or presumptions are the failure by a debtor to comply with its payment obligations in respect of two or more creditors and the existence of the following two conditions: 35 per cent or more of its liabilities outstanding are 30 days past due and the debtor fails to have liquid assets and receivables, which are specifically defined, to support at least 80 per cent of its obligations that are due and payable.

Specific instances, such as insufficiency of assets available for attachment or a payment default in respect of two or more creditors, are considered by the Concurso Law to be facts that by themselves will result in a presumption of insolvency.

In theory, the 2014 amendments allow the debtor to file for *concurso* if it can be anticipated that it will generally be in default in respect of its payment obligations or is falling within either of the conditions leading to a presumption of insolvency, as mentioned above, within 90 days of the petition filing. The 'generally in

default requirement', strictly applied by the courts, even with the amendment, is a major pitfall of *concurso* as a tool for financial reorganisation; courts will admit only cases in which the debtor is faced with imminent disaster or its finances are beyond repair.

As to involuntary filings, they have been largely unsuccessful because of the many formalities that must be met. Delaying tactics are commonly resorted to, laying obstacles that result in considerable interruptions to the proceedings.

Jurisdiction

The federal courts have jurisdiction over *concursos*, notwithstanding that even this basic principle has been – unsuccessfully – challenged. As of March 2022, there are two specialised federal courts with exclusive jurisdiction on *concurso mercantil*. Although it is a fact that district judges are overburdened with constitutional challenges (*amparos*) and have little practice regarding mercantile matters, the selection process, supervision, continued education (other than in insolvency) and preparation of federal judges have been substantially improved in the recent past. Although salaries were materially increased and there has been greater impartiality, the current administration has slashed health- and insurance-related benefits and cut other allowable expenses. Recently, courts have been reluctant to accept insolvency cases, given their considerable workload, exacerbated by budget cuts, temporary closures as a result of the covid-19 pandemic and, in the few major *concurso* cases filed and accepted, the sheer size of them, which have made it a huge task to address and preside over these proceedings efficiently. The very recent creation of two specialised federal bankruptcy courts could lead to an improvement.

Experts

The Concurso Law provides for the use and training of experts in the field of insolvency, with IFECOM as an entity to coordinate their efforts and provide continuing education.

The specialists who have a role in proceedings under the Concurso Law are the examiner, whose duties are to determine whether the debtor complies with the commencement standards and who participates in the proceeding up to the judge's declaration of insolvency;[3] the conciliator, who is appointed in such a declaration and who has broad powers to mediate, to take steps to protect the enterprise as an ongoing concern or to immediately begin bankruptcy, and who takes on significant responsibilities and in material cases a major role in a *concurso*; and the receiver, who may or may not be the conciliator and whose principal function is to proceed with the sale of assets and payment of claims.

The judge also has a principal role, although the function of the conciliator is considerable (including the authority to approve DIP financings).

Those who wish to act as examiner, conciliator or receiver must request IFECOM to register them in its special registry. It is unfortunate that the registry, especially for complex cases, is not available for the large accounting or insolvency advisory firms but only to a limited number of individuals.

There are numerous restrictions prohibiting conflict-of-interest relationships. The appointment procedure is supposedly based on a random, electronic selection from the classes and ranges of experience pertaining to the experts registered with IFECOM, which vary in accordance with the complexity and asset size of the business enterprise.

A qualified majority of creditors may replace or appoint a professional as conciliator or receiver even if the professional is not registered with IFECOM. In cases involving the insolvency of a company operating under a federal concession, the conciliator may be appointed at the request of the corresponding authority, such as the Ministry of Communications regarding corporations in the telecommunications industry. In prearranged filings, the debtor and a majority of creditors supporting the pre-pack plan may appoint a conciliator who is not registered with IFECOM. In both exceptions, the conciliator may be a firm or corporate entity.

Related companies

Insolvency proceedings of two or more related entities are not joined, although controlling and controlled companies' proceedings will be joined but will be handled in separate records. A petition must be filed individually by each group member. The 2014 amendments introduced provisions to allow for a joint petition by multiple group members. This technique was applied efficiently in the *Empresas ICA* case.[4] Mexican courts do not, however, recognise substantive consolidation.

Identification of creditors and declaration of insolvency

A debtor that requests a judgment of declaration of *concurso mercantil* must furnish detailed lists of creditors and debtors, with a description of the nature of the debts. The amendments of 2014 introduced several relevant additions to the petition request, including a copy of the corporate resolutions that approved the filing (requiring 'undoubtable shareholder approval'), a proposed reorganisation plan and an enterprise conservation plan, which were intended to include DIP financing terms, to the extent available.

Absent a pre-pack, the day after the judge admits the petition, which, in practice, might take weeks or months, they must send a copy to IFECOM, ordering it to designate an examiner within five days. The judge will order the visit and immediately notify the debtor. The examiner will review the books and records of the debtor and will prepare minutes of the visit, which must also include a list of all creditors in IFECOM formats. The examiner may request that the judge issue precautionary measures needed to preserve the assets of the debtor, although the debtor's counsel usually addresses them upon filing. The examiner will render a report to the judge that will be sent to the debtor and the creditors for their respective comments, if any.

Within a maximum term of 83 days of the termination of the examination proceeding, the Concurso Law provides that the judge must render a judgment of mercantile insolvency, which, among other things, must contain:

a. an order to IFECOM to appoint a conciliator;
b. a declaration of the opening of the conciliatory stage unless the debtor has requested bankruptcy;
c. an order to the debtor to deliver all books and records to the conciliator, although management remains in place;
d. an order to the debtor to suspend the payment of its pre-petition indebtedness, other than those that are deemed to be essential for the continuation of the business enterprise;
e. an order to freeze all asset foreclosure and attachment proceedings; and
f. an order to publish a notice to all creditors so that they may appear in the proceeding, although this requirement (a filing proof of claim) is no longer mandatory.

The extensive participation of the conciliator in the proceedings should also be noted. The conciliator is also responsible for proposing the creditors who should be recognised and is mandated to proceed with notices and publications pursuant to provisions that are very specific as to terms. Formalities are always a major issue, and creditors must be aware of tactics to delay the publications, which might lead to material postponements and ambiguities.

Effects of a declaration of insolvency

Once the initial judgment declares the debtor in a stage of insolvency or *concurso mercantil*, attachment or foreclosure of assets is suspended during the conciliatory stage, with the sole exception of labour-related obligations. Tax-related attachments or liquidations under specific provisions of the Concurso Law are specifically stayed.

The debtor maintains the administration during the conciliatory stage, although the conciliator may request the court removal of the administration, which is uncommon. With the express purpose of conserving the enterprise as a going concern within the conciliatory stage, the conciliator is given broad powers to decide on the

acceptance or rejection of contracts (within certain parameters), the contracting of new loans – although most litigators insist that the judge must approve – and the sale of non-essential assets. In all cases, the conciliator must report to the court every 72 hours – which, obviously, is burdensome in major filings – every payment to any supplier or person.

Debts in foreign currency

The Concurso Law attempts to correct prior judicial practice, which converted foreign currency debt to Mexican pesos early in the proceeding. The Concurso Law establishes provisions that are designed to protect the monetary value of creditor loans. All peso-denominated obligations are converted into inflation-linked units known as UDIs; foreign currency-denominated obligations are converted into pesos at the prevailing rate of exchange on the date the insolvency judgment is rendered and then converted into UDIs. Only claims with a perfected security interest (mortgages or pledges – but not in respect of guarantee trusts) will be maintained in their original currency or unit of account and will continue to accrue interest, but only to the extent of the value of the collateral.

Fraudulent conveyances; clawback periods

The Concurso Law provides for a general rule as to the period when insolvency is presumed to have begun, which is 270 calendar days prior to the judgment declaring insolvency (the 'retroactive period'). Nevertheless, upon the reasoned request of the conciliator, the controllers, who may be appointed by the creditors to oversee the process, or any creditor, the judge may determine a longer period (at most three years). Conveyances that are not arm's length or commercially sound and the creation or increase of security interests within the retroactive period will be presumed fraudulent to creditors and will not be recognised. Proving fraudulent conveyances is a complicated task and rarely admitted. There are no judicial precedents as to the application of these provisions. Claw actions have rarely been resorted to. Requests for substantial extensions have been largely unsuccessful, although in rare exceptions, claw periods of up to two years have been allowed.

Netting

The general concept of 'netting' is recognised by the Concurso Law, which specifies that netting is mandatory for parties to a transaction recognised by the Concurso Law, pursuant to terms agreed upon in the relevant contract, on the date of the declaration of insolvency, in respect of liabilities and rights arising from master or specific agreements entered into in connection with financial derivative transactions, *reportos* (Mexican law-governed repurchase transactions), securities lending transactions and other equivalent structures.

Mandatory netting is also recognised by the Concurso Law as an exception to the 'cherrypicking' powers given to the conciliator (i.e., mandatory netting applies, regardless of whether the conciliator decides to assume or reject the relevant executory contract).

Obviously, as a prerequisite to netting, the Concurso Law accepts the principle of early termination. It establishes that financial derivative transactions and *reportos* maturing after the date of the declaration of insolvency shall be deemed terminated precisely on that date.

In connection with financial derivative transactions, the Concurso Law provides that if the relevant agreement does not specify the terms pursuant to which a transaction is to be closed out and netted, the value of the underlying assets and liabilities is to be determined on the basis of their market value on the date of the declaration of insolvency; if such a market value is not available or cannot be demonstrated, the conciliator may request an experienced third party to determine such a value.

The general concept of netting reflected in the Concurso Law should be broad enough to encompass transactions such as New York or English law-governed repurchase transactions, securities loan agreements and any other transactions that may be expressed in other currencies. However, the broad terms of the relevant provisions in the Concurso Law may result in abuses that would seem to go beyond the intent of the drafters of the Concurso Law (i.e., creditors claiming that transactions that are not financial derivative transactions and therefore not benefiting from netting provisions should be considered as derivatives, by virtue of the manner through which such transactions were documented). It is also expected that complex derivatives could be challenged as invalid, based on arguments of *ultra vires*, lack of authority and disproportional elements and the like, specifically in times of unforeseen financial market volatility. Although such issues have been addressed by US courts (principally in New York) in favour of creditor banks in matters whereby Mexican companies were plaintiffs, the subject of complex derivatives is far from settled in Mexico.

Restructuring plan: pre-packaged insolvency

A pre-packaged voluntary insolvency must have the support at filing of the debtor and at least 50 per cent of creditors (taking into account all liabilities). In any event, with or without a pre-pack to become effective, a final restructuring plan must be subscribed to by the debtor and recognised creditors representing more than 50 per cent of the sum of the total recognised amount corresponding to unsecured creditors and the total recognised amount corresponding to secured or privileged creditors subscribing the plan. For acceptance, the favourable

vote of 75 per cent of third-party unsecured claims if unsecured intercompany claims account for more than 25 per cent of unsecured claims must be obtained. Any such plan, with the validation of the court, would become binding on all creditors and the insolvency proceeding will be considered as final and concluded.

One significant problem with the statute is that there are no provisions allowing qualified majorities to impose a plan on any recalcitrant participant regarding secured creditors, although there are different, largely untested theories as to how such an imposition may be accomplished.

Key procedural events

The key procedural events, in summary – and only in theory – are as follows (approximate terms for their completion are in parentheses).

Conciliatory stage

The conciliatory stage consists of:

a. filing;
b. acceptance of filing (by day 10);
c. appointment of an examiner (by day 21);
d. judgment declaring insolvency (by day 80);
e. appointment of conciliator (by day 85);
f. judgment recognising creditors and establishing preferences (by day 145); and
g. restructuring agreement (by day 365); if not, bankruptcy is declared (on day 365, at the latest).

Bankruptcy stage

The bankruptcy or liquidation stage may begin earlier if requested at any time by the debtor or if the conciliator determines that it will be impossible to reach agreement in respect of a restructuring agreement. Creditors may demand that the *concurso* begin at the bankruptcy stage, but it is extremely unlikely that any such demand will prevail. Once the bankruptcy stage is declared:

a. a receiver is appointed, who may be the same person who acted as conciliator (by day five of the declaration);
b. the receiver takes over possession of the enterprise and its management (by day 20);
c. the receiver prepares and delivers liquidation balance sheets and inventories (by day 75);
d. the individual assets or the enterprise as a whole are slated for the sale and notices are sent out to potential bidders (by day 135);
e. asset sales begin (the general rule is to conclude liquidation by day 180); and
f. payment to recognised creditors, subject to the preference of labour and, thereafter, secured creditors and taxing authorities, will begin as soon as is practicable.

In practice, very few cases have reached this stage and, except for only one case, they have all failed to adhere to the time frames set forth by the Concurso Law, missing the mark by many years.

Priority of creditors under the Concurso Law

The Concurso Law establishes the following priorities:

a. labour claims (salaries, three months of salaries and benefits, 12 days of salary for each year of employment, mandatory profit sharing and proportional benefits) for the previous 24-month period: the Social Security Institute Law considers that pending fiscal social security contributions have the same priority as labour claims;
b. claims derived from DIP financing and those that were incurred during the proceeding to maintain the ordinary course of business, and approved costs and expenses for the conservation of the business as approved by the conciliator or the court;
c. creditors secured by mortgages or pledges or that otherwise have a privileged priority recognised as such under commercial law (e.g., further to a trust);
d. further to the Federal Tax Code, federal taxes and duties, although the application of this order of priority has been erratic because the tax authority cannot be compelled to participate in any insolvency proceeding;
e. unsecured creditors; and
f. claims of contractually subordinated creditors and related-party creditors of the insolvent debtor (intercompany loans).

The above order must be applied on an absolute priority basis. Nevertheless, and although equity should be considered only after all the above claims are satisfied, judicial interpretations of Mexican corporate law require that shareholders must approve any capitalisation of credits further to the plan, and in some instances the plan itself, giving shareholders a de facto ultimate veto right and thus considerable leverage concerning the approval of any plan. However, in a bankruptcy or liquidation, equity is placed at the very end of the list of priorities.

Duties of directors

The Concurso Law includes a regime for director liability for all business entities, which could have an impact on the way directors behave in the imminence of insolvency and the way in which these issues are addressed by the courts. However, it is noted that no lawsuits have been filed against board members based on the provisions of the Concurso Law.

Disinterested directors are protected from liability under 'business judgement' provisions, based on the presumption that directors have acted on an informed, good faith basis, on the belief that the action taken was an adequate alternative, if based on reliance on management and the advice of the corporation's external auditors or legal and financial advisers.

It is the view of the authors that, as a legal matter, directors and officers must manage an insolvent company and maximise its value for the benefit of all its stakeholders. The focus should be on maximising the value of the enterprise, rather than on attempting to maximise recoveries for any particular constituency.

Significant transactions, key developments and most active industries

Despite pessimistic financial forecasts derived from the covid-19 pandemic, the global economy has proven to be more resilient than expected. However, numerous challenges need to be addressed before chanting victory in the aftermath of the pandemic, such as inflation levels, financial stability risks, monetary policy, China's property sector crisis and the potential impact it may have on the global economy, and geopolitical conflicts, among others.

Several industries were hit hard and required concerted restructuring efforts through in-court proceedings and out-of-court negotiations. Airlines, consumer financing, energy equipment and services, hotels, restaurants, leisure and specialty retail suffered great financial disruption.

There have been, generally, a greater number of restructuring successes than failures. Special mention should be given to Mexico's shadow banking industry, which was hit hard by non-performing loans, resulting in greater accounting disclosure of losses and, ultimately, substantial financial distress. Bondholders holding portions in the billions of dollars have suffered substantial losses as unsecured creditors. This whole sector has, in consequence, fallen out of favour with investors as portfolio receivables have plummeted. A number of major participants in the sector turned to *concurso mercantil* to protect assets for the benefit of creditors, turning to restructuring plans tantamount to orderly liquidations. Undoubtedly, *concurso mercantil* proved to be a useful tool to implement liquidation of accounts and eventually a more orderly delivery of final balances to unsecured creditors.

In many of such *concursos mercantiles*, the debate as to priority of claims in trust structures and 'bankruptcy remote' vehicles has been prevalent. In an approach based much more on form over substance, arguments have been presented in the sense that only registered mortgages and pledges have been given statutory preference on a clearly reliable basis, given a literal reading of the Concurso Law. Creditors holding security rights under trusts or escrows have been recognised in most cases as common creditors only (notwithstanding that the underlying assets were legally and validly transferred to the trust estate), although they have been given the 'privilege' of continuing to be serviced in connection with their credit facilities through the relevant trust

throughout the *concurso* proceeding and, exceptionally, of separating assets in trust from those of the company in question, a concept that makes little sense in view of the stated purpose of the Concurso Law of maintaining the debtor as an ongoing concern during the workout or conciliatory stage of the *concurso*. Breaking up operating assets is inconsistent with this objective.

Although still common and generally recognised, in recent years, guarantee trusts involving future contractual flows assigned to creditors have come under attack, although, fortunately, they have been defended by rulings of the Eighth Circuit Collegiate Court.

Another development that has created considerable concern and controversy is the practice, if not abuse, of resorting to 'precautionary measures' issued by local courts in *ex parte* filings, by which ample "protective measures' are technically designed to preserve the status quo if litigation is considered imminent, favouring mainly debtor entities. Basic creditor rights are stayed during prolonged periods of time, measured in months at the very least, resulting in significant obstacles to creditors seeking to access the courts.

Finally, as a development meriting mention, bondholders that have attempted to access Chapter 11 as a means of seeking a more reliable judicial proceeding through involuntary filings have had to deal with many obstacles, which have made efforts unsuccessful regarding Mexican debtor corporations. To date, only voluntary Chapter 11 filings (whether with or without a pre-pack feature) have been successful.

International

The Concurso Law embraces, unfortunately, only in form, the United Nations Commission on International Trade Law (UNCITRAL) Model Law on cross-border insolvency and international judicial cooperation. Mexican courts have only twice in the past 20 years recognised and given judicial assistance to foreign insolvency proceedings (ruling that such proceedings did not contradict Mexican law or general principles of law). At the time the Concurso Law was enacted, in which its Title 12 was intended to resemble the UNCITRAL Model Law, the Mexican Congress enacted provisions that have made the process unreliable, if not impossible, as it focuses on channelling full-blown, time-consuming procedures through a conciliator, and thus effectively imposes the need to file a full *concurso* proceeding regarding any significant assets in Mexico. Recognition of foreign proceedings in Mexico, for all practical and legal purposes, is not an option.

Related to this topic, Mexican companies have frequently, on the other hand, filed for recognition and protection in the US bankruptcy courts under Chapter 15 of the US Bankruptcy Code. Such courts have responded efficiently, recognising the *concurso* as a main proceeding. Unless a conciliator takes the initiative of

establishing an indirect channel of communication between the Mexican judge presiding over the main proceeding and courts outside Mexico, cross-border communication is practically non-existent.

Outlook and conclusions

As mentioned above, a more relevant welcome development has been that the judiciary, through its Federal Judiciary Council, decreed the creation of the first and second district courts with exclusive nationwide jurisdiction regarding *concurso mercantil* proceedings. The two specialised insolvency district courts initiated their activities in March 2022. Progress is continuing with greater transparency and more interaction by the two specialised courts with IFECOM and professional associations.

In addition, IFECOM published a long overdue code of ethics applicable to its registered examiners, conciliators and receivers, underscoring five principles: impartiality; professionalism; excellence; confidentiality; and honesty.

Mexican Bar Associations and IFECOM made efforts, yet to advance, in amendments to the Concurso Law, including revisions that would allow Title 12 of the Concurso Law to be readopted in a manner more consistent with the express terms of the UNCITRAL Model Law, so that it may work in practice. In this regard, we note that for the first time a successful and comprehensive restructuring of certain financial indebtedness through two interconditional and parallel restructuring plans governed by English law, which included Mexican guarantors, was actually implemented with success without having to include a foreign proceeding recognition under Title 12 of the Concurso Law.

Although the recognition of the dire need to address improvements to the Concurso Law had gained considerable momentum in the federal judiciary, IFECOM and the Mexican Bar Associations, 2024 is an election year, and Congress has focused only on other legislative priorities that may have greater political impact. The necessity of a thorough revision of the Concurso Law remains to be attended to.

Footnotes

1. ^ International Monetary Fund. 2024. World Economic Outlook—Steady but Slow: Resilience amid Divergence. Washington, DC. April.
2. ^ The relevant 1934 statute has no provisions as to creditors' rights, nor any recognition process or ranking of claims, priority rules, voting requirements or other basic rules found in any rudimentary insolvency statute. It is simply a basic corporate statute.

3. ^ Although the 2014 amendments introduced the possibility of avoiding the 'visitation stage' in pre-pack filings, thus saving weeks of bureaucracy, the authors are of the view that there could be a benefit in having an examiner complete the many IFECOM formats necessary to process a *concurso mercantil*, which may prove to be advantageous in the ongoing proceeding.
4. ^ The *ICA* case proved that a Mexican prearranged or pre-pack filing, even with complex local and international facilities and other liabilities – well over US$3.5 billion – could be successfully implemented and approved by a substantial majority, and applying principles of absolute priority, to the detriment of all shareholders in a Mexican public company; the whole process took less than six months to be concluded.