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A COMPARISON BETWEEN THE LEY DE QUIEBRAS Y SUSPENSION DE PAGOS AND THE LEY DE CONCURSOS MERCANTILES

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This article will briefly examine the *Ley de Quiebras y Suspencion de Pagos* (The Bankruptcy and Suspension of Payments Law)¹ and show what it has done to the banking system. It will then tie it in with the introduction of the new *Ley de Concursos Mercantiles* (Business Reorganization Law)² and the effects it has had on the different portfolios of Bancomer. One of the foregone conclusions is that the law is working, as we have not seen any new *concurors* (reorganizations) coming in.

Here is my interpretation of this new law and its elements:

One legal improvement is that the new *Ley de Concursos Mercantiles* now takes into account the financial aspects of an entity, the reason for having experts in the *Instituto Federal de Especialistas de Concursos Mercantiles* (IFECOM).³ Obviously, the other point we see here is maximizing the value of the entity that is subject to whatever economic condition they are facing at the time, as well as its social role within a particular community.⁴ The previous law did not contain those elements.

There are a couple of things that are very important. The official number of *quiebras* (bankruptcies) and *suspenciones de pago* (suspension of payments) that have occurred in Mexico could not be found. By examining the portfolio of the bank, by basically merging Bancomer, Banco Mercantil, Bancounion, Cremi, and Promex, you have about 31 percent of the banking assets of the country, so it should be fairly representative of the numbers that occurred under the *Ley de Quiebras y Suspencion de Pagos*.

What is important is that prior to the crisis, we had three cases, with a total accumulation of 170 million pesos. Obviously at the end of 1994, when the crisis happened, the exchange rate slipped and interest rates jumped from around 12 percent to 125 percent. With that jump, there was a tremendous increase in the portfolio volume of companies that had filed for *suspencion de pagos*. The year ended with a portfolio of 4.2 billion pesos.

Bancomer was able, from 1995 to 1996, to solve one salient case, and it was a fairly large case. This was a company called Grupo Zapata, and the total outstanding amount there obviously allowed us to have a substantial drop. But had it not been for that, the trend would have continued to increase.

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1. Diario Oficial de la Federacion, April 20, 1943.

2. Diario Oficial de la Federacion, May 12, 2000

3. Business Reorganization Law (*Ley de Concursos Mercantiles*), Diario Oficial de la Federacion, Article 311, May 12, 2000.

4. Business Reorganization Law (*Ley de Concursos Mercantiles*), Diario Oficial de la Federacion, Article 1, May 12, 2000.

As interest rates commenced to drop, Bancomer was able to bring down the portfolio to relatively good levels, but the number of cases that we were able to reduce was not notable. What happened was mostly with the large companies, not in the smaller creditors.

And then, of course, came the public discussions to form the *Ley de Concursos Mercantiles* (Business Reorganization Law). Many of the companies that doubted the new law applied for the *Ley de Quiebras* and the benefits that this represented for them; many of them literally embargoed on a quest to seek protection under this law. In other words, they were trying to eliminate the contingency, the *Ley de Concursos Mercantiles*. One of the big cases for us was Altos Hornos de Mejico, which has been in suspension of payments for two-and-a-half years. Clearly many other cases filed for the suspension of payments.

As the law has come into effect, Bancomer has reduced the portfolio significantly, for various reasons. One reason is that the debtors, although under the previous law, saw no other alternative, and we in the banking system were very concerned with all the contamination effects. That is, if you settled a suspension in a particular manner, we were setting a precedent for other suspensions. But given that we knew that no other suspensions would be coming, we could then take some very proactive approaches toward reducing the portfolio.

Clearly the *Ley de Concursos Mercantiles* applies to the new cases. Because of this, there was an increase in large corporations that filed just before the new law came in, whereas in 1995 and 1996, this was more middle market. If you try and tie in the number of cases to the actual volume, it will indicate to you more of the middle market. Generally speaking, if there was a case involving textiles and the lawyer was a particular lawyer, there would be a *suspension de pagos* (suspension of payments). There were several attorneys promoting the suspension of payments.

The all-important issue is the accumulated number of cases. Bancomer's prediction is that at year-end, 2001, we should be at sixty (60) cases, and that is due to the contamination effect and the launching of a program we did on the *Ley de Quiebras y Suspencion de Pagos*. We are better capitalized now, so we were able to address these issues.

From the Creditor's point of view, what has the change to *Ley de Concursos Mercantiles* done for us? This has reduced the excessive power that the debtor had and brought in a balance between debtor and creditor. Also, there is the new element of forced conciliation, whereas in the past, it really was the debtor that was in charge. Debtors in the past had the privilege of going to the suspension. As a creditor, it was very difficult to prevent the debtor from going into the suspension. So, we are taking away that other advantage from the debtor.

Another issue relates to time and recognition. In the *Ley de Quiebras y Suspencion de Pagos*, you typically would freeze the balance, and if you have a debt denominated in dollars, you would freeze it at the exchange rate of the date of the suspension, and you have a legal interest rate that accumulates. So obviously time was in favor of the debtor. With the new law, at the moment that the Reorganization is accepted or filed, you change all of the *saldos* (balances) into *Unidades de Inversion* (Investment Units; UDI's) which affect into inflation so that inflation actually now plays against the debtor.

These are the main changes, though not an extensive list. One other change is toward Federal control of the reorganization rather than local control. A second

change is the addition of time limitations rather than an indefinite time period for the bankruptcy to proceed.

This is a comparative analysis. This is the new *Ley de Concursos Mercantiles*, from the bankers' point of view, and the old *Ley de Quiebras y Suspencion de Pagos*. The new law has both the debtor and the creditor take a role in the process. In the past, wrongfully so, it was the debtor that had most of the initiative. Here we have a neutral third party, the *Instituto Federal de Especialistas de Concursos Mercantiles* (IFECOM).⁵ In the past, we couldn't have access to the numbers. Now, all parties know the facts.

The new law is much more under the domain of the federal government. In the past, people were filing for suspensions in very ill prepared jurisdictions. Both the ill preparedness of the judge as well as the local element didn't help the process.

As stated earlier, debt is converted into UDI's. Now there is also a time frame. Under the *Ley de Concursos Mercantiles*, it typically takes up to 180 days to reorganize a business. In the past, a couple of suspensions have taken up to six years.

Obviously here there are legal repercussions. To get closer to the criminal process is much easier in this process than it was in the previous law.

Bancomer has reviewed new cases with the economic downturn in Mexico. It has received and worked out about 2.7 billion pesos this year, and about 30 cases. And it has gone through a very thorough review as to whether the cases should go into reorganization. Bancomer has selected six cases where it is going to initiate procedures, and amongst the things it is doing, it is taking into account geographic diversification. The term "deep pockets" is used. Bancomer is trying to select debtors that do not have deep pockets because it is very concerned that if you go against a large debtor, they are going to raise constitutional issues. You would be in for a very long litigation where you would probably have a solution within three to four years. So, Bancomer is trying to select debtors that do not have deep pockets. And clearly it is analyzing the debtor's legal support. In other words, with people who have lawyers that we know have questioned the constitutionality of the law, we try to settle, and not pursue this avenue.

Now, there is a new process here that in the Mexican National Banking and Securities Commission (*Comision Nacional Bancaria y de Valores*)⁶ is called Circular 1480, and what that does for banks is to now have reserve based on unexpected loss. That also means that we banks have to take on more and more security. In other words, we reserve less based on this Circular. So that is also going hand-in-hand with the *Ley de Concursos Mercantiles*, and will reduce the number, or shall we say the exposure that is unsecured over time.

As an academic exercise, a bankruptcy packet was created. In the United States, for Chapter 11 Bankruptcies, you have your packet, and off you go to court to file. This is not the case in Mexico. From creating a packet, two recommendations came about. One recommendation is regarding Article 160. If somebody has a specific security and the rest of the creditors don't, he can decide not to pursue the process

5. Federal Institute of Bankruptcy Specialists (*Instituto Federal de Especialistas de Concursos Mercantiles*), (visited on April 10, 2002) <www.ifecom.cgf.gob.mx>

6. National Banking and Securities Commission (*Comision Nacional Bancaria y de Valores*), (visited on April 10, 2002), <<http://www.cnbv.gob.mx/>>

of the *Concurso* (reorganization) but to either collect his principle or the underlying security. So it makes it very difficult to have a unified posture, and that is one issue that should be addressed. And finally the other recommendation is that Mexican states, the individual states, are now raising financing in the markets here in Mexico. The rating agencies are reviewing the legal system of each individual state. One of the items that will be reviewed is the adequate implementation of different laws, such as this law.