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## **Mexican Supreme Court Upholds Right of Bankers to Charge Compound Interest**

by LADB Staff

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In a partial ruling that angered the debtors-rights organization Asamblea Ciudadana de Deudores (ACDB), Mexico's highest court (Suprema Corte de Justicia de la Nacion, SCJN) upheld the right of private banks to charge compound interest on overdue debts. The ACDB, more commonly known as El Barzon, had brought the case to the SCJN seeking relief for thousands of farmers, mortgage holders, and small-business owners facing ruinous debts.

The SCJN justices ruled 8-3 that Mexico's commercial law supersedes civil law. The Mexican civil code outlaws charging interest on unpaid interest, while the commercial code allows unpaid interest to be added to the principal under certain circumstances. While a final decision had yet to be made, the partial decision seemed likely to favor the bankers.

In the statement explaining the decision, the SCJN said the court's role was to interpret current legislation and not to recommend changes. The justices said any modifications to existing law would have to come via the legislative branch. "The court has established the juridical criteria for all tribunals in the country, in the sense that if there is a dispute between a debtor and a bank, then yes, it is possible to capitalize interest," a court official told Reuters.

In Mexico, decisions issued by the SCJN frequently go unnoticed, with most interest in actions of the executive and legislative branches. However, the SCJN ruling, issued on Oct. 7, was widely noticed because of the recent attention on the failed bank-rescue fund (Fondo Bancario de Proteccion al Ahorro, FOBAPROA). Debtors perceive FOBAPROA as a program that helped out "fat-cat" bankers.

### ***Debtors-rights group El Barzon questions ruling***

The SCJN's decision drew strong negative reactions from El Barzon, which threatened to organize a "strike" urging debtors to withhold all payments to the bankers. "Debtors ought to take whatever actions are necessary to prevent the seizure of their property," said El Barzon leader Alfonso Ramirez Cuellar. Ramirez, who also is a member of the center-left Partido de la Revolucion Democratica (PRD) in the Chamber of Deputies, described the ruling as a "legalized mugging" of debtors. "This leaves millions of people without any legal defense and unable to pay off their debts," Ramirez said. "The justices have really dealt a nasty blow to millions."

PRD leader Andres Manuel Lopez Obrador accused President Ernesto Zedillo and the banking sector of influencing the SCJN's decision. "No one is going to believe that Zedillo did not have a hand in this decision," Lopez Obrador said in an interview with the cable network Multivision. "No one will believe that the bankers did not take the necessary steps to gain a favorable ruling." The national lawyers organization Barra Nacional de Abogados (BNA) also questioned whether the SCJN's ruling was truly impartial. The BNA has asked the Chamber of Deputies and the Senate to

investigate reports that four of the eight justices who voted in favor of allowing compound interest received favorable treatment in restructuring their debts with commercial banks.

As expected, the Asociacion de Banqueros de Mexico (ABM) supported the SCJN decision. ABM president Carlos Gomez y Gomez said the decision gives the banking sector the tools to slow the growth in overdue debt. But Gomez pledged that bankers will continue to work with debtors to solve the country's overwhelming problem of past-due loans. "The court's decision will have no bearing on the bank's willingness to continue to dialogue with clients who have fallen into overdue debt," said Gomez y Gomez. At the same time, the ABM president said legal action would continue against 130,000 borrowers who are overdue on payments, particularly on mortgages.

Members of the five political parties in the Chamber of Deputies expressed disappointment regarding the SCJN's decision, which they described as "legal, but not just." "The deputies have an obligation to listen to the social outcry and develop legislation that will create greater equity between the bankers and the debtors," said Deputy Rafael Carrio Alvarez of the governing Partido Revolucionario Institucional (PRI). Legislators from the PRD, PRI, and center-right Partido Accion Nacional (PAN) were expected to introduce initiatives to change Mexico's financial codes regarding the payment of interest. "These reforms should have been considered 22 years ago," said Salvador Diaz Rocha, a former SCJN justice.

While the five political parties are expected to work together to change the country's financial codes, a rift remains between the PRD and the other four parties regarding the fate of FOBAPROA. Congress has rejected outright Zedillo's original plan to transfer FOBAPROA liabilities to the public debt, but legislators have been willing to work with the administration on an alternate plan. Four parties proceed with legislation on bank-rescue fund In early October, the PAN, PRI, Partido Verde Ecologista Mexicano (PVEM), and the Partido del Trabajo (PT) said they had developed a 13-point plan to guide negotiations on a solution to the FOBAPROA question. The plan was drafted in consultation with the Secretaria de Hacienda y Credito Publico (SHCP). However, the PRD refused to take part in the deliberations because of wide differences with the other parties on the scope of the plan.

The PRD has proposed that the majority of assistance provided under a debtor-rescue plan be channeled to small-scale borrowers with overdue debts of less than 1 million pesos (US\$98,425). The four other parties support a plan that restructures debts for borrowers with delinquent loans of less than 5 million pesos (US\$492,000). But the PRD is not united in its refusal to participate in drafting legislation for the FOBAPROA plan. The PRD executive committee, led by party president Lopez Obrador, has said the party will not participate in FOBAPROA negotiations under the current plan. "Our executive committee does not want us to return to the negotiations, and that's why we are not participating," PRD legislative leader Porfirio Munoz Ledo said in a press conference.

Still, the legislative delegations of the PAN and the PRD have formed a commission to discuss common ground regarding FOBAPROA and to possibly develop a joint proposal. The commission, known as Grupo de los Doce, comprises six legislators from each party. Legislative leaders for the two parties agree that a consensus proposal on FOBAPROA would serve the best interests of Mexico. "By drafting this legislation through consensus, we increase the chances that the initiative

will be viewed favorably by debtors, our domestic financial system, and by overseas markets," said PAN Deputy Santiago Creel Miranda, a member of the Grupo de los Doce.

While the parties have expressed willingness to work together on a plan, Lopez Obrador and his PAN counterpart Felipe Calderon Hinojosa have continued to trade accusations. In a letter to Calderon, Lopez Obrador accused the PAN of siding with Zedillo, former president Carlos Salinas de Gortari, and the bankers. In his reply, Calderon accused Lopez Obrador of placing electoral concerns ahead of the good of the country. He also warned the PRD leader not to "sabotage" the progress made by PAN and PRD legislators in formulating a joint FOBAPROA plan. Meantime, the PRI, PAN, PVEM, and PT have continued discussions with the SHCP to develop a legislative initiative based on the 13-point plan drafted in early October.

A key element of the plan is to transfer 552 billion pesos (US\$54.3 billion) in bad bank loans into a separate public entity instead of counting it as public debt as the government had originally proposed. Another important provision requires banks to assume all the major loans they had passed on to the FOBAPROA trust. This would force the banks, rather than the federal government, to collect the debt from delinquent borrowers with large debts.

In exchange for assuming the large loans, banks would be allowed to transfer the equivalent amount of small debtor loans into the FOBAPROA trust. The plan proposes to restructure debts for thousands of small-scale debtors who received agricultural, mortgage, or small-business loans. PAN Deputy Rogelio Zambrano Sada said the four parties involved in the negotiations hope to finish drafting the legislation by the end of October.

If the process drags into November, said Sada, the plan could become embroiled in the debate on the 1999 budget, which the Zedillo administration is drafting. [Note: Peso-dollar conversions in this article are based on the Interbank rate in effect on Oct 14, reported at 10.16 pesos per US\$1.00] (Sources: Reuters, 10/01/98, 10/07/98, 10/08/98; The News, 10/02/98, 10/08/98; The Dallas Morning News, 10/08/98, 10/09/98; Excelsior, 10/01/98, 10/02/98, 10/06-09/98; El Universal, 10/01/98, 10/02/98, 10/06/98, 10/08/98, 10/09/98; El Financiero International, 10/05/98, 10/12/98; El Diario de Yucatan, 10/07/98; Proceso, 10/11/98; Novedades, 10/01/98, 10/07/98, 10/08/98, 10/12/98; Spanish news service EFE, 10/13/98; El Economista, 10/01/98, 10/02/98, 10/06/98, 10/07/98, 10/08/98, 10/09/98, 10/12/98, 10/14/98; La Jornada, 10/01/98, 10/06/98, 10/07/98, 10/08/98, 10/09/98, 10/12/98, 10/14/98)

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