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Citibank Sues Mexico's Savings-Protection Agency for 
Paying Off Debt Early

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Citibank Mexico has filed a lawsuit against four Mexican government agencies for paying off a promissory note too early. The lawsuit, filed in Mexico City, is directed at the savings-protection agency (Instituto de Proteccion al Ahorro Bancario, IPAB), the Secretaria de Hacienda y Credito Publico (SHCP), the Comision Nacional Bancaria y de Valores (CNBV), and the Banco de Mexico (central bank). The lawsuit relates to an agreement signed by Citibank with IPAB's predecessor, the Fondo de Proteccion al Ahorro Bancario (FOBAPROA), in 1997.

Under the accord, Citibank agreed to acquire financially troubled Banca Confia, a subsidiary of Abaco Grupo Financiero, from FOBAPROA with the understanding that the government would assume 24.85 billion pesos (US$2.62 billion) of Confia's debt and repay it to Citibank over an eight-year period (see SourceMex, 1999-09-03).

Prepayment would save taxpayers 3.3 billion pesos

The controversy arose when IPAB, the agency in charge of repaying the debt, decided to retire the debt in full in May of this year. IPAB executive secretary Vicente Corta said the prepayment would save Mexican taxpayers at least 3.3 billion pesos (US$346 million) in interest. "The agreement with Citibank did not prohibit paying off the debt ahead of time," said Corta.

But Citibank immediately rejected the prepayment as a violation of the original terms of the contract because the bank stands to lose the hundreds of millions of dollars in interest it expected over the next six years. Julio de Quesada, president and director general of Citibank Mexico, said the bank would never have agreed to acquire Confia without the clause requiring that payments be extended over an eight-year period. "The payment of the lump sum does not translate in any way to huge earnings for Citibank," said Julio Armando de Quesada, president and director general of Citibank Mexico.

De Quesada said the interest payments are being used to clean up the financial mess the bank inherited through Confia. "We want to demonstrate to authorities that we have a project that is progressing well," said de Quesada, "and that certain communication and support is needed to complete the cleanup of this bank."

While disagreeing with Citibank's argument, Corta said the bank acted properly in bringing the matter before the courts, which he called an impartial third party. "We believe we have sufficient elements to win the argument in this process," Corta told reporters in early July. "We believe the action we took benefits the entire society." Corta said IPAB would abide by any ruling handed down by the Mexican courts, expected later this year. "If at the end of the day they are in the right, we will pay them everything they are due," Corta said. "But if we are in the right, then all we ask is that they accept the court's decision and publicly declare that we always acted in accordance with the law."
Banking analyst Lawrence Madsen said IPAB is probably on solid legal ground in making the prepayments. In an interview with The New York Times, Madsen said he would be "very surprised" if the IPAB legal team had not thoroughly researched the legality of making advance payments. In an article published in late June, the weekly news magazine Proceso said Citibank Mexico officials have even threatened to shut down operations in Mexico unless IPAB reconsiders its decision to make the prepayment. But de Quesada told the official news agency Notimex that the bank has no plans to end its presence in Mexico nor cancel its planned expansions. Citibank, which has operated in Mexico since 1929, is the foreign bank with the longest presence in the country.

**Citibank says prepayment violates Mexican Constitution**

Citibank Mexico experienced a small setback in late May when District Judge Jesus Antonio Nazar ruled against its petition to negate the IPAB action. But the court's decision primarily considered the commercial merits of the case and did not touch on Citibank's argument that IPAB's action violates Articles 14 and 16 of the Mexican Constitution.

In essence, Citibank contends that IPAB has no power to change the terms of the deal, which was made with FOBAPROA. The Mexican Congress voted in December 1998 to create IPAB, whose primary function was to dispose of the huge liabilities incurred by FOBAPROA (see SourceMex, 1998-12-16). The bank said IPAB is functioning under the law approved by the Mexican Congress in December 1998. By attempting to change the terms of the Confia payment agreement, IPAB would be violating Article 14 of the Mexican Constitution, which bans making a law retroactive. But IPAB has received support from senators who were instrumental in drafting the legislation to create IPAB.

Sen. Fauzi Hamdan of the conservative Partido Accion Nacional (PAN), who chairs the Senate committee that first proposed the law to create IPAB, said the agency is well within its rights to make the payments ahead of time. Sen. Alfonso Ramirez Cuellar of the center-left Partido de la Revolucion Democratica (PRD) has also supported IPAB's position. Ramirez also said the rescue of Confia was one of the most expensive transactions conducted under FOBAPROA and should be investigated further. In particular, the Congress should determine whether Confia and bank owner Jorge Lankenau benefitted from illegal concessions from the federal banking agency, CNBV.

Other experts agree that many Mexican banks, including Citibank, received special privileges during President Ernesto Zedillo's administration. Syndicated columnist Sergio Sarmiento, in a piece published June 12, said the federal government convinced Citibank to acquire Confia by offering a much higher interest rate than the prevailing market levels. "What is significant about this case is that it shows us once again the hidden arrangements made by the government to convince foreign institutions to take over Mexican banks following the massive bankruptcies at the end of 1994," said Sarmiento.

Sarmiento said the government made similar guarantees to Britain's HSBC Holdings and Canada's Bank of Nova Scotia to ensure that they would invest in financially troubled Mexican banks rescued through FOBAPROA. Until recently, HSBC was one of the principal owners of Serfin, while Bank of Nova Scotia has been a major investor in Inverlat. [Note: Peso-dollar conversions in this article are based on the Interbank rate in effect on July 12, reported at 9.46 pesos per US$1.00] (Sources: Agence France-Press, 05/10/00; Novedades, 05/11/00; Excelsior, 05/11/00, 05/12/00, 05/15/00, 06/07/00,