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In early January, the US Securities and Exchange Commission (SEC) filed a civil lawsuit in a US federal court charging Mexico's second-largest television network TV Azteca, its chairman Ricardo Salinas Pliego, and two other executives with defrauding investors in the US and Mexico. The SEC contends that Salinas reaped "a tremendous personal profit" by concealing from shareholders a complex debt scheme involving Azteca, its telephone subsidiary Unefon SA, and Codisco Investments a third company formed by Salinas and an associate.

US regulators require companies to disclose related-party transactions because they may involve conflicts of interest. The SEC said Codisco Investments bought Unefon debt at a deep discount from Canada's Nortel Networks. Four months later, it sold the Unefon debt back at full price to TV Azteca, earning more than US$109 million in illicit profits.

The SEC launched an investigation into the transactions after a group of New York investors initiated legal action against Salinas and TV Azteca. In the SEC lawsuit, regulators said Salinas "coordinated a scheme" to conceal his involvement in the transaction from investors, TV Azteca's board of directors, and financial-market regulators.

Also named in the suit were TV Azteca executives Pedro Padilla Longoria and Luis Echarte Fernandez. Padilla is the former director of TV Azteca, while Echarte currently heads the company's US subsidiary Azteca America. Echarte, a US citizen, eventually settled with the SEC by paying a civil fine of US$200,000. He neither admitted nor denied any wrongdoing.

Moises Saba Masri, Salinas' partner in Codisco Investments, was not named in the SEC lawsuit. The SEC, however, sued Saba and his broker Albert Sutton last year for allegedly manipulating the closing price of TV Azteca's US-traded shares in 1999 to avoid a US$4.3 million loss. The current SEC lawsuit seeks to force Salinas to return any illicit profits and to bar the TV Azteca executive from holding a position of director or officer of any company whose shares trade on a US exchange.

Timing of Court ruling uncertain

The US federal court did not indicate when a ruling would be forthcoming. Case to test SEC ability to regulate Mexican companies The case is widely seen as a test of whether US authorities can force Mexican companies to comply with US rules when trading on US stock markets. TV Azteca, whose depository shares are listed on the New York Stock Exchange (NYSE), is a subsidiary of Azteca Holdings, a company controlled by Salinas.

These are the first charges brought by US securities regulators against a Mexican company after stricter US financial reporting standards were introduced under the Sarbanes-Oxley Act of 2002.

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"Geographic boundaries will not protect those who seek to defraud investors, and all public companies, whether domestic or foreign, that choose to avail themselves of opportunities in US markets also have the responsibility to adhere to US securities laws," SEC enforcement officer Spencer Barasch told The Dallas Morning News.

The case is also considered a test of the US Sarbanes-Oxley Act of 2002, which encourages attorneys to notify directors about potential material violations of securities laws. The New York legal firm of Akin Gump Strauss Hauer & Feld withdrew as Azteca's legal representative in December 2003 after notifying the company's board of directors that Salinas may have violated US securities laws.

Salinas disputes charges

The SEC lawsuit angered Salinas, who accused the US agency of presenting charges that were "false, in bad faith, and discriminatory." He also accused the regulator of using TV Azteca as a scapegoat for its regulatory failures in the US. "From my point of view, they are trying to compensate politically for their past deficiencies in supervising US companies."

The TV Azteca chairman predicted that the US court would exonerate him. "We will prevail because we acted properly," said Salinas. The SEC presented Salinas with the opportunity to settle the case, but the Mexican executive turned down the offer. "Principles are not negotiable. We could have settled for money, but this is not about money, it is about standing up for what you believe to be right," Salinas said in a statement released by TV Azteca.

US and Mexican market analysts said the SEC conducted the investigation in cooperation with its Mexican counterpart, the Comision Nacional Bancaria y de Valores (CNBV). "We do not know if Mexican authorities will seek to apply the same type of punishments against the accused," said a report published by Valores Banamex, the securities subsidiary of Grupo Banamex-Citibank. "But we do not rule out this possibility."

Valores Banamex and other brokers recommended that their clients sell their shares in TV Azteca, which also trades on the Bolsa Mexicana de Valores (BMV). "We urge investors to stay on the sidelines not only on fundamental value grounds, but until the company makes an appropriate response to the SEC's formal notification," said Xavier Escala, an equity analyst at Banif Securities in Mexico City. Other analysts said the investigation and the lawsuit could hamper the ability of all of Salinas' companies to issue bonds and renegotiate debt.

In addition to TV Azteca, Salinas owns the Elektra retail chain and Banco Azteca. "The credibility of Grupo Salinas is nonexistent, and the company will have difficulties regaining it," analyst Jorge Lagunas of Interacciones said shortly after the SEC launched its investigation in 2004. The CNBV declined to comment on the SEC's lawsuit, but suggested it is conducting its own probe. "They are separate investigations," a CNBV spokesman said.

The Secretaria de Hacienda y Credito Publico (SHCP) confirmed that an investigation is in process but declined to offer other details. "The revisions [of the Azteca transactions] are proceeding," said Finance Secretary Francisco Gil. "As long as the case is not concluded, we cannot legally divulge any other information."

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Some analysts said the case has the potential for transforming business practices in Mexico by promoting greater transparency and respect for minority shareholders. "Owners of Mexican companies that are listed in the US have to be looking at this and saying 'Wow.' It will have an influence," said Jim Harper, director of corporate research at US-based BCP Securities. (Sources: Agencia de noticias Proceso, 01/04/05; Reuters, 01/04/05, 01/05/05; La Cronica de Hoy, El Financiero, The New York Times, The Dallas Morning News, Spanish news service EFE, Bloomberg news service, 01/19/04, 02/25/04, 01/05/05; The Herald-Mexico City, 01/14/04, 01/06/05; El Universal, 01/05-07/05; La Jornada, 01/27/04, 01/06/05, 01/11/05, 01/12/05)

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