# Restructuring and insolvency in Mexico: overview

***by Alejandro Sainz***

Law stated as at 01 Apr 2016 • Mexico

*A Q&A guide to restructuring and insolvency law in Mexico.*

*The Q&A gives a high level overview of the most common forms of security granted over immovable and movable property; creditors' and shareholders' ranking on a company's insolvency; mechanisms to secure unpaid debts; mandatory set-off of mutual debts on insolvency; state support for distressed businesses; rescue and insolvency procedures; stakeholders' roles; liability for an insolvent company's debts; setting aside an insolvent company's pre-insolvency transactions; carrying on business during insolvency; additional finance; multinational cases; and proposals for reform.*

## Forms of security

### 1. What are the most common forms of security granted over immovable and movable property? What formalities must the security documents, the secured creditor or the debtor comply with? What is the effect of non-compliance with these formalities?

#### Immovable property

**Common forms of security and formalities.** The most common security for immovable property is the mortgage, which is governed by state law. This security must be documented in a notarial instrument and must comply with publicity principles through registration in public record offices, in order for it to be enforceable against third parties. Depending on the asset granted in collateral there are some cases in which an additional registration is required (for example, the Federal Telecommunication Registry and the Maritime Registry, among others).

**Effects of non-compliance.** If the mortgage is documented in a notarial instrument but not registered before the corresponding public record office, a third party can register their claim. Although the unregistered security will not be declared as void, the party with registered security will have a priority claim over the asset.

### Movable property

**Common forms of security and formalities.** The most common securities for movable or intangible assets are:

- **Guarantee trusts.** The guarantee trust must be documented in a notarial instrument if, within the trust, immovable property is being incorporated or if the movable assets transmitted to the trust exceed the amount provided by law (that is, MXN250,000).
- **Floating lien pledges.** A floating lien pledge can ideally be documented in a notarial instrument and be registered in the Sole Guarantee Registry (*Registro Único de Garantías Mobiliarias*) (SGR) so that it can be enforceable against third parties. However, there are some cases where the security does not require registration before public record offices and a direct notification to the debtor of the collector's rights is sufficient.

These forms of security are governed by federal law.

**Effects of non-compliance.** The law and regulations applicable to the SGR or any other Mexican law or regulation to that effect, provide that pledges over equity interests must be recorded at the SGR in order to be perfected as opposed to a floating lien pledge. Mexican law provides that all rights and movable property can be pledged under a floating lien pledge, except for those rights that are strictly personal to its holder, which is the case of equity quotas. The SGR is of a declarative nature and does not grants rights to recording parties, meaning that it only has a publicity effect. Therefore, under Mexican law, the pledge in no event is rendered invalid or in any form the guarantee amount is less that the actual amount included in the pledge or the loan agreement.

## Creditor and contributory ranking

### 2. Where do creditors and contributories rank on a debtor's insolvency?

The existing Mexican insolvency law (*Ley de Concursos Mercantiles*) (LCM) classifies creditors into the following categories or classes (and with the following order of priority):

- First priority claims against the "estate" of the debtor (*creditos contra la masa*), which includes (collectively, the "claims against the estate"):
    - Special Labour Claims (*section XXIII, chapter A, Article 123, Constitution, and applicable regulations*);

- debt incurred for the management of the estate (*masa*) of the debtor with the authorisation of the conciliator or the receiver, or those contracted directly by the conciliator;
- debt incurred to cover ordinary expenses for the safety of the estate assets, their repairs, conservation and management; and
- debt incurred from the judicial or extra-judicial acts for the benefit of the estate, provided that under Article 225 of the LCM against the secured creditors, with mortgages or pledges, or creditors with special privilege, the preference or privilege of the claims against the estate does not apply, with the exception of the Special Labour Claims referred to above; the litigation expenses incurred for the defence or recovery of the goods or assets subject to the security interest of the secured claims or over those assets related to the "special privilege" and the expenses necessary for the repair, conservation and sale of those assets.

- Singularly privileged creditors.
- Secured creditors (with mortgages and pledges over assets of the debtor) and tax claims secured with a security *in rem* (up to the value of such guarantee) are paid first with proceeds from the sale of mortgaged or pledged items. If the items have a value or a price in excess of the debt, any excess or remaining value is directed to cover subsequent debt payments to other creditors. If the price does not cover the debt, mortgage or pledge, the corresponding creditor may participate, pro rata, as a common or unsecured creditor, to collect the remaining amount:
    - other tax claims and labour claims;
    - creditors with a special privilege (that is, those with a guarantee trust);
    - common or unsecured creditors; and
    - subordinated creditors.

## Unpaid debts and recovery

### 3. Can trade creditors use any mechanisms to secure unpaid debts? Are there any legal or practical limits on the operation of these mechanisms?

Trade creditors generally rank as unsecured creditors and there are no particular mechanisms to secure their unpaid debts by statue.

### 4. Can creditors invoke any procedures (other than the formal rescue or insolvency procedures described in *Questions 6* and *7*) to recover their debt? Is there a mandatory set-off of mutual debts on insolvency?

There are various legal actions available to creditors prior to a formal insolvency proceeding to recover on a defaulted loan or obligation of a debtor. The form of the action proceedings (for example, foreclosure, attachment of assets, temporary restraining orders, preliminary discovery or pre-filing motions and so on) can vary depending on, among others:

- The type of agreement.
- The source of the action to be followed (for example, civil, mercantile, ordinary or special).
- Whether collateral was granted.
- Whether promissory notes were issued.
- The type of collateral granted.

In this regard, under Mexican law there are different types of securities that can be constituted over different types of assets.

Without a valid restructuring agreement with the debtor and approval by the conciliator, creditors cannot offset debts owed to them by the debtor in an insolvency proceeding. Additionally, creditors must not recover expenses of participating in the process unless agreed with the company (that is, through lock-up agreements) and approved by the conciliator.

Under Mexican law, foreign creditors must always be treated equally to local creditors. However, there are specific rules relating to debt recovery by foreign creditors (*see Question 13*).

## State support

### 5. Is state support for distressed businesses available?

The government plays an active role in special reorganisations considered in the Mexican insolvency law (LCM), including:

- Business reorganisations of debtors that provide public services under government concessions.
- Business reorganisation of credit institutions.
- Business reorganisation of auxiliary credit institutions.

# Rescue and insolvency procedures

## 6. What are the main rescue/reorganisation procedures in your jurisdiction?

Mexican insolvency law (LCM) provides for a single insolvency proceeding known as "*concurso mercantile*" (conciliation or bankruptcy procedure). The *concurso* procedure consists of two main stages (that is, the conciliation stage and bankruptcy stage) (*see Question 7*), each of them supervised by the Federal Institute of Specialists in Mercantile Insolvency and Bankruptcy Procedures (IFECOM).

### Concurso Mercantile Procedure - Conciliation

**Objective.** The first stage of a *concurso* procedure is the conciliation stage, which aims to encourage a binding reorganisation agreement between the debtor and its creditors and, as a result, avoid the debtor's bankruptcy or liquidation. A conciliator, who initially acts as an intermediary between the company and its creditors, must direct this attempt. The objective of the conciliation stage is to preserve the operation of the debtor's business while reaching an agreement between the debtor and its creditors. The reorganisation agreement generally takes the form of a restructuring plan or creditors' agreement.

**Initiation.** The following parties can file insolvency claims:

- The debtor.
- Any creditor.
- The district attorney.
- A judge.
- Tax authorities in their capacity as creditors.

With the petition filed by creditors (involuntary) or the insolvency petition filed by the company (voluntary), a guarantee or bond must be posted to guarantee the examiner's fee payment.

The court will order the party that filed the insolvency claim/petition to pay the attorney's fees and expenses (*gastos y costas*), including the insolvency examiner's fees, if any judgment is issued declaring no insolvency of the company. The amount of the attorney's fees and expenses is regulated by statute. Immediately after the insolvency petition is filed and accepted by the court, the court must file a petition before the IFECOM for the appointment of an examiner. Once the examiner has been appointed, the examiner must, within the following 15 to 30 days, report to the court if the debtor is insolvent (according to the measures provided for under the LCM) and can be declared in *concurso*.

The debtor and, if the insolvency petition is filed by creditors (involuntary procedure), the creditors can challenge the examiner's report. The court must determine the solvency or insolvency of the debtor within the 15 days following the date of its receipt of the examiner's report. If the court determines that the debtor is solvent, the *concurso* procedure ends. If the court resolves that the debtor is legally insolvent, it will issue the corresponding declaration or judgment of insolvency, which formally begins the conciliation stage.

The declaration of insolvency must establish that the debtor has incurred a general default of its payment obligations, and must include a provisional list of creditors identified in the debtor's accounting records. This list does not exhaust the proceeding for recognition, ranking and determination of the priority of creditors' claims.

Under the LCM, the declaratory of insolvency must include:

- The retroactivity date (that is, the date to which the effects of the *concurso* procedure will be applied retroactively, known as the "hardening" or "look-back" period).
- A declaration that the conciliation stage has commenced.
- Instructions for the IFECOM to appoint a professional conciliator.
- An order for the debtor to immediately provide to the conciliator the debtor's books, records and all other necessary documents, and allow the conciliator and interveners, if any, to carry out the activities necessary to perform their duties, and to suspend the payment of debts.

**Substantive tests.** A debtor can be declared insolvent if it has generally failed to perform its obligations. For the purposes of the LCM, an individual or entity has generally failed to perform its obligations if:

- It has defaulted on its contractual obligations with two or more different creditors.
- The obligations of the debtor that have been due for at least 30 days represent, at least, 35% or more of all the debtor's obligations on the date on which the demand or insolvency petition is filed.
- The debtor does not have any of the following assets in an amount sufficient to perform at least 80% of its obligations due on the date on which the demand or insolvency petition is filed:
    - cash and demand deposits;

- term deposits and investments becoming exercisable or maturing in a term no longer than 90 calendar days following the date on which the demand or insolvency petition is filed before the court;
- customer receivables with a maturity date not exceeding 90 calendar days following the date on which the demand or insolvency petition was filed before the court; or
- securities or negotiable instruments available at the relevant markets that can be sold within a term of 30 business days, with a known value on the date on which the demand or insolvency petition was filed before the court.

**Consent and approvals.** During the conciliation stage, the debtor must work with its creditors to reach a creditors' agreement or reorganisation plan. If a creditors' agreement is reached and approved by the court, the *concurso* procedure ends. An express procedure for "cramming down" creditors that does not approve proposals approved within these procedures, as permitted under other foreign jurisdictions, is not expressly provided for by the LCM. However, it is possible to reach a plan of reorganisation without the vote of all the creditors if certain mandatory conditions and percentages of votes are met, as provided for under the LCM.

To be effective, the reorganisation plan must be subscribed by the debtor and the recognised or acknowledged creditors representing over 50% of the sum of the:

- Amount recognised to the totality of the recognised or acknowledged unsecured and subordinated creditors.
- Amount recognised to these recognised or acknowledged secured creditors or with special privilege subscribing the plan.

Under the recent amendments to the LCM if the subordinated creditors represent more than 25% of all the acknowledged loans, a new voting and majority rule is foreseen so that the restructuring agreement is valid (that is, the majority of the remaining common creditors will vote in favour of the restructuring agreement without then counting the subordinated creditors).

**Supervision and control.** The *concurso* procedure is supervised by the IFECOM and the conciliator supervises and controls the debtor's affairs. Under the LCM, an intervener can represent the interests of creditors in the *concurso* procedure and can be assigned the responsibility of overseeing actions of the conciliator and of the receiver, as well as the actions of the debtor in relation to the operation of its business.

Any creditor or group of creditors representing, at least, 10% of the value of the credits owed by the debtor, under the the provisional list of credits, has the right to request the court to appoint an intervener in the *concurso* procedure. Any creditor or group of creditors can file before the court requests for the appointment of an intervener.

On a case-by-case basis, the creditors' committees play an important role in the process. Creditors can form ad hoc committees aimed to have more leverage and negotiation power in relation to the debtor under *concurso* procedure.

In Mexico, there are no bankruptcy courts that specialise only in *concursos*. Federal district courts are competent to hear these insolvency processes in addition to other matters.

**Protection from creditors.** No protection from the creditors is provided by statue. The debtor can terminate contracts if this was expressly agreed in the corresponding agreement, but subject to special rules and limitations provided in the LCM. The LCM provides special rules for:

- The termination of leases.
- The purchase of goods that are not delivered.
- Deposits.
- Repurchase and derivative agreements.
- Security loan transactions.
- Differential or future contracts.
- Lump sum construction contracts and insurance contracts.

**Length of procedure.** The conciliation stage must not last more than 185 calendar days, unless extended for up to two additional consecutive periods of 90 calendar days each. However, the conciliation stage must not last more than 365 calendar days.

**Conclusion.** The conciliation stage concludes and the debtor is declared bankrupt if the:

- Conciliation stage ends without the parties reaching a creditors' agreement.
- Debtor fails to comply with the creditors' agreement.
- Debtor requests its bankruptcy.
- Conciliator requests the debtor's bankruptcy and the court agrees to grant it.

## 7. What are the main insolvency procedures in your jurisdiction?

### Concurso Mercantil Procedure - Bankruptcy

The second stage of a *concurso* procedure, if applicable, consists of the bankruptcy stage. The debtor can be declared bankrupt if the conciliation stage ends for any of the reasons given in *Question 7, Conclusion*.

The Mexican insolvency law (LCM) does not provide different insolvency proceedings for individuals and companies or make distinction between "preventative" insolvency proceedings and "actual" insolvency proceedings.

**Objective.** The liquidation of the debtor. Additionally, to the effects attributed to the declaration of insolvency, the bankruptcy judgment:

- Suspends the ability of the debtor to perform legal acts, which then affects its business and assets.
- Causes the appointment of a receiver, with full authority to replace the debtor or the conciliator in the management of the debtor's business.
- Orders the debtor and any third party having possession of the debtors' assets to deliver all such assets to the receiver.
- Requires that payments to the debtor only be made with the receiver's authorisation (failure to obtain such authorisation leads to double payments).
- Invalidates any acts performed by the debtor or its representatives following the bankruptcy judgment without the receiver's authorisation.
- Invalidates any payments executed by the debtor after the bankruptcy judgment.
-

**Initiation.** The debtor can be declared bankrupt if the conciliation stage ends for any of the reasons given in *Question 7, Conclusion*.

**Length of procedure.** The length of bankruptcy proceedings varies depending on the industry and the time required to auction, sell, and reach agreements among creditors and the conciliator to offset claims.

**Conclusion.** The liquidation process is aimed to terminate any pending operation of the company, collect any amounts in favour of the debtor and liquidate any outstanding amounts of the debtor in favour of any type of creditor and its shareholders. The liquidation of a company concludes with the cancelation of the bylaws registration therefore becoming extinct.

# Stakeholders' roles

**8. Which stakeholders have the most significant role in the outcome of a restructuring or insolvency procedure? Can stakeholders or commercial/policy issues influence the outcome of the procedure?**

## Stakeholders

All of them have a significant role and the amount that they represent is very important for the thresholds that must be met to reach a restructuring agreement. Unlike other jurisdictions, the debtor's (its shareholders) participation is of great importance and is necessary to reach a restructuring agreement.

## Influence on outcome of procedure

Stakeholders have a significant role and the amount they represent is important to reach a restructuring agreement. Unlike other jurisdictions, the debtor's (shareholders) participation is of great importance and necessary to reach an agreement. If the plan provides for an increase in capital stock, the conciliator must give notice to existing shareholders so they can exercise any pre-emptive rights they may have. Similarly, if as part of the reorganisation plan, the claim holders and the debtor agree to capitalise debt the shareholders of the debtor must approve it.

Therefore, stakeholders do have a practical influence on the type of procedure used and they should approve it before it is adopted.

Commercial and policy issues often affect the outcome, that is, foreign investment issues and concessions granted by the state are clear examples of matters that may affect the outcome of a restructuring or insolvency procedure. The insolvency laws are intended to favour both, the debtor rehabilitation and the recovery by creditors although the survival of the debtor is the main target of the law.

Interests such as labour and tax liabilities are given a high level of protection and are ranked at the top of the list of recognised claims.

# Liability

**9. Can a director, partner, parent entity (domestic or foreign) or other party be held liable for an insolvent debtor's debts?**

Directors of a company declared insolvent by a competent court, engaging in any malicious act or conduct that causes the non-performance of the company's payment obligations, can be held liable to civil actions or even subject to criminal prosecution, in the event of fraudulent acts. However, if the company has not been declared insolvent by a competent court, the directors cannot be liable for continuing to operate a company under financial distress. Transactions related to creditors' collections rights that have not been segregated may be more vulnerable to attack.

Additionally, according to the Mexican insolvency law (LCM) some transactions can be invalidated if entered into during the period starting on the day which is 270 calendar days prior to the declaration of insolvency by a competent court (*see Question 10*).

In addition to the above considerations, a presumption exists that the following transactions are executed in fraud of creditors, unless the debtor proves good faith:

- Creation of a new security interests or the increase of any existing security interests if the original obligation did not contemplate the foregoing.
- Payments made with assets other than money if such form of payment was not originally agreed.
- Transactions entered into by a debtor with related individuals or entities, including:
    - its spouse;
    - concubine (that is, long term unmarried partner);
    - relatives;
    - members of the board or decision-making individuals within the business; or
    - companies where at least 51% of their capital stock is owned or voted by any of the above individuals.

The LCM provides for events during which a director or managing officer will become accountable or liable to the debtor, for the benefit of the estate of the company in a *concurso* procedure, for any damages and losses of anticipated earnings caused by any unlawful decision they had made, provided they cause damage to the estate of the debtor that led to the insolvency situation of the company. This is regardless of any liability incurred by the director or managing officer under any other law.

Except where good faith and compliance with the duties of care and loyalty can be shown, members of the board of directors of the debtor are liable for damages and losses due to some of the following activities:

- Voting in board meetings or making decisions regarding the estate of the debtor when conflict of interest is involved.
- They favour a shareholder or group of shareholders in detriment of the remaining shareholders.
- They obtain, due to their position and without legitimate cause, direct or indirect economic benefits.
- Produce, publish, provide or order information they acknowledge is false.
- Order or cause to omit the registration of operations carried out by the debtor or modify the registry to conceal the real nature of the operations carried out affecting any concept of the financial statements.
- Order or accept the registration of false information in the debtor's books.
- Destroy, modify or order the destruction or modification of systems or accounting registries or the documentation on which these are based.
- In general commit, malicious or illegal acts.

This also applies to relevant employees of the debtor.

Additionally, criminal liability can be pursued against the members of the debtor's board of directors, administrators, managers or liquidators of the legal entity, who were the authors of, or participated in, the criminal offence, if any. In practice, in certain cases such liabilities are commonly enforced.

## Parent entity (domestic or foreign)

The *concurso* procedures of companies that are part of a corporate group are cumulative, but are handled separately.

The entities considered as part of a corporate group are the holding corporations and subsidiary corporations.

Debtors that are a part of the same corporate group can simultaneously request the joint judicial *concurso* decree, without the need for estate consolidation. For the joint *concurso* procedure it is sufficient that one of the parties of the group is under the assumptions of insolvency under the LCM, and that such a condition places one or more of the parties forming the corporate group under the same situation.

Creditors of debtors that are part of a group that meet the above assumptions, can claim the joint judicial *concurso* procedure. The joint judicial *concurso* procedure can be cumulative with other *concurso* procedures.

# Setting aside transactions

## 10. Can an insolvent debtor's pre-insolvency transactions be set aside? If so, who can challenge these transactions, when and in what circumstances? Are third parties' rights affected?

In cases of setting aside by the seller that received a part of the price, the setting aside is subject to the condition that the portion of the price already received is refunded. The price refund must be made in proportion to its aggregate amount, about the quantity or number of goods set aside.

The seller and the other parties seeking the setting aside must previously refund everything that was paid or which is owed as taxes, transportation, commissions, insurance, gross average and goods preservation expenses

Regarding the existence or identity of the goods who's setting aside is requested, the following must be taken into consideration:

- Any setting aside actions will proceed only when the goods are in the Businessman's possession from the moment of the *concurso* procedure declaration.
- Should the goods perish after the *concurso* procedure declaration and they were insured, the party seeking the setting aside shall be entitled to the payment of any recovery received or to assume the rights to claim such recovery.
- If the goods were sold before the *concurso* procedure declaration was issued, it is not allowed to set aside the price received; however, if payment was not made, the parties seeking the setting aside can assume any rights against the third party buyer, and, if so, must deliver to the Estate any excess amount resulting from whatever he collected and the amount of his credit.
- In the second event, pursuant to the preceding paragraph, the party seeking the setting aside may not hold himself as creditor in the *concurso* procedure.
- Any goods that were transmitted, received as payment or exchanged for any other legal title, similar to those that can be set aside, can be set aside.
- The identity test can occur even if the goods were taken out of their packing, were removed from their packaging or partially sold.
- Provided that any separable goods were pledged to third parties in good faith, the pledge may object to the delivery as long as he has not paid guaranteed obligation and any related amounts to which he can be entitled.

The setting aside can be subject to the condition that the parties seeking the setting aside previously fulfill their obligation as a result of such goods.

## Carrying on business during insolvency

**11. In what circumstances can a debtor continue to carry on business during rescue or insolvency proceedings? In particular, who has the authority to supervise or carry on the debtor's business during the process and what restrictions apply?**

During the conciliation stage, the debtor can continue its ordinary course of business with a conciliator reviewing the debtor's operations and accounting. In principle, the debtor keeps management of its business, unless the conciliator requests the court to remove the debtor in order to protect the pool of assets. With some exceptions, any contractual stipulation, which due to the filing of a voluntary petition for *concurso* or the issuance of the declaration of insolvency sets modifications that worsen the contract terms for the debtor, is deemed not included.

If the debtor retains management, the conciliator will:

- Supervise the accounting and all transactions performed by the debtor.
- Decide if any existing agreements binding on the debtor must be terminated.
- Approve, with the prior opinion of the interveners appointed by the creditors, new credits in favour of the debtor, the creation of new security interests, the substitution of any existing security interests or the sale of any assets not involved in the ordinary course of business of the debtor.
- Call the board or any other decision-making committee of the debtor to discuss and approve any kind of matters relating to the debtor's business.

If debtor is removed from the management of its business, the conciliator will become the administrator and will be granted full authority to conduct the business, on the understanding that the authorities of the debtor and its decision-making committees will cease. The conciliator can also request the court to suspend the debtor's operations if the pool of assets or an increase in the debtor's liabilities is at risk. The court can adopt measures to safeguard assets of the debtor for the benefit of the creditors and assure that no actions are taken outside the ordinary course of business.

## Additional finance

**12. Can a debtor that is subject to insolvency proceedings obtain additional finance both as a legal and as a practical matter (for example, debtor-in-possession financing or equivalent)? Is special priority given to the repayment of this finance?**

Debtors can obtain financing while in insolvency, subject to the judge and conciliator's approval to preserve the ordinary course of business and to provide the required liquidity during the procedure and by following certain rules provided under the Mexican insolvency law (LCM). The lender can be certain that any loan they grant to such debtor will be repaid before any other loan, under the order of preference rules provided in the LCM. This special or urgent financing is deemed as a claim against the estate of the debtor and has preference over common creditors. It is aimed at preserving the ordinary course of business and providing the required liquidity during the *concurso* procedure. However, the dip financing does not have preference over already secured creditors; the new rules include possible loans with priority liens but cannot affect existing priority secured creditors (with mortgages and pledges over certain assets).

## Multinational cases

**13. What are the rules that govern a local court's recognition of concurrent foreign restructuring or insolvency procedures for a local debtor? Are there any international treaties or EU legislation governing this situation? What are the procedures for foreign creditors to submit claims in a local restructuring or insolvency process?**

### Recognition

Local creditors and foreign creditors will always be treated equally under Mexican law, without any different treatment. Moreover, the Constitution contains the general principle of law that everyone must be treated equally. All creditors of the debtor, whether domestic or foreign, can have access to the *concurso* procedure, and will collect in equal proportion (according to the class) from the assets located within the territorial jurisdiction of the court. According to the Mexican insolvency law (LCM), a foreign proceeding is defined as a collective or universal proceeding, whether judicial or administrative, including provisional proceedings, followed in a foreign state under a law governing bankruptcy, liquidation, or insolvency matters of the debtor. Because of these proceedings, the property and

businesses of the merchant can be subject to the control or supervision of a foreign court, for purposes of reorganisation or liquidation.

The LCM recognises foreign proceedings in bankruptcy, insolvency and reorganisation matters, and it recognises foreign representatives appointed through a recognition request. In this regard, the LCM recognises foreign proceedings when legally held in a foreign country in accordance with bankruptcy or insolvency laws applicable to the debtor due to its activities, the location of assets or other similar causes.

Under the LCM a "foreign representative" is the individual or entity that has been:

- Empowered under a foreign bankruptcy procedure to administrate the reorganisation or settlement of the business.
- Designated as the representative of such foreign bankruptcy procedure.

The LCM states that any representative of a foreign bankruptcy procedure can request the presiding Mexican court for the recognition of the foreign bankruptcy procedure during a *concurso* procedure.

Under the LCM, any foreign representative is entitled to appear directly before the presiding Mexican court in all procedures brought under the LCM. Such a filing should be made by means of an interlocutory procedure before the civil federal court knowing of the *concurso* principal proceeding. The interlocutory recognition procedures follow the following stages:

- Delivery of a copy of the recognition request to the creditors who have appeared at the procedure abroad, so that within the term of five days, they declare which is in their best interest. The foreign representative's allegations will be taken as certain in the case of the creditors who fail to deliver their reply during the term specified for such effects.
- Evidence will be offered in the interlocutory claim and in the interlocutory reply.
- Once the term of the five days has elapsed, the Mexican court will summon the parties to a hearing of proofs and pleas that will be held within the ten following days.
- When offering expert or testimonial tests, at the time of offering the test, one copy of the interrogations will be exhibited to each one of the parties so that they can formulate verbal or written questions when verifying at the hearing. Three witnesses are allowed for each fact. The Mexican court can designate an expert or those that it considers necessary, in order to render joint or separate opinions with the parties'

experts. With the purpose that the parties produce their proofs at the hearing, the authorities or civil employees have the obligation to dispatch them promptly.

- Once the hearing is concluded and within the term of three days and without summons, the Mexican court will pronounce the interlocutory judgment relative to the recognition of a foreign procedure.

In terms of the LCM, there are two ways under which a Mexican court can recognise a foreign bankruptcy procedure:

- As a principal procedure, when the foreign procedure is brought to a court with jurisdiction in the place where the business has its main place of interests.
- As a non-principal procedure, when the foreign procedure is brought to a court with jurisdiction in the place where the business has an establishment.

The main difference between the recognition of a foreign bankruptcy procedure as a principal procedure or as a non-principal procedure is in the direct effect of such recognition over the business's assets located in Mexico.

Under the LCM, if a foreign bankruptcy procedure is recognised as a principal procedure, any and all foreclosure over the business's assets, and any and all rights to transfer or grant any lien over business' assets, will be suspended.

A Mexican court will recognise the foreign bankruptcy procedure as a non-principal procedure if the debtor has a permanent place of business outside Mexican territory, but not as a principal foreign bankruptcy procedure.

The recognition aspects of a non-principal foreign bankruptcy procedure are as follows:

- The granting of appropriate injunctions that concede to a Mexican court to protect the business's assets or the creditors' interests, who may request through the foreign representative, that the receiver, conciliator or examiner, as the case may be:
    - suspends all execution injunctions against the business assets;
    - suspends the rights exercised to transmit or to mortgage the business assets, as well as to dispose of such assets in any other way;
    - orders the delivery of evidence or the provision of information regarding the business's assets, activities, rights, or liabilities of the business;
    - entrusts the foreign representative, the receiver, conciliator or examiner, with the administration or foreclosure of all or part of the business' assets located in Mexican territory;

- extends every granted injunction granted by the foreign recognition procedure request; and
- grants any other injunction that under Mexican law can be granted to a receiver, conciliator or examiner.

Once a foreign procedure is recognised, the foreign representative can ask the receiver, conciliator or examiner, to entrust, through a foreign representative, the distribution of all the business' assets located in Mexican territory. The Mexican court must make sure that the creditors' interests that are domiciled in Mexico are sufficiently protected so that it can decree the injunctions briefed above.

The foreign representative has the power and capacity to ask that the examiner, the conciliator or the receiver, initiates the recovery of assets actions for the recovery of assets that belong to the entirety of a property, and of nullity acts concerning the defrauding of creditors. The authorisation of the foreign representative to take part in the procedures promoted against the businessman that are in the proceedings and that have a patrimonial content can take place.

The injunctions that can arise from the recognition of a foreign bankruptcy procedure under a *concurso* procedure depend on the procedural phase, namely as from the filing of the recognition request throughout the corresponding resolution, and as from the issuance of the recognition resolution.

Therefore, provided that the above is followed, if a company organised under the laws of Mexico entered into extraterritorial bankruptcy or insolvency proceedings those proceedings are recognised within Mexican jurisdiction.

## Concurrent proceedings

Courts co-operate with foreign courts where there are concurrent rescue or insolvency proceedings in other jurisdictions. There is actually a title included in the *Concursos* Law that provides for the co-operation with foreign courts. This co-operation will be exercised under the provisions of the LCM by the judge, the Institute or the person appointed by the Federal Institute of Specialists in Mercantile Insolvency and Bankruptcy Procedures (IFECOM).

## International treaties

Mexico is party to numerous international treaties and model laws. With respect to the insolvency matters the international documents that served the most to draft the current

provisions of the LCM are the UNCITRAL Model Law on Cross-Border Insolvency 1997 (UNCITRAL Model Insolvency Law) and the "Effective Insolvency Systems" of the World Bank.

Some of the international treaties to which Mexico is party that are related to insolvency matters are those regarding powers of attorney, judicial requests, request letters, and notifications of judicial or extrajudicial documents in civil and commercial matters.

## Procedures for foreign creditors

Creditors can request the acknowledgment or recognition of their credits as of the date of publication of the declaration of insolvency. Irrespective of the above conditions, the conciliator must provide the court with a provisional list of the debtor's liabilities within 30 days following the last publication of the declaration of insolvency in the *Federal Official Gazette*. The court will provide creditors a short time period for the approval of the list and will issue the judgment for acknowledgment or recognition and preference of credits.

The LCM, in principle, does not expressly recognise (nor does it permit the full participation of) bondholders under an indenture. However, there is nothing preventing the full participation of an individual bondholder, provided that it is able to evidence its claim against the debtor.

As opposed to other jurisdictions where the beneficial holders of bonds and other debt securities often participate directly in the bankruptcies of companies in which they invest, a Mexican company will solely recognise, in principle, the indenture trustee as the holder of the claim, which prevents beneficial bondholders to exercise their right to accept or reject the creditors' agreement. In Mexico, if not properly advised, the beneficial bondholders can face difficulties in exercising the rights that they are afforded abroad (even though the beneficial holders are foreigners, and even though their bonds were issued abroad).

For example, in these foreign insolvency proceedings, the US' indirect holdings system for bonds may confront a foreign legal system in which only a creditor named on a note can sue to enforce that note. In Mexico, the name on the note constitutes the initial creditor taken into consideration. Therefore, initially, the indenture trustee will generally be recognised as the sole creditor under a bond issuance. As a result, foreign investors can encounter difficulty evidencing their support for a restructuring plan, but it will be possible to obtain their recognition by evidencing their individual participations. In Mexico, the "sole creditor" perspective can be redirected through the submission of proper documentary evidence (that is, filing of documents demonstrating the link between the individual bondholder and the

indenture trustee, DTC, DTC participant, nominee name, custodian and so on). In this case, the Mexican court will recognise the individual creditor standing of the bond holder.

## Reform

### 14. Are there any proposals for reform?

As part of an integral financial reform (that is, 13 bills involving 34 statutes), the proposal to the Mexican Congress to reform various articles of the Mexican insolvency law (LCM) was approved and effective from 10 January 2014.

In addition to the provisions already described in this document, the recent amendments provide, among other important matters, the following:

- The officers taking part in the *concurso* procedure must protect the creditors and the interests on the debtor's estate, under the relevance, judicial economy, swiftness, publicity and good faith principles of the law, besides the general principle of keeping companies as a going concern and preventing their general failure to comply with their liabilities.
- Establishing that any *concurso* procedure is public, strengthening the principle of publicity to *concurso* procedures, and allowing any person to request access, at the applicant's cost, to the documents contained in the file or docket, respecting any reserved or confidential information, under the applicable laws.
- Incorporating the joint *concurso* procedures concept.
- Making it feasible that the *concurso* procedure can also be requested or petitioned under any of the insolvency assumptions provided in the LCM, provided that it is imminent the debtor will fail to comply with its liabilities within the following 90 days.
- Making it easier to appoint and approve of the creditors' representatives and give them broader powers in the *concurso* procedure, as an action to protect creditors' rights.
- Expediting the separation or segregation of certain assets from the estate of the debtor.
- Making it legally feasible that in the event of a special guarantee for which the debtor has transferred ownership over certain assets before the filing of a *concurso* procedure, such as a security-pledged loan, then the underlying assets of such security instrument may be immediately applied as a repayment and will not become part of the estate of the debtor.

- Making it feasible for the creditors to exert an action for liability against the debtors' relevant managers or directors and senior officers, in the event of any fraudulent conveyance they might have performed, under the rules to be provided in the LCM.
- Expressly providing that the one-year term to process any *concurso* procedure, in the phase or conciliation or restructuring, cannot be extended.
- Reducing the percentage of creditors needed to appoint a conciliator not included in the lists of the Federal Institute of Specialists in Mercantile Insolvency and Bankruptcy Procedures (IFECOM).
- Ensuring that the debtor has the power to submit its own proposal for a restructuring plan to creditors, a power that was reserved to the conciliator.
- Ensuring that the participation of joint obligors of the main debtor is regulated; that is, regarding rules on third-party joint obligors it would be clearer that valid joint obligations should not be affected by the restructuring of the main debtor.
- Rules on the applicable jurisdiction of competent courts in the event of collective or consolidated proceedings of related parties.
- Reducing the percentage of acknowledged creditors required to request that the receiver is replaced.
- Providing a requirement to place a guarantee or bond if the judgment declaring the debtors' *concurso* procedure, following a voluntary petition, is appealed.

## Online resources

### Federal Institute of Specialists in Mercantile Insolvency and Bankruptcy Procedures (IFECOM)

**W** www.ifecom.cjf.gob.mx

**Description.** Official website of the Federal Institute of Specialists in Mercantile Insolvency and Bankruptcy Procedures.

### Chamber of Deputies (Camára de Diputados)

**W** www.diputados.gob.mx/LeyesBiblio/index.htm

**Description.** Official website of the Chamber of Deputies, including the text of federal laws in force (this list is up-to-date and maintained).

## Contributor details


### Alejandro Sainz Orantes, Partner

**Cervantes Sainz, SC**

**T** +52 5591 7850 54

**E** asainz@cervantessainz.com

**W** www.cervantessainz.com


**Professional qualifications.** Mexico, Lawyer

**Areas of practice.** Corporate; transactional; restructuring and insolvency; mergers and acquisitions.