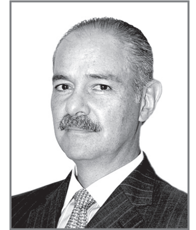
This article appeared in slightly different form in the May 2006 issue of the *International Financial Law Review*.

Mexican Insolvency Put to the Test



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Restructuring discussions among Satélites Mexicanos, S.A. de C.V. ("Satmex") and its principal creditors went on for a frustrating period of nearly two years. Overwhelmed by seemingly insurmountable obstacles, holders of a majority Satmex's Senior Secured Floating Rate Notes due 2004 (the "FRNs") and holders of more than two-thirds of its 10 1/8 percent Senior Notes due 2004 (the "HYBs" and, collectively with the FRNs, the "Creditors"), brought an involuntary bankruptcy procedure in the US Bankruptcy Court for the Southern District of New York in late May 2005.

Satmex is a regulated Mexican corporation, subject to the principal provisions of the Federal Telecommunications Law of Mexico. Prior to its privatization in late 1997, Satmex was operated by the Mexican government. Satmex was awarded three orbital concessions and a fourth which allows the Company to base its ground station equipment within the telecommunications facility that belongs to the Mexican Government. It is a Mexican taxpayer, and its workers enjoy the many benefits embodied by the labor laws of Mexico. Primary jurisdiction by a US bankruptcy court would certainly be contested in heated debates.

Yet given that the Government holds an interest as an equity holder and as a creditor of Satmex's parent company, in addition to its role as regulator, the Creditors—which represent 98 percent of the total indebtedness of the Company—were concerned that any hearings held in Mexico might be biased, which why they felt moving the jurisdiction to the US was warranted. In addition, there was an inherent mistrust of the rigid Mexican procedural practice and, to some extent, in the judiciary itself. Although Mexico enacted a new, much improved insolvency statute ("*Ley de Concursos Mercantiles*", *the "Concurso Law*") in May 2000, many provisions remain relatively untested and other than in the case of a consensual plan arrived at within the Concurso Law with respect of Grupo Industrial Durango, and to a lesser extent, the insolvency proceeding of construction consortium Grupo Tribasa, it has not been applied in cases of massive debt held almost exclusively by non-Mexican securities holders. To complicate matters, the holders of the existing US$203.4 million of FRNs held a comprehensive security package over the orbital concessions of Satmex, its satellites—including its state of the art Satmex 6, sitting in the manufacturers premises in Palo Alto, California and being prepared for launch in French Guyana—and its operating assets. Furthermore, all shares owned by Satmex's parent were

placed in a Trust for the benefit of FRNs. Indeed, the interests of the FRNs and the HYBs, were often at odds, given the obvious preferences in the event of a liquidation.

The fact that the principal technology supplier and foreign indirect shareholder of Satmex, Loral Space & Communiations, Ltd. ("Loral"), was itself in the final stages of a voluntary Chapter 11 procedure, added to the complexity of the case.

In late June 2005, Satmex responded by seeking the protection of the Federal Courts in Mexico, through a voluntary filing under the Concurso Law. In September, the Mexican Bankruptcy Court declared the Company in *concurso mercantil* (*i.e.*, in a state of insolvency) under the Concurso Law.

With the support of the Federal Institute of Insolvency Specialists, an agency of the Federal Judiciary known by its Spanish anacronym, *IFECOM*, and pursuant to a new untested section of the Concurso Law, private sector restructuring lawyer Thomas Heather, a partner with White & Case in Mexico City, was appointed "*conciliador*", an insolvency administrator, at the request of Mexico's Ministry of Communications and Transportations.

The restructuring phase under the Concurso Law thus commenced in mid October, 2005 under the responsibility of the *Conciliador*, who began discussions with and soon developed a close working relationship with the Creditors, the Ministry, Satmex, Loral and the many lawyers involved in the process, both in Mexico as well as in New York.

The involuntary Chapter 11 proceeding was withdrawn and an ancillary proceeding to the *Concurso Mercantil* was commenced pursuant to Section 304 of the Bankruptcy Code in the US Bankruptcy Court for the Southern District of New York, in order to protect the assets of Satmex—mainly the Satmex 6 satellite- in the United States.

It took a substantial team effort approach by all stakeholders, including the Ministry, to reach a first definitive milestone: a basic understanding in February of 2006, which after weeks of intense negotiations and marathon sessions, culminated in the signing of a comprehensive restructuring agreement in early April (the Agreement).

The Agreement resolved numerous implementation issues and provides a clear blueprint for effectuating the successful restructuring of Satmex. The Agreement does provide for the filing with, and approval by, the Mexican court where the Company's *concurso mercantil* proceeding is pending, of a *concurso plan*, which in turn, will provide for the final implementation of the restructuring through a pre-negotiated bankruptcy plan under Chapter 11 of the US Bankruptcy Code. This complex combination, based on the preeminence of the concurso plan, but requiring further implementation through Chapter 11, was devised to provide certainty that the restructuring, as agreed in April, will become fully effective.

Many practical considerations have arisen from this complex matter. Certainly borrowers must take into account the consequences and the expense of accessing a mature capital market, and in particular, those arising from the registration of securities in the United States. While the market is extremely broad and deep, investors in the distressed debt arena have very different objectives as compared to those of commercial banks. Accounting and tax repercussions are very different. In addition, issuers and creditors alike should carefully consider whether a trustee is advisable over a paying or collateral agent, and if clauses requiring unanimity are inherently equitable or not. Furthermore, creditors should clearly understand the limitations in respect of the exercise of collateral rights, when such exercise may impact the rendering of a public service. Clauses dealing with advisors—legal, financial and otherwise—and the reimbursement of fees and expenses must be looked at closely as their impact on an extended and difficult restructuring will have a substantial impact on the continuing viability of a troubled borrower. Choice of law and jurisdiction clauses must be analyzed on a case by case basis. Finally, regulators, shareholders, and stakeholders generally, should give careful consideration to the manner in which their respective interests interact, specially in periods of financial strain.

There are solid reasons to expect a final, successful conclusion of the Satmex restructuring. Nevertheless, the *concurso mercantil* of Satmex's parent is in its initial stages, and because the consummation of Satmex's restructuring will satisfy all of Satmex's holding Company's obligations to the Mexican Government, both processes are inevitably interrelated. All in all, progress to date has been the result of a massive team effort by all parties concerned and is definitively a positive example of cross-border legal cooperation.

Thomas S. Heather is a partner in White & Case's Mexico City office. Mexico's Communications Ministry appointed Heather as mediator in the SatMex restructuring.

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