

1991

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### Recommended Citation

Carsten T. Ebenroth & Rüdiger Woggon, *The Development of the Equal Treatment Principle in the International Debt Crisis*, 12 MICH. J. INT'L L. 690 (1991).

Available at: <https://repository.law.umich.edu/mjil/vol12/iss4/2>

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# THE DEVELOPMENT OF THE EQUAL TREATMENT PRINCIPLE IN THE INTERNATIONAL DEBT CRISIS

*Carsten Thomas Ebenroth\* and Rüdiger Woggon\*\**

## I. INTRODUCTION

Since the outbreak of the international debt crisis at the beginning of the 1980s, debtor countries have reached a series of agreements with private creditor banks, with the aim of reducing the financial strain on the debtor countries and enabling them to service their debts. Long-term extensions of maturities are a central aspect of many of these arrangements. Included in the restructurings are all the medium- and long-term claims of the creditor banks, often short-term trade credits and interbank lines, and, in individual cases such as the restructuring of the debts of Poland, Yugoslavia, Costa Rica, and some African States, bonds as well.<sup>1</sup> In addition, the restructuring packages often include the provision of new credits, in order to maintain, at least for a time, the liquidity of the debtor countries.

A further characteristic of the arrangements is the introduction of a series of financial innovations — debt equity swaps, onlending, relending, and redenomination in currencies other than that of the original loan, with adaptation to the corresponding market rate of interest — and, particularly very recently, partial remission of debt.<sup>2</sup> And yet, to date little progress has been made in solving the problem of indebtedness or in enabling the debtor countries to return to the international financial markets.

Although the countries that are mainly affected, the deeply indebted developing countries, naturally continue to depend on a trans-

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1. Mauger, *Sovereign Debt Restructurings: The Practical Background*, 2 J. INT'L BANKING L. 100, 111 (1986); Clark, *Sovereign Debt Restructurings: Parity of Treatment between Equivalent Creditors in Relation to Comparable Debts*, 20 INT'L LAW. 857 (1986).

2. See Berger, *Neue Ansätze im Schuldenmanagement für Entwicklungsländer*, 1988 SPARKASSE 123; INTERNATIONAL MONETARY FUND, INTERNATIONAL CAPITAL MARKETS - DEVELOPMENTS AND PROSPECTS 55 (Jan. 1988).

fer of resources from the industrialized countries, they have, at the same time, become net exporters of capital.<sup>3</sup> Apart from its impact on the export industries of the industrialized countries, the consequent drastic reduction in imports hindered the economic adjustment of the debtor countries. Imports of capital and intermediate goods, which enter into the domestic production process, had to be curtailed. Since the developing countries were not able to replace these imported production factors with domestic ones, economic growth was hampered.<sup>4</sup> Therefore, without debt reduction or new financing, the ability to service debts deteriorated further.

The current debt strategy, which is based on the Brady Initiative, a set of proposals named after the United States Secretary of the Treasury who launched them, consequently requires the creditor banks to combine debt relief and new credits.<sup>5</sup> The banks, however, have not adopted a uniform policy in deciding which measures should be put into practice. Their responses depend on a variety of factors. Apart from varying subjective assessments of future developments in the debtor countries, the general earnings situation of the creditor banks, and their long-term interests in particular debtor countries, an important role is played, above all, by the differences in the overall legal framework in their countries of domicile. The banks are subject to different banking, accounting, and tax regulations, four examples of which will now be outlined.

#### A. *United States*

For U.S. banks, provision against risk is only tax deductible in the case of country risks within the framework of the officially prescribed Allocated Transfer Risk Reserves. The body responsible for implementation is the Interagency Country Exposure Review Committee (ICERC), which the federal authorities responsible for the supervision of banks — the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (FED), and the Federal Deposit Insurance Corporation (FDIC) — called into being.<sup>6</sup>

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3. WORLD BANK, 1 WORLD DEBT TABLES 1989-1990, at 124 (1989).

4. *Recent Trends in International Technology Flows and their Implications for Development Report by the UNCTAD Secretariat*, U.N. Doc. TD1B1 C.6/145 (Aug 18, 1988).

5. Treasury Secretary Brady, Remarks to the Brookings Institution and the Bretton Woods Committee Conference on Third World Debt, Washington, D.C., Mar. 13, 1989 *reprinted in* Deutsche Bundesbank Auszüge aus Presseartikeln Mar. 13, 1989, at 7 [hereinafter Brady]. See also Mulford, *The Ideas for Strengthening the International Debt Strategy*, in RESTORING FINANCIAL FLOWS TO LATIN AMERICA: COMBINING DEBT REDUCTION WITH THE STIMULATION OF NEW FINANCING 37 (NMB Bank ed. 1989).

6. For a detailed treatment, see Ebenroth & Wolff, *Bankaufsichtsrecht und Forderungshandel mit Umschuldungsländerkrediten als Auswege aus der Verschuldungskrise*, 89 ZEITSCHRIFT FÜR

To date, however, the ICERC has prescribed the creation of such reserves for claims against only fourteen debtor countries. With the exception of Argentina and, since June 1990, Brazil, these are all states with relatively small amounts due to U.S. banks.<sup>7</sup> In addition, the banks are able to create Allowances for Possible Loan Losses (APLL), which are not tax-deductible. The lack of recognition for tax purposes makes the creation of these reserves expensive. In terms of capital requirements that define the ratio of a bank's capital to its assets, the APLL were included in the definition of regulatory capital up to the end of 1990.<sup>8</sup> A reduction of these reserves as a result of remitting a claim led, consequently, to a lowering of the lending limit.

Where corresponding reserves have not already been created, the so-called "ninety-days-rule" has specific financial effects. If the repayment of interest on a loan is overdue for ninety days or more, the banks must stop accruing interest on the loan; in addition, the past interest arrears must be deducted from the earnings of the quarter.<sup>9</sup> As the costs of cover financing continue to accrue, the classification of a loan as nonaccrual causes a loss.

On the whole, therefore, the overall legal conditions to which U.S. banks are subject favor the provision of new credits rather than the remission of debts. Most banks have, however, increased their room for maneuvering in recent years by creating allowances for possible loan losses. For the middle of 1989 the average reserves of the Money Center Banks were estimated at fifty-eight percent and those of the regional banks as high as sixty-five percent.<sup>10</sup>

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VERGLEICHENDE RECHTSWISSENSCHAFT 8 (1990); J. WULFKEN, JURISTISCHE STRUKTUREN UND OKONOMISCHE WIRKUNGEN VON DEBT EQUITY SWAPS 74-77 (1989).

7. The states concerned are Argentina, Bolivia, Brazil, Costa Rica, the Dominican Republic, Ecuador, the Ivory Coast, Liberia, Nicaragua, Panama, Peru, Poland, the Sudan, and Zaire. See J. HAY & M. BOUCHET, THE TAX, ACCOUNTING AND REGULATORY TREATMENT OF SOVEREIGN DEBT 24 (Washington D.C. World Bank 1989); Neue US-Bonitätseinstufungen, NEUE ZÜRCHER ZEITUNG - FERNAUSGABE, May 15, 1990, at 14, col. 4; *Brazil's Trade Lines "Substandard"*, INT'L FIN. REV., July 21, 1990, at 25, col. 1.

8. In accordance with the Basel Agreement on capital adequacy, only 1.5% of the Allowances for Possible Loan Losses will be included in the regulatory capital beginning in 1991, and only 1.25% beginning in 1993. See M. CREMER, MÖGLICHKEITEN UND GRENZEN PRIVATRECHTLICHER VERTRÄGE ALS INSTRUMENT ZUR BEILEGUNG STAATLICHER INSOLVENZKRISEN - NEUE ANSÄTZE IN DER ENTWICKLUNG EINES INTERNATIONALEN RECHTS DER STAATINSOLVENZ 81 (1990); J. HAY & M. BOUCHET *supra* note 7, at 26.

9. M. CREMER, *supra* note 8, at 89-90; J. HAY & M. BOUCHET, *supra* note 7, at 19; M. BOTHE, J. BRINK, C. KIRCHNER & A. STOCKMAYER, RECHTSFRAGEN DER INTERNATIONALEN VERSCHULDUNGSKRISE 224 (1988) Baumann & Harvey, *LDC Debt Strategies: Accounting and Tax Issues*, BANK ACCT. & FIN., Summer 1989, at 3, 12-13.

10. WORLD BANK, *supra* note 3, at 54.

### B. Japan

Protection against risk is even more difficult in the case of Japanese banks. Two possibilities have to be distinguished. On the one hand, for high-risk claims, a fifty percent reserve can be created, which is recognized for tax purposes and not treated as a part of the regulatory capital. Originally, it only applied to claims against private debtors, but it was extended to include sovereign debtors in March 1988. It is a precondition, however, that a declaration of default has been made or that no payments whatsoever have been made on the claim in the past three years.<sup>11</sup> On the other hand, country risks arising from claims against third world debtors may be covered by so-called "Reserves for Specified Overseas Receivables." These reserves were formerly subject to a limit, which was raised from fifteen percent to twenty-five percent in January 1990, and not abandoned until June 1990.<sup>12</sup> The reserves are recognized for tax purposes only to the extent of one percent and, as with the allowances for possible loan losses in the United States, they were fully included in regulatory capital until the end of 1990.<sup>13</sup>

A certain degree of relief from these restrictive regulations was made possible by the foundation of the Japanese Bankers' Investment Association by twenty-eight Japanese banks in the Cayman Islands in 1987. It was founded with the approval of the Japanese Ministry of Finance, which in individual cases permits the sale of claims below nominal value to this corporation, while recognizing the resultant losses for tax purposes.<sup>14</sup> Consequently, by the middle of 1989, Japanese banks were able to dispose of claims against Brazil, Mexico, and Argentina with a nominal value of approximately \$1.5 billion. It should be noted, however, that the total of the claims of all Japanese banks in regard to these three countries alone amounts to approximately \$25 billion.<sup>15</sup> All in all, therefore, Japanese banks' country risk provision is very slight.

### C. United Kingdom

In the United Kingdom, provision against country risks is organized on a matrix system, which has been developed by the Bank of

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11. See J. HAY & M. BOUCHET, *supra* note 7, at 91-92. As a general rule, however, neither of these two conditions is met in the case of the Third World claims under consideration here.

12. See *Japans Grossbanken erhöhen Dritte-Welt-Reserven*, *Neue-Zürcher Zeitung - Fernausgabe*, June 21, 1990, at 12, col. 1.

13. INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT, *supra* note 7, at 92-93.

14. Evans, *Japan's Debt and Tax Anomalies*, *EUROMONEY*, Sept. 1987, at 89; J. HAY & M. BOUCHET, *supra* note 7, at 94.

15. J. HAY & M. BOUCHET, *supra* note 7, at 97.

England since 1987. It involves an assessment of claims against problematic debtor countries on the basis of debt restructuring, postponement of payments, payment policies, and economic situation of the countries concerned.<sup>16</sup> The revised matrix of January 1990 requires the creation of reserves, to the amount of fifty percent on average<sup>17</sup>, which are not part of the capital resources.<sup>18</sup> The matrix is not binding on the Inland Revenue, the British taxation authority, but the Inland Revenue does at least accept it as the basis for recognition, for tax purposes, of sums reserved for medium and long term claims.<sup>19</sup>

In comparison to the United States, therefore, there are more favorable opportunities to provide against risk and, consequently, to remit debts. The provision of new credits can, however, be rendered more difficult by the compulsion to create new reserves for them.

#### D. Federal Republic of Germany

In Germany there are no concrete guidelines similar to the matrix of the Bank of England or the prescriptions of the U.S. ICERC for Allocated Transfer Risk Reserves. Under the terms of commercial law, with its minimum value principle, write-downs must be made at the market price or the "estimated value" by revaluating individual loans as to their future collectibility.<sup>20</sup> Thereby, the banks concerned have a considerable margin of assessment.<sup>21</sup>

This approach via commercial law is accepted for tax purposes in as far as the amount involved does not fall below the fractional value as defined by § 6, cap. 1, N 2 Income Tax Code. An important guide for the determination of the fractional value is provided by two decisions taken by the Financial Court of Hesse in 1982 and 1983.<sup>22</sup> In response to newspaper reports, according to which Poland would not be able to repay western bank loans in the foreseeable future, a value adjustment of fifty percent on claims against the Polish state bank,

16. See U. MESSER, RECHTLICHE RAHMENBEDINGUNGEN FÜR DIE BETÄTIGUNG VON GESCHÄFTSBANKEN IM INTERNATIONALEN FORDERUNGSHANDEL 118-19 (1989); *Who's Leading Who?*, INT'L FIN. REV., Feb. 3, 1990, at 20, col. 1; J. HAY & M. BOUCHET, *supra* note 7, at 102.

17. Some examples of the levels are: Argentina 76-89%, Brazil 59-75%, Chile 14-23%, Mexico 24-37%, and Venezuela 38-58%. See *Recommended Provisioning Level for UK Banks*, INT'L FIN. REV., Feb. 17, 1990, at 32, col. 2.

18. J. HAY & M. BOUCHET, *supra* note 7, at 102.

19. See U. MESSER, *supra* note 16, at 123-24; J. HAY & M. BOUCHET, *supra* note 7, at 107; *Tax Relief Changes*, INT'L FIN. REV., March 24, 1990, at 35, col. 3.

20. German Commercial Code, § 253, cap. 3.

21. M. CREMER, *supra* note 8, at 100.

22. Court order of Aug. 25, 1982, W. Ger., 1983 BETRIEBS BERATER [BB] 228; Judgment of Sept. 16, 1983, W. Ger., 1984 BB 36.

Bank Handlowy, was approved. These decisions were accepted by the financial authorities and now also serve as the basis for the assessment of other country risks.<sup>23</sup> It has been estimated that by the middle of 1989, German banks had in this way created tax deductible reserves averaging fifty-five percent for their claims against problematic debtor countries.<sup>24</sup>

According to § 10, cap.2 Kreditwesengesetz (Banking Act), these valuation allowances do not form part of the regulatory capital. They are, however, deducted from the nominal value of the credits advanced in the assessment of the equity ratio, in accordance with Principle 1, cap. 1 of the Principles on Capital Resources and the Liquidity of Credit Institutes.<sup>25</sup>

Thus, German banks are, on the one hand, in a relatively favorable position to prepare themselves for a reduction in their claims by means of adequate precautions against risk; on the other hand, because of the room for maneuvering they have, they are not automatically obliged when evaluating claims to accept write-downs on new credits.

In spite of the different interests of the creditor banks that necessarily follow from this situation, an attempt has been made in debt management to date to maintain equal treatment of all creditors. In order to prevent a "litigation race" between the banks, deviation from a joint strategy needed to be avoided; until recently there were virtually no plans to concede preferential treatment to banks that showed willingness to make an additional contribution to the solution of the crisis. Instead, the clauses guaranteeing equal treatment of all creditors in the original syndicated loans were in the main accepted and in part even extended. In what follows, the basic form of the legal measures adopted to ensure equal treatment will first be outlined (II), and then the steps that have been taken since 1985, particularly in the most recent round of debt restructuring, to permit more flexible debt management will be presented (III).

## II. CLAUSES GUARANTEEING EQUAL TREATMENT OF CREDITORS

### A. *Sharing Clauses*

International syndicated credit contracts frequently contain a so-

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23. Schobert, *Wertberichtigungen auf Auslandsforderungen, insbesondere bei Kreditinstituten*, 1986 DIE STEUERLICHE BETRIEBSPRÜFUNG 73, 76; M. CREMER, *supra* note 8, at 105.

24. WORLD BANK, *supra* note 3, at 54.

25. Bekanntmachung Nn. 1/69 of the Bundesaufsichtamt für das Kreditwesen of Jan. 20, 1969 (BANz. No. 17), most recently modified in the Bekanntmachung of May 15, 1990 (BANz No. 92).

called sharing clause<sup>26</sup>. This serves to ensure an equal internal distribution of the debtor's payments on interest and principal among all the banks involved in a particular syndicated credit. This is achieved, in the first place, by one bank, the so-called agent bank, functioning as the collecting bank and then passing the funds received on to the other banks in accordance with their share. This system ceases to function, however, the moment the debtor breaches the agreement and makes payments directly to the creditors without concern for equal treatment of all creditors. Consequently, in its original form, the sharing clause provided that all those banks that had received a proportionally higher amount than others must pay the excess amount to the agent bank, which then ensured a correct distribution. A variant of this, mostly found in contracts drawn up by American lawyers, does not foresee redistribution by the agent bank, but instead, obliges the banks having obtained more than a *pro rata* repayment to acquire participations from the other banks.<sup>27</sup>

A modification was made in the sharing clause as a result of developments during the Iran crisis. When, after the fall of the Shah, Iran failed to meet its commitments to a banking syndicate led by the Chase Manhattan Bank, some of the U.S. banks satisfied their claims by setting off their losses against the foreign assets Iran held with them. They were able to turn down the subsequent sharing request of the other banks, as no payments had actually been made by Iran. Since then, sharing clauses not only include payments by the debtor, but also other methods of compensation; for example, through set-offs, litigation, or the exercise of liens.<sup>28</sup> In connection with payments of the debtor made only as a result of legal proceedings, it is sometimes provided that the sharing bank is not obliged to share if it has informed the other banks of its intention to take legal action, and those banks have not accepted the invitation to join the litigation.<sup>29</sup>

In this form the sharing clause was included in debt restructuring agreements. On one point, however, a change was necessary, as re-

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26. The sharing clause from the MEXICAN NEW RESTRUCTURE AGREEMENTS OF 1985 is reprinted as an example in Appendix I.

27. On the advantages and disadvantages of this arrangement, see Walker & Buchheit, *Legal Issues in the Restructuring of Commercial Bank Loans to Sovereign Borrowers*, in SOVEREIGN LENDING: MANAGING LEGAL RISK 139, 144 (1984).

28. See the MEXICAN NEW RESTRUCTURE AGREEMENT OF 1985, at § 5.03(b), *infra* Appendix I.

29. For details on the development and content of the clause, see Brown, *Sharing Strains on Euromarket Syndicate*, INT'L FIN. L. REV., June 1982, at 4-8; L. HINSCH & N. HORN, DAS VERTRAGSRECHT DER INTERNATIONALEN KONSORTIALKREDITE UND PROJEKTFINANZIERUNGEN 167-70 (1985); Youard, *Enough is Enough*, EUROMONEY, Nov. 1983, at 107; M. CREMER, *supra* note 8, at 139-150.



structuring agreements generally involve a series of syndicated and single credits. Consequently, the tasks of the existing agent banks have been centralized and transferred to a single bank, usually described in the restructuring agreement as the servicing bank. At the same time, of course, the number of banks among whom the payments of the debtor are to be redistributed, and the number who might be affected by the obligation to share, has increased.

There is disagreement among the banks about the significance of a sharing clause when the debtor does not make payments in the agreed currency, but secures the acquiescence of single creditor banks in payment in the local currency, for example, in connection with debt-equity swaps, debt-for-product swaps, or debt-for-bond swaps. The contracts do not deal expressly with this question, as there was no need before the outbreak of the debt crisis. The expression "payment" used in most of the sharing clauses is not, however, necessarily restricted to the delivery of money, but may also be applied generally to any kind of performance.<sup>30</sup> As the question has not yet been clarified legally, any bank participating in a debt swap runs the risk of being required to share if no explicit exception is made in the agreement.<sup>31</sup>

An important point in connection with set-offs is that every bank can choose for itself which claims to offset. If, therefore, it has other claims which are not part of the syndicated credit agreement, it may offset them without being subject to the sharing requirement. Accordingly, the choice made by a bank is of decisive importance, if it is involved in several syndicates.<sup>32</sup> It will primarily offset its claims from that syndicated credit in which it has the largest proportional share in relation to the other creditors, in this way ensuring that it must remit a relatively smaller quota.

It is, moreover, customary in the agreements to provide for the possibility of exemption from the sharing clause, either by means of a waiver valid only in individual cases or through an amendment to the agreement. In both cases, however, the agreement of all the creditors or of a majority of at least ninety percent of the individual banks, weighted on a *pro rata* basis, is required.<sup>33</sup>

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30. BLACK'S LAW DICTIONARY 1016 (5th ed. 1979).

31. See Buchheit & Reisner, *The Effect of the Sovereign Debt Restructuring Process on Inter-Creditor Relationships*, 1988 U. ILL. L. REV. 493, 513 (1988); Bouchet & Hay, *The Rise of the Market-Based Menu Approach and its Limitations*, in *DEALING WITH THE DEBT CRISIS* 146, 153 (1989).

32. L. HINSCH & N. HORN, *supra* note 29, at 169.

33. The unanimity requirement can be found, for example, in the MEXICAN NEW RESTRUCTURE AGREEMENT OF 1985, § 13.01(e) and the MEXICAN MULTI-FACILITY AGREEMENT OF 1987, § 14.01 (ii); the VENEZUELAN RESTRUCTURING AGREEMENT OF 1986, § 15.01(a)(G); the PHILIPPINES RESTRUCTURING AGREEMENT OF 1985, § 12.01(d); and the ARGENTINIAN TRADE

### B. *Mandatory Prepayment Clauses*

An innovation in regard to syndicate credits is the mandatory prepayment clause contained in most restructuring agreements. It requires the debtor to make payments before the agreed payment date, if it repays other creditors not involved in the restructuring package on or prior to the original payment date.<sup>34</sup> It is thus a pendant to the sharing clause, which only regulates the internal relationship between the creditor banks involved in a syndicate credit or a restructuring agreement and has no influence on external creditors.

Two points are of decisive importance here. On the one hand, the clause is designed to prevent preferential treatment of free riders, those creditors whose claims (determined primarily according to payment date, category of debt, and creditor group) were originally meant to be included in the restructuring agreement, but who refused to participate. Their right to performance continues to be governed by the original contracts and the payment dates agreed within them. The creditors involved in the rescheduling wish to prevent these non-cooperative creditors from being treated better than themselves, particularly as the banks would otherwise rarely be willing to participate in the restructuring. An agreement with the debtor that the creditors who have refused to participate in the restructuring should not be serviced on the old conditions but only on the conditions accepted by the majority of the creditors cannot be considered, as the creditors accepting the restructuring could then possibly face claims for damages on the grounds of inducing breach of contract.<sup>35</sup> For this reason a different solution is adopted: the debtor is in principle allowed to service the debts of the noncooperating banks on the old conditions. But if payments to them exceed the amount fixed in the restructuring package or are made before the payment date agreed to in it, the debtor is then required to make payments in the same proportion to the creditors involved in restructuring.

On the other hand, the mandatory prepayment clause also takes effect in the case of payments of other debts not intended for inclusion in the restructuring, if these payments are made earlier than foreseen by the payments plan scheduled for them. This is due to the fact that

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CREDIT AND DEPOSIT FACILITY AGREEMENT OF 1986, § 12.01(e). In contrast, the approval of 95% of the creditor banks is required by the BRAZILIAN MULTI-YEAR FACILITY AGREEMENT OF 1988, § 12.01(a)(ii)(A)(v); and the NIGERIAN RESTRUCTURING AGREEMENT OF 1987, at cl. 54.01.

34. The text of the mandatory prepayment clause from the MEXICAN NEW RESTRUCTURE AGREEMENT OF 1985 is reprinted in Appendix II.

35. Clark & Hughes, *Approaches to the Restructuring of Sovereign Debt*, in SOVEREIGN LENDING: MANAGING LEGAL RISK 131, 133 (1984); Clark, *supra* note 1, at 863.

the creditors involved in the restructuring, in return for their willingness to make considerable concessions, also wish to profit, at least proportionally, from any unexpected improvement in the liquidity of the debtor, permitting him to make repayments before the due date.<sup>36</sup> For this reason, the mandatory prepayment clause is also frequently included in new credit agreements that are connected with restructuring agreements. The scope of the clause is usually restricted to payments in foreign currency. Payments made by the debtor with the assent of individual creditors in local currency or, for example, in the form of commodities, are not included. Payments below a certain limit are also frequently excluded. It is thus possible for the debtor to meet the claims of banks with a limited commitment that have not participated in the restructuring, without then being forced to make more substantial payments to the other creditors.

Exemptions are, moreover, possible by means of waivers or by making appropriate amendments to the agreement. As is customary with the deferment of payment dates in syndicate credit agreements,<sup>37</sup> however, the requirement of unanimity<sup>38</sup> or virtual unanimity<sup>39</sup> generally applies in this case too. In this respect, the Brazilian agreements are a special case. Although they also require a majority of ninety-five percent for amendments<sup>40</sup>, claims arising under the clause are automatically triggered only in the event of prepayments to official creditors. Payments to private creditors only lead to corresponding claims from the creditors involved in the restructuring if it is agreed on by a majority of over fifty percent.<sup>41</sup>

### C. *Negative Pledge Clauses*

#### 1. Content of the Clause

The negative pledge clause regulates the furnishing of security by the debtor. The syndicated Eurocredits provided for restructuring are not as a rule secured.<sup>42</sup> The only exception is the case of guarantees,

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36. Buchheit & Reisner, *supra* note 31, at 511.

37. L. Hinsch & N. Horn, *supra* note 29, at 164.

38. See, e.g., the ARGENTINIAN TRADE CREDIT AND DEPOSIT FACILITY AGREEMENT OF 1985, § 12.01(c); the MEXICAN NEW RESTRUCTURE AGREEMENT OF 1985, § 13.01 (c); the MEXICAN MULTI-FACILITY AGREEMENT OF 1987, § 14.01(2)(c); and the VENEZUELAN RESTRUCTURING AGREEMENT OF 1986, § 15.01(a)(c).

39. See the PHILIPPINE RESTRUCTURING AGREEMENT OF 1986, § 12.01(a): 90%; the NIGERIAN RESTRUCTURING AGREEMENT OF 1987, clause 54.01: 95%.

40. See the BRAZILIAN PARALLEL FINANCING AGREEMENT, § 12.01(a); and the BRAZILIAN MULTI-YEAR DEPOSIT FACILITY AGREEMENT OF 1988, § 12.01(a).

41. *Id.*, § 4.02.

42. L. HINSCH & N. HORN, *supra* note 29, at 102.

particularly those made by the governments of debtor countries. Such guarantees, however, provide no protection against difficulties arising from the lack of foreign currency. In order to ensure the access of the creditor banks to the assets of the debtor, the creation of securities is forbidden without exception in the case of Eurocredits and the more recent restructuring agreements. In section 9.04 (a) of the Mexican New Restructure Agreement of 1985, for example, the prohibition runs as follows:

So long as any credit shall remain unpaid, the guarantor will not create or suffer to exist, nor permit any governmental agency to create or suffer to exist, any lien, upon or with respect to any of the present or future properties (including, without limitation, oil, gas and international monetary assets) or revenues of the guarantor or any governmental agency in each case to secure or provide for payment of external indebtedness, or any interest or other amount payable in connection therewith, of any person . . . .<sup>43</sup>

The agreements apply both to the indebtedness of the Mexican State and to that of other public sector entities for which the State acts as guarantor. A corresponding prohibition of securities also exists for the principal debtor in each particular case.<sup>44</sup>

In this agreement the concept of "lien" is defined as follows:

Lien means any lien, pledge, mortgage, security interest, deed of trust, charge or other encumbrance on or with respect to, or any preferential arrangement which has the practical effect of constituting a security interest with respect to the payment of any obligation with or from the proceeds of, any assets or revenues of any kind.<sup>45</sup>

An alternative possibility is to permit the creation of securities for other creditors but to make it a condition that the banks participating in the restructuring agreement are secured to the same extent. Section 10.01 (c) of the Restructuring Agreement of February 24, 1986, with Venezuela<sup>46</sup> can serve as an example:

The Republic will ensure that its obligations hereunder will at all times constitute unconditional general obligations of the Republic, ranking at all times at least *pari passu* in priority of payment, in right of security and in all other respects with all other debt of the Republic now or here-

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43. In this particular case, it is also forbidden to transfer future claims arising from the sale of oil or gas, with the exception of transfers to the Mexican state itself, the Mexican central bank, the Bank for International Settlements, other multilateral financial authorities, and foreign central banks or treasuries. In addition, the receipt of advance payments from the sale of gas and oil above a limit of \$3 billion is also forbidden. The MEXICAN NEW RESTRUCTURE AGREEMENT OF 1985, § 9.04(c).

44. *Id.*, § 9.03.

45. *Id.*, § 1.01.

46. The principal debtor in this agreement is the Republic of Venezuela. Further restructuring agreements were concluded at the same time with debtors of the public sector for whose indebtedness the State acted as guarantor.

after outstanding. . . If any lien. . . is created to secure the external public debt, the Republic will cause such lien to equally and ratably secure the obligations of the public sector restructure obligors under their respective restructuring agreements and the relending facility agreement.<sup>47</sup>

Negative pledge clauses were already customary in the original credit agreements, but their application was restricted to the individual borrower. In restructuring agreements, the prohibition is frequently extended if states are involved as principle debtors or guarantors. In such cases, the debtor country must commit itself to not secure foreign indebtedness from its own assets and, in addition, to prevent certain other institutions, particularly institutions in the public sector which are legally independent of the State, from granting such securities. The reason for this is the realization of the creditor banks that the main problem is not the credit risk of individual debtors, but the debtor country's lack of foreign currency.<sup>48</sup> By expanding the scope of the clause to include all public sector entities or state-owned enterprises, the lending banks are denied access to the assets or revenues of these instrumentalities. Otherwise, the debtor state could try to meet his need for foreign exchange by secured lending channeled through any state-controlled entities. The creditor banks would be subordinated *de facto* to the secured lenders, as the debtor country probably would service the secured debt first, to avoid the expropriation of its assets.

In this respect, there are often quite substantial differences between agreements. In the clause from the Mexican Restructure Agreement quoted *infra*, for example, the prohibition of securities refers to any "governmental agency." According to the definition in the contract, this includes not only government agencies, but all enterprises in general which belong to or are controlled by the Mexican State.<sup>49</sup>

The Venezuelan Restructuring Agreement of 1986 contains a different arrangement. The requirement of equal treatment posited in it refers primarily to the state itself, but, in fact, it enters into force as soon as any external public debts, *i.e.* foreign currency indebtedness of the public sector,<sup>50</sup> are secured. A less restrictive regulation can, for

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47. The definition of the concept of "lien" corresponds to the example mentioned above from the MEXICAN NEW RESTRUCTURE AGREEMENT OF 1985.

48. Buchheit & Reisner, *supra* note 31, at 513-514. Therefore, the negative pledge clause is generally restricted to indebtedness in foreign currency, as can be seen from the examples quoted.

49. MEXICAN NEW RESTRUCTURE AGREEMENT OF 1985, at § 1.01. An exception is made only in the case of subsidiaries of Mexican state banks, insofar as they are not financial institutions.

50. According to this agreement, however, only those institutions listed in article 2 of the Venezuelan Public Credit Law at the time the agreement was concluded are regarded as part of the public sector.

example, be found in the Brazilian round of restructuring agreements in 1988. The prohibition of securities envisaged here applies only to the provision of securities by the Central Bank or the State itself.<sup>51</sup> The furnishing of securities for credits by other institutions in the public sector is, therefore, possible in principle.

## 2. Exceptions

In view of the broad interpretation of the concept of "lien," it is necessary in all cases to permit a series of exceptions. Otherwise, the severe restrictions on the economic maneuverability of the debtor would have counterproductive effects. Consequently, the agreements contain a catalogue of exceptions permitting certain liens. The following are typical examples:<sup>52</sup>

(a) Liens on properties acquired by debtor states to secure the purchase price of the properties, or to secure external indebtedness incurred for the purpose of financing the acquisition of such properties, or to secure any renewal or extension of the original financing of the properties.

(b) Liens in favor of lessors to secure claims arising from financial leases.

(c) Liens for a period not exceeding one year in the course of ordinary commercial transactions.

(d) Liens to finance the production and exportation of goods in as far as the exportation takes place within one year.

(e) Liens arising in connection with project financing, provided that they are limited to properties which are the subject of such project financing or to other properties created in the course of the project.

(f) Liens already in existence when the restructuring or new credit agreements are concluded.

(g) Liens arising by operation of law.

(h) Liens arising pursuant to orders of attachment, distraint or similar legal process, provided the lien is released or discharged within one year.

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51. BRAZILIAN MULTI-YEAR DEPOSIT FACILITY AGREEMENT OF 1988, arts. 8.01(b) and 8.02(b).

52. There is agreement on the provision of all of these exceptions in, for example, the MEXICAN NEW RESTRUCTURE AGREEMENT OF 1985, § 9.04(a) and the similarly worded § 8.02(a) of the MEXICAN MULTI-FACILITY AGREEMENT OF 1987 (*reprinted in* Appendix III); the VENEZUELAN RESTRUCTURING AGREEMENT OF 1985, at Schedule X-A; and the BRAZILIAN MULTI-YEAR DEPOSIT FACILITY AGREEMENT OF 1988, at Annex F. On the other hand, the ARGENTINIAN TRADE CREDIT AND DEPOSIT FACILITY AGREEMENT OF 1985, at § 8.03(c), refers specifically only to exceptions (a), (e)-(g), and (i). In these agreements, however, foreign liabilities with a maturity of up to one year are excluded entirely from the negative pledge clause.

(i) Liens in favor of the Bank for International Settlements and foreign central banks or treasuries to secure credits whose duration does not exceed one year.<sup>53</sup>

In addition, some agreements permit without qualification the securing of claims up to a certain limit.<sup>54</sup> A further degree of flexibility is achieved by permitting other liens if the "majority banks" — a percentage of the creditor banks laid down in the agreement and calculated according to the amount of the outstanding claims in each case — agree to waive the negative pledge clause.<sup>55</sup> In 1988, for example, the Mexican Government requested such a waiver in connection with its offer to exchange existing indebtedness for bonds of lower nominal value which were to be secured by zero bonds of the U.S. Treasury. The required majority of the creditor banks approved the waiver.<sup>56</sup> Exemption by means of waiver is, however, a rather laborious procedure in view of the participation, in some cases, of several hundred banks in a restructuring agreement. The fact that details of a planned transaction must be disclosed may also have a deterrent effect.<sup>57</sup>

### 3. Consequences of Breaching Negative Pledge Clauses

As the prohibition of securities in negative pledge clauses is only contractual, the creation of securities in favor of third parties cannot, in the final analysis, be prevented. In the event of a breach of contract, the creditors affected can only have recourse to the sanctions against the debtor foreseen by the agreement, in particular the termination of the agreement and the demand for immediate settlement of the outstanding loan. Such measures would, however, hardly lead to complete reimbursement of the debt, particularly in view of the problems involved in compulsory enforcement. Consequently, it seems an obvious step to recover the losses incurred from the third party as the beneficiary of the breach of the contract. If the borrower, bound by the

53. See Bradfield & Jacklin, *The Problems Posed by Negative Pledge Covenants in International Loan Agreements*, 23 COLUM. J. TRANSNAT'L. L. 131, 134 n.11 (1984).

54. See, e.g., the VENEZUELAN RESTRUCTURING AGREEMENT OF 1985, at Schedule X-A (total of \$150 million); the BRAZILIAN MULTI-YEAR DEPOSIT FACILITY AGREEMENT OF 1988, at Annex F (\$150 million in 1988, \$200 million in 1989, and \$250 million in each of the following years).

55. Of the cases mentioned *supra* note 33, the agreements with Brazil and Mexico require over 50% approval, and the agreements with Argentina, Nigeria, the Philippines, and Venezuela require more than 66 2/3% approval. Changes in the negative pledge clauses can also be made under these conditions.

56. For details, see Ebenroth & Cremer, *Mexikos Umschuldungspaket - Ein Ansatz zur Lösung der Schuldenkrise?*, DIE BANK, Sept. 1988, at 488, 491; Chamberlin, Gruson & Weltchek, *Sovereign Debt Exchanges*, 1988 U. ILL. L. REV. 415, 450-457; see also *infra* notes 99-103 and accompanying text.

57. Chamberlin, Gruson & Weltchek, *supra* note 56, at 421.

contract itself, or the guarantor have furnished security to the third party, suing for damages under the law of torts can be considered.

In German law, the Civil Code would provide the basis for such claims.<sup>58</sup> It is a requirement, however, that the third party has deliberately influenced the debtor, inciting him to breach existing contractual obligations. Moreover, the influence exercised must seem morally reprehensible. According to the ruling of the German courts and the dominant legal opinion, however, this is not *per se* the case with incitement to breach of contract. What is in fact required is an additional reprehensible factor, a "qualified incitement," for example, a threat, an offer of special advantage, or an intensive intervention to dispel existing doubts.<sup>59</sup>

An analogue to this requirement can be seen, for example, in the "tort of interference with contractual relations" in common law, which, however, takes on different forms in England and the United States. According to U.S. courts, the requirements are fulfilled if a third party exerts an intentional and improper influence on the debtor, thus inducing him to breach of contract.<sup>60</sup> The mere exploitation of an existing willingness of the debtor to breach the contract is not, however, in itself sufficient.<sup>61</sup>

English courts have reduced even further the requirements of this tort under which claims can be made. It is sufficient under English law if the third party has knowledge of conflicting contractual obligations but persists in entering into a contract, thus making a breach possible. In this case it is of no significance whether the debtor was willing to breach the contract anyway or whether his willingness was induced by the third party.<sup>62</sup> The granting of a credit involving the provision by the debtor of securities that are not excluded from the negative pledge clause would, consequently, be extremely risky for the creditors, as they could scarcely claim to be ignorant of the contents of the existing restructuring agreements.

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58. BGB § 826.

59. See Schäfer in STAUDINGER, KOMMENTAR ZUM BÜRGERLICHEN GESETZBUCH § 826 annot. 171 (12th ed. 1985). Contrary to the view expressed in L. HINSCH & N. HORN, *supra* note 29, at 105, inducement to breach of a principal covenant is not necessary. This requirement of the Bundesgerichtshof, judgment of May 20, 1960, W. Ger., 13 NEUE JURISTISCHE WOCHENSCHRIFT 1853, refers only to claims for damages arising exclusively from the law of competition. Cf. H. MERKEL, DIE NEGATIVKLAUSEL 150 (1985).

60. PROSSER AND KEETON ON TORTS 978 (W. Keeton, D. Dobbs, R. Keeton & D. Owen 5th ed. 1984); Buchheit & Reisner, *supra* note 31, at 498-99.

61. PROSSER AND KEETON ON TORTS, *supra* note 60, at 990.

62. See *British Motor Trade Association v. Salvadori*, 1949 Ch. 556; *D.C. Thomson & Co. Ltd. v. Deakin*, 1952 Ch. 646; *Sefton v. Tophams Ltd.*, 1965 Ch. 1140; for a detailed treatment of this point and of the De Mattos principle see Cohen-Grabelsky, *Interference with Contractual Relations and Equitable Doctrines*, 45 MOD. L. REV. 241, 249-50 (1982).



If a negative pledge clause does not forbid securities but requires equality of security, the creditors favored by this arrangement could enjoy additional protection according to some older decisions of U.S. courts.<sup>63</sup> If the third party accepting a security has knowledge of this provision, the security granted to it also serves to cover the claims of the other creditors. In this case, the negative pledge clause establishes an equitable lien that the secured party and the other creditors have to share on a *pro rata* basis. Assuming that the courts would recognize an equitable lien, it is still, however, doubtful whether a provision requiring equal security would be more advantageous than a general prohibition of securities, as the measures taken by the debtor to secure the third party would also have to fall within the scope of U.S. law or another law that recognizes equitable liens under equivalent circumstances.<sup>64</sup>

#### 4. Scope of the Clause

The restrictions imposed on debtors by the negative pledge clause provide an incentive to circumvent the clause by means of forms of financing which formally do not amount to securities, but in fact fulfil the same economic purpose.<sup>65</sup> The following forms can be considered:<sup>66</sup>

- the sale of assets with an obligation to repurchase them at an increased price (sale and repurchase);
- raising funds by selling equipment and the simultaneous agreement to lease it back from the purchaser (sale and lease-back);
- selling accounts receivable before their due date at a discount to a third party who retains recourse against the seller in the event of the seller's customer failing to pay (recourse factoring);<sup>67</sup>
- the deposit of foreign assets in a blocked account with a creditor,

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63. Kaplan v. Chase National Bank, 281 N.Y.S. 825, 156 Misc. 471 (1934); Chase National Bank v. Sweezy, 281 N.Y.S. 487 (1931), *aff'd* 236 App. Div. 835, 259 N.Y.S. 1010 (1932), *aff'd* 261 N.Y. 710, 185 N.E. 803 (1933); Kelly v. Hanover Central Bank and Trust Co., 85 F.2d 61 (2d Cir. 1936). *But see* Chase Manhattan Bank, N.A. v. Gems-by-Gordon, Inc., 649 F.2d 710, 713 (1981).

64. According to a debatable decision of the California Supreme Court, Coast Bank v. Minderhout, 61 Cal. 2d 311, 38 Cal. Rptr. 505 (1964), a straightforward prohibition of security can be regarded as an equitable lien. On this point, see D. MÜHL, RECHT DER KREDIT-SICHERHEITEN IN DEN VEREINIGTEN STAATEN VON AMERIKA, TEIL II: IMMOBILIAR-SICHERHEITEN UND PERSÖNLICHE SICHERHEITEN 40 (1985).

65. See Walker & Buchheit, *supra* note 27, at 147; Ebenroth, *Finanzinnovationen im LDC-Merchant Banking*, in BANKBETRIEB UND EIGENKAPITALFINANZIERUNG, AKTUELLE RECHT-SFRAGEN 119, 140-41 (B. Lüthje ed. 1990).

66. See 2 ENCYCLOPAEDIA OF BANKING LAW para. F (3410) (P. Cresswell, W. Blair, G. Hill, & P. Wood eds. 1991).

67. In practice, there are doubts about the acceptability of recourse factoring as a form of financing that evades the negative pledge clause. See the case presented in Ebenroth, *supra* note 65, at 141.

enabling it offset against a claim.<sup>68</sup>

According to U.S. and English common law,<sup>69</sup> there is no security interest in these cases.<sup>70</sup> There are, however, a number of arguments in favor of a broader interpretation of the negative pledge clause. First of all, the purpose of the clause must be taken into account.<sup>71</sup> The debtor should not be permitted to evade enforcement of claims by creditor banks by granting individual creditors preferential access to its assets. What matters to the parties concerned is not the legal form, but the economic significance of a transaction. Furthermore, Section 9 of the Uniform Commercial Code (UCC)<sup>72</sup>, for example, assumes that in answering the question whether a security interest exists, the goal pursued by the participants is of primary importance.<sup>73</sup> Consequently, whether or not contractual arrangements that do not contain a security interest according to common law may, nevertheless, be treated as secured transactions, depends on the economic motives of the parties. Moreover, in section 1-201 (37) of the UCC, the circumstances under which a leasing contract may be seen as creating a security is regulated in detail.

On the other hand, in the interpretation of contracts under Anglo-American law, great importance is attached to the wording of the contract.<sup>74</sup> In the situation under discussion, this is justifiable to a particularly high degree, as outside third parties, such as potential business partners of the debtor, could be affected by the clause. If, therefore, the definition of "lien" laid down in the contract is restricted essentially to a list of the security interests possible and recognized under common law, without, for example, referring to the UCC, with its broader understanding of the security interest, then the negative

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68. This only makes sense, however, in the case of credits not involving syndicates, as the sharing clause would otherwise apply.

69. Most syndicated loans to developing countries and restructuring agreements are subject to New York state law; a few are subject to English law. Other legal systems play virtually no part. See Stoakes, *The Lawyer and Rescheduling*, EUROMONEY, Oct. 1984, at 275; L. HINSCH & N. HORN, *supra* note 29, at 152.

70. 2 ENCYCLOPAEDIA OF BANKING LAW, *supra* note 66, at para. F (3410), (3554); R. GOODE, LEGAL PROBLEMS OF CREDIT AND SECURITY 173 (2d ed. 1988). This, however, may not be true if permission to offset is provided for in a contract. See Pergam, *The Borrower's Perspective on Euroloan Documentation*, INT'L FIN. L. REV., Aug. 1983, at 14, 15; P. WOOD, ENGLISH AND INTERNATIONAL SET-OFF, para. 5-185 (1989).

71. Walker & Buchheit, *supra* note 27, at 139, 147.

72. The UCC, a model law that has been adopted (with variations) by all of the U.S. states but Louisiana, regulates most aspects of secured transactions, except personal and real estate securities.

73. See 2 ENCYCLOPAEDIA OF BANKING LAW, *supra* note 66, para. F (3410); *Sierra Financial Corporation v. Brooks-Farrer Co.*, 15 Cal. App. 3d 698, 93 Cal. Rptr. 422 (1971).

74. 2 K. ZWIEGERT & H. KÖTZ, EINFÜHRUNG IN DIE RECHTSVERGLEICHUNG AUF DEM GEBIETE DES PRIVATRECHTS (2d ed. 1984).

pledge clause should be interpreted more strictly. In order to dispel any doubts that might arise, every agreement which *de facto* has the effect of a security is regularly included in the definition of a "lien,"<sup>75</sup> as in the examples listed above in II.C.3. In the final analysis, however, there is no foolproof way of preventing transactions that evade the clause, if only because the creditor banks do not have the necessary means of control at their disposal.<sup>76</sup>

#### D. *Pari Passu* Clauses

While the negative pledge clause is designed to prevent preferential treatment of other creditors through the provision of securities, the so-called *pari passu* clause aims at avoiding the subordination of the lending banks to other unsecured indebtedness. A typical clause runs as follows:

So long as any credit shall remain unpaid, the obligor will ensure at all times that its obligations hereunder constitute its unconditional general obligation ranking at least *pari passu* with all of its other unsecured external indebtedness now or hereafter outstanding.<sup>77</sup>

The clause is commonly found in loan contracts with private borrowers and is intended to prevent the accordance of priority to individual unsecured creditors in the event of the debtor's insolvency.<sup>78</sup>

In dealings with sovereign debtors, which cannot be liquidated like a corporation or subjected to bankruptcy proceedings, the clause serves the purpose of preventing the debtor from pursuing measures that create different classes of creditors. At issue here are legal regulations of the debtor country which would require it to use the foreign currency primarily to satisfy particular creditors,<sup>79</sup> for example, in favor of the International Monetary Fund, in order not to endanger membership in this organization, or to benefit those banks that are willing to provide fresh money. The earmarking of certain sources of hard currency earnings for the servicing of particular debts is also inadmissible.<sup>80</sup>

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75. Pergam, *supra* note 70, at 15.

76. P. WOOD, *LAW AND PRACTICE OF INTERNATIONAL FINANCE* § 6.02(2)(d) (1989).

77. The PHILIPPINE RESTRUCTURING AGREEMENT OF 1986, § 8.01(d). Insofar as it is not itself the principal debtor, the Philippine State acts as guarantor and commits itself to the corresponding *pari passu* obligations. See also the VENEZUELAN RESTRUCTURING AGREEMENT OF 1986, at § 10.01, which includes a negative pledge covenant in the form of a guarantee of equal security.

78. P. WOOD, *supra* note 76, § 6.03(2); Semkow, *Syndicating and Rescheduling International Transactions: A Survey of the Legal Issues Encountered by Commercial Banks*, 18 INT'L LAW. 869, 899 (1984).

79. 2 ENCYCLOPAEDIA OF BANKING LAW, *supra* note 66, paras. F (3418), F (3450); P. WOOD, *supra* note 76, § 6.03(3).

80. Semkow, *supra* note 78, at 869, 899.

Differentiation between creditors is nevertheless possible in a number of other areas: sovereign debtors may exclude creditors who have not taken part in restructuring or new credit agreements from participating in debt-equity swap programs, with the result that their claims can in practice no longer be traded on the secondary market.<sup>81</sup> Banks are further treated unequally when individual creditors profit from securities granted by third parties which do not, consequently, fall under the negative pledge clause.<sup>82</sup> Also relevant are the commitments of debtor countries to selected groups of creditors, excluding them from future restructurings and demands for new credits ("exit option"). This means that their claims are accorded priority if the debtor country is prevented by lack of foreign currency from servicing the debt or if it is not in a position to meet the entire foreign debt. Such a commitment was made, for example, by the Mexican government in favor of those creditors who, at the beginning of 1988, accepted the offer to exchange existing claims for bonds with a lower nominal value.<sup>83</sup>

Finally, the decision as to which claims are to be included in a restructuring package and which are to be serviced in accordance with the original agreement involves in itself a segmentation of the creditors. As pointed out in the introduction, claims with a duration of less than a year and bonds are not usually included in restructuring agreements. But there are also differences in the treatment of private and public creditors. Although the commercial banks and the bilateral creditors represented in the Paris Club are concerned with ensuring that their restructuring rounds are accompanied by corresponding measures of the other groups,<sup>84</sup> the conditions agreed on in the restructuring packages are by no means identical. Striking examples are provided by the recent Mexican and Philippine Restructuring Agreements, which resulted in a partial remission of debts by the banks without any provision for a similar remission on the part of foreign states.<sup>85</sup> The multilateral institutions, the World Bank and the International Monetary Fund, have been exempted from any restructuring

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81. See Buchheit, *Unseating Free Riders*, INT'L FIN. L. REV., Sept. 1989, at 14, 15; M. CREMER, *supra* note 8, at 165.

82. In the case of the MEXICAN MULTI-FACILITY AGREEMENT OF 1987, for example, facilities II and III were in part guaranteed by the World Bank.

83. On this point, see *infra* notes 99-103 and accompanying text.

84. Clark, *supra* note 1, at 860; M. BOTHE, J. BRINK, C. KIRCHNER & A. STOCKMAYER, *supra* note 9, at 162.

85. *The Mulford Interview: No Brady Plan II - Official*, INT'L FIN. REV., March 24, 1990, at 4, col. 1. A severe criticism of this differentiation by the commercial banks can be found in *Kritik an zunehmend ungleichmässiger Behandlung und Skepsis über Brady-Plan*, HANDELSBLATT, May 7, 1990, at 15, col. 1.

of their claims.<sup>86</sup>

What all of these possible forms of differential treatment have in common is that they have no influence on the maintenance of claims or on their legal enforceability. Accordingly, no formal priorities between different claims are established. Only a formal segmentation could, however, be regarded as a breach of the *pari passu* clause.<sup>87</sup>

Exemptions from the *pari passu* clause are also possible, provided that the majority banks agree to them.<sup>88</sup> In any event, the clause has not achieved any practical significance in the management of restructurings to date.

### III. EFFECTS OF RECENT DEVELOPMENTS IN LIMITING THE PRINCIPLE OF EQUAL TREATMENT

The establishment of equal treatment for all creditors occurred in the first phase of debt management, which successfully achieved its purpose, the prevention of the collapse of the international financial markets. However, it also impeded a solution of the debt crisis by means of the menu approach.<sup>89</sup> As a result, the deeply indebted developing countries are still by and large excluded from the credit markets, although they continue to be in need of financing. Their lack of creditability prevents the provision of unsecured credits and the negative pledge clause prevents the provision of securities. Bank credits to finance the balance of payments, other no-purpose loans, and credits to finance necessary infrastructural improvements or to refinance the servicing of debts cannot, therefore, be secured.

Even where exceptions to the negative pledge clause are permitted, these may be inadequate. For example, the first exception listed in the catalogue presented above (II.B.1.) permits liens to secure the purchase price of properties or credits acquired in connection with imports. Only the acquired goods themselves can, however, serve as security. But these are not a satisfactory form of security, as they are usually situated in the debtor country after their acquisition.

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86. Clark, *supra* note 1, at 859; M. BOTHE, J. BRINK, C. KIRCHNER, & A. STOCKMAYER, *supra* note 9, at 157.

87. See Walker & Buchheit, *supra* note 27, at 146; Buchheit & Reisner, *supra* note 31, at 497; P. WOOD, *supra* note 76, § 6.03(3); 2 ENCYCLOPAEDIA OF BANKING LAW, *supra* note 66, paras. F (3418), F (3450).

88. See *supra* note 50 and accompanying text. The NIGERIAN RESTRUCTURING AGREEMENT is an extreme case, in that a change in the *pari passu* clause is made dependent upon the approval of 95% of the banks, weighted according to the degree of participation. See the RESTRUCTURING AGREEMENT OF NOVEMBER 23, 1987, cl. 25.01 and 54.01.

89. Ebenroth, *The Changing Legal Framework for Resolving the Debt Crisis: A European's Perspective*, 23 INT'L LAW. 629, 638 (1989).

It is, therefore, questionable whether the negative pledge clause serves its purpose. When the situation is most critical, it can prevent the acquisition of the means needed for adjustment without ultimately guaranteeing a satisfaction of the demands of the creditors it is designed to protect.<sup>90</sup>

The clauses described above can also lead to problems in connection with the remission of debt. For banks willing to forego a part of their claims there must be incentives offering them advantages over other creditors in return for the renunciation of their claims. The provision of security for the remaining claims could be considered. But this would violate the negative pledge clause. The immediate satisfaction of the remaining claims, prior to maturity and with a discount on nominal value, could also be taken into consideration. But in this case the sharing clause would come into effect, requiring the creditor who has foregone part of his claims to share the payments with other creditors, and requiring the debtor to observe the mandatory prepayment clause and make corresponding payments to other syndicates or to the creditors involved in other restructuring agreements.<sup>91</sup>

The sharing clause also has a negative effect on endeavors to complement restructurings by means of new money packages. The free riders, who do not take part in this involuntary lending, thus profit from the willingness of the other banks to refinance the servicing of the old stock by providing new funds.

The negative effects of the equal treatment clauses are also taken into account in the Brady Initiative of March 1989. It calls for a general waiver of sharing and negative pledge clauses for a certain period of time, for example three years, in order to enable agreements on the voluntary remission of debt to be reached.<sup>92</sup>

## A. *Modifications in the Equal Treatment Principle to 1988.*

### 1. Qualified Capital Stock

Even before the Brady Initiative, modifications in the clauses guaranteeing equal treatment were introduced in a series of financing packages with the aim of reducing the amount of foreign debt by means of

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90. McDaniel, *Are Negative Pledge Clauses in Public Debt Issues Obsolete?*, 38 *BUS. LAW.* 867, 879 (1983). Cf. Clark, *supra* note 1, at 864-65 (provision of security facilitates restructuring with new money).

91. On debt buy-backs that evade the sharing and mandatory prepayment clauses, see Ebenroth, *supra* note 65, at 143; *Third World Debt Traders: The Unsolved Mystery*, *Fin. Times*, Dec. 19, 1989, at 29, col. 3.

92. Brady, *supra* note 5, at 9.

debt-equity swap programs.<sup>93</sup> Section 5.11 of the Mexican Restructuring Agreements of 1985 is an example.<sup>94</sup> The arrangement contains an exception to the sharing and mandatory prepayment clauses and permits an exchange of the claims arising under the agreement for equity interests in private or public enterprises, referred to as "qualified capital stock." A number of restrictions are, however, foreseen.<sup>95</sup> For example, only foreigners are permitted to acquire such interests and a transfer to Mexican investors is only possible after 1997. Furthermore, the investor cannot be granted any claim to repayments of any kind before the due date of the debt exchanged. A conversion also requires the approval of the relevant Mexican authorities in accordance with Mexican domestic law.

In subsequent years, comparable arrangements were also included in agreements with other countries, although the form was sometimes substantially changed. Section 5.11 of the Philippine Restructuring Agreement of 1986, for example, does not require direct conversion into equity interests but permits repayment of a credit in local currency, provided the creditor bank agrees. Conversion is possible not only for foreign creditors but also for Philippine citizens who may have acquired claims on the secondary market. To what extent, if at all, and under what conditions the payments received must be invested in Philippine enterprises depends entirely on internal Philippine regulations.<sup>96</sup>

According to estimates, however, the foreign debt of all developing countries could only be reduced by about \$20 billion in this way, the total volume of debt being \$1.3 trillion.<sup>97</sup> But the situation is considerably more favorable for certain debtor countries. One of these is Chile, whose debts were reduced by more than \$5 billion between 1985 and August 1989.<sup>98</sup>

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93. The countries concerned were, in particular, Argentina, Brazil, Chile, Costa Rica, Ecuador, Mexico, the Philippines, and Venezuela. See INTERNATIONAL MONETARY FUND, *supra* note 2, at 58.

94. The modified, 1987 version of § 5.11 is reprinted in Appendix IV.

95. For details, see Chamberlin, Gruson & Weltchek, *supra* note 56, at 422-23; J. WULFKEN, *supra* note 6, at 130-35; Mudge, *Mexico Leads the Way*, INT'L FIN. L. REV., June 1988, at 25, 28.

96. See Ebenroth & Roth, *Konversionsfonds für die Philippinen*, 87 ZEITSCHRIFT FÜR VERGLEICHENDE RECHTSWISSENSCHAFT [ZVGLRWISS] 393 (1988); Ebenroth & Bühler, *Schuldenkonversion auf den Philippinen - Neuere Entwicklung und Probleme*, 88 ZVGLRWISS. 302 (1989).

97. Cooke, *Salvaging Debt Equity Swaps*, INSTITUTIONAL INVESTOR, Sept. 1989, at 149. For the reasons, see C. EBENROTH, *GLOBALE HERAUSFORDERUNGEN DURCH DIE VERSCHULDUNGSKRISE* 23 (1987).

98. Carey, Leventhal, & Irvine, *Chile's Debt-for-Equity Programme: Hotter than Most?*, INT'L FIN. L. REV., Feb. 1990, at 28, 31.

## 2. Qualified Investments/Qualified Debts

There was an extension of the debt-equity swap clauses in many of the agreements in 1987 and 1988. First of all, in section 5.11 of the restructuring and new credit agreements with Mexico,<sup>99</sup> the exchange of claims for “qualified investments” and “qualified debts” was excluded from the sharing and mandatory prepayment clauses. The term “qualified investment” in the 1987 agreement with Mexico applies to the repayment of indebtedness to Mexican banks or trusts in Mexican pesos, the acquisition of capital assets in Mexico, and other capital expenditures. This kind of conversion is, moreover, open only to “Mexican persons,” *i.e.*, Mexican citizens and enterprises with their principal places of business in Mexico.<sup>100</sup> This newly introduced exception is aimed, therefore, at the repatriation of flight capital. For such an exchange, the approval of the appropriate Mexican authorities is also required.

Whereas qualified investments involve, in essence, an extension of the debt-equity swap clause to include Mexican persons, the possibility of conversion into “qualified debt” presents a fundamental innovation. According to this procedure, it is permissible to convert existing indebtedness into new debts which either have a longer maturity than the previous credits or are offered to all banks *pro rata*, that is, in shares corresponding to the amount of their claims.<sup>101</sup> This possibility was taken up for the first time at the beginning of 1988. Mexico offered all foreign creditor banks the exchange of existing claims for newly issued registered bonds with a lower nominal value, which was to be fixed by auction, at a variable rate of interest.<sup>102</sup> The bonds will be due for repayment in 2008, whereas the existing restructuring and credit agreements run to 2006 at the latest. The preconditions for qualified debt were thus fulfilled and, consequently, the bonds are not subject to the Mexican sharing and mandatory prepayment clauses.

In order to create an incentive for the acceptance of the exchange offer, Mexico also arranged to secure the principal by pledging zero bonds of the U.S. Treasury. To this end a waiver of the negative pledge clause was necessary, and it was in fact conceded by the majority banks — in the case of Mexico, fifty percent of the banks involved. If no exception had been made for qualified debts, a waiver of the sharing clause would also have been necessary. According to the

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99. Reprinted in Appendix IV.

100. Chamberlin, Gruson, & Weltchek, *supra* note 56, at 423.

101. *Id.* at 453.

102. Ebenroth & Cremer, *supra* note 56, at 490; Chamberlin, Gruson, & Weltchek, *supra* note 56, at 450.



terms of the Mexican Agreement, this would have required the approval of all the creditor banks.

Further regulations on qualified debt, comparable to section 5.11 of the Mexican Agreement, were included in agreements with Brazil, Ecuador, the Philippines, and Venezuela, among others.<sup>103</sup>

### 3. Debt Buy-Backs

In 1988 Bolivia and Chile were able to repurchase a portion of their foreign debt at a discount with the approval of the creditor banks. The distaste of the banks for debt buy-backs involving a discount on the nominal value is based primarily on the fact that in such transactions the currency reserves are withdrawn from debt servicing. Furthermore, the debtors can influence prices on the secondary market by their behavior in regard to payments. If debt buy-backs were possible, the debtors would have good reason to force prices down by refusing to pay.<sup>104</sup> In the case of Bolivia, however, a donation from an unknown party was involved. The creditor banks agreed to the use of this donation in the debt buy-back under the control of the International Monetary Fund. In this way Bolivia's indebtedness was reduced by \$253 million.<sup>105</sup>

Although the circumstances were not so unusual in the case of Chile, there too the creditor banks agreed to debt buy-backs by changing the existing agreements. The amount to be used by Chile, however, was restricted to a maximum of \$500 million.<sup>106</sup>

#### B. Restructurings Under the Brady Initiative

Since the proposals of the U.S. Secretary of the Treasury were published, the Philippines and Mexico, in particular, have concluded restructuring agreements with their creditor banks.<sup>107</sup>

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103. Chamberlin, Gruson, & Weltchek, *supra* note 56, at 423.

104. In the international debt crisis of the 1930s, in contrast to today's syndicated loan agreements, repurchasing defaulted bonds at market prices was not precluded by sharing, mandatory prepayment, or other clauses. Debt buy-backs became a commonly used measure for debtor countries to reduce their foreign debt. See B. EICHENGREEN & R. PORTES, *SETTLING DEFAULTS IN THE ERA OF BOND FINANCE 23-25* (Centre for Economic Policy Research, Discussion Paper No. 272, 1988).

105. See INTERNATIONAL MONETARY FUND, *supra* note 2, at 63; INTERNATIONAL MONETARY FUND, *INTERNATIONAL CAPITAL MARKETS - DEVELOPMENTS AND PROSPECTS*, April 1989, at 39.

106. See INTERNATIONAL MONETARY FUND, *supra* note 105, at 40.

107. Further Brady plan restructurings, concerning Costa Rica, Venezuela and Uruguay, use elements similar to those found in the new Mexican and Philippine agreements.

### 1. The Philippine Restructuring Agreement of 1989-90

The Philippine package, negotiated at the end of 1989, saw changes in all clauses guaranteeing equal treatment, with the exception of the *pari passu* clause.<sup>108</sup> The legally relevant modifications can be sketched as follows.

Following the waiver of the sharing, mandatory prepayment, and negative pledge clauses, it is permissible, over and above the arrangements made in 1987 for qualified debts, to engage in any transactions up to a maximum value of \$1.5 billion that serve the purpose of reducing the indebtedness or the burden of interest (eligible debt reduction and eligible debt service reduction transactions).<sup>109</sup> The funds used for this purpose must stem from official foreign sources, for example, the World Bank, the International Monetary Fund, or foreign governments. Once these funds are exhausted, however, at the latest by January 1, 1992, these measures to reduce indebtedness may only be continued to the amount of \$300 million annually. The Philippines may then, however, fall back on its own currency reserves.<sup>110</sup>

To facilitate the implementation of this debt reduction, the creditor banks have agreed to a further exception to the principle of equal treatment. The contracts do provide for a *pro rata* limitation, according to which the offers made by the Philippines concerning debt reduction and debt service reduction transactions must be made on a *pro rata* basis to all banks involved in the restructuring agreement or the new credit agreement. However, the Philippines may dispose freely of up to \$150 million each calendar year regardless of this limitation.<sup>111</sup>

An additional exception to the negative pledge clause<sup>112</sup> also serves to facilitate the borrowing of new credits. According to this regulation, the Philippines can provide liens up to a total of \$200 million for new credits.<sup>113</sup>

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108. To change the sharing clause, the approval of all the creditor banks was required; to change the mandatory prepayment and the negative pledge clauses, quotas of over 90% and 66 2/3% respectively, weighted *pro rata*, were sufficient. See the PHILIPPINE RESTRUCTURING AGREEMENT OF 1986, at § 12.01.

109. The SECOND AMENDMENT TO THE PHILIPPINE RESTRUCTURING AGREEMENT, parts A4, A5, and A6; the SECOND AMENDMENT TO THE PHILIPPINE CREDIT AGREEMENT, parts A5, A6, and A8.

110. The SECOND AMENDMENT TO THE PHILIPPINE RESTRUCTURING AGREEMENT, part A2 and The SECOND AMENDMENT TO THE PHILIPPINE CREDIT AGREEMENT, part A2: "Available Debt Reduction Resources".

111. The SECOND AMENDMENT TO THE PHILIPPINE RESTRUCTURING AGREEMENT, part A2; the SECOND AMENDMENT TO THE PHILIPPINE CREDIT AGREEMENT, part A2: "pro rata limitations".

112. The SECOND AMENDMENT TO THE PHILIPPINE RESTRUCTURING AGREEMENT, part A6; the SECOND AMENDMENT TO THE PHILIPPINE CREDIT AGREEMENT, part A8.

113. See the SECOND AMENDMENT TO THE PHILIPPINE RESTRUCTURING AGREEMENT,

A special feature of the Philippine package is, moreover, the fact that it relies upon voluntary participation of the creditor banks in regard to both debt reduction and new money loans. Consequently, each bank may also choose not to participate in this package.<sup>114</sup>

The first of the measures taken by the Philippines in the course of changing the conditions of the agreements was a substantial debt buy-back. In this way the foreign debt was reduced by about \$1.3 billion, with a large number of the banks terminating their commitments in the process.<sup>115</sup>

## 2. The Mexican Restructuring of 1989-90

### a. The Structure of the Package

In contrast to the Philippine package, the restructuring and new credit agreements between Mexico and its creditor banks, which were negotiated in the summer of 1989 and signed in February 1990, provide that all banks whose claims were intended for inclusion in the new arrangement<sup>116</sup> should participate in at least one of the options offered — debt reduction (Options I and II) or fresh money in the form of new money loans and bonds (Options III-VI).

The first option involves an exchange of existing claims for Mexican bonds at only sixty-five percent of the nominal value of the exchanged debts and a variable rate of interest of thirteen to sixteen percent over LIBOR (floating rate discount bonds). Option II enables the banks to exchange their claims for Mexican bonds at the nominal value of the existing debts, but with a fixed rate of interest of only six and a quarter percent<sup>117</sup> (fixed rate par bonds).

Both kinds of bonds are registered securities with a maturity of thirty years. In regard to the principal they are secured to the full

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part A2; see also the SECOND AMENDMENT TO THE PHILIPPINE CREDIT AGREEMENT, part A2: "Eligible Collateralized New Money Transactions".

114. For a detailed examination of the conditions of this package, see Ebenroth & Bühler, *Die Implementierung der Brady-Initiative in Mexiko und den Philippinen*, 1990 RECHT DER INTERNATIONALEN WIRTSCHAFT 23, 26-28.

115. See Ebenroth & Bühler, *supra* note 114 at 27; *Philippines Finalises Debt Buy-back*, *Fin. Times*, Nov. 30, 1989, at 22, col. 4.

116. MEXICAN 1989-92 NEW CREDIT AGREEMENT OF 1990; MEXICAN NEW MONEY BOND RESTRUCTURE AGREEMENT OF 1990. The package includes the lion's share of Mexico's medium and long-term debts with private creditor banks, the total amounting to over \$48 billion. *A Modest Deal for Mexico*, *Financial Times*, Jan. 17, 1990, at 18; *Bad Press Throws a Shadow Over Mexico Deal*, *INT'L FINANCING REV.*, Jan. 27, 1990, at 28.

117. WORLD BANK, 1 WORLD DEBT TABLES 1990-1991, at 78-81 (1990). This rate applies only to bonds denominated in U.S. dollars. For bonds in other currencies it varies between 3.75% (Swiss francs) and 10.75% (Italian lire). MEXICAN DISCOUNT AND PAR BOND EXCHANGE AGREEMENT OF 1990, Annex A to Exhibit 1A, at 8.

amount by the pledging of U.S. zero bonds;<sup>118</sup> in regard to interest they are partially secured by a revolving interest guarantee for a period of eighteen to twenty-four months. For this purpose a waiver of the majority banks involved in the old agreements was necessary.<sup>119</sup> And yet, because the maturity was longer than that of the previous claims, these bonds were qualified debt in the sense determined by section 5.11 of the existing agreements. Consequently, they no longer fall under the sharing and mandatory prepayment clauses. Furthermore, these bonds also take the form of exit bonds, as Mexico has committed itself to excluding them from any future restructurings or new money requests.<sup>120</sup>

The other four options contain different kinds of fresh money commitments amounting to twenty-five percent of the previous commitments of the banks involved. The outstanding claims of the banks that decided in favor of one of these options remain unchanged in regard to both the principal amount and the rate of interest.<sup>121</sup>

Whereas those banks which have decided in favor of discount or par bond swaps are free from sharing obligations towards other creditors because of the longer maturity of the bonds, this is problematic in the case of those providing fresh money. As they were meant to retain their old claims, those creditors would have had to share all payments from Mexico with the "free riders," *i.e.*, those banks that were not willing to accept either a reduction of the debt or the provision of new funds and refused to participate in the new Mexican package. In view of the problems with these free riders, many banks could probably not have been persuaded to take part in the restructuring. In order to create an incentive for them to participate, therefore, the old agreements were not simply taken over unchanged, but were replaced by new credit agreements with the same principal amounts, rates of interest, and maturity. This novation was the obvious path to take, as the sharing clause is only operative among the creditors participating in a specific agreement.<sup>122</sup>

It is, in principle, doubtful whether the contractual obligations to-

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118. This again applies only to bonds in U.S. dollars. MEXICAN DISCOUNT AND PAR BOND EXCHANGE AGREEMENT OF 1990, Exhibit 1B, at 15. DM bonds are collateralized, for example, by means of a 30-year, zero coupon bond of the German Post Office. *Id.* at Exhibit 1B. See UNITED MEXICAN STATES COLLATERALIZED 5.01% DEUTSCHE MARK BONDS AGREEMENT OF 1990-2019, at § 8(1).

119. More than 50% of the creditor banks, weighted according to the amount of the claims outstanding. *Cf. supra* note 55.

120. MEXICAN DISCOUNT AND PAR BOND EXCHANGE AGREEMENT OF 1990, *supra* note 117, at § 5.01(b).

121. For details on the individual options, see Ebenroth & Bühler, *supra* note 114, at 24.

122. See *infra* II.A.

ward other members of a syndicate can be evaded simply by novation,<sup>123</sup> especially as changes in the sharing clauses of the Mexican agreements require unanimity.<sup>124</sup> Accordingly, it is also regarded as possible that the nonparticipating banks will try to enforce in the courts claims arising from the sharing clause.<sup>125</sup> The novation is, however, covered by section 5.11 of the Mexican agreements. According to this clause, qualified debt includes not only the exchange of old for new indebtedness with a longer maturity, but also each and every conversion offered to all the creditors on a *pro rata* basis.<sup>126</sup> The procedure adopted in Mexico meets this requirement. All of the options proposed — including the twenty-five percent fresh money commitment, which involved a novation of the old indebtedness — were offered equally to all creditors. This increases the risk for the free riders that they may fail completely to vindicate their claims.<sup>127</sup>

## b. Equal Treatment Clauses

The Mexico package also limits the application of the sharing, mandatory prepayment, and negative pledge clauses. The regulations differ, however, from option to option.

### (i) Sharing Clauses

The sharing clause was abandoned completely for the three groups of bonds (discount, par, and new money bonds). Payments on these bonds before maturity are, however, subject to restrictions. Mexico can, for example, make use of a call option to redeem the bonds prior to maturity. But if the redemption is only partial, it must take all the creditors into account on a *pro rata* basis.<sup>128</sup> It is also permissible to buy back the bonds, in which case Mexico is subject to no restrictions in the choice of the creditors to whom repayment is offered.<sup>129</sup> For buying back discount and par bonds, however, it is a condition that Mexico must not be in arrears with the payment of interest and that the revolving security on interest is completely guaranteed. This second condition ceases to apply as soon as the commercial bank bridge

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123. Bouchet & Hay, *supra* note 31, at 150.

124. See sources cited *supra* note 33.

125. WORLD BANK, *supra* note 3, at 52.

126. See *infra* III.A.2.

127. Very few of the more than 400 creditor banks have, consequently, refused to participate in the new Mexican package.

128. See MEXICAN DISCOUNT AND PAR BOND EXCHANGE AGREEMENT OF 1990, Exhibit I A, at 14; MEXICAN NEW MONEY BOND SUBSCRIPTION AGREEMENT OF 1990, Exhibit I, at 9.

129. *Id.*

facility<sup>130</sup> has been repaid, but at the earliest by January 1, 1995.<sup>131</sup> At a later date the buying back of discount and par bonds from any creditors is permissible provided that there are no interest payments outstanding.

In the other agreements — that is, the new credit agreements<sup>132</sup> (with the exception of the New Money Bond Subscription Agreement) and the agreements which form part of the novation replacing the existing agreements — the sharing clause is retained but two further exceptions are added. On the one hand, a new section 5.12 permits a buy-back of debts prior to maturity, with Mexico required to offer the buy-back to all the creditors participating in the agreement. The sum of permissible debt buy-backs per calendar year is limited to a maximum calculated on the basis of currency reserves, expenditures on imports, current interest payments, and the new credits to be granted to Mexico in the future.<sup>133</sup>

On the other hand, the concept of “qualified debt” in section 5.11 was extended. Previously, this had accorded a privileged position only to conversions that involved an exchange of existing debts for new indebtedness with a longer maturity or that were offered to all the creditors on a *pro rata* basis.<sup>134</sup> A third variant was now added permitting exchanges for new debt with a shorter maturity than the older indebtedness, provided they went hand in hand with a sufficient remission of debt in Mexico’s favor. In order to calculate this amount, section 5.11 contains a detailed formula according to which the length of maturity can be shorter, if the the amount of remission accepted by the creditor is higher.<sup>135</sup>

## (ii) Mandatory Prepayment Clause

The mandatory prepayment clause was not included in the agreements on the three different types of bonds. This means that Mexico’s payments on other debts before the due date originally fixed for these

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130. A \$1.2 billion package granted by a group of commercial banks — in addition to funds extended by the World Bank, the International Monetary Fund and the Japanese Export-Import Bank — for the purpose of financing the collateral of the bonds.

131. MEXICAN DISCOUNT AND PAR BOND EXCHANGE AGREEMENT OF 1990, Exhibit I A, at 15.

132. The MEXICAN 1989-1992 CREDIT AGREEMENT OF 1990; The MEXICAN ONLENDING AND TRADE CREDIT AGREEMENT OF 1990.

133. See the MEXICAN COMBINED OLD NEW MONEY AGREEMENT OF 1990, §§ 5.12 and 8.02, reprinted in Appendix V.

134. See *supra* notes 99-103 and accompanying text.

135. The definition of Qualified Debt from § 5.11 of the new agreements is reprinted in Appendix VI.

agreements and payments to free riders who have not participated in the financing package have no effect on the claims of the bondholders.

The clause is inserted in the new credit agreements. It takes effect, however, only in the event of payments prior to maturity on claims of the International Monetary Fund, the World Bank, and other public creditors.<sup>136</sup>

The mandatory prepayment clause in the then-customary form, *i.e.*, also dealing with payments to other private creditors, was included in those agreements that replaced the old agreements of creditors providing fresh money.<sup>137</sup> In this case, conversions in accordance with section 5.11 and debt buy-backs in accordance with section 5.12 of the original Mexican Agreements were excluded from the sphere of operation of the clause.

### (iii) Negative Pledge Clause

In all agreements apart from the New Money Bond Agreements, the furnishing of securities to third parties continues to be forbidden.<sup>138</sup> The catalogue of exceptions valid up to that time<sup>139</sup> was, however, extended to include some further cases.<sup>140</sup> The following are to be permitted:<sup>141</sup>

(a) securities in favor of the discount and par bond creditors and — to an equal extent — securities on other existing loans and new indebtedness entered into by Mexico in connection with debt conversions;

(b) liens on cash on hand, deposits in banks, certificates of deposits, bankers' acceptances, debt and equity securities, and intangible assets, with the exception of accounts receivable deriving from the sale of goods and the provision of services. These are limited to a maximum amount, calculated on the basis of currency reserves, the cost of imports, the scope of buy-backs in accordance with section 5.12, and the amount of current interest payments;

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136. The MEXICAN 1989-92 CREDIT AGREEMENT OF 1990, § 4.02; The MEXICAN ONLENDING AND TRADE CREDIT AGREEMENT OF 1990, § 4.02.

137. MEXICAN COMBINED OLD NEW MONEY AGREEMENT OF 1990, at § 4.02; COMBINED FACILITIES 2 AND 3 AGREEMENT OF 1990, § 4.02; MEXICAN COMBINED MULTI-YEAR RESTRUCTURE AGREEMENT OF 1990, § 4.02. In the last-named agreement, however, payments prior to maturity to public creditors are excluded.

138. In the case of discount and par bonds, this prohibition only applies if Mexico is in arrears with the payment of interest to the bond holders; *see* the MEXICAN DISCOUNT AND PAR BOND EXCHANGE AGREEMENT OF 1990, Exhibit VII, § 16(a).

139. *See supra* note 52 and accompanying text.

140. *See, e.g.*, the MEXICAN 1989-1992 CREDIT AGREEMENT OF 1990, § 7.02(a).

141. The text of the newly introduced exceptions is reprinted in Appendix VII.

(c) the use of the proceeds from new credits as security, provided this occurs within three months after disbursement;

(d) liens on accounts receivable (insofar as they do not stem from the sale of oil or gas) and other tangible assets apart from gold and the assets already mentioned in (b);

(e) liens on the foreign currency indebtedness of Mexico and its governmental agencies which are owed directly or indirectly to the banks it controls (Mexican banks), their affiliates and branches, in as far as they are established with the sole purpose of raising new funds for these banks (special purpose affiliates), or which are owed to any other governmental agencies;

(f) liens on the properties or revenues of the Mexican banks and their special purpose affiliates to secure short-term indebtedness arising in connection with customary business or to secure new debts incurred in connection with the refinancing of existing debts to foreign banks.

All in all, therefore, Mexico has been accorded substantial room to maneuver in regard to the furnishing of securities. Future new indebtedness in connection with conversions designed to reduce debt can, in accordance with (a), be secured to the same degree as discount and par bonds. The other exceptions also apply to borrowing for the purpose of covering future financial needs. For Mexico, as an oil-exporting country, the fact that accounts receivable deriving from the sale of oil and gas continue to be excluded from use as security, does, however, represent a fundamental restriction.

#### IV. SUMMARY

As a result of the persistence of the debt crisis and, above all, the launching of the Brady Initiative, the principle of equal treatment has been modified by the introduction of various options into the terms of the restructuring packages. This permits differences in the treatment of the creditor banks, which can now behave in accordance with their individual interests, without having to subject themselves to a joint strategy. The restructuring process thus splits the former creditors into two groups. On the one hand, there are the banks that wish to maintain their presence in the debtor countries concerned and, consequently, are willing to provide fresh money. On the other hand, there are the banks that want to withdraw by opting for debt buy-backs or some form of conversion, or which adopt a passive attitude. Furthermore, some Third World debtors are successfully finding their way back to the international financial markets and covering a part of their



capital requirements by issuing bonds at high rates of interest.<sup>142</sup>

The move away from the principle of equal treatment will lead in the future to competition among creditors over the distribution of foreign currency by the debtor countries. In view of their continuing need for capital, the debtors will offer preferential treatment to those banks that are willing to provide fresh money. Apart from the possibility of providing security, the debtors will endeavor to service the debts of these banks preferentially in order to create incentives for the provision of new credits. At the same time, those banks that wish to withdraw from the Third World countries by opting for buy-backs or some form of conversion, or that choose to adopt a passive attitude, will no longer profit from sharing obligations of the new money banks. In view of the continuing lack of foreign currency of the debtors, they will also be forced to accept greater reductions in their claims.

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142. See *Pemex kehrt an den Euromarket zurück*, *HANDELSBLATT*, March 30/31, 1990, at 35, col. 3; *Public Eurobond Sale Successful*, *INT'L FIN. REV.*, March 24, 1990, at 33, col. 3.

APPENDIX I  
THE SHARING CLAUSE OF THE MEXICAN NEW  
RESTRUCTURE AGREEMENT OF 1985

SECTION 5.03. *Sharing of Payments; Etc.* (a) *Certain Terms Defined.* As used in this Section, the "Applicable Rate" for converting any amount denominated in one currency into another currency on any Calculation Date shall be the average of the buy and sell spot rates of exchange in the latter currency for the former currency at the close of business on the fifth Business Day next preceding such Calculation Date as quoted, in the absence of manifest error, by the *Financial Times* of London or, if such rates are not so quoted, by a comparable publication or source to be selected by the Servicing Bank; "Bank Payment Date" means the first Business Day falling at least five calendar days after the Calculation Date; "Calculation Date" means, with respect to any Reporting Period, the first Business Day falling at least 20 days after the end of such Reporting Period; "Sharing Request" means a notice to the Servicing Bank by any Bank, which notice may not be given prior to the first Interest Payment Date for a Credit of such Bank following the later of the Interest Change Date and the Reconciliation Date for such Credit, stating that such Bank has not received a payment of interest or principal or other amount due to such Bank under this Agreement, that such Bank considers such unpaid amount to be significant and that such Bank requests that the sharing provisions of this Section 5.03 be implemented; "Reporting Bank" means, with respect to any Reporting Period, a Bank that has delivered a report to the Servicing Bank pursuant to subsection (d) of this Section; and "Reporting Periods" means successive periods commencing on the date of a Declaration or the Servicing Bank's receipt of a Sharing Request, the first of which shall be two calendar months and the remainder of which shall be three calendar months.

(b) *General Requirement of Sharing.* Each Bank agrees that if it shall at any time, through exercise of a right of banker's lien, setoff, litigation or counterclaim or otherwise, obtain payment with respect to the principal of or interest on the Credits owed to it that is proportionately greater than the payment obtained by any other Bank with respect to the principal of or interest on the Credits owed to such other Bank, the Bank obtaining such proportionately, greater payment shall purchase from each such other Bank, in the manner and on the terms set forth in this Section, a participation in the principal of or interest on such other Credits in such amount (and such other adjustments shall be made from time to time) as shall be required to ensure that the Banks share such payments ratably as contemplated by this Section, *provided* the obligation to share as required by this Section shall not exist until there has been a Declaration or a Sharing Request, whereupon each Bank shall perform its obligations under this Section strictly in accordance with its terms and *provided further* that this Section shall not impair any right of any Bank to apply amounts recovered by it to pay indebtedness other than amounts due under this Agreement. Disproportionate payments of interest shall be shared by the purchase of separate participations in unpaid interest obligations and disproportionate payments of principal

shall be shared by the purchase of separate participations in unpaid principal obligations. In addition, the Banks agree to share disproportionate payments of amounts other than interest on and principal of the Credits due under this Agreement, any disproportionate payment of any such other amount to be shared separately by participation and by type of payment (expenses, etc.) due and obtained.

(c) *Notifications.* Each Bank shall immediately notify the Servicing Bank of the amount and type of any payment obtained by such Bank after the later of the Interest Change Date and the Reconciliation Date of any Credit of such Bank with respect to such Credit, other than through the Servicing Bank, of any amount due to such Bank under this Agreement, and the Servicing Bank shall promptly notify the other Banks thereof. The Servicing Bank shall immediately notify all Banks of its receipt of a Sharing Request, which notice shall identify (i) the Bank or Banks submitting a Sharing Request and (ii) the first Reporting Period.

(d) *Reports by Banks.* Within five days after the end of each Reporting Period, each Bank shall deliver a report to the Servicing Bank stating whether or not it obtained any payment during such Reporting Period and, if so, the separate amounts of such payments received for principal, interest of other amounts due under this Agreement (and, in the case of the first such Reporting Period, the existence and amounts of any such payments received by such Bank prior to such Reporting Period), *provided* that a Bank need not report any such payment received as a distribution of funds by the Servicing Bank.

(e) *Calculations.* On each Calculation Date, the Servicing Bank shall:

(i) determine the aggregate amount of all payments for principal, interest and other amounts reported to the Servicing Bank pursuant to subsection (d) of this Section within the time period therein specified (excluding payments shared pursuant hereto as of any previous Calculation Date);

(ii) determine the portion of such aggregate amounts of principal, interest and other amounts that would be allocated to each Reporting Bank to ensure that the Reporting Banks share such aggregate amounts ratably in proportion to the aggregate unpaid principal, interest and other amounts owed to a Reporting Bank as of the end of the immediately preceding Reporting Period;

(iii) give notice by telex or cable to each Reporting Bank that has received payments in excess of its ratable share specifying (A) the amounts of such excess in U.S. Dollars and the amounts of participations in the principal of or interest on the Credits and in the other amounts owed to other Reporting Banks in each currency to be purchased by such Bank with such excess to accomplish such ratable sharing and (B) the Bank Payment Date on which sharing payments shall be made; and

(iv) give notice by telex or cable to each Reporting Bank that has received payments of less than its ratable share specifying the aggregate amounts of participations in the principal of or interest on the

Credits and in the other amounts owed to it to be purchased from it to accomplish such ratable sharing.

For purposes of calculations under this Section the Servicing Bank shall convert to U.S. Dollars all relevant amounts in other Credit Currencies at the appropriate Applicable Rate for the relevant Calculation Date and shall make distributions pursuant to subsection (f) of this Section on the basis of the U.S. Dollar amounts so calculated.

(f) *Payment for Participations.* On each Bank Payment Date, each Bank required to purchase participations shall pay the excess amounts specified in such notice to the Servicing Bank in the currency in which such excess amounts were due to such Bank hereunder. The Servicing Bank shall convert all such payments received by it in currencies other than U.S. Dollars into U.S. Dollars and for such purpose is authorized to enter into currency exchange transactions on such dates and in such amounts as it, in its sole discretion, shall determine. On the first Business Day falling at least ten calendar days after the Calculation Date and from time to time thereafter, at such intervals as the Servicing Bank in its sole discretion shall determine, the Servicing Bank shall distribute to the Banks from which participations are to be purchased their respective proportionate shares of the U.S. Dollars theretofore received by the Servicing Bank pursuant to this subsection (less any commissions or other costs arising out of such currency exchange transactions). No adjustment shall be made in the amount of any participation because the exchange value of any U.S. Dollars received by the seller of such participation is different on the date of receipt from the exchange value used to determine the amount of such participation or because commissions and other costs were deducted from amounts otherwise payable to such Bank or because of any fluctuation of exchange rates.

(g) *Accounting for Participations.* The Servicing Bank shall keep records (which shall be conclusive absent manifest error) of participations in principal, interest and other amounts purchased and sold pursuant to this Section. Notwithstanding any provisions hereof to the contrary, the Servicing Bank shall give effect to the purchases and sales of participations reflected from time to time in such records for purposes of (i) subsequent distributions to the Banks pursuant to this Article V and (ii) subsequent calculations and distributions pursuant to this Section. The rights of the owner of any such participation in a Credit against the Bank to which such Credit is owed shall be limited to the right to receive distributions with respect thereto from the Servicing Bank as provided in this Section and to share in any other payments received by such Bank as provided in this Section. It is understood that each Bank shall retain all voting rights with respect to its Credits, irrespective of the sale of any participations in any such Credits pursuant to this Section.

(h) *Interest on Sharing Payments in Default.* Any Bank which defaults in its obligation to make a sharing payment pursuant to subsection (f) above shall pay interest to the Servicing Bank for the account of the Banks entitled to participate in the sharing payment of such Bank, such interest to accrue on the amount of the sharing payment in default from the relevant Bank Payment Date, to be payable on demand and to be

calculated at a rate per annum equal to the highest interest rate applicable to the Credits of such defaulting Bank, or, if Credits of such defaulting Bank are no longer outstanding, to the highest interest rate which would be applicable to such Credits if they were outstanding.

(i) *Rescission of Shared Payment.* If any payment obtained by any Bank from the Obligor, the Guarantor or Banco de Mexico is rescinded or otherwise restored, and such payment has been shared by such Bank pursuant to the provisions of this Section 5.03, then each Bank shall promptly return to the Servicing Bank for the account of such Bank the amount in U.S. Dollars calculated by the Servicing Bank to be attributable to the amount of the payment previously shared which is rescinded or restored.

(j) *Further Implementation.* The Servicing Bank may (but shall not be required to) suggest such additional procedures or adjustments under this Section as it in its reasonable discretion may consider necessary or appropriate to effectuate the purposes of this Section, but no such suggestion by the Servicing Bank shall bind or charge the obligations of the Banks or the Servicing Bank under this Section unless accepted in writing by all Banks.

(k) *Obligor and Guarantor Acknowledgment.* The Obligor and the Guarantor each acknowledges and consents to the foregoing provisions of this Section 5.03.

APPENDIX II  
THE MANDATORY PREPAYMENT CLAUSE OF THE  
MEXICAN NEW RESTRUCTURE AGREEMENT  
OF 1985

SECTION 4.02. *Mandatory Prepayments.* (a) *Upon More Favorable Payments of 1984 Debt Subject to Restructure.* If after the date hereof any Foreign Currency of the Obligor, the Guarantor, Banco de Mexico or any other Mexican Public Sector Borrower shall be applied to repay, in whole or in part, the principal amount of any 1984 Debt Subject to Restructure, the Obligor shall on the next Interest Payment Date for each Credit prepay such Credit by a principal amount which bears the same relationship to the principal amount of such Credit then outstanding (before giving effect to such repayment) as the principal amount of the 1984 Debt Subject to Restructure so repaid bears to the aggregate principal amount of such 1984 Debt Subject to Restructure outstanding on the date of such repayment (before giving effect to such repayment), *provided* that this subsection shall not apply to any repayment of any 1984 Debt Subject to Restructure:

(i) in the case of a repayment of 1984 Debt Subject to Restructure of the Obligor, if both (x) the sum of such repayment and all other repayments of 1984 Debt Subject to Restructure of the Obligor made in the calendar year in which such repayment is made does not exceed the amount specified in item 19 of Schedule I to this Agreement (or its equivalent in other currencies) and (y) the sum of such repayment and all other repayments of 1984 Debt Subject to Restructure of all Mexican Public Sector Borrowers (including the Obligor) made in the calendar year in which such repayment is made does not exceed U.S.\$50,000,000 (or its equivalent in other currencies), *provided* that any portion of either such permitted amount not utilized in any calendar year may be utilized in the following calendar year as more fully described below; or

(ii) in the case of a repayment of 1984 Debt Subject to Restructure of a Mexican Public Sector Borrower other than the Obligor if both (x) such repayment does not require mandatory repayment under the New Restructure Agreement, if any, of such Mexican Public Sector Borrower and (y) the sum of such repayment and all other repayments of 1984 Debt Subject to Restructure of all Mexican Public Sector Borrowers (including the Obligor) made in the calendar year in which such repayment is made does not exceed U.S. \$50,000,000 (or its equivalent in other currencies), *provided* that any portion of such permitted amount not utilized in any calendar year may be utilized in the following calendar year as more fully described below; or

(iii) if such repayment is (x) an involuntary prepayment made pursuant to illegality provisions of existing contracts applicable to such 1984 Debt Subject to Restructure or (y) a prepayment permitted by substitute LIBO provisions of another New Restructure Agreement whose substitute LIBO provisions are comparable to the substitute LIBO provisions of this Agreement; or

(iv) if such repayment is a prepayment made pursuant to the mandatory prepayment provisions of another New Restructure Agreement whose mandatory prepayment provisions are comparable to the mandatory prepayment provisions of this Agreement; or

(v) if such repayment is made from assets or revenues subject to a Lien existing on August 23, 1982 and created to secure or provide for the payment of such 1984 Debt Subject to Restructure or from the proceeds of such assets or revenues; or

(vi) if such repayment is made pursuant to a repayment schedule for 1984 Specified Debt consistent with the Financing Principles.

For purposes of determining that portion, if any, of the permitted amounts referred to in clauses (x) and (y) of subsection (i) and clause (y) of subsection (ii) above which is available to be carried forward to a succeeding year, repayments of 1984 Debt Subject to Restructure made in any calendar year shall be applied, first, against that part, if any, of such permitted amount which was not utilized in, and was carried over from, the preceding calendar year, and, *second*, against that part of such amount which first became available for the calendar year of such repayment. Each partial prepayment with respect to a Credit pursuant to this Section shall reduce the principal installments applicable to such Credit in the inverse order of their maturities. The Obligor shall give the Servicing Bank irrevocable notice of any prepayment pursuant to this Section at least five Business Days prior thereto, specifying the principal amount of Credits to be prepaid and the date of such prepayment, whereupon the principal amounts so specified, together with interest accrued thereon, shall become due and payable on the date so specified.

(b) *Upon Repayments of Other Debt.* In the event the Obligor, the Guarantor, Banco de Mexico or any other Governmental Agency shall voluntarily repay Other Debt (as defined below) earlier than as required by the payment schedule therefor as in effect on the date hereof (each such repayment being a "Prepayment of Other Debt"), then the Obligor shall prepay each Credit by a principal amount which bears the same relationship to the principal amount of such Credit then outstanding (before giving effect to such repayment) as the principal amount of the Other Debt so repaid bears to the principal amount of such Other Debt outstanding on the date of such repayment (before giving effect to such repayment), *provided* that this subsection shall not apply to any repayment of any Other Debt:

(i) if such repayment is (x) an involuntary prepayment made pursuant to illegality provisions of contracts applicable to such Other Debt, (y) a prepayment permitted by increased cost or substitute LIBO provisions of contracts applicable to such Other Debt, or (z) a prepayment made pursuant to any other similar contractual provision specifically designed to enable the obligor to avoid economically burdensome results; or

(ii) to the extent a credit facility relating to such Other Debt is utilized again by the obligor within thirty days of such repayment.

Prepayments of each Credit shall be made in the Credit Currency of such Credit and shall be made on the first Interest Payment Date for

each Credit falling after the prepayment obligation arises, and on each Interest Payment Date thereafter in the event of additional Prepayments of Other Debt. As used herein, "*Other Debt*" means all External Indebtedness outstanding on August 23, 1982 which does not constitute either Specified Debt, 1984 Specified Debt or obligations under leases. The prepayment obligation under this subsection (b) shall arise in each calendar year when the U.S. Dollar equivalent (as computed in accordance with Section 13.16) of the Prepayments of Other Debt made in such year equals the sum of (i) U.S. \$50,000,000 plus (ii) any additional amount available for use in such year pursuant to the next sentence. Any portion of such U.S. \$50,000,000 minimum permitted Prepayments of Other Debt which is not utilized in any calendar year may be utilized in subsequent calendar years. Within 30 days after the end of each calendar quarter, the Guarantor will report to the Servicing Bank all Prepayments of Other Debt, if any, during the preceding calendar quarter, and the Servicing Bank shall give prompt notice thereof to the Banks. Any prepayment of the Credits pursuant hereto shall be applied to the principal installments of each Credit in the inverse order of maturity.



APPENDIX III  
CATALOGUE OF EXCEPTIONS TO THE NEGATIVE PLEDGE  
CLAUSE OF THE MEXICAN NEW  
RESTRUCTURE AGREEMENT OF 1985

- (i) Liens upon any property acquired or held by any Governmental Agency incurred to secure the purchase price of such property or to secure External Indebtedness incurred for the purpose of financing the acquisition of such property and any renewal or extension of any such Lien which is limited to the original property covered thereby and which secures any renewal or extension of the original secured financing; or
- (ii) Liens existing on such property at the time of its acquisition and any renewal or extension of any such Lien which is limited to the original property covered thereby and which secures any renewal or extension of the original secured financing, *provided* that the aggregate principal amount of the External Indebtedness secured by the Liens referred to in clause (i) above and this clause (ii) above does not exceed 120% of the purchase price of such property at any time outstanding; or
- (iii) Liens in favor of the Bank for International Settlements or other multilateral monetary authorities or central banks or treasuries of sovereign states other than the United Mexican States securing extensions of credit the duration of which does not exceed one year; or
- (iv) Liens arising in the course of ordinary commercial banking transactions (and expiring within one year thereafter) to finance the importation or exportation of goods or services into or from the United Mexican States; or
- (v) Liens on property acquired (or deemed to be acquired) by the Guarantor or any Governmental Agency under a financial lease, or claims arising from the use or loss of or damage to such property, *provided* that (A) any such Lien secures only rentals and other amounts payable under such lease and (B) either (x) such property was not owned by the Guarantor or any Governmental Agency at any time prior to becoming subject to such lease unless at the time of the acquisition of such property contractual arrangements contemplated that such lease would be executed or (y) such property was acquired from an entity other than the Guarantor or a Governmental Agency within one year prior to the execution of such lease; or
- (vi) Liens which arise pursuant to any order of attachment, distraint or similar legal process arising in connection with court proceedings and Liens which secure the reimbursement obligation for any bond obtained in connection with the release of property from Liens arising pursuant to such legal process, so long as the execution or other enforcement of such Liens arising pursuant to such legal process is effectively stayed and the claims secured thereby are being contested in good faith by appropriate proceedings, *provided* that any such Lien is released or discharged in any case within one year of its imposition; or
- (vii) Liens arising by operation of law (and not pursuant to any agreement) which have not been foreclosed or otherwise enforced against the properties to which they apply; or
- (viii) Liens securing or providing for the payment of External Indebted-

ness incurred in connection with any Project Financing, *provided* that the properties to which any such Lien applies are (A) properties which are the subject of such Project Financing or (B) revenues or claims which arise from the operation, failure to meet specifications, failure to complete, exploitation, sale or loss of, or damage to, such properties; or

(ix) Liens in existence on the date hereof, *provided* that such Liens remain confined to the properties presently affected thereby and properties which become affected by such Liens under contracts in effect on the date of this Agreement and *provided further* that such Liens secure or provide for the payment of only those obligations so secured or provided for on the date hereof or any refinancing of such obligations; or

(x) Liens arising in connection with contracts entered into substantially simultaneously for sales and purchases at market prices of precious metals; or

(xi) any Lien on Exportable Assets securing External Indebtedness incurred to finance the business of producing and/or exporting such Exportable Assets, *provided* that (A) such Lien applies only to goods which are expected to be sold or documents evidencing title thereto and the proceeds of any insurance thereon, and the proceeds of sale of which are expected to be received within 12 months after such goods or proceeds become subject to such Lien and (B) such External Indebtedness (i) is incurred in the normal course of business, (ii) is to be repaid primarily out of proceeds of sale of the Exportable Assets, subject to such Lien and (iii) does not arise out of financing provided by the lender with a view to obtaining repayment of other External Indebtedness or on condition that other External Indebtedness be repaid and (C) such Lien is not on oil or gas or the right to receive payment for oil or gas.

As used in this subsection, "*Exportable Assets*" means goods which are sold or intended to be sold for a consideration consisting of or denominated in Foreign Currency and any right to receive Foreign Currency in connection with the sale thereof; and "*Project Financing*" means any financing (but not a refinancing) of the acquisition, construction or development of any properties in connection with a project if the Person or Persons providing such financing expressly agree to look to the properties financed and the revenues to be generated by the operation of, or loss of or damage to, such properties as the principal source of repayment for the moneys advanced and have been provided with a feasibility study prepared by competent independent experts on the basis of which it was reasonable to conclude that such project would generate sufficient foreign currency income to repay substantially all of the principal of and interest on all External Indebtedness incurred in connection with such project.

APPENDIX IV  
SECTION 5.11 OF THE MEXICAN AGREEMENTS IN THE  
RESTRUCTURING ROUND OF 1987

**SECTION 5.11. *Exchange of Advances.*** (a) *General; Definitions.* This Section 5.11. sets forth procedures for the exchange of Advances for Qualified Capital Stock, Qualified Debt or a Qualified Investment. For purposes of this Section 5.11, the following terms shall have the following meanings:

“*Mexican Person*” means any Person who, in the case of an individual, is a national of the United Mexican States or, in the case of an entity, has its principal place of business in the United Mexican States.

“*Qualified Capital Stock*” means capital stock (including equivalent interests) of any Mexican public sector entity or Mexican private sector company (including a partnership or trust) (i) which is issued in registered, certificated form in the name of such Bank or a Person designated by such Bank which is not a Mexican Person, (ii) which is not transferable on the registration books of such public sector entity or private sector company before January 1, 1998 to any Mexican Person and the certificate of which bears a legend with such restriction, (iii) which is not by its terms subject to redemption earlier than the amortization of the Advance or Advances exchanged for such capital stock, (iv) which is not entitled to guaranteed dividends payable irrespective of earnings and profits, except as expressly contemplated by Article 123 of the *Ley General de Sociedades Mercantiles*, and (v) which is not convertible into any instrument or security other than Qualified Capital Stock.

“*Qualified Debt*” means indebtedness of any Mexican public or private sector entity that (a) has a Weighted Average Life to Maturity not less than the Weighted Average Life to Maturity of the Advance of Advances exchanged for such indebtedness at the time of such exchange or (b) is offered in exchange for all Advances (or a portion thereof) under any Facility to all Banks *pro rata* in accordance with the principal amount of their Advances under such Facility on the same terms; where

“*Weighted Average Life to Maturity*” means, with respect to any indebtedness at the time of determination, the number of years obtained by dividing the then Remaining Dollar-Years of such indebtedness by the then outstanding principal amount of such indebtedness, and

“*Remaining Dollar-Years*” means, with respect to any indebtedness at the time of determination, the amount obtained by (a) multiplying the amount of each then remaining required repayment, including each final maturity, sinking fund payment, installment maturity, serial maturity or other required payment or redemption, by the number of years (calculated to the nearest one-quarter) which will elapse between the time of determination and the date of the making of that repayment or redemption and (b) totalling all of the products obtained in (a).

“*Qualified Investment*” means the payment by a Mexican Person of indebtedness denominated in Mexican pesos owed to a Mexican bank or trust (including FICORCA), the purchase by a Mexican Person of capital assets located in Mexico (including capital stock of a Mexican com-

pany) and capital expenditures and other categories of approved expenditures by a Mexican Person, to the extent such payments, purchases and expenditures are specifically authorized by all appropriate Mexican governmental authorities.

“*Section 5.11 Notice*” means a notice substantially in the form of Exhibit 22 delivered to the Agent pursuant to this Section 5.11 upon the exchange of an Advance for Qualified Capital Stock, Qualified Debt or a Qualified Investment.

“*Section 5.11 Notice Acknowledgment*” means for each exchange of Advances described in a Section 5.11 Notice, a notice substantially in the form of Exhibit 23 delivered by the Agent to the Bank and the Borrower pursuant to this Section 5.11 acknowledging the particulars of such exchange.

(b) *Exchange of Advances for Qualified Capital Stock.* Subject to written agreement between the Borrower and any Bank and subject to all required Mexican governmental authorizations, including authorization by the Ministry of Finance and Public Credit, the National Commission on Foreign Investment and the Ministry of Foreign Relations of the United Mexican States, all or a portion of the Advances held by such Bank may be exchanged for Qualified Capital Stock. The Borrower and such Bank will promptly notify the Agent in writing of any such agreement that has been so authorized, which notice shall specify each Advance (or portion thereof) to be exchanged for such Qualified Capital Stock. Upon delivery of such Qualified Capital Stock by or on behalf of the Borrower to such Bank or its designee, (i) each Advance (or portion thereof) in respect of which such Qualified Capital Stock is delivered shall cease to be an “Advance” and “External Indebtedness” for all purposes of this Agreement and the Borrower shall have no further obligations hereunder in respect of any such Advance (or portion thereof) and (ii) the Borrower and such Bank shall deliver to the Agent a Section 5.11 Notice reducing the principal amount of each such Advance by the principal amount exchanged for such Qualified Capital Stock.

(c) *Exchange of Advances for Qualified Debt.* Subject to written agreement between the Borrower and any Bank and subject to all required Mexican governmental authorizations, including authorization by the Ministry of Finance and Public Credit, all or a portion of the Advances held by such Bank may be exchanged for Qualified Debt. The Borrower and such Bank will promptly notify the Agent in writing of any such agreement that has been so authorized, which notice shall specify each Advance (or portion thereof) to be exchanged for such Qualified Debt. Upon delivery of such Qualified Debt by or on behalf of the Borrower to such Bank or its designee, (i) each Advance (or portion thereof) in respect of which such Qualified Debt is delivered shall cease to be an “Advance” and “External Indebtedness” for all purposes of this Agreement and the Borrower shall have no further obligations hereunder in respect of any such Advance (or portion thereof) and (ii) the Borrower and such Bank shall deliver to the Agent a Section 5.11 Notice reducing the principal amount of each such Advance by the principal amount exchanged for such Qualified Debt.

(d) *Exchange of Advances for Qualified Investments.* In the event that the appropriate Mexican governmental authorities shall at any time so authorize, subject to written agreement between the Borrower, a Mexican Person and any Bank, all or a portion of the Advances held by such Bank may be acquired by a Mexican Person and used to make one or more Qualified Investments in accordance with applicable Mexican governmental rules and regulations. The Borrower and such Bank will promptly notify the Agent in writing of any such agreement that has been so authorized, which notice shall specify each Advance (or portion thereof) to be acquired by such Mexican Person and used for such Qualified Investment. Upon such Bank's notification to the Agent of its transfer of each such Advance (or portion thereof) to such Mexican Person in contemplation of a Qualified Investment approved by all appropriate Mexican governmental authorities, (i) each Advance (or portion thereof) to be used for such Qualified Investment shall cease to be an "Advance" and "External Indebtedness" for all purposes of this Agreement and the Borrower shall have no further obligations hereunder in respect of any such Advance (or portion thereof) and (ii) the Borrower and such Bank shall deliver to the Agent a Section 5.11 Notice reducing the principal amount of each such Advance by the principal amount thereof acquired by such Mexican Person.

(e) *Limited Responsibility of the Agent.* The Agent shall have no responsibility to review or verify (i) the accuracy of the statements of the Bank and Borrower contained in any notice or Section 5.11 Notice received by it under this Section 5.11, (ii) that any exchange under this Section 5.11 satisfies the definition of Qualified Capital Stock, Qualified Debt or Qualified Investment or (iii) that any required authorization for any exchange under this Section 5.11 has been obtained. The Agent shall be entitled to rely on the information contained in each Section 5.11 Notice as to whether the requirements of this Section 5.11 have been satisfied.

(f) *Effect of a Section 5.11 Transaction.* It is understood and the parties concur that any exchange or cancellation of an Advance (or portion thereof) hereunder pursuant to this Section 5.11 or any exchange or cancellation of any credit or advance or other payment obligation (or portion thereof) pursuant to Section 5.11 of the 1983 New Money Agreement, the 1984 New Money Agreement, any Restructure Agreement or any New Restructure Agreement or pursuant to any comparable provision of the FICORCA Facility Agreement shall not constitute for purposes of this Agreement receipt of a payment in respect of any Advance hereunder or of any other credit or advance or other obligation so exchanged or cancelled and shall not (i) give rise to a prepayment obligation under Section 4.02 of this Agreement or (ii) be subject to the sharing requirements of Section 5.03 of this Agreement.

(g) *Closing Date for a Section 5.11 Exchange.* The Borrower and the Bank shall give the Agent not less than ten calendar days' notice of any proposed exchange under this Section 5.11, and the closing date for any such exchange shall be subject to mutual agreement between the Borrower and the Agent in order to facilitate the efficient administration of this Agreement. Each Section 5.11 Notice shall be effective upon ac-

knowledge (including telex acknowledgment) by the Agent pursuant to a Section 5.11 Notice Acknowledgment.

(h) *Special Provision for Notices to the Agent.* Each Section 5.11 Notice is a communication to the Agent from both the Borrower and a Bank. Each such Notice specifies the amount of the reduction in the principal amount of one or more Advances. The form of each such Section 5.11 Notice requires that both the Borrower and such Bank send each such Notice to the Agent. The requirement of joint notice by the Borrower and the Bank may be satisfied in any one of three ways:

(i) By joint signature and delivery to the Agent by the Borrower and a Bank of any such Notice;

(ii) By separate transmittal to the Agent (including telex or facsimile transmittal acceptable to the Agent) by each of the Borrower and a Bank of a substantially identical Notice; or

(iii) By transmittal to the Agent (including telex or such facsimile) by either the Borrower or a Bank of any such Notice, followed by the Agent's receipt of written confirmation (including telex or such facsimile) by the other party to such Notice of the information set forth in such Notice, which confirmation shall be in form and substance satisfactory to the Agent.

(i) *Notice to IBRD.* A copy of each Section 5.11 Notice and each Section 5.11 Notice Acknowledgment describing any exchange pursuant to this Section 5.11 for a Facility 2 Advance or a Facility 3 Advance shall be sent to IBRD.

(j) *Reduction of IBRD Guaranty Amounts.* From the closing date of the reduction in the principal amount of any Facility 2 Advance occurring pursuant to an exchange under this Section 5.11, the IBRD Facility 2 Guaranty Amount shall be reduced by an amount equal to 50% of the U.S. Dollar equivalent of the amount of such reduction as provided in the definition of IBRD Facility 2 Guaranty Amount. From the closing date of the reduction in the principal amount of any Facility 3 Advance occurring pursuant to an exchange under this Section 5.11, the IBRD Facility 3 Guaranty Amount shall be reduced by an amount equal to 50% of the U.S. Dollar equivalent of the amount of such reduction as provided in the definition of IBRD Facility 3 Guaranty Amount.

APPENDIX V  
SECTION 5.12 OF THE MEXICAN COMBINED OLD NEW  
MONEY AGREEMENT OF 1990

SECTION 5.12. *Purchase of Advances.* (a) *General; Definitions.* This Section sets forth procedures for certain purchases of Advances. For purposes of this Section, the following terms have the following meanings:

“Section 5.12 Notice” means a notice substantially in the form of Schedule F delivered to the Agent under this Section upon the purchase of an Advance (or portion thereof) by the Borrower under this Section.

“Section 5.12. Notice Acknowledgment” means, for each purchase of an Advance (or portion thereof) by the Borrower described in a Section 5.12 Notice, a notice substantially in the form of Schedule G delivered by the Agent to the Bank and the Borrower pursuant to this Section 5.12 acknowledging the details of such purchase.

(b) *Purchase of Advances.* Subject to agreement between the purchaser and any Bank, the Borrower or (subject to Section 12.10 (b)) any Governmental Agency may purchase all or a portion of the Advances held by such Bank; *provided that*

(i) such purchase is made pursuant to an offer made to all Banks *pro rata* in accordance with the principal amount of their Advances on the same terms, and

(ii) immediately after and giving effect to such purchase, the sum of (x) the U.S. Dollar equivalent (as determined in accordance with Section 12.16 (a)) of the aggregate amount of cash used during the calendar year in which such purchase is made for all purchases of indebtedness (other than purchases of New Money Bonds) subject to the requirements of Section 5.12 (b) (ii) of any Mexican Debt Agreement (including this Agreement) and (y) the amount of Available Assets pledged during such calendar year in accordance with Section 8.02 (a) (xiii) and (xiv) does not exceed the sum of (1) the aggregate of the amounts specified in clauses (A) and (B) of Section 8.02 (a) (xiii) and (2) the amount permitted under Section 8.02 (a) (xiv).

Upon the purchase of all or a portion of an Advance by the Borrower, such Advance (or portion thereof) shall be deemed cancelled and shall cease to be an “Advance” and “External Indebtedness” for all purposes of this Agreement and the Borrower shall have no further obligations hereunder in respect of any such Advance (or portion thereof), and the Borrower and such Bank shall deliver to the Agent a Section 5.12 Notice reducing the principal amount of each such Advance by the principal amount of such Advance (or portion thereof) purchased by the Borrower.

(c) *Exceptions for Certain Purchases of Advances by Mexican Banks.*

(i) The requirements of Section 5.12 (b) (i) and (ii) shall not apply to the purchase of any Advance (or portion thereof) by any Mexican Bank (A) for its trading account in the ordinary course of business; (B) for its own account or for the account of another Governmental Agency (including the Borrower), in each case to the extent that such

Advance (or portion thereof) so purchased is used to make a Section 5.11 Qualified Investment or (C) for the account of any customer that is not a Governmental Agency.

(ii) The requirements of Section 5.12 (b) (i) shall not apply to the purchase of any Advance (or portion thereof) by a Mexican Bank (or any Special Purpose Affiliate) for its own account or for the account of another Governmental Agency (including the Borrower), in each case to the extent that the Advance (or portion thereof) so purchased is pledged to secure External Indebtedness of such Mexican Bank (or any Special Purpose Affiliate) or Governmental Agency.

(d) *Limited Responsibility of Agent.* The Agent shall have no responsibility to review or verify (i) the accuracy of the statements of the Bank and the Borrower contained in any Section 5.12 Notice or other notice received by it under this Section 5.12, (ii) that any purchase under this Section 5.12. satisfies the requirements of subsection (b) or (c) above, or (iii) that any required authorization for any purchase of Advances under this Section 5.12 has been obtained. The Agent shall be entitled to rely upon the information contained in each Section 5.12 Notice as to whether the requirements of this Section 5.12 have been satisfied. Promptly after its receipt of a Section 5.12 Notice, the Agent shall confirm that the information set forth therein is consistent with its records and, upon such confirmation, promptly acknowledge such Notice. Each Section 5.12 Notice shall be effective upon acknowledgment (including acknowledgment by telex or facsimile transmission) by the Agent pursuant to a Section 5.12 Notice Acknowledgment.

(e) *Effect of a Section 5.12 Transaction.* It is understood and the parties concur that any purchase or cancellation of an Advance (or portion thereof) hereunder pursuant to this Section 5.12, or any purchase or cancellation of any Other Indebtedness pursuant to Section 5.12 of any other Mexican Debt Agreement, shall not constitute for the purposes of this Agreement receipt of a payment in respect of any Advance hereunder or of any Other Indebtedness so purchased or cancelled and shall not (i) give rise to a prepayment obligation under Section 4.02 or (ii) be subject to the sharing requirements of Section 5.03. Any purchase of a portion of an Advance pursuant to this Section 5.12 shall be applied ratably to the principal installments of such Advance.

(f) *Closing Date for a Section 5.12 Purchase.* The Borrower and the Bank shall give the Agent not less than ten calendar days' notice of any proposed purchase by the Borrower under this Section, and the closing date for any such purchase shall be subject to mutual agreement between the Borrower and the Agent in order to facilitate the efficient administration of this Agreement.

(g) *Special Provision for Notices to the Agent.* Each Section 5.12 Notice is a communication to the Agent from both the Borrower and a Bank. Each such Notice specifies the amount of the reduction in the principal amount of one or more Advances. The form of each such Section 5.12 Notice requires that both the Borrower and such Bank send each such Notice to the Agent. The requirement of joint notice by the Borrower and the Bank may be satisfied in any one of three ways:



(i) by joint signature and delivery (including delivery by facsimile transmission) to the Agent by the Borrower and a Bank of any such Notice;

(ii) by separate transmittal to the Agent (including telex or facsimile transmission) by each of the Borrower and a Bank of a substantially identical Notice; or

(iii) by transmittal to the Agent (including telex or facsimile transmission) by either the Borrower or a Bank of any such Notice, followed by the Agent's receipt of written confirmation (including telex or facsimile transmission) by the other party to such Notice of the information set forth in such Notice, which confirmation shall be in form and substance satisfactory to the Agent.

(h) *Expenses to the Agent.* The Bank or Banks party to each purchase of Advances by the Borrower under this Section shall pay the reasonable expenses of the Agent to administer and record such purchase, unless the Borrower shall otherwise agree to pay such expenses.

APPENDIX VI  
THE NEW DEFINITION OF QUALIFIED DEBT IN THE  
NEW MEXICAN AGREEMENTS

“*Qualified Debt*” means indebtedness of any Mexican public or private sector entity (or of any non-Mexican entity that is owned or controlled by a Mexican Person or a Mexican public or private sector entity) that

(a) is offered in exchange for all Advances (or portion thereof) to all Banks *pro rata* in accordance with the principal amount of their Advances (or such portion thereof) on the same terms, or

(b) has a Duration at least equal to the Specified Duration, or

(c) has a Duration that is not less than the Specified Duration *minus* 1.5 years; *provided* that indebtedness exchanged for Advances in any single transaction shall not constitute “Qualified Debt” under this clause (c) unless the U.S. Dollar equivalent (as determined in accordance with Section 12.16 (a)) of the aggregate principal amount of such indebtedness:

(i) does not exceed U.S. \$500 million; and

(ii) when added to the U.S. Dollar equivalent (as so determined) of the aggregate principal amount of all other indebtedness constituting Qualified Debt pursuant to this clause (c) (but not pursuant to clause (a) or (b) above) and all Other Qualified Debt exchanged, in each case, for Advances or Other Indebtedness during the same calendar year, does not exceed the sum of (x) U.S. \$2.5 billion *plus* (y) the excess (if any) of U.S. \$2.5 billion over the U.S. Dollar equivalent (as so determined) of the aggregate principal amount of such Qualified Debt and Other Qualified Debt exchanged for Advances and Other Indebtedness during the immediately preceding calendar year.

For purposes of this definition of “Qualified Debt”:

(i) “*Specified Duration*” means, with respect to any new debt to be exchanged for Advances or for Other Indebtedness, a number of years equal to:

$$\frac{D_a \times PV_n}{PV_a}$$

where:

$D_a$  = the Duration of such Advances or Other Indebtedness;

$PV_n$  = the Present Value of such new debt; and

$PV_a$  = the Present Value of such Advances or Other Indebtedness;

*provided* that, if any new debt to be exchanged for Advances or Other Indebtedness is not denominated in the currency of such Advances or Other Indebtedness, the calculations of Specified Duration and Duration shall be made using the U.S. Dollar equivalent (as determined in accordance with Section 12.16 (a)) of the Present Value of such new debt and of such Advances or Other Indebtedness;

(ii) “*Duration*” means, with respect to any indebtedness, the number of years obtained by dividing (x) the Present Value Remaining Payment-Years of such indebtedness by (y) the Present Value of such indebtedness;

(iii) “*Present Value Remaining Payment-Years*” means, with respect to

any indebtedness, the sum of each of the products obtained by multiplying (x) the Present Value of each then remaining required repayment or payment (including each final maturity, sinking fund payment, interest payment (assuming, where the amount of such interest payment is based upon a variable or floating reference rate of interest, that such rate of interest is fixed at the rate in effect on the date of determination), installment maturity, serial maturity or other required payment) or redemption with respect to such indebtedness by (y) the number of years (calculated to the nearest one-quarter of a year) which will elapse between the time of determination and the date of the making of such repayment, payment or redemption;

(iv) "*Loan Currency Discount Rate*" means, (A) with respect to any indebtedness denominated in any Loan Currency (other than Italian Lire), the LIBO Rate for LIBO Rate Advances denominated in such Loan Currency (assuming an Interest Period of three months beginning on the date of determination) *plus* 13/16% per annum, (B) with respect to any indebtedness denominated in Italian Lire, the Italian Lira Domestic Rate (assuming an Interest Period of three months beginning on the date of determination) *plus* 13/16% per annum, and (C) with respect to any indebtedness denominated in a currency that is not a Loan Currency hereunder, the rate per annum determined by the Borrower to be the comparable yield in such currency;

(v) "*Other Qualified Debt*" means indebtedness that constitutes "Qualified Debt" pursuant to clause (c) of the definition of that term contained in Section 5.11 of the Mexican Debt Agreements other than this Agreement (but that would not constitute "Qualified Debt" pursuant to clause (a) or (b) of that definition); and

(vi) "*Present Value*" means, with respect to any indebtedness, the present value (calculated using the Loan Currency Discount Rate) of the aggregate amount of principal and interest to be payable in respect of such indebtedness.

APPENDIX VII  
ADDITIONAL EXCEPTIONS TO THE NEGATIVE PLEDGE  
CLAUSE IN THE NEW MEXICAN AGREEMENTS

(xii) (A) Liens in favor of the collateral agent for the Discount and Par Bonds securing the repayment of principal at maturity of the Discount and Par Bonds and the payment of interest on such Bonds in an amount not exceeding, for each Series of Bonds, the Original Level (as defined in the Discount and Par Bonds) (*less* any amounts released from such Lien after the Exchange Date under (and as defined in) the Discount and Par Bond Exchange Agreement as a result of any redemption, or purchase and cancellation, of all or part of the Discount and Par Bonds),

(B) any Liens securing the repayment of principal of, or the payment of interest on, other public issues of bonds of Mexico outstanding on the date hereof to the extent created to secure such bonds equally and ratably with the Discount and Par Bonds,

(C) any Liens securing the repayment of principal at maturity of, and the payment of a portion of the interest on, up to U.S. \$3.5 billion (or equivalent) principal amount of loans, bonds or other debt instruments ("*Exchanged Debt*") issued by Mexico upon surrender of instruments issued in connection with Mexico's debt conversion program in exchange for any Discount or Par Bond or indebtedness under any Mexican Debt Agreement, to the extent that such Liens are created to secure such Exchanged Debt on a basis comparable to the Discount and Par Bonds and

(D) any Liens securing the repayment of principal at maturity of, and the payment of a portion of the interest on, loans, bonds or other debt instruments ("*Substituted Debt*") issued upon surrender of Discount or Par Bonds, to the extent such Liens are created to secure such Substituted Debt on a basis comparable to the Discount and Par Bonds; *provided* that the terms of such Substituted Debt (including, but not limited to, interest rate and amortization) are no more favorable to the holders thereof than those of the Discount or Par Bonds, as the case may be, surrendered in exchange therefor; or

(xiii) Liens on Available Assets (as defined below) not permitted by any other clause of this subsection; *provided* that, after giving effect to any such Lien, the sum of (x) the U.S. Dollar equivalent (as determined in accordance with Section 12.16 (a)) of the aggregate Available Assets that become subject to such Liens (valuing each such Available Asset at its market value at the time the Lien on such Available Asset arises) in the calendar year in which such Lien is created (and excluding from such aggregate Available Assets any Available Assets previously subject to a Lien to secure External Indebtedness of the Borrower or any Governmental Agency and later released from such Lien) *plus* (y) the U.S. Dollar equivalent (as so determined) of the cash used during such calendar year to purchase indebtedness (other than purchases of New Money Bonds) subject to the requirements of Section 5.12 (b) (ii) of the Mexican Debt Agreements (including this Agreement) does not exceed the sum of

(A) U.S. \$500,000,000 *plus*

(B) 50% of the amount, if any, by which the aggregate amount of International Monetary Assets (adjusted as provided in clause (xiv) below) at the last day of the most recently ended February, May, August or November

*exceeds* the sum of

(1) U.S. \$500,000,000 *plus*

(2) 50% of the sum of (x) the U.S. Dollar equivalent (as determined in accordance with Section 12.16 (a)) of the aggregate cost of imports into the United Mexican States for the six-month period ending most recently before the date of determination, *plus* (y) the U.S. Dollar equivalent (as so determined) of the aggregate amount of interest payments required to be made during such six-month period by the Borrower and Governmental Agencies on External Indebtedness; or

(xiv) Liens on the proceeds of any loans or advances made to the Borrower of any Governmental Agency (other than Excluded Proceeds (as defined below)) that arise within three months after the date of disbursement of such loans or advances, it being understood that any portion of such proceeds not so pledged or used for the purchase of indebtedness under Section 5.12 of any Mexican Debt Agreement (including this Agreement) shall not be considered a part of International Monetary Assets for purposes of clause (xiii) above until three months after the date of its disbursement; or

(xv) Liens on Accounts Receivable (as defined below) and Tangible Assets (as defined below); or

(xvi) Liens on External Indebtedness of the Borrower or of any other Governmental Agency owed to any Mexican Bank, any Special Purpose Affiliate or any other Governmental Agency; or

(xvii) Liens on the properties or revenues of any Mexican Bank or any Special Purpose Affiliate:

(A) to secure the repayment of any liability that by its terms matures more than one year after the date of its incurrence and that is incurred by such Mexican Bank or any Special Purpose Affiliate in connection with the refinancing of

(1) any liabilities of the foreign agencies and branches of such Mexican Bank to one or more non-Mexican commercial banks, or

(2) in the case of any Mexican Bank that does not have a foreign agency or branch, existing money market lines of credit (including replacements thereof) payable in a Foreign Currency by such Mexican Bank to one or more non-Mexican commercial banks, including, in each case, a refinancing by means of the purchase of existing liabilities or money market lines and the pledge thereof in connection with such refinancing or,

(B) to secure any liability that by its terms is payable on demand or matures within one year after the date of its incurrence and that arises in the ordinary conduct of the commercial banking business of such Mexican Bank.

As used in this subsection (a),

“*Accounts Receivable*” means amounts payable on the Borrower or

any Governmental Agency in respect of the sale, lease or other provision of goods, energy, services or the like (other than oil or gas), whether or not yet earned by performance.

*"Available Assets"* means cash on hand or on deposit in banks, certificates of deposit and bankers acceptances, debt and equity securities and intangible assets (other than Accounts Receivable and accounts receivable deriving from the sale of oil and gas).

*"Excluded Proceeds"* means the proceeds of

(A) loans or advances made or bonds issued under the 1989 New Money Agreements,

(B) purchases under the 1989 IMF Extended Arrangement, to the extent such proceeds are intended to be used to purchase collateral for the Discount and Par Bonds,

(C) loans from IBRD, to the extent such proceeds are intended to be used to purchase collateral for the Discount and Par Bonds,

(D) loans from the Export-Import Bank of Japan in the amount of U.S. \$2,050,000,000 (including interim financing relating thereto) extended in conjunction with the official credits referred to in clauses (B) and (C) above,

(E) the 1989 Official Bridge Loan,

(F) the letters of credit issued pursuant to the Commercial Bank Bridge Facility, and

(G) loans or advances under the Oil Contingency Revolving Credit Agreement.

*"Tangible Assets"* means assets of the Borrower and Governmental Agencies other than (i) Available Assets, (ii) gold, (iii) oil and gas and accounts receivable deriving from the sale of oil and gas and (iv) Accounts Receivable.