

On the Feasibility of a Bi-National Bond Financing Mechanism for Strategic Border Infrastructure: Reviewing the U.S. and Mexican Legal Frameworks^(†)

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ABSTRACT

There is a growing gap between infrastructure needs and available funding along the U.S.-Mexico border. A recent proposal to address the situation calls for the creation of a bi-national mechanism of bond financing to enable sub-national governments from both countries to issue bonds jointly. Creating the legal infrastructure to attain this goal requires an evaluation of key aspects of existing regulations. It also calls for a discussion of the feasibility of regulatory harmonization. This article compares bond issuance rules and investor protection mechanisms in both countries and discusses how these differences may affect the viability of a bi-national bond mechanism.

Key words: U.S.-Mexico, border infrastructure, sub-sovereign bond markets, regulatory harmonization

RESUMEN

Existe una brecha creciente entre las necesidades de infraestructura y los fondos disponibles a lo largo de la frontera entre Estados Unidos y México. Una propuesta reciente para enfrentar la situación llama a la creación de un mecanismo binacional de financiamiento mediante la emisión de bonos que permita a los gobiernos subnacionales de ambos países emitirlos conjuntamente. Crear la base legal para lograr esta meta requiere la evaluación de aspectos clave en las regulaciones existentes y también supone una discusión abierta acerca de la viabilidad de la complementación regulatoria. Este artículo compara las normas para la expedición de bonos y los mecanismos de protección a los inversionistas en ambos países, y discute cómo estas diferencias pueden afectar la viabilidad de un mecanismo de emisión de bonos binacional.

Palabras clave: México-Estados Unidos, infraestructura fronteriza, mercados infrasoberanos de bonos, armonización regulatoria

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INTRODUCTION

Trade between Mexico and the United States has increased exponentially as a result of the North American Free Trade Agreement (NAFTA), but it has created a great need for border infrastructure. This need has not been paired with sufficient financial resources. Estimates show that, as of 2005, there was a funding shortfall in the area of transportation infrastructure of US\$860 million in Mexico and of US\$10.5 billion in the United States (Shane, 2005). Traditionally, border infrastructure in the United States has been funded with multi-year appropriations administered by federal agencies, state agencies, or metropolitan planning organizations. In Mexico, most funds for border infrastructure development come from the federal government, since it is responsible for federal and inter-state highways, international border crossings, bridges, and roadway projects (SourcePoint, 2004). These funding sources have been decreasing due to intense competition for federal funds and shifting priorities in the both countries' policy agendas. The issue has forced policymakers to think about innovative funding methods to attract alternative capital sources to the border region.

In Mexico, the tendency has been to rely on concessions and service delivery agreements with the private sector (SCT, 2006). The U.S. has relied upon various forms of credit assistance (for example, section 129 loans, state infrastructure banks, and TIFIA funds),¹ tolling options (for example, general toll provisions, interstate reconstruction and rehabilitation programs, and value pricing pilot programs), or innovative management of federal funds (advance construction, partial conversion of advance construction, toll credits, or tapered and flexible match strategies, etc.) (Federal Highway Administration, 2002). Despite their usefulness, these mechanisms have been insufficient in closing the gap between infrastructure needs and available funds.

Even further, since the implementation of NAFTA, studies suggest that although trade has almost tripled, obstacles exist that increase transaction costs and undermine the benefits gained from the removal of tariffs (Villa, 2007). Some of these obstacles are related to insufficient investment in strategic border infrastructure (Colegio de la Frontera Norte and Woodrow Wilson International Center for Scholars, 2009). Financing for some of these projects can be obtained from philanthropic organizations, taxation, user fees, partnerships with the private sector, or bond markets (Erickson and Eaton, 2002). Our focus, however, is on an emerging body of literature that addresses the issue of infrastructure finance from a cross-border perspective.

The starting point for the study is a recent proposal to create a bi-national mechanism of debt finance for environmental infrastructure along the U.S.-Mexico border

¹ Transportation Infrastructure Finance and Innovation Act.

(Espinosa, 2012). The aim would be to facilitate private investor participation in border infrastructure development through the purchase of bonds issued jointly by U.S and Mexican state or local governments. Countries grouped in the ASEAN+3 community have undertaken similar efforts in their attempts to create a regional market for Asian bonds (Asian Development Bank, 2008).² In this case, the objective has been to diversify debt markets and use them as a supplement to bank finance (Eichengreen, 2006). A core element of this initiative is the creation of standardized debt instruments and regional-level institutions to facilitate cross-border investments and reduce transaction costs. The expectation is that these measures would benefit Asian economies by funneling the substantial savings that these economies generate to regional projects (Dalla, 2003; Pei, 2005). Developing robust regional bond markets entails numerous challenges. Two major challenges have to do with crafting an institutional infrastructure facilitate cross-border investment, as well as enacting measures to assure that bond investors receive comparable levels of legal protection across jurisdictions. Overcoming these challenges can be difficult due to the divergence of jurisdictional legal systems or countries being at different stages of market development. This is precisely the case of Mexico and the United States.

Mexico and the United States have sizeable economic differences, but also contrasting legal systems. While Mexico's legal framework is based on the civil law tradition, the U.S. legal framework follows the principles of English common law. For scholars like La Porta, Lopez-de-Silanes, and Shleifer (2008), this is relevant because of the close link between the origins of a legal system and economic development. La Porta, Lopez-de-Silanes, and Shleifer (2006) explain the divide between common and civil law in the context of securities regulations and capital market development and conclude that investor protection is stronger in nations with a common law system than in nations with a civil law system. What does this statement entail for countries seeking to develop financing alternatives for infrastructure development but whose regulations are anchored in different legal systems? Addressing this question is of great importance if the aim is to craft a cross-border bond financing mechanism. As Dalla (2003) illustrates when referring to Asian bond market regulations, fostering the development of regional bond markets would require effective harmonization in areas such as rating requirements, trading platforms and conventions, clearing and settlement procedures, accounting standards, tax treatment, and foreign exchange regulations, among others.

² The Association of Southeast Asian Nations (ASEAN) includes Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, and Vietnam. China, Korea, and Japan, the "+3" nations, are not members but participate actively in the regional bond market project.

This article seeks to contribute to the discussion on regulatory harmonization by comparing two aspects that we consider central for its success: the legal provisions that regulate the issuance of public bonds –our emphasis will be on bonds issued by sub-national governments, which we refer to in this article as SNG bonds³ and the current legal mechanisms to protect bond investors. The article is organized as follows: Section 2 sets the context for the discussion by providing the reader with an overview of recent reforms in securities regulations in Mexico and the United States. Section 3 explains the methodology for our study. Section 4 compares the regulations applicable to the issuance of sub-national debt and investor protection in Mexico and the United States. Section 5 discusses the policy reforms that would need to be considered to improve the feasibility of a bi-national bond financing mechanism. Section 6 concludes and introduces the topics for further research.

BACKGROUND

The analysis begins with an overview of some of the most significant reforms to further the development of sub-national bond markets in Mexico and the U.S in recent years.

Hildreth and Zorn (2005) provide us with a useful overview of the reforms in the United States between 1980 and 2005. Sub-national governments in this country have used a well-developed bond market to secure funding for many regional and local infrastructure projects. But, as the authors point out, reforms are still needed to protect the timeliness, cost-efficiency, and effectiveness of the U.S. municipal bond market. Hildreth and Zorn (2005) consider that a central element that contributed to the development of the U.S. municipal bond market was the 1986 Tax Reform Act and other relevant policies aimed at promoting market innovation and transparency (stricter rules for bond issuers, the creation of state bond banks, regulations facilitating the creation of credit enhancement mechanisms to protect investors, and the introduction of the tax-exempt status for municipal bond instruments, among others).

³ Two clarifications are pertinent at this point. The first refers to the meaning of the term “municipal bond.” In the literature on U.S. bond markets it is commonly used to refer to instruments issued by state and local governments (for example, cities, counties, or special districts). This article refers to these instruments as sub-national bonds or SNG bonds to avoid confusion with the term *municipio*, which describes a particular level of government in Mexico. The second clarification refers to the levels of government participating in the regulation of SNG bond markets. In the case of Mexico, the vast majority of bond market regulations pertain to the federal government (state Congresses have some participation, particularly in the establishment of legal limits to indebtedness). The participation of U.S. states in the regulation of SNG bond markets is far more extensive, particularly on issues involving the issuance of SNG bonds in their jurisdictions.

More recently, the United States has witnessed a new wave of regulatory efforts. To a large extent, they have been a response to the perceived laxity in the enforcement of previously enacted rules. They have also addressed the need for effective regulations in a field that has become quite sophisticated. A central piece of legislation in this regard is the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act. This is a comprehensive piece of legislation that introduced a gamut of new regulations affecting almost every participant in securities markets and expanded the supervisory powers of key U.S. federal government agencies. Doty (2010) considers that the Dodd-Frank Act's implications are far-reaching and will have an effect on municipal securities markets. He considers that one of its most salient aspects is the power that Congress confers on the Securities Exchange Commission (SEC) and the Municipal Securities Rulemaking Board (MSRB). These supervisory agencies have received an expanded mandate with the intention of reducing the probability of fraud and mismanagement in securities markets and to prevent investors being misled.

Regulatory efforts are also noteworthy in the area of information disclosure, particularly in terms of municipal securities disclosure.⁴ In this case, recently enacted reforms have resulted in additional regulations for bond issuers, such as the prohibition for underwriters to purchase municipal securities if issuers do not make a contractual promise to disclose information continuously, or the expansion of the list of events subject to disclosure (Pope, 2001; Robbins and Simonsen, 2010).

Interestingly, a common denominator in these reform efforts is a noticeable tendency toward centralization of enforcement responsibilities (particularly in the case of the SEC), and increased strictness of newly enacted regulations. This tendency could be advantageous in terms of the cross-border mechanism of bond financing (U.S. states have traditionally played a preponderant role in regulating the securities that are issued in their jurisdictions, which could complicate regulatory harmonization efforts).

In the case of Mexico, regulatory efforts in the last 15 years have geared toward the creation of a robust SNG bond market. Hernández-Trillo and Smith-Ramírez (2009) explain that before 1997, federal bailouts favoring financially distressed states and municipalities were a common practice. To correct the situation, the federal government introduced a market-based mechanism requiring sub-national governments issuing securities to negotiate the terms of their indebtedness directly with

⁴ Municipal bonds are indirectly regulated through Rule 15c2-12. Enacted under the Securities Exchange Act of 1934, this rule requires underwriters to receive, review, and disseminate official statements prepared by issuers of most primary offerings of municipal securities and to obtain continuing disclosure agreements from issuers and other obligated persons to provide material event disclosures and annual financial information on a continuing basis; it also stipulates that broker-dealers must have access to information in order to recommend municipal securities on the secondary market (MSRB, n.d.).

creditors, make their own trust arrangements, use block transfers as collateral of debt, and assume all the risks involved in the issuance of debt instruments. These authors consider, however, that there are several elements that still need to be considered to ensure the success of the enacted reforms (a credible commitment from the federal government in the sense that bailouts will no longer happen, that the federal government will effectively enforce capital market rules, that the fiscal information to be released by sub-national governments will be reliable, and that accounting standards across states will be homogeneous, among others).

Castellanos and Martínez (2008) discuss the 2001 reforms to Mexico's Securities Market Law (LMV), which sought to lower the cost of entry into the domestic bond market and enable states to collateralize debt-service obligations by selling stock certificates through master trusts. Uribe-Lara (2008) considers that these reforms have contributed to reducing investment risk in the SNG bond market. But, as he correctly points out, important reforms in state legislations prevent markets for these types of bonds from developing further (for example, reforms to state budget laws to ensure continuity in the repayment of debt obligations if the annual budget is not approved on time).

Evidently, the circumstances in which these reforms have been approved in Mexico and the United States differ. But even if recent regulatory efforts may give the impression that the enacted reforms in both nations seek to attain different objectives or address different problems, one may argue that they are geared toward improving regulating bodies' capacity to monitor and sanction market players, and to ensuring that investors understand the inherent financial risks. But would the existing U.S. and Mexican legal infrastructure allow policymakers to craft a bi-national bond financing mechanism? To assess the feasibility of such a proposal one must analyze the features of the existing securities regulations and evaluate whether the harmonization of bond market rules between the two countries can occur. This is the objective that we pursue in this article.

Following Zweigert and Kötz's advice (1998) that any question guiding a comparative study must be posed in purely functional terms, we begin this analysis by posing the following question: How do existing securities laws regulate sub-national bonds and protect investors?

METHODOLOGY

We used a two-step approach to answer the research question posed above. First, we identified the legislation where the legal provisions of interest were contained (see Table 1).

Table 1
RELEVANT U.S. AND MEXICAN REGULATIONS AFFECTING SECURITIES MARKETS

Level of Government	Mexico	United States
Federal Legislation	<ul style="list-style-type: none"> • Mexican Constitution • Stock Market Law (<i>Ley del Mercado de Valores</i>) • Fiscal Coordination Law (<i>Ley de Coordinación Fiscal</i>) • National Banking and Securities Commission, circular 11-29 	<ul style="list-style-type: none"> • U.S. Constitution • Securities Act (1933) • Securities Exchange Act (1934) • Trust Indenture Act (1939) • Tax Reform Act (1986) • Chapter 9 of the U.S. Bankruptcy Act • SEC Rule 15c2-12 (1989)
State Legislation	<ul style="list-style-type: none"> • Debt Laws (<i>Leyes de deuda</i>) • Revenue Law (<i>Ley de ingresos</i>) • Expenditures Law (<i>Presupuesto de egresos</i>) • Financial Code (<i>Código financiero</i>) 	<ul style="list-style-type: none"> • The issuance of debt instruments is regulated by each state (e.g., California Corporate Securities Law Act [1968], Arizona Securities Act, New Mexico Uniform Securities Act [1978], Texas Securities Act [1935])

Source: Authors' compilation.

The second step consisted of a thorough review of these sources, which enabled us to understand the procedural rules that issuers of sub-national bonds must follow, and the existing legal mechanism for investor protection. Given the complexity and extension of some of the legal provisions consulted, we considered the principles for securities regulations established by the International Organization of Securities Commissions (2003)⁵ and the work by La Porta, Lopez-de-Silanes, Shleifer, and Vishny (1998; 2000) and La Porta, Lopez-de-Silanes, and Shleifer (2006) for identifying relevant variables for the analysis. The latter research was particularly useful when organizing the legal factors to be compared about Mexico and the United States; however, since this line of research focuses on corporate governance and our interest was on SNG bonds, some of the elements they identified were not applicable to govern-

⁵ This organization introduces 30 principles considered desirable features of a country's securities regulation, which are based upon three broad objectives: protecting investors, ensuring that markets are fair, efficient, and transparent, as well as reducing systematic risk. We paid particular attention to the following principles when deciding on the features of legal systems that would be assessed in our study: rules aimed at providing investors with full, accurate, and timely information material to their investment decisions; rules protecting them from misleading, manipulative, and fraudulent practices; and rules and procedural mechanisms to address grievances or resolve conflicts.

ment issuers. The original list was hence refined to include only legal properties thought relevant for the analysis of government bonds. To make sure that no relevant information was being left out, we validated the information by interviewing experts on securities regulation and SNG bond markets in Mexico and the United States. The features of the Mexican and U.S. securities regulations compared in this analysis are summarized in Table 2 (see Appendix).

BOND MARKET RULES AND INVESTOR PROTECTION MECHANISMS IN THE U.S. AND MEXICO

This section article describes parts of the U.S. and Mexican legal frameworks dealing with procedural rules and creditor rights. This review is followed by a discussion of differences that we identified in these legal frameworks, and the implications they may have for a project aimed at creating bi-national bond instruments.

We begin with a brief review of Mexico's SNG bond market legislation. The starting point is the Mexican Constitution, which states that sub-national governments can only raise funds in local debt markets and cannot acquire debt in any foreign currency. In addition, foreign entities, governments, or corporations cannot be creditors (Mexican Constitution, Art. 117). Sub-national governments interested in issuing debt instruments can only raise capital from Mexican investors or companies registered in Mexican territory.

The legal framework includes general guidelines for securities issuers, as well as detailed procedural rules for private and public entity borrowers. The most important guidelines for an offering of securities in Mexico are described in the Securities Market Law (LMV). This legislation includes provisions that define the roles and responsibilities for all participants in the securities market⁶ and the types of securities and their characteristics,⁷ highlights conditions that purchasers or securities must meet,⁸ and lists the steps to register and offer securities on Mexico's stock exchange.⁹

⁶ Rules and regulations pertaining to companies participating in the stock exchange are contained in Articles 10 to 60; those referring to intermediaries, in Articles 113 to 224; investment advisors, Articles 225 to 227; organizations in charge of the development and implementation of operation standards and codes of conduct for the industry, Articles 228 to 231; other entities participating in the securities market, in Articles 322 to 341; external auditing services, Articles 342 to 348; and regulations applicable to financial authorities, Articles 349 to 361.

⁷ Articles 61-69 list the different types of securities.

⁸ Articles 109-112 discuss the cases where investors must disclose information about a purchase to the regulatory entities and to the public.

⁹ Issuers must register the securities at Mexico's National Banking and Securities Commission (CNBV) before offering it to the public. The steps that must be followed are contained in Articles 70 to 103.

An interesting stipulation in the law refers to fiduciary stock exchange certificates (*certificados bursátiles fiduciarios*) (LMV, Articles 61-69). Mexican local governments have used these types of financial instruments widely to finance multiple activities. These certificates require potential issuers of bond instruments to set up a master trust (*fideicomiso irrevocable*) to deposit the funds that issuers will pledge for the repayment of the bond. There is no legal mandate requiring sub-national governments to issue only this type of debt instruments. However, using a trust has been perceived as an effective guarantee for investors and as a measure to try to separate the credit quality of the bond and the risk associated with the credit quality of the issuing state or municipality.

A salient matter that emerges when creating debt securities involves the revenues that states can pledge to secure bond repayment. The tax capacity of state and municipal governments in Mexico is extremely limited and own-source revenues are, on average, less than 10 percent of total revenues (author's calculations with data from SHCP [2005]). Consequently, the tendency has been to commit revenue flows that they expect to receive from the federal government. These financial sources include revenue-sharing transfers and some earmarked funds whose amounts need to be determined during annual budget negotiations. Since this is usually considered a stable source of revenue, investors have shown preference for securities using such transfers as guarantees. (In some cases, earmarked funds can be used to secure bond repayment, although in this case a piece of legislation known as the Fiscal Coordination Law contains provisions that must be observed).¹⁰

It is important to highlight that trust arrangements play an important role in Mexico's sub-national bond market. These trusts are a type of special-purpose vehicle where a sponsor—in this case a sub-national government—transfers assets to carry out a specific activity (Gorton and Souleles, 2005).¹¹ To some extent, using these legal contracts was a response to the federal government's policies aimed at introducing

¹⁰ The Fiscal Coordination Law (*Ley de Coordinación Fiscal*) regulates fiscal relations among states, municipalities, and the federal government. As stated in Article 50, sub-national governments will be able to pledge revenues from these funds with the approval of state legislatures, and if the decision to do so is registered at a federal registry of debt obligations at the Ministry of Finance and Public Credit. But most importantly, the Fiscal Coordination Law makes it clear that if resources from these funds are used as a guarantee when issuing a new debt instrument, the money raised shall be used to finance projects that benefit disadvantaged segments of the population (Article 33), or for activities that explicitly permitted by Article 47 of the law (infrastructure, modernization of cadastral systems, technological development, or scientific research, among others).

¹¹ The existence and use of these legal contracts is regulated by the General Credit Titles Law (*Ley General de Títulos de Crédito* [LGTIC]), which stipulates that for the issuance of participation certificates (*certificados de participación*), any economic unit can set up trusts (Art. 228c). These legal instruments allow the sponsoring entity to issue fiduciary debt certificates (Art. 228f).

market-based mechanisms into the regulatory framework, but also to avoid any possibility of a federal bailout.¹²

In terms of the legal protection that securities investors receive under the existing Mexican legal framework, we consulted the general guidelines for investor protection described in the LMV and more specific provisions contained in the various norms that the National Banking and Securities' Commission releases.¹³ We first focused on the regulations that would allow us to explain how difficult it would be for an investor to recover losses if they were caused by misleading statements in the prospectus.¹⁴ Interestingly, the Mexican legal framework does not include explicit provisions on the issue of restitution of losses. If elements existed leading to the belief that the bond issuer had misled investors through the content of the prospectus, plaintiffs would need to resort to civil courts to try to prove their claim.¹⁵

Another salient issue refers to creditor protection when the possibility of a default arises. No specific procedures or norms exist detailing what holders of sub-national bonds may do if an issuer defaults on its debt obligations. It is partly due to this lack of a legal infrastructure that creditors will have an incentive to try to negotiate a solution outside the courts. Such negotiations may include voluntary debt restructuring agreements or an increase in the amount of resources to be deposited in already existing trusts. (The latter alternative would depend on the sub-national government's capacity to commit additional revenue streams to cover any outstanding debt.) Bond purchasers in the United States have more certainty about these types of procedures, as many of them are clearly specified in Chapter 9 of the U.S. Bankruptcy Code.¹⁶ Holders of bond instruments issued by sub-national governments in Mexico do not have the same degree of certainty or comparable levels of protection. Bankruptcy procedures are regulated but their provisions apply only to private entities (see the Law on Bankruptcy Protection Proceedings [*Ley de Concursos Mercantiles*]). From a legal standpoint, the issuer of a sub-sovereign bond cannot file for bankruptcy.

¹² As Hernández-Trillo and Smith-Ramírez (2009) explain, with the regulatory framework for debt management introduced in 1997, sub-national governments have been forced to make their own trust arrangements, to collateralize debt with their own resources (either local taxes or block grants), and to assume all risks associated with the issuance of a new debt instrument.

¹³ See CNBV, n. d.

¹⁴ The LMV defines what is to be considered misleading information (Arts. 368 and 369) and who will be responsible for the contents disclosed—Art. 86-VIII states that the issuer's legal representative must state in writing that no relevant information has been omitted from the investment prospectus—and establishes sanctions when these mandates are not met (Art. 376).

¹⁵ The general principle, as stated in Art.1910 of the Federal Civil Code, is that investors are legally entitled to restitution when they incur losses due to illegal acts (defined as acts carried out against the law or that fail to comply with legal requirements) (La Porta, 2005).

¹⁶ Chapter 9 contains specific procedures to regulate the debt restructuring process of cities, towns, villages, counties, taxing districts, municipal utilities, and school districts in the United States. See U.S. Courts, n. d.

In the case of the United States, there has been a wave of recent regulatory efforts to regulate securities markets more efficiently. Two salient components in these reforms are the amendments to the 1934 Securities Exchange Act and the enactment of the Dodd-Frank Wall Street Act. The amendment of rule 15c2-12 of the 1934 Securities Exchange Act has been of particular relevance for municipal securities offerings, as it has placed more emphasis on issues related to issuer accountability and SEC oversight.¹⁷ Important features of the U.S. framework also deal with bondholder protection. The problem, however, is that the legal proceedings that need to be followed are quite complex. One example is when a creditor is seeking damages or retribution from an issuer. The main challenge is getting the violator (issuer) to comply with subpoenas and court orders to pay fines for their violation. Another challenge arises when transactions occur outside the U.S. jurisdiction or when transactions involve foreign investors and when there is the possibility of a disagreement among settling parties over the amount of damages. Finally, potential exists for issuers to delay payment to investors if it can be proven that the issuers will suffer financial hardship because of legal fees and other court-related costs.

It is also important to highlight that in the event issuers file for Chapter 9 bankruptcy, payment due to creditors and investors may be significantly delayed. The U.S. legal system permits municipal bankruptcy cases to be handled by federal and quasi-federal governing entities (MSRB and the Securities Exchange Commission) and the courts. This indicates that the federal government is directly involved with these proceedings to ensure SNG compliance with bankruptcy laws. According to Chapter 9 of the 1978 Bankruptcy Reform Act, issuers are required to take the necessary steps (for example, reorganization, forfeiture of property management) to resolve internal organizational issues in order to meet their financial investment obligations owed to creditors and investors. Issuers must also carry out actions related to protecting creditors' rights. The top 20 creditors that hold the 20 largest unsecured debts are paid first.¹⁸ But, federal bankruptcy courts forbid creditors from demanding collateral from issuers until a legal ruling has been handed down and reorganization plan for the issuers' debts has been developed. Second, only the debtor (issuer) can file for reorganization 120 days after the courts rule for their debt relief. Third, secured creditors gain possession of their security once the reorganization petition is approved (14 days after the order or relief).¹⁹ Thus, debtors (issuers) must forfeit all securities owed to

¹⁷ The reforms include provisions establishing new compliance requirements for certain types of financial instruments, additional disclosure rules for events used to determine tax exemption, or events that are considered relevant for issuers' and/or trustees' decisions (for example, mergers, bankruptcy, unscheduled payments, default in payments) (SEC, n.d. a and b).

¹⁸ Bankruptcy Act Rule 3020(e).

¹⁹ Bankruptcy Act Rule 3020(e).

creditors upon approval for reorganization.²⁰ Fourth, debtors must also rank the top 20 creditors that will first receive the distribution of proceeds from the disposition of unsecured assets (including any interest owned).²¹ Last, the courts assume control of the debtors' properties²² until there is confirmation of a reorganization plan.²³

Chapter 9 of the U.S. Code specifically states strict legal procedures issuers must abide by in a bankruptcy claim. This statute was established to protect investors by requiring issuers to follow federal processes in disclosing information and abiding by legal proceedings regarding their securities assets. According to this federal statute, issuers who file for bankruptcy under Chapter 9 must do the following in this order: 1) file a plan with the SEC to readjust their debt obligations; 2) the plan must comply with this statute; investors must be paid for claims due; issuers are able to reorganize to get out of bankruptcy as determined by the court; 3) the plan must be confirmed by the court and accepted by creditors; 4) the court will oversee the implementation of the plan to repay investors and reestablish issuers until it is determined that the case has been completed.²⁴

Finally, we should note that in addition to the extensive federal regulations in the U.S. legal framework, there are many state-level regulations governing securities transactions within their jurisdiction (see table 1 above). This adds a layer of complexity to the regulation of SNG bond markets, since bond issuers will also need to comply with the specific rules of the jurisdiction where they release financial instruments into the market.

DISCUSSION: ON THE FEASIBILITY OF A BI-NATIONAL BOND FINANCING MECHANISM

Now that some of the main components of the U.S. and Mexican securities regulations have been introduced, it is important to think about the environment that potential bond buyers would encounter if they were to invest in debt instruments issued by sub-sovereign entities in these two countries.

One can argue that in the case of Mexico, the existing regulations tend to limit foreigners' participation in SNG bond markets, due to the restrictions included in constitutional Article 117. At the core of this article is Section VIII, which stipulates that

²⁰ Section U.S.C. 1141.

²¹ Bankruptcy Act Rule 1007(e).

²² Bankruptcy Act Rule 3020 (d).

²³ Section U.S.C. 1125 (b).

²⁴ U.S. Bankruptcy Title 11, Chapter 9 (United States Code, n. d.).

Mexican states cannot acquire obligations to foreign governments, companies, or individuals, or enter into contractual agreements in a foreign currency or payable in a foreign country. This has numerous implications. For one, investors can only receive the applicable legal protection if the bond is bought through a company located within Mexico. But even if a potential investor purchases public bond instruments through a Mexican financial intermediary, the current legal framework has additional limitations that tend to reduce the attractiveness of SNG bonds (for example, increased transaction and information costs).

One salient limitation has to do with the lack of specific legal provisions defining the scope of responsibility of sub-sovereign bond issuers in the event of default or fraud. It is important to note that the concept of sub-national bankruptcy does not exist in Mexico's legal framework. This legal vacuum creates uncertainty and impedes the proper development of the public bond market because matters like the patrimony that could be affected in case of a default are not explicitly addressed in the applicable law.²⁵

The lack of a solid regulatory infrastructure is also evident when one inquires about the legal provisions to deal with possible violations to the Securities Market Law (LMV). Let us assume, for example, that a bondholder has reasons to believe that he/she has been misled by the actions or omissions of an issuer.²⁶ As stated in section 4 of this article, cases like this would be treated as an administrative matter and would fall within the realm of civil law. Contrary to what exists in the U.S., where there are specialized municipal bankruptcy attorneys and a federal bankruptcy law that includes specific provisions for municipal bankruptcy procedures, legal procedures in Mexico rely on stipulations in a Civil Code. Its provisions will apply to any case regardless of the nature of the claim. This is problematic because there is a disconnect between what Mexico's securities regulations seek to accomplish and the available regulatory infrastructure to attain those goals.

The review of current securities regulations shows that despite the reforms in recent years, SNG bond markets in Mexico remain highly under-regulated. To a large extent, this is because a substantial portion of the financing needs of state and local governments is still covered by the central government. Evidence shows, however, that the financial resources states and local governments receive are insufficient to

²⁵ This situation has been partially addressed with the creation of Stock Exchange Certificates (*Cebures*). As explained in previous sections of the article, issuers warranty bond repayment by committing future revenue streams to a trust. Since this trust is not a public entity, its regulation falls under the domain of private law.

²⁶ An unfortunate example of this kind of situation is the case of the northern state of Coahuila, which purposely released false and misleading information to be able to issue debt far beyond the limit authorized by its Congress, and beyond its capability to pay (Bloomberg News, 2011).

cover their needs. Bond markets could become an alternative source of financing in the future provided proper public bond market regulations are enacted.

In the case of the United States, one observes that, although federal laws outline the general rules for securities market participants, much of the regulation applicable to SNG bonds remains the responsibility of state governments. This can substantially increase the cost that bond buyers must pay to acquire legal information and specialized advice due to varying state laws. This is crucial in defining the contracting framework for SNG securities.

Another aspect of the current regulatory framework that should be carefully considered is an assessment of the adequacy of current securities laws in a potential cross-border bond financing mechanism. Existing legal provisions in the United States stipulate that when a borrowing entity wants to participate in an initial public offering, there must be an approved bond resolution or ordinance and a sales document for the securities (commonly known as an Official Statement). But as a legal expert consulted for this article explained, there is no mandate requiring the SEC (or other regulatory body) to approve or even review documentation related to the sale of debt to the public. Thus, no existing statutory framework prevents the sale of low-quality, high-risk securities. Hence, important decisions regarding the quality of securities to be sold to investors are left to the market.²⁷

In terms of provisions specifying creditor rights, U.S. regulations establish strict liability standards for municipal bond issuers (particularly for information disclosure). Situations may arise in which an investor could consider that the issuer released misleading information about a security. If this occurs, the affected party may claim the restitution of his investment. However, contrary to what happens in Mexico, U.S. legal municipal or corporate securities proceedings are used as case law to deal with subsequent matters pertaining to issuer fraud and deceit (in these cases, the burden of proof lies with the investor).

But what does all this entail in terms of a proposal to create a bi-national bond financing mechanism? Evidently, assessing the feasibility of such a proposal requires various steps. We think a crucial step in this assessment has to do with the challenges involved in the required harmonization of Mexican and U.S. bond market rules. This

²⁷ An exception would be if the issuer fails to disclose complete and accurate information in the investment prospectus, as this is regulated under federal anti-fraud provisions (see rule 15c2-12 in the 1934 Securities Exchange Act). Failure to comply with such disclosure-related provisions would provide investors with a valid claim to seek the restitution of losses in court. Interestingly, in municipal securities markets there is no road map for what should be considered as fair and accurate disclosure –this is different in the corporate borrowers' market. The parties to each transaction collectively decide what is to be considered proper disclosure.

need stems from the alleged differences among legal origins that scholars like La Porta, Lopez-de-Silanes, and Shleifer (2006) highlight.

Reviewing the existing regulations for the issuance of SNG bonds and the legal mechanism to protect investors in the U.S. and Mexico allowed us to identify some of the immediate challenges for crafting a cross-border bond financing mechanism. The first consists of aligning securities rules between two nations where rules are enacted and enforced at various levels of government. In spite of the most recent regulatory efforts in the United States, state governments have a great deal of responsibility in the regulation of SNG bond markets. This significantly augments coordination and information costs for policy makers and investors, as they would need to comply with a different mix of regulations depending on the jurisdiction issuing the bond. The decentralized nature of the U.S. legal framework for SNG (municipal) bonds implies that not only would policymakers need to consider the alignment of federal regulations, but they must also seek harmonization of existing state legal provisions by participating members (for example, the California Corporate Securities Law Act [1968], the Arizona Securities Act, the New Mexico Uniform Securities Act [1978], and the Texas Securities Act [1935]).

This situation would not exist in Mexico, since the bulk of SNG bond market regulations fall within the domain of the central government. In this case, the challenge results from the lack of an adequate state-level legal infrastructure and the incompatibility between existing regulations and market needs. As explained in section 2 of this article, the Mexican market for SNG is just starting to emerge. States are beginning to see debt markets as a mechanism for satisfying their funding needs and have been enacting reforms to comply with requirements imposed by the investors' community and federal authorities (enactment of state laws to keep debt growth under control or current efforts to harmonize accounting rules, among others). However, there are still noticeable gaps in most state laws that need to be filled to establish financial certainty and confidence for potential bond investors. As Uribe-Lara (2008) suggests, some of the observable gaps include the lack of multi-annual budget appropriations to increase certainty of bond repayment, the need for better trained government officials, and, more generally, the need for a solid legal infrastructure that contributes to attaining policy goals of utmost relevance for SNG bond market participants.

A second major challenge pertains to the alignment of the legal provisions aimed at protecting investors' legal rights. This challenge goes far beyond what written rules dictate because U.S. and Mexican legal provisions are rooted in their distinct legal origins (common law vs. civil law). The United States has developed a sophisticated legal framework with specific provisions to deal with municipal bankruptcy (i.e., Chapter 9

of the U.S. federal bankruptcy code). Mexico does not have a similar framework in place. If a sub-national government defaults on its bond payments, or if an investor seeks any kind of restitution, and instead relies on a civil code, no specific provisions exist to deal with the situation. And although this should clearly not be interpreted as a weakness, it should pave the way for a thorough debate on the properties that a legal system to protect bond investors should have.

What this analysis makes clear is that the existing legal infrastructure does not permit the issuance of bond instruments of a bi-national nature. The feasibility of that endeavor would therefore depend on the capacity of the U.S. and Mexican governments to devise and implement reforms to harmonize key aspects of existing bond regulations. What type of reforms would need to be implemented? Evidently, any agenda for reform would need to consider the fact that the sub-national bond markets are at two very different levels of development.

As Leigland (1997) suggests, emerging economies like Mexico could accelerate the development of their sub-national bond markets by using the strengths of the U.S. municipal market as a guideline for policy design.²⁸ The process would necessarily require the enactment of *ex-ante* and *ex-post* rules to regulate sub-sovereign bond markets effectively. *Ex-ante* rules should stipulate the purposes, types, and limits for SNG debt instruments, as well as issuance procedures; *ex-post* rules, on the other hand, would establish the measures to be taken in the event that an issuer becomes insolvent (Canuto and Liu, 2010).

The review of the Mexican legal framework allows us to conclude that, while a debate on regulatory harmonization is a necessary step for the creation of a bi-national mechanism of bond financing, it is crucial for Mexican policymakers to decide whether foreign bond buyers should be allowed to acquire instruments issued by sub-sovereign entities and whether these entities would be allowed to incur debt obligations with foreign creditors. A subsequent task calls for the enactment of a legal framework that clearly defines the rights and responsibilities of market participants. The current market for SNG bonds in Mexico is in its infancy stage as it has only recently emerged. Despite the enactment of recent key regulations, there is a strong need for specific provisions and court procedures to deal with the possibility of potential problematic events such as bond issuers' default. Reforming the existing securities legal structures can contribute to increasing bond buyers certainty, reduce transaction and information costs for bond instrument purchases, and change investors'

²⁸ For this author, the essential strengths of the U.S. municipal bond market are reflected in its capacity to attract investors and issuers by promoting investor familiarity and confidence, or by establishing market conditions that result in acceptable returns on investment, sufficient information regarding risks, and tolerable borrowing costs, among others.

perceptions of risk (especially when a comparison is made with bond instruments issued by U.S. state and local governments).

In the case of the United States, as Mahoney (2009) correctly points out, although securities regulations were originally conceived as a contracting system, Congress and the SEC have added a number of regulatory features over time. Doty (2010) reviews some of the recent reforms enacted by Congress and highlights the effect they have on the municipal securities market. We must note that in spite of the apparent centralization of enforcement and monitoring responsibilities, the regulation of SNG (municipal) bonds falls ultimately within state government jurisdiction. Moreover, although securities regulations established regulatory schemes for corporate securities, they exempted offerings of municipal securities (Liu, 2010). This can pose important coordination problems if the aim is to promote the alignment of bond market rules in Mexico and the United States. The feasibility of a cross-border finance mechanism would also require a clearer definition of the responsibilities that U.S. states would have *vis-à-vis* the federal government.

CONCLUSION AND TOPICS FOR FURTHER RESEARCH

Developing a bi-national bond financing mechanism between Mexico and the U.S. could help reduce the gap between border infrastructure needs and available funding. This is a multi-stage project that, among other things, calls for the harmonization of bond market rules. This article contributes to the discussion by offering readers a review of the provisions that regulate the issuance of SNG bonds and rules aimed at protecting bond investors in these two countries. It shows that while both nations have a securities legal framework in place, there are differences that need to be addressed if the aim is to envision a bi-national bond financing mechanism. Evidently, the complexities and intricacies of the Mexican and U.S. securities frameworks go far beyond what has been discussed in this article. Our study has reviewed some of the key features of the existing securities rules with the intention of initiating a discussion on the challenges that regulatory harmonization would entail. Future research endeavors should be geared toward answering the pending issues not fully addressed in this article.

One such issue involves the design of an institutional infrastructure capable of enforcing binding agreements among entities corresponding to different sovereignties. Part of these responsibilities could be allocated to an already operating bi-national institution: the North American Development Bank (NADBANK). This institution was created to enhance the environmental conditions and quality of life along the

border region. It carries out financing activities as permitted by the amended 2004 Charter Agreement signed by the Mexican and U.S. governments.²⁹ NADBANK could turn into the perfect vehicle for attaining objectives associated with the crafting of a bi-national bond financing mechanism (for example, issuing the bonds, or providing implicit or explicit guarantees to investors, or acting as underwriter). This possibility should be part of a crucial discussion aimed at revising and expanding the bank's current mandate.

A second issue has to do with the differences between the civil law and common law approaches, how these differences are reflected in bond market regulations, and the way they would affect the issuance of cross-border bonds. This article highlights some of those differences by comparing existing securities rules. However, it recognizes the need to further analyze the extent to which contrasting legal traditions could complicate the enactment of reforms to harmonize the legal frameworks of the two countries.

Finally, we should take into account the salient role that state governments play in regulating municipal bonds markets in the United States, contrary to Mexico, where most bond market regulation is federal. If the intention of the proposed bi-national bond financing mechanism is to attract investors to border infrastructure projects, a careful comparison of bond market regulations in the U.S. border states (California, Arizona, New Mexico, and Texas) will be needed. This type of comparison would help enhance our understanding of the differences in these frameworks, and the regulatory harmonization challenges they would pose. We consider regulatory harmonization one of the necessary conditions for the development of a bond financing cross-border mechanism. But, as is usually the case, the devil is in the details.

²⁹ See www.nadbank.org.

Appendix

SALIENT FEATURES OF U.S. AND MEXICAN SECURITIES REGULATIONS	
Procedural Rules for Issuing SNG (Municipal) Bonds	
Variables	United States
Disclosure Requirements	<p>Securities Act (1933)</p> <p>a) Sec. 6: Securities sold as public offerings must be registered with the SEC; SEC and the U.S. representative must be notified of offerings of U.S. securities in foreign countries (Section 8A).</p> <p>b) Sec 18: Gives authority to states to regulate.</p> <p>c) Sec 3: Deals with exempted securities.</p> <p>Securities Exchange Act (1934)</p> <p>a) Sec. 12: Registration requirements for IPOs.</p> <p>b) Sec. 12b. 1-7: On the public offering of securities.</p> <p>c) Sec. 15b: On municipal securities.</p> <p>d) Sec. 7: Details specific disclosure requirements and content required in reporting and IPOs; Lists documents and fees required for reporting.</p> <p>State securities laws</p> <p>Individual states possess securities statutes that require IPO of securities to provide certain specific information (see individual state securities laws for the necessary documents to prepare when making a new public offering).</p>
Conditions applicable to the offering of securities for public sale	<p>LMV</p> <ul style="list-style-type: none"> • Art. 7: Securities to be sold in public offerings must be registered at the National Banking and Securities Commission (CNBV); the CNBV must be notified of offerings of Mexican securities in foreign countries. • Arts. 70-82: Registration requirements for IPOs. • Arts. 83-103: On the public offering of securities. • Various articles in this law discuss specific conditions for IPOs that different types of issuers must fulfill. • Art. 104: Issuers must disclose any information considered relevant. The article lists the documents that need to be presented. Includes applicable provisions for cases where the issuer is a sub-national government.

Table 2
SALIENT FEATURES OF U.S. AND MEXICAN SECURITIES REGULATIONS (continued)

Procedural Rules for Issuing SNG (Municipal) Bonds	
Variables	United States
	<p>Mexico</p> <p>CNBV Circular 11-29</p> <ul style="list-style-type: none"> • Art. 3: States and municipalities must include the following documents <i>when registering</i> a new offering: <ol style="list-style-type: none"> a) Document certifying that the person doing the registration is authorized to do so; b) Revenue act, debt act, approved budget, and authorization from the local legislature to issue bonds; c) Audited revenue and expenditure statements for the last 3 fiscal years with an explanation of the accounting rules used to prepare them; d) Copy of the report describing the financial situation of the issuing entity (<i>cuenta pública</i>) in the preceding fiscal year; e) Investment prospectus containing the information described in appendix L of CNBV Circular 11-29. • Title 4 (Arts. 33-49): <i>On the information that needs to be disclosed</i> to the CNBV, Stock Exchange (BIV), and investors. Art. 36 lists the information that government issuers shall disclose.
Information that SNG issuers need to disclose	<p>Securities Exchange Act (1934) Section 13: Every issuer must submit duplicate original reports to SEC.</p> <p><i>Annually:</i> Annual reports required by independent accountants (auditors) to be reported to the SEC.</p>
	<p>Annually</p> <ul style="list-style-type: none"> • Report to the legislative body (state Congress or city council [<i>Cabildo</i>]) informing the financial situation of the jurisdiction. • Revenue and expenditure statements evaluated by an external auditor. • Document explaining the accounting rules used in the preparation of the revenue and expenditure statements.

<p>• Report containing information on socio-economic characteristics of the issuing entity, legislation, human resources, assets, and comparisons to other jurisdictions (See circular 11-29, appendix O).</p> <p><i>Quarterly</i></p> <ul style="list-style-type: none"> • Updated revenue and expenditure statements. • The economic, accounting, and financial information required by the regulator. • Comparison of the financial information of the quarter to be reported and the previous fiscal year. <p><i>3rd day after the event occurs.</i></p> <ul style="list-style-type: none"> • Copy of the official publication that contains the amount of total public debt of the jurisdiction. • Report of the head of the executive branch to the legislature on the sources and uses of public funds, status of programs included in the revenue act, and information on outstanding debt. • Information related to the registration of debt obligations, as required by Article 9 of the Fiscal Coordination Law. <p>LMV: Prospectus characteristics (Arts. 86, 88)</p> <p>CNBV Circular 11-29:</p> <ul style="list-style-type: none"> • Instructions to develop investment prospectuses described in CNBV Circular 11-29, appendices H and I • Instructions for preparing prospectuses for securities issued by SNG governments described in CNBV Circular 11-29, appendix L 	<p><i>Quarterly:</i> Quarterly reports as required by independent accountants (auditors) to be reported as prescribed by the SEC.</p> <p>SEC Rule 15c2-12</p> <ul style="list-style-type: none"> • Requires annual financial information. • Material event disclosure. • Other information deemed material and noted in disclosure agreements. <p>Indicates 14 specific events that must be disclosed in the event of Chapter 11 bankruptcy.</p> <p>Securities Act (1933) Section 10 (a-f): Indicates information required in the preparation and disclosure of the prospectus. Section 12: False statements in prospectuses are subject to legal action</p> <p>Securities Exchange Act (1934) d) Sec. 5: Cannot advertise security sales via inter-state commerce channels.</p>
<p>Content and distribution of prospectuses</p>	<p>Advertising in connection with the offering</p> <p>CNBV Circular 11-29:</p> <ul style="list-style-type: none"> • Chapter 6: Advertising public offering in foreign countries • Appendix K: Instructions to prepare informative brochures for public offerings.

Table 2
SALIENT FEATURES OF U.S. AND MEXICAN SECURITIES REGULATIONS (continued)

Procedural Rules for Issuing SNG (Municipal) Bonds	
Variables	United States
Information material to the price or value of a listed security	<p style="text-align: center;">Mexico</p> <p>LMV:</p> <ul style="list-style-type: none"> • Art. 2 (XII): Defines what is to be considered "relevant information". <p>CNBV Circular 11-29, Annex H: Instructions for developing investment prospectuses, flyers, and any supplementary information about the IPO. The document includes disclosure information requirements.</p> <p style="text-align: center;">United States</p> <p>U.S.: See Robbins and Simonsen (2010).</p>
Periodic reports	<p>LMV: Art. 104: Issuers must disclose information considered relevant. The article lists the documents that need to be presented annually, quarterly, regularly, and as soon as certain events occur.</p> <p style="text-align: center;">Securities Exchange Act (1934)</p> <p>Section 13: Indicates required periodic reporting of relevant information regarding the security. Annual and monthly reports required to keep information current on a particular security.</p>
Procedural difficulty in recovering losses in a civil liability case due to misleading statements in the prospectus	<p>LMV</p> <ul style="list-style-type: none"> • Art. 86-VII: when the issuer (or legal representative) signs, he/she asserts that no relevant info is omitted from prospectus. • Art. 368: Prohibits including false information. • Art. 376: Prohibited actions and sanctions. • Art. 383: Sanctions if misleading prospectus is submitted. <p>CNBV Circular 11-29, Art. 89: Sanctions to be defined based on what is stipulated in the LMV.</p> <p>What does the law say about misleading prospectus information (for example, sanctions)?</p> <p>1933 Securities Act:</p> <p>Section 12, (a) (2)</p> <ul style="list-style-type: none"> • Any security transaction made by an issuer that includes an "untrue" statement or omits a fact in a prospectus or oral communication which is unknown, gives the purchaser (investor) the right to legally sue the distributor (issuer) for the security with interest or for monetary damages resulting from the previously owned security [burden of proof on issuer.]

Provisions on restitution of losses:

The general principle (Federal Civil Code, Article 1910) is that investors are legally entitled to restitution when incurring losses due to illegal acts (defined as acts carried out against the law or that fail to comply with legal requirements) (La Porta, 2005).

- Even if issuer can prove that all or a portion of the security's value is unaffected by misleading prospectus allegations, they are unable to recover those losses [loss causation, Section 12 (b)].

Section 13

- Legal action against issuers who mislead investors must be taken within one year of the discovery. No action can be made if security has been sold for more than 3 years.

Section 15

- Even those connected with the controlling persons (issuers) are liable for misleading prospectus statements unless they are unaware of the alleged misleading information.

Section 16

Lawsuits under these procedures are called "covered class actions."

Their criteria are as follows:

- Affects 50+ investors; or one or more representatives who seek to recover from grievances committed by misleading issuers.

Section 18

- The Securities Commission or agency within a state has jurisdictional authority to investigate and prosecute issuers who provide misleading info to investors.

What procedures to be followed to recover losses?

SECURITIES EXCHANGE ACT 1933:

Section 20

- States the procedures under which the sec can investigate and call for judicial review over providing misleading information.
- Criminal proceedings may take place at the discretion of the Attorney General.
- Upon recommendation by the sec, U.S. courts have jurisdiction to make the convicted issuer(s) comply with the sec law.

Table 2
SALIENT FEATURES OF U.S. AND MEXICAN SECURITIES REGULATIONS (continued)

Procedural Rules for Issuing SNG (Municipal) Bonds	
Variables	United States
Mexico	<p>Section 20 (2)</p> <ul style="list-style-type: none"> • Penalties: <ol style="list-style-type: none"> a) First-tier court shall determine the fine. <ol style="list-style-type: none"> i. Up to US\$5 000 for U.S. citizen and up to US\$50 000 for non-U.S. citizen or ii. Gross amount of financial gain due to the plaintiff. b) Second-tier <ol style="list-style-type: none"> i. Up to US\$50 000 for U.S. citizen and up to US\$250 000 for non-U.S. citizen. ii. Gross amount of financial gain due to the defendant if the violation involved fraud, deceit, manipulation, reckless disregard of a regulation. c) Third-tier <ol style="list-style-type: none"> i. Up to US\$100 000 for U.S. citizen and up to US\$500 000 for non-U.S. citizen. ii. Gross amount of financial gain due to the defendant if the violation involved fraud, deceit, manipulation, reckless disregard of a regulation AND if the violation directly or indirectly resulted in substantial losses or risk of substantial losses for investors. <p>Section 20 (3)</p> <ul style="list-style-type: none"> • Procedures for collecting: a) Payment of payment penalty to Treasury Dept.; b) Collection of penalty (in district courts as ordered by Atty. Gen.); c) Remedy not exclusive (these penalties may be added to existing orders set by the Atty. Gen., and the Commission); d) Jurisdiction and venue (based on the district court case is assigned as indicated in Section 22.

Section 20 (4): Violation of Cease-and-Desist Order: A cease-and-desist order is issued by the commission; results in each separate violation will be a separate offense, except when a violation occurs during a failure to comply (each day will be counted as a separate offense).

On procedural difficulty:

SECURITIES EXCHANGE ACT 1933, Section 22

- Main challenge is getting violator (issuer) to comply with subpoena and court orders to pay fines for misleading investors.

- Another challenge is if the security transaction(s) occur(s) inside the U.S. and involve foreign transactions with foreign investors or if transactions occur outside of the U.S. and have a substantial predictable effect on the U.S.

Section 27 (B)

- Potential disagreement over amount of damages among settling parties (ii.)

Section 23 (3) (B)

- Potential for issuers to delay payment to investors if it can be proven that there will be financial hardship for the issuers due to legal fees and other court-related costs.

Investor protection mechanisms

Creditor rights

Rule establishing automatic stay on the assets (e.g., secure creditors cannot get possession of collateral)

N/A

LCM

- **Bankruptcy Act Rule 3020(e):** Fourteen-day automatic stay on assets commences unless otherwise specified by the court
- Who gets paid first in the case of a default? The top 20 largest creditors that hold the 20 largest unsecured claims are paid first based on the list in Rule 1007(e).
- Can secure creditors get possession of collateral? No, the automatic stay prevents secure creditors from obtaining collateral from debtors to ensure payment of debts. The court puts a hold on all debtors' assets until the order is approved and the plan is accepted.

Table 2
SALIENT FEATURES OF U.S. AND MEXICAN SECURITIES REGULATIONS (continued)

Procedural Rules for Issuing SNG (Municipal) Bonds	
Variables	United States
The country imposes restrictions on filing for reorganization (e.g., creditors' consent on minimum dividends)	<p>Bankruptcy Act Rule U.S.C. 1121</p> <ul style="list-style-type: none"> Only debtors can file for reorganization (it is a voluntary action). The debtor must submit its reorganization plan to the bankruptcy court 120 days after the order of relief. <p>U.S.C. 1126 (c)</p> <ul style="list-style-type: none"> Reorganization plan of debtor must be approved by 2/3 majority by creditors committee.
Secured creditors recover their security once the reorganization petition is approved (no automatic stay)	<p>Bankruptcy Act Rule 3020(e)</p> <p>14 days after order or relief, creditors may recover their security from the debtor once the reorganization petition is approved.</p> <p>Section U.S.C. 1141</p> <p>Debtor is bound to forfeit securities or any other claim due to the creditor upon approval of reorganization petition.</p>
Secured creditors are ranked first in the distribution of proceeds from the disposition of assets	<p>Bankruptcy Act Rule 1007 (e)</p> <ul style="list-style-type: none"> Debtor must file within 2 days after the order of relief the list (name and address) of top 20 largest creditors that hold the 20 largest unsecured claims (excludes insiders). <p>Debtor must also file within 14 days of order the list of its equity security holders (names and addresses), showing interest owed.</p>
Debtors do not retain management of their property pending the resolution of the organization	<p>Bankruptcy Act Rule 3020 (d)</p> <ul style="list-style-type: none"> The court assumes authority to manage the debtor's property (estate). <p>Section U.S.C. 1125 (b)</p> <p>Debtor possesses property until there is a confirmed plan or a summary of a reorganization plan.</p>

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