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# Debt Collateralization and Business Insolvency: A Review of the Mexican Legal System

Agustín Berdeja-Prieto

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# DEBT COLLATERALIZATION AND BUSINESS INSOLVENCY: A REVIEW OF THE MEXICAN LEGAL SYSTEM

AGUSTÍN BERDEJA-PRIETO\*

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## I. INTRODUCTION AND OVERVIEW

This Article describes the most significant issues concerning business and finance collateralization and insolvency proceedings in Mexico, focusing on some of the methods available for creditors to secure their interests in property.<sup>1</sup> Part II of this Article addresses the debt enforcement mechanisms available to creditors prior to bankruptcy. Prior to bankruptcy, the creditor has either a debt secured by property or an unsecured debt. The creditor's ability to enforce the security prior to bankruptcy will differ depending on whether the debt is secured or unsecured. Parts III and IV of this Article address Mexican bankruptcy proceedings. These Parts cover the main issues, from a bankruptcy's commencement to its termination.<sup>2</sup> Suspension of pay-

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1. This Article reflects a draft prepared by the co-chairs for the Third National Institute on Multinational Commercial Insolvencies, although it has been amended to incorporate issues relevant in light of finance collateralization and bankruptcy practice.

Also, the author wishes to express his appreciation to Patrick Meaney, an Australian intern at Berdeja y Asociados, S.C. in Mexico City, for his valuable assistance in the preparation of this Article.

2. In Mexico, bankruptcy is regulated by the Ley de Quiebras y Suspensión de

ments is the last major component of bankruptcy. Part IV examines the differences between bankruptcy proceedings and suspension of payments proceedings. Finally, this Article addresses other general issues of debt collection, including multinational insolvencies.

As this Article reveals, Mexican bankruptcy law protects collateral before and during insolvency proceedings assuming due diligence to secure the interest was performed properly. Thus, creditors need not be discouraged by uncertain laws. Further, debtors are secure in knowing precisely what is required to manage their debts. In short, Mexico's system of collateralization provides both the creditor and the debtor with a certainty commensurate with the world's advanced legal systems.

## II. PRE-BANKRUPTCY CLAIMS AND ENFORCEMENT

To finance an agreement, creditors often secure those agreements with collateral in either real or personal property.

### A. *Security in Real Property: Mortgages*

The mortgage is the most common form of security in real property. Real property, meanwhile, is used to secure many major transactions. For instance, real estate mortgages typically secure major credit transactions such as loans, credit lines for factoring agreements, and performance bonds. These mortgages have certain documentary and recording requirements to ensure proper perfection as secured interests.

The value of the real property mortgaged dictates the type of documentation necessary to evidence the mortgage.<sup>3</sup> In most cases, mortgaged real property exceeding 500 pesos in value must be evidenced by a public deed.<sup>4</sup> Mortgaged real property valued at less than 500 pesos can be secured by private contract,

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Pagos [Bankruptcy and Suspension of Payments Law] [hereinafter L.Q.S.P.]. See L.Q.S.P. art. 3. For an English translation of the L.Q.S.P., see 2 DOING BUSINESS IN MEXICO app. 8 (Michael W. Gordon ed., 1993).

3. CÓDIGO CIVIL PARA EL DISTRITO FEDERAL [CIVIL CODE FOR THE FEDERAL DISTRICT] [hereinafter C.C.D.F.] art. 2917. Article 2917 states that, for financing guaranteed by a mortgage, one must observe the formalities established in articles 2317 and 2320.

4. C.C.D.F. arts. 2317, 2320, 2917.

executed before two witnesses whose signatures are confirmed by a public notary.<sup>5</sup>

Once the proper documentation is obtained, a mortgage must also meet recording requirements to ensure its perfection against third parties.<sup>6</sup> Only a mortgage with its "preventive registration"<sup>7</sup> at the Public Registry of Property and Commerce<sup>8</sup> (RPPC) will be effective against third parties. The effect of this registration is retroactive—a final resolution will date back to the preventive registration, provided the final registration was made within the statutory grace period.<sup>9</sup>

### 1. Limitations on Foreigners Taking Real Property as Security

There are no special rules or restrictions applicable to foreign creditors taking real property as security in Mexico. However, there are important restrictions on foreigners acquiring land and/or fixtures in Mexico.<sup>10</sup> Specifically, Mexican law restricts foreign acquisitions of land classified as restricted.<sup>11</sup> Land classified as restricted includes land within one-hundred kilometers of international land borders and land within fifty kilometers of the coastline.<sup>12</sup> Notably, the Mexican government has announced a new Foreign Investment Law, to be enacted in Mexico by the end of 1993,<sup>13</sup> which will presum-

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5. *Id.* arts. 2317, 2320, 2917.

6. *Id.* art. 2919.

7. *Id.* art. 3044; see also *id.* arts. 2919, 3015.

8. The Spanish term for the Public Registry of Property and Commerce is the *Registro Público de la Propiedad y de Comercio* (RPPC). Each state of the Mexican Republic, as well as the Federal District, has its own RPPC.

9. See C.C.D.F. art. 3017.

10. The distinction between using property as security and acquiring property is important. A foreigner may not want to secure a transaction with property the foreigner cannot acquire if the only method of enforcing the underlying debt is acquiring the property. In such a case, the foreign creditor could not acquire the property, and might be forced to sell the property at a loss to avoid violating the Mexican Constitution. See CONSTITUCIÓN MEXICANA [MEX. CONST.] art. 27-I.

11. See MEX. CONST. art. 27-I (foreigners are expressly prohibited from having direct ownership over land in certain locations; however, they can directly own land in other locations provided they agree to consider themselves nationals for all purposes); *Ley para Promover la Inversión Mexicana y Regular la Inversión Extranjera* [Law to Promote Mexican Investments and Regulate Foreign Investments] [hereinafter *Investment Law*] art. 7.

12. MEX. CONST. art. 27-(I).

13. Mexico enacted the law in December of 1993. See generally Agustín Berdeja-Prieto, *Mexico Streamlines Foreign Investment Law*, INT'L FIN. L. REV., Feb.

ably loosen some of these existing restrictions.

## 2. Enforcing Secured Claims

A mortgage is enforced by a foreclosure action. In Mexico, foreclosure is effected by a summary action.<sup>14</sup> When a creditor petitions the court for foreclosure, the court issues an injunction order that prohibits acts affecting the property and orders the recordation of the injunction order in the corresponding Public Registry of Property and Commerce.<sup>15</sup> The debtor then has nine days to present to the court his objections to the foreclosure.<sup>16</sup> Once this nine-day period expires or the debtor's objections are dismissed, an expert values the property and the property is ordered for sale by public bidding.<sup>17</sup>

Despite the summary nature of the foreclosure proceedings, mortgages are expensive to record. The expense of perfecting a mortgage may be as great as one percent of the amount of the credit, depending on the jurisdiction where the mortgage has to be recorded.<sup>18</sup>

### B. Possessory Security

#### 1. Pledge and Perfection Requirements

Pledges<sup>19</sup> are the most common form of security on personal property. Pledges can be either civil or commercial in nature. The distinction is important because civil and commercial pledges are regulated by different codes. Civil pledges are regu-

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1994; Michell Nader & Jorge Cervantes Trejo, *Mexico Liberalizes Foreign Investment Regime*, MEXICO TRADE & L. REP., Mar. 1, 1994, available in LEXIS, NSAMER Library, ALLNSA File.

14. See CÓDIGO DE PROCEDIMIENTOS CIVILES PARA EL DISTRITO FEDERAL [CIVIL PROCEDURES CODE FOR THE FEDERAL DISTRICT] [hereinafter C.P.C.D.F.] art. 468.

15. C.P.C.D.F. art. 470.

16. *Id.*

17. See *id.* arts. 486, 573. The property will only be sold if the highest bid reaches at least two-thirds of the assigned value of the property.

18. For example, the State of Guerrero, where Acapulco is located, uses the following formula to calculate the recording charge. Half of one percent (0.5%) of the amount of the credit to be recorded, plus an additional tax of fifteen percent of 0.5% of the credit used for education, the environment, tourism, and the construction of roads. The total charge is approximately 0.8% of the credit amount.

19. The Spanish term for a pledge is *prenda*.



lated by the *Código Civil* while commercial pledges are regulated by the *Ley General de Títulos y Operaciones de Crédito*.<sup>20</sup>

Civil pledges require that the goods be delivered either physically or constructively to the creditor.<sup>21</sup> Where goods are delivered constructively, the pledge is subject to further restrictions to ensure its perfection against third parties.

A civil pledge agreement for constructive delivery must be evidenced by either a written contract executed in two counterparts, one for each party, a public deed, or some other authenticated documents.<sup>22</sup> Civil pledge agreements for constructive delivery, which are formalized before a Public Notary<sup>23</sup> in a public document, are effective against third parties only when registered at the RPPC.<sup>24</sup> In contrast, civil pledge agreements initially evidenced by private contract are only effective against third parties once filed in the Public Commercial Registry.<sup>25</sup>

Commercial pledges are broadly defined as those pledges involving "acts of commerce."<sup>26</sup> In general, to perfect a commercial pledge, the pledged goods or credit instruments must be physically delivered to the creditor.<sup>27</sup> The rules governing how to perfect a commercial pledge and its effectiveness against third parties varies depending upon the nature of the collateral.<sup>28</sup> For instance, a commercial pledge involving a contract for equipment, operating, or financing credit can be perfected before a Public Commercial Registry<sup>29</sup> prior to the commercial pledge's registration at the RPPC.<sup>30</sup>

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20. Ley General de Títulos y Operaciones de Crédito [General Law of Credit Instruments and Credit Operations] [hereinafter Credit Instr. & Operations Law].

21. C.C.D.F. art. 2858.

22. *Id.* art. 2860.

23. The Spanish term for public notary is *notario público*.

24. C.C.D.F. art. 2859.

25. See generally C.C.D.F. arts. 2859, 2860.

26. CÓDIGO DE COMERCIO [COMMERCIAL CODE] [hereinafter Cód. COM.] art. 75; Credit Instr. & Operations Law art. 1.

27. Credit Instr. & Operations Law arts. 334.

28. As regards commercial contracts, however, Cód. COM. arts. 77-79 establish the principle that commercial pledges bind the parties thereto without the need for formalities or other requirements, except as otherwise expressly provided for in the law.

29. The Spanish term for a Public Commercial Registry is *Corredor Público*.

30. Credit Instr. & Operations Law arts. 326, 334-VII.

## 2. Enforcing Pledges

Regardless of whether the pledge is civil or commercial, the creditor has the right to retain possession of the goods until the debt is satisfied. If the debtor fails to fulfill its obligation within the period stipulated in the underlying agreement, the creditor may enforce its security interest. The creditor can enforce the security interest using several methods. Creditors holding a civil pledge may petition a court to sell the pledged goods by public auction if the debtor fails to pay within the stipulated period in the agreement.<sup>31</sup> Further, creditors may sell the pledged goods and avoid court involvement altogether, provided the creditor has obtained the debtor's express agreement.<sup>32</sup>

Any consent agreement authorizing the sale of the pledged goods without court involvement, however, must not prejudice the rights of third parties. Notably, any time after the date on which the pledge is executed, the debtor may consent to the creditor becoming the owner of the property.<sup>33</sup>

Similarly, a creditor holding a commercial pledge may petition the court for permission to sell the pledged collateral, once the guaranteed obligation matures.<sup>34</sup> However, unlike the civil pledge, the creditor of a commercial pledge may also petition the court before the obligation matures if the collateral's value becomes less than 120% of the debt amount.<sup>35</sup> In addition, the commercial creditor may become the owner of the pledge, provided the pledgor expressly consents in writing after the date of the pledge's execution.<sup>36</sup>

### *C. Non-Possessory Security Interests*

Creditors may also secure their debts by nonpossessory security interests. Title retention and installment sales con-

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31. C.C.D.F. art. 2881.

32. *Id.* art. 2884. The language of article 2884 suggests that this express agreement to sell the pledged goods without court involvement could be contained within the contract or by a subsequent agreement amending the contract. *Id.*

33. *Id.* art. 2883.

34. Credit Instr. & Operations Law art. 341.

35. *Id.* arts. 340, 342.

36. *Id.* art. 344.

tracts,<sup>37</sup> purchase financing agreements,<sup>38</sup> and trusts<sup>39</sup> comprise three of the major non-possessory security mechanisms under Mexican law.<sup>40</sup>

### 1. Purchase Finance Agreements<sup>41</sup>

A purchase finance agreement is an agreement where the creditor loans money to the debtor enabling the debtor to purchase specific raw material equipment, and/or pay for certain operating expenses.<sup>42</sup> The equipment the debtor acquired and/or the products produced as a consequence of the loan, serves as the security for the debt.<sup>43</sup>

To perfect purchase finance agreements, the debtor and the secured party must execute a loan document identifying the terms of the transaction, including the security interest to be transferred.<sup>44</sup> This written loan document must then be registered either with the Registry of Mortgages where the property is located, or with the Public Commercial Registry, provided the security does not consist of real property.<sup>45</sup> The loan document

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37. The Spanish phrase for an installment sales contract is *contrato de compraventa a plazos con reserva de dominio*.

38. In Spanish purchase finance agreements are known as *créditos de habilitación o avío y créditos refaccionarios*.

39. The Spanish word for trust is *fideicomisos*.

40. There are other non-possessory security mechanisms available. For example, a security bond (*caución bursátil*) is a security mechanism where the debtor uses financial securities to guarantee its obligation to the creditor. If the debtor defaults on any obligation, the security bond enables the bond's beneficiary (usually the creditor) to instruct a pre-appointed trustee to sell the securities guaranteeing the bond and to deliver the proceeds thereof to the beneficiary. The legality of a security bond has not yet been tested in the courtroom. The bond's sale procedures raise some due process questions under the Mexican Constitution. Overall, however, security bonds seem to offer a sensible and cost-efficient alternative to other financing mechanisms that entail lengthy court proceedings. See *Ley del Mercado de Valores* [Securities Market Law] arts. 22, 99.

41. Purchase finance agreements are governed by the Credit Instr. & Operations Law. See Credit Instr. & Operations Law arts. 321-33. Among the uses for purchase finance agreements, the Credit Instr. & Operations Law distinguishes between a *crédito de habilitación o avío* and a *crédito refaccionario*. *Crédito de habilitación o avío* is normally used for working capital purposes, whereas *crédito refaccionario* is used to start up or promote a business. See Credit Instr. & Operations Law arts. 321, 323.

42. Credit Instr. & Operations Law art. 321.

43. See *id.* art. 324.

44. See *id.* art. 326.

45. See *id.* art. 326.

must then be registered at the RPPC in the jurisdiction of the property encumbered in order to be enforceable against third parties.<sup>46</sup>

The creditor of a purchase finance agreement enforces his claim on a purchase finance agreement by petitioning the court for the auction of the property serving as the security for the loan document.<sup>47</sup> Under article 333 of the Credit Instr. & Operations Law, a creditor with a duly perfected and registered purchase finance agreement will have preference over all other secured creditors with one exception. Mortgage creditors with interests recorded prior to the registration of the purchase finance agreement will have a higher preference.

## 2. Trust Agreements

In a trust arrangement, the debtor or a third party on behalf of the debtor, as settlor,<sup>48</sup> executes a trust in which title to certain property is transferred to a trustee.<sup>49</sup> The trustee holds this property in trust in favor of the beneficiary<sup>50</sup> as collateral for a loan or other credit transaction.<sup>51</sup> The use of these types of transactions are extensive because all classes of goods and rights, except those which are by law strictly personal rights, may comprise trust arrangements.<sup>52</sup>

To defeat third-party interests, a trust agreement must be perfected. It must be in writing and must comply with the applicable laws governing the transfer of the rights or property com-

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46. *Id.* art. 326.

47. *Id.* art. 341.

48. The Spanish word for settlor is *fideicomitente*.

49. See Credit Instr. & Operations Law art. 346. The Spanish term for trustee is *fiduciario*.

50. The Spanish word for beneficiary is *beneficiario*.

51. See Credit Instr. & Operations Law arts. 346, 351-57; see also Ley de Instituciones de Crédito [Credit Institutions Law] art. 46-XV.

52. See Credit Instr. & Operations Law art. 351. Traditionally, only banks were allowed to act as trustees. However, other entities can now act as a trustee so long as the underlying transactions are directly related to their activities. See Ley General de Instituciones y Sociedades Mutualistas de Seguros [General Law of Insurance Institutions and Companies] [hereinafter Insurance Law] art. 34-IV (authorizing insurance companies to act as trustees); Nueva Ley Federal de Instituciones de Fianzas [New Federal Law of Bonding Institutions] [hereinafter Bonding Inst. Law] art. 16-XV (authorizing bonding companies to act as trustees); Securities Market Law art. 22-IV (authorizing brokerage houses (*casas de bolsa*) to act as trustees).

prising the trust's corpus.<sup>53</sup> Title to the property then passes to the trustee. So long as the trust agreement is duly perfected and registered, the property which is the subject of the trust's corpus may be excluded from any bankruptcy proceedings against the debtor.<sup>54</sup>

If the debtor under a trust arrangement—normally the settlor—should default, the trustee can enforce the trust agreement by selling the transferred property without the need for court proceedings, in accordance with the provisions of the trust indenture.<sup>55</sup> Thus, in the event of a settlor's insolvency, it is essential from the beginning of this process to expressly and specifically authorize a trustee to carry out the beneficiary's instructions.<sup>56</sup>

### 3. Installment Sales Contracts

Compared with purchase finance agreements, installment sales contracts are a more common form of sales contracts for commercial and consumer buyer-seller transactions in Mexico. Commercial installment sales contracts are governed by the *Código de Comercio* and the *Código Civil*. Further, they are regulated by consumer protection statutes.<sup>57</sup> Under a title retention contract, the debtor takes possession of the goods while title remains with the seller until the debt is fully paid.<sup>58</sup> A written contract provides the requisite documentation; but real property transactions may require additional formalization.<sup>59</sup>

Registration at the RPPC of a title retention or installment

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53. Credit Instr. & Operations Law art. 352.

54. There are at least two precedents which seem to support this proposition. See Judgments 619/91 and 653/91 of Jan. 9, 1992 and Feb. 13, 1992, Tercer Tribunal Colegiado en Materia Civil del Tercer Circuito, *Semanario Judicial de la Federación* [S.J.F.] Octava Época, Tomo X, 362, Julio de 1992. In these cases, the Circuit Court decided that the defendant's property, which was held in trust at the time the suit was brought, was not subject to attachment because it was "part of the assets of the trustee and outside the realm of the defendant's assets." See *id* (translation provided by the author).

55. See Credit Instr. & Operations Law art. 356.

56. See *id*. The trustee also has an obligation to exercise due care to avoid unjustified diminution of the trust's corpus. Accordingly, the trustee is responsible for any unreasonable loss or damage to the debtor's property. *Id*.

57. See, e.g., Ley Federal de Protección al Consumidor [Federal Law on Consumer Protection] [hereinafter L.F.P.C.] arts. 2, 6, 66-72.

58. C.C.D.F. art. 2312.

59. *Id*. art. 2316.

sales contract is essential to produce effects *vis-à-vis* third parties.<sup>60</sup> This registration ensures that no member of either the preferred or privileged classes of creditors in a bankruptcy proceeding can assert a better claim over the goods.<sup>61</sup> This would, otherwise, entitle the creditor to have the goods separated from the bankrupt estate.<sup>62</sup> Failure to register creates inexcusable risks. An unregistered title retention holder who petitions for separation, for example, may find his claim defeated by the claim of a bona fide third party purchaser.<sup>63</sup>

Once certain formal requisites are met, under both commercial installment sales contracts and commercial title retention contracts, the creditor is entitled to bring an executory action to expeditiously foreclose on the debt.<sup>64</sup>

#### D. Unsecured Claims

##### 1. Non-Judicial Collection Techniques and Set-off

Unsecured claims hold a precarious fate in Mexico because the Mexican approach to claims collection tends to favor judicial, rather than extra-judicial involvement. However, set-off is one extra-judicial method by which an unsecured creditor might recover an unsecured claim, adjusting the debtor's debt against the creditor's debt to the debtor.<sup>65</sup> Set-off availability requires that the two debts be due and payable,<sup>66</sup> be calculated in a money amount, or exchangeable in fungible goods of the same type and quality.<sup>67</sup> Further, the set-off amount must be determined or capable of determination within nine days.<sup>68</sup> Where the debts are for unequal amounts, they are set-off by an amount equal to the lesser of the two debts.<sup>69</sup>

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60. *See id.* arts. 2310, 2312 (excluded are goods not susceptible to identification); *see also* Reglamento del Registro Público de la Propiedad del Distrito Federal [Regulations of the Public Property Registry in the Federal District] arts. 61-70.

61. L.Q.S.P. art. 158.

62. *Id.*

63. *See id.* art. 160; *see also* C.C.D.F. arts. 2310, 2312.

64. Cód. COM. art. 1391. In Spanish an executory action is called *acción ejecutiva*.

65. C.C.D.F. art. 2185.

66. *Id.* art. 2188.

67. *Id.* art. 2187.

68. *Id.* art. 2189.

69. *Id.* art. 2186. The L.Q.S.P., however, contains some limiting rules regarding

## 2. Judicial Collection Remedies

If an unsecured creditor does not qualify for set-off, the creditor must bring an action in court to recover the debt. The most significant benefit of bringing this action is the availability of provisional attachment.<sup>70</sup> Provisional attachment requires that the creditor prove the need for the attachment and that the creditor is entitled to such attachment.<sup>71</sup> Provisional attachments may be granted either before or after commencing an action when: (i) there are reasonable grounds to suspect the debtor will hide or sequester the property;<sup>72</sup> (ii) in an action *in rem*, there are reasonable grounds to suspect the debtor will damage the property which is the subject of the action;<sup>73</sup> or (iii) in an *in personam* action in which the designated property is the only property of the debtor, there are reasonable grounds to suspect the debtor will alienate or hide the property.<sup>74</sup>

Holders of (i) public instruments;<sup>75</sup> (ii) judicial confessions of the debtor;<sup>76</sup> (iii) properly executed bills of exchange, promissory notes and other negotiable instruments;<sup>77</sup> (iv) insurance policies;<sup>78</sup> (v) experts awards in insurance matters;<sup>79</sup> and (vi) invoices, current accounts and other commercial contracts,<sup>80</sup> are entitled to bring an executory action against the debtor.<sup>81</sup> Further, those holders are entitled, as a matter of right, to prejudgment attachment of the defendant's property.

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set-off. See L.Q.S.P. art. 128-IV.

70. The Spanish words for provisional attachment are *secuestro provisional*.

71. Cód. COM. arts. 1172-73, 1178, 1184. In order to establish the need for attachment, a creditor can use documents and/or the testimony of three witnesses. *Id.* art. 1173. The pleading demanding the attachment must request the amount to be attached with precision. *Id.* art. 1178.

72. *Id.* art. 1168.

73. *Id.*

74. *Id.*

75. *Id.* art. 1391.

76. *Id.* In order to be acknowledged by a court, a judicial confessions must conform to the requirements of Cód. COM. art. 1287.

77. Cód. COM. art. 1391.

78. *Id.* Insurance policies must conform to the requirements of the Insurance Contract Law art. 19.

79. Cód. COM. art. 1391.

80. *Id.*

81. Cód. COM. art. 1391. In Spanish, prejudgment attachment is known as *embargo de precaución*.

The holders of final judgments or non-appealable awards are also entitled to this executory action. However, it is possible that the debtor's property previously assigned to a bank or financial institution as part of a valid trust arrangement may not be attached.<sup>82</sup>

Depending on the kind of action available, it generally takes two to four years to obtain a final judgment. Court costs are negligible. An official schedule of legal fees,<sup>83</sup> setting forth attorney's fees according to the nature of the work, exists,<sup>84</sup> but that schedule has not been updated in twenty-five years. In practice, however, legal fees are negotiable and some lawyers accept work on a contingency basis.

### 3. Enforcing Domestic Judgments

Generally, the judge of first instance executes the judgment.<sup>85</sup> If no goods have been attached when the court issues a judgment, the creditor can demand the execution of the judgment. The judge will then attach the collateral.<sup>86</sup>

Following attachment, the judgment creditor may then petition for an auction judgment, whereby the goods are valued by brokers or experts and then sold at auction.<sup>87</sup> Alternatively, the parties may agree, during the proceedings, to value and sell the attached goods.<sup>88</sup>

Attachment judgments are especially important to preserve unregistered assets. In at least one case involving creditors of equal class that attached unregistered assets, the court decided that the date of the attachment order determined the priority of payment, not the date of the contract giving rise to the debt.<sup>89</sup>

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82. See *supra* notes 54-55 and accompanying text.

83. The Spanish word for legal fees is *arancel*.

84. See Ley Orgánica de los Tribunales de Justicia del Fuero Común del Distrito Federal [Organic Law of the Federal District Courts, General Jurisdiction] arts. 222-56.

85. Cód. COM. art. 1346 (a court of "first instance" is the civil law equivalent of the common law trial court).

86. *Id.* art. 1347.

87. *Id.* art. 1410. Unless the brokers or experts designated by the parties can agree on the value of the goods, the judge will designate a third broker or expert. *Id.*

88. Cód. COM. art. 1413.

89. Judgment 124/91 of May 21, 1991, Primer Tribunal Colegiado en Materia Civil del Décimo-Sexto Circuito, S.J.F., Tomo VII, 267-68, Junio de 1991.



Thus, an unsecured creditor wishing to cover its debt by attaching unregistrable assets should seek an immediate attachment judgment.

#### 4. Access by Foreigners to Domestic Judgments

Generally, there are no express limitations on foreign access to Mexican courts. Mexican law applies equally to all persons and all acts or events occurring within Mexican territory.<sup>90</sup> However, foreigners must have standing to enforce their claims in Mexican courts.<sup>91</sup>

Mexican rules regarding standing are similar to those in the United States and other common law countries. Only persons having an interest in a right's declaration or establishment or in the imposition of punishment or penalty, or in opposing them, may commence or intervene in Mexican legal proceedings.<sup>92</sup> Foreigners should be aware that foreign law will only apply if Mexican law mandates its application, or if a treaty or convention provision, to which Mexico is a party, provides that foreign law applies.<sup>93</sup>

#### 5. Access by Foreigners to Domestic Courts on Foreign Claims

There are no express limitations on foreigners gaining access to Mexican courts to institute proceedings relating to foreign claims. Mexican jurisdiction over extraterritorial matters applies equally to Mexicans and foreigners.

According to article 1093 of the *Código de Comercio*, for example, parties to a commercial contract may elect to submit to any jurisdiction they choose. That jurisdiction, however, must rest on either (i) the domicile of any one of the parties,<sup>94</sup> (ii) the place of performance of any of the parties' obligations,<sup>95</sup> or (iii) the place where the subject matter of the contract is located.<sup>96</sup> Where no choice of forum provision is available, courts of a par-

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90. C.C.D.F. art. 12.

91. C.P.C.D.F. art. 1.

92. *Id.*

93. C.C.D.F. art. 12.

94. Cód. COM. art. 1093.

95. *Id.*

96. *Id.*

ticular Mexican jurisdiction will be competent if that jurisdiction is (i) the place of payment designated by the debtor;<sup>97</sup> (ii) the place where the contract is to be performed;<sup>98</sup> (iii) the debtor's domicile;<sup>99</sup> (iv) in the absence of a fixed domicile, the place of the contract's execution in actions *in personam*, and the place of the contract's subject matter, in actions *in rem*;<sup>100</sup> or (v) in the case of an insolvency, the debtor's domicile.<sup>101</sup> For purposes of jurisdiction, a corporation's domicile is either the place of incorporation, the corporation's principal place of business, or, if both incorporation and the principal place of business are outside Mexico, the place where the corporation executed legal acts relating to the matter in dispute.<sup>102</sup>

## 6. Enforcing Foreign Judgments

In general, a judgment rendered by a foreign court or an award rendered by a foreign arbitration panel will be enforceable through the competent Mexican court without re-examination or re-litigation of the merits of the matter. However, the enforcement of foreign judgments and awards has requirements. First, one must present the Mexican court with a letter rogatory from the court which rendered the judgment.<sup>103</sup> Second, the foreign judgment must not have been rendered in an action *in rem*.<sup>104</sup> Third, the court issuing the judgment must also be considered competent under internationally accepted rules which comport with Mexican law.<sup>105</sup> Fourth, process in the action must have been served personally on the other party.<sup>106</sup> Fifth,

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97. *Id.* art. 1104. Article 567 of the C.F.P.C., which together with the C.P.C.D.F. supplements the *Código de Comercio*, provides that a choice of forum clause will be invalid if it benefits one of the parties exclusively. *See also* C.P.C.D.F. art. 605. Additionally, arts. 13-15 of the C.C.D.F. provide that a choice of law clause will only be invalid if the clause is a fraud on the law or against the public interest.

98. *Id.*

99. *Id.* art. 1105.

100. *Id.* art. 1107. If property the subject of the *in rem* action is located in several locations and jurisdictions, then the appropriate forum may be within any of the jurisdictions. *Id.* art. 1108.

101. *Id.* art. 1109.

102. C.C.D.F. art. 33.

103. *See* Cód. COM. art. 1347.

104. *Id.*

105. *Id.*

106. *Id.* Requiring personal service obviously increases the likelihood of the defe-

the judgment must be final, against which there is no further recourse according to the laws of the foreign jurisdiction.<sup>107</sup> Sixth, the final judgment must not concern a lawsuit among the same parties pending before a Mexican court.<sup>108</sup> Seventh, the final judgment must not seek to enforce an obligation which violates Mexican public policy, a Mexican treaty, or general principles of international law.<sup>109</sup> Finally, the judgment must fulfill the necessary requirements of authenticity,<sup>110</sup> and as a matter of reciprocity, the foreign court issuing the judgment would enforce Mexican judgments in a similar case.<sup>111</sup>

Mexico is also a party to other conventions which control enforcement of certain foreign judgments. These include the *1958 U.N. Convention on the Recognition and Enforcement of Foreign Arbitral Awards* and the *1984 Inter-American Convention on International Competence for Extraterritorial Validity of Foreign Judgments and Awards*.<sup>112</sup>

If a foreign court specifically petitions a Mexican court to implement a foreign judgment, that petition must be honored, without need for formal recognition.<sup>113</sup> However, that petition must meet the requirements for authenticity, and the laws of the respective petitioning foreign court must comply with Mexican law.<sup>114</sup>

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ndant's appearance and thus ensures the presentation of any existing defenses.

107. *Id.*

108. *Id.*

109. *See id.*; *see also* C.P.C.D.F. art. 604.

110. CÓD. COM. art. 1347.

111. C.P.C.D.F. art. 604. Mexican reciprocity is not automatic. For instance, *see* Aeronaves de México, S.A. de C.V., *Quiebra*, Juez Primero de lo Concursal, Expediente 23/88, Distrito Federal, 29 de enero de 1990, published in "*El Foro*", *Organo de la Barra Mexicana y del Colegio de Abogados*, Octava Epoca, Tomo III, Número 4, México, D.F., 1990 15-63, where reciprocity was denied in a matter concerning a taxation judgment.

112. For a comprehensive list of the private international law treaties that Mexico has signed, *see* FERNANDO A. VÁZQUEZ PANDO, *NUEVO DERECHO INTERNACIONAL PRIVADO* (1990).

113. The Spanish word for formal recognition is *homologación*.

114. C.P.C.D.F. art. 605.

### III. LIQUIDATION IN BANKRUPTCY

#### A. *Principal Laws Governing Liquidation*

The L.Q.S.P., the Federal Labor Law<sup>115</sup> and the Fiscal Code of the Federation<sup>116</sup> principally regulate bankruptcy and liquidation of commercial entities. Other laws may be applicable, depending on the bankrupt's trade and the nature of the proceedings.<sup>117</sup>

#### B. *Courts which Administer Liquidation*

To commence a bankruptcy action, the debtor must bring the action in a court of competent jurisdiction. In Mexico, the state court of first instance, located in the merchant's principal place of business,<sup>118</sup> or the district court<sup>119</sup> have jurisdiction to hear merchant bankruptcies.<sup>120</sup> Jurisdiction of corporate bankruptcies is proper at the corporate headquarters or, otherwise, in the corporation's principal place of business.<sup>121</sup> Venue determines which particular state or federal court has jurisdiction to hear a bankruptcy action. Jurisdiction of subsidiaries is also proper at the location stipulated in a contract for payment of an obligation or the location for contract performance.<sup>122</sup> Absent a fixed domicile, a court in the place of contract execu-

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115. The Federal Labor Law is translated, *Ley Federal del Trabajo* [hereinafter L.F.T.].

116. The Fiscal Code of the Federation is translated, *Código Fiscal de la Federación* [hereinafter C.F.F.]. Civil bankruptcy (*concurso*), which is applicable to individuals or entities other than commercial entities or individual merchants, is regulated by State Civil Codes. Which state civil code applies is determined by the domicile of the person or entity. In the Federal District, civil bankruptcies are governed by the C.P.C.D.F.

117. The laws which could apply are the Credit Instr. & Operations Law, the C.C.D.F., the Credit Institutions Law, the Insurance Law, and the Bonding Inst. Law.

118. The Spanish phrase for state court of first instance is *juzgado de primera instancia*. The state court of first instance is the civil law equivalent of the common law trial court.

119. The Spanish term for the district court is *juzgado de distrito*.

120. See L.Q.S.P. art. 13.

121. *Id.*

122. C.C.D.F. art 33. The debtor's domicile is usually either the place of incorporation, the place where the debtor carries on business, or where the execution of legal acts in relation to the matter took place. *Id.*

tion has proper jurisdiction. In the case of an action *in personam*, and, in the case of an action *in rem*, a court in the location of the contract subject matter has proper jurisdiction.<sup>123</sup>

### C. Commencing Liquidation

#### 1. Requirements

##### a. Corporations and Corporate Authority

A debtor corporation filing for bankruptcy must present a petition to the court signed by the debtor, its legal representative or special attorney-in-fact.<sup>124</sup> If the debtor is a corporation, the petition must be signed by a person empowered to sign on behalf of the corporation.<sup>125</sup>

According to article 10 of the General Law of Mercantile Corporations,<sup>126</sup> the corporation's managers<sup>127</sup> are the persons statutorily empowered to represent the corporation.<sup>128</sup> For a person to have authority to bring legal actions on behalf of a corporation, the respective individual should be granted a general power for lawsuits and collections without limitation.<sup>129</sup> Alternatively, the appropriate individual can be one granted a special power of attorney for lawsuits and collections, limited to a specific bankruptcy proceeding.<sup>130</sup>

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123. Cód. COM. art. 1107.

124. The petition must also state the reasons for the debtor's bankruptcy. Along with the petition, the debtor must submit its accounting books, the balance sheets for the business, a list of creditors and debtors of the business and a valuation of the business and its assets. See L.Q.S.P. art. 6. There are few legal practitioners in Mexico who specialize in insolvency cases. To the best of the author's knowledge, there exists no legal directory of specialized counsel. To a great extent, the field is controlled by a few, well-known bankruptcy trustees. The best alternative for choosing Mexican counsel may be the Litigation Committee of the Mexican Bar (*Barra Mexicana, Colegio de Abogados*).

125. L.Q.S.P. art. 7.

126. The Spanish phrase for the General Law of Mercantile Corporations is *Ley General de Sociedades Mercantiles*.

127. The corporation can also authorize an appointee to represent it. General Law of Mercantile Corporations art. 6-IX.

128. The Spanish word for a corporation is *sociedad mercantil*.

129. C.C.D.F. art. 2554. Individuals also may authorize another person to bring a legal action on their behalf by granting them a general power of attorney in accordance with article 2554. *Id.*

130. Note, however, that there is at least one judicial decision limiting the com-

*b. Domicile or Assets Located Within the Jurisdiction*

A Mexican entity can commence a bankruptcy action if its place of incorporation or principal place of business is within Mexico.<sup>131</sup> In contrast, Mexican branches of foreign entities, which file bankruptcy proceedings in Mexico only affect those assets located and those creditors who have done business with the bankrupt branch located within the Mexican Republic.<sup>132</sup>

The L.Q.S.P. has no specific provision addressing jurisdiction of a foreign company's bankruptcy, when the foreign company has assets in Mexico, but no company branches in Mexico. However, the jurisdiction of preference should be the place where the assets are located. This solution would also be most consistent with the approach of article 13 of the L.Q.S.P.<sup>133</sup>

*c. Eligibility for Relief: Excluded Entities*

The L.Q.S.P. encompasses all merchants.<sup>134</sup> Merchants include corporate entities and individuals engaged in trading or commerce.<sup>135</sup> Further the L.Q.S.P. contains provisions specifically addressing banks and other credit institutions,<sup>136</sup> public service enterprises,<sup>137</sup> insurance companies,<sup>138</sup> and financial institutions. Non-trading corporations, such as charitable institutions having no business activities, are excluded by implication.

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pany's power to authorize representation in bankruptcy proceedings exclusively to the company's management. Judgment 555/90 of July 12, 1990, Quinto Tribunal Colegiado en Materia Civil del Primer Circuito, S.J.F. Octava Epoca, Tomo VI, 250, Julio-Diciembre de 1990.

131. L.Q.S.P. art. 13.

132. See *id.*; see also generally Cód. COM. art. 1109.

133. See Cód. COM. art. 1107 (providing that absent a permanent domicile, *in personam* jurisdiction rests on the location of the contract's execution; *in rem* jurisdiction upon the location of the *res*); *id.* art. 1110 (providing that in the case of a confirmed legal absence, the jurisdiction is the absentee's previous permanent domicile or where the majority of the assets are located).

134. The Spanish word for merchants is *comerciantes*.

135. See generally L.Q.S.P. arts. 3, 6, 7, 90, 190.

136. *Id.* arts. 430-42.

137. *Id.* arts. 450-54.

138. *Id.* arts. 443-49.

## 2. Requirements to Commence a Bankruptcy Case

Creditors or district attorneys<sup>139</sup> petitioning the court for a declaration of bankruptcy<sup>140</sup> must prove that the debtor comes within one of the presumptions of bankruptcy set out in article 2 of the L.Q.S.P.<sup>141</sup> These presumptions are of three types: (i) those related to the debtor's economic resources;<sup>142</sup> (ii) those related to the debtor's behavior;<sup>143</sup> and (iii) those related to the debtor's procedural acts.<sup>144</sup>

Two presumptions concern the debtor's economic resources: the general default in the payment of its due and payable monetary obligations (*obligaciones líquidas y vencidas*)<sup>145</sup> and the lack or insufficiency of assets that could be attached to cover breach of an obligation or enforcement of a judgment.<sup>146</sup>

Numerous presumptions of bankruptcy concern the debtor's behavior such as: (i) a concealment or absence within the corporation of persons responsible for payment of corporate obligations without authorizing someone to pay such obligations;<sup>147</sup> (ii) under the circumstances described in (i) above, the closing of entity premises;<sup>148</sup> (iii) the assignment of corporate assets to some of its creditors;<sup>149</sup> (iv) debtors' resorting to ruinous, fraudulent, or fictitious means to discharge or avoid discharging its obligations.<sup>150</sup>

The presumptions related to the procedural acts of the debtor include: (i) the debtor's petition to the court for a bankrupt declaration;<sup>151</sup> (ii) the debtor's unsuccessful petition to the

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139. The Spanish phrase for district attorney is *Ministerio Público*.

140. L.Q.S.P. art. 5.

141. See *id.* art. 2. These presumptions can be rebutted by proof that the debtor can meet its obligations and pay its outstanding debts. *Id.*

142. *Id.*; see also JOAQUIN R. RODRÍGUEZ, *LEY DE QUIEBRAS Y SUSPENSIÓN DE PAGOS* 19 (1993).

143. L.Q.S.P. art. 2.

144. *Id.*

145. *Id.* art. 2-I.

146. *Id.* art. 2-II.

147. *Id.* art. 2-III.

148. *Id.* art. 2-IV.

149. *Id.* art. 2-V.

150. *Id.* art. 2-VI.

151. *Id.* art. 2-VII.

court for suspension of payments relief;<sup>152</sup> and (iii) the debtor's noncompliance with its obligations under suspension of payments agreement.<sup>153</sup>

In summary, the debtor's economic resources, behavior, and procedural acts all involve *prima facie* presumptions. They can be rebutted by proof that the debtor is able to meet its due and payable monetary obligations with its available assets.<sup>154</sup>

#### D. Parties to a Liquidation

##### 1. Judge

The bankruptcy judge supervises the bankruptcy process. This judge is granted broad powers to facilitate bankruptcy's proper administration.<sup>155</sup> These powers include the power to authorize the seizure of all assets and documents of the bankrupt to ensure the "security and preservation of the [debtor's] assets."<sup>156</sup> The judge also has appointment and removal powers, and authority to supervise trustee activities.<sup>157</sup> Most importantly, the judge is empowered to resolve all claims and disputes relating to the bankruptcy.<sup>158</sup>

##### 2. Fiduciaries

The bankruptcy trustee<sup>159</sup> is, as fiduciary, an auxiliary to the administration of justice.<sup>160</sup> Though the precise legal scope of this title is subject to debate, it is clear that the trustee is primarily responsible for assisting the judge in carrying out the duties of safekeeping and ordinary management of the assets.<sup>161</sup> The trustee is also obligated to exercise all the debt-

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152. *Id.* art. 2-VIII.

153. *Id.* art. 2-IX.

154. *Id.* art. 2.

155. *Id.* art. 2-XI.

156. *Id.* arts. 26-I, 26-III.

157. *Id.* arts. 26-V through 26-IX.

158. *See id.* art. 26-XI.

159. The Spanish word for bankruptcy trustee is *síndico*.

160. L.Q.S.P. art. 44.

161. Compare L.Q.S.P. art. 26 (enumerating the powers of the judge) with L.Q.S.P. art. 46 (listing the rights and duties of the trustee). In some cases, there may be a judicial depository (*depositario judicial*) acting before a trustee in the bankruptcy is permanently appointed. L.Q.S.P. arts. 187, 202. There is at least one judi-



or's rights of action in relation to his assets, as well as the debtor's rights in actions by the creditor and third parties.<sup>162</sup> Finally, the trustee proposes to the judge whether to sell the business, sell part of the business, continue the business, or take any other "extraordinary measures" benefitting the estate.<sup>163</sup>

The judge is limited in who he can designate as a trustee.<sup>164</sup> The judge must choose the bankruptcy trustee from a list of institutions and persons qualified to serve as trustees.<sup>165</sup>

Intervenors are temporarily appointed by the judge at bankruptcy declaration until a creditor's meeting appoints permanent intervenors.<sup>166</sup> Intervenors, as fiduciaries, play a key role in safeguarding creditors' interests by monitoring the trustee's actions and bankruptcy administration.<sup>167</sup>

#### *E. Meetings of Creditors or Holders of Equity Interests*

The judge must convene creditors meetings.<sup>168</sup> There, the creditors collectively address the perfection of claims,<sup>169</sup> the appointment or removal of definitive intervenors,<sup>170</sup> and the approval of bankruptcy agreements.<sup>171</sup> Each recognized creditor attending a creditor's meeting represents one vote, irrespective of the size of its claim.<sup>172</sup> A simple majority is needed to pass resolutions, except where the law specifically provides that voting will correspond with the capital represented or where a special majority is stipulated.<sup>173</sup>

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cial decision comparing the function of a judicial depository to the function of a trustee while distinguishing it from the role of an intervenor. Judgment 855/90 of October 18, 1990, Quinto Tribunal Colegiado en Materia Civil del Primer Circuito, S.J.F., Octava Epoca, Tomo VI, 251, Julio-Diciembre de 1990.

162. L.Q.S.P. art. 48-II.

163. *Id.* art. 48-III.

164. *See id.* art. 28.

165. *Id.* art. 29.

166. L.Q.S.P. art. 59.

167. *Id.* art. 58; *see also id.* art. 67 (enumerating the intervenor's powers).

168. *Id.* art. 74.

169. *Id.* art. 220.

170. *Id.* arts. 60, 62.

171. *See id.* art. 48-I.

172. *Id.* art. 79.

173. *Id.*

### *F. The Liquidation Estate*

Generally, the bankruptcy estate includes all of the bankrupt's present and future property and assets.<sup>174</sup> However, the L.Q.S.P. contains exemptions. The bankrupt can continue to possess and manage (i) inherently personal rights;<sup>175</sup> (ii) properties that are not capable of disposal by legal provision such as family estate, alimony, and the bankrupt's earnings following the bankruptcy declaration through the bankrupt's personal activities;<sup>176</sup> and (iii) rights over the property of third parties that are non-transferable or are transferable only after the owner's prior consent.<sup>177</sup> The L.Q.S.P. also allows third parties to institute proceedings to have their property separated from the bankrupt estate.<sup>178</sup>

#### 1. Property Returned to the Estate for Liquidation

Certain pre-bankruptcy transfers are reviewable and subject to avoidance. Thus, the bankruptcy declaration must specify the date the bankruptcy became effective.<sup>179</sup> Initially, the judge fixes that retroactive date according to the date from which the commercial entity ceased paying its obligations.<sup>180</sup>

The courts must set a retroaction period within twelve days following the recognition of claims.<sup>181</sup> However, the courts have discretion to lengthen or shorten the retroaction period.<sup>182</sup> In practice, depending on the circumstances of the case, Mexican courts willingly extend the so-called retroaction period.<sup>183</sup> Thus, a retroaction period in practice can nullify pre-bankruptcy transfers occurring anywhere from six to eighteen months preceding the bankruptcy petition's filing. In addition, a

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174. *Id.* arts. 83 & 115; *see also* C.C.D.F. art. 2964 (stating that debtors assure the satisfaction of their debts with all their assets, except those which, according to law, are inalienable or not subject to attachment).

175. L.Q.S.P. art. 115.

176. *Id.*

177. *Id.*

178. *Id.* arts. 158-62.

179. *See id.* art. 15-IX.

180. *See id.* arts. 1, 2, 9, 10, 15-IX.

181. *Id.* art. 121.

182. *Id.* art. 118; *see also* RODRÍGUEZ, *supra* note 142, at 107.

183. The Spanish phrase for retroaction period is *período de retroacción*.

debtor's pre-bankruptcy actions, effected before the retroactive date, will be ineffective if the third party was aware of the debtor's situation and the action knowingly defrauded the creditors.<sup>184</sup>

Articles 168 through 174 define debtor fraud. Debtor fraud can be actual, when both the third party and the debtor are aware of the latter's insolvent situation.<sup>185</sup> It can also be presumed in law, for example, when a transfer or payment is effected on an undue claim or without fair consideration.<sup>186</sup>

## 2. Property Excluded from the Bankruptcy Estate

The L.Q.S.P. allows third parties to institute legal actions to separate identifiable assets not definitely transferred to the bankrupt estate.<sup>187</sup> Indefinite transfers include situations where the relevant personal or real property can be repossessed in accordance with the law,<sup>188</sup> and where real property was sold to the debtor, the sale was not duly registered, and the bankrupt did not pay for the real property.<sup>189</sup> Personal property for which the bankrupt has not fully paid can also constitute an indefinite transfer.<sup>190</sup> Personal or real property purchased on credit, where non-payment was stipulated and publicly recorded as cause for rescission of the agreement and properly documented, constitutes a third type of indefinite transfer.<sup>191</sup> Finally, indefinite transfers can also arise where the bankrupt has properties in numerous forms. These include properties held in deposit, administration, lease, usufruct, trust, consignment, purchase or sale commission, or in transit, delivery or collection for a third party, pledge guaranty evidenced by public instrument, in a policy granted before a broker, or in bonds either of a general warehouse<sup>192</sup> or in favor of a bank.<sup>193</sup>

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184. L.Q.S.P. art. 168. *But see id.* art. 171 (providing that security interests registered before bankruptcy will be valid).

185. *Id.* arts. 168-74.

186. *Id.*

187. *Id.* art. 158.

188. *Id.* art. 159.

189. *Id.*

190. *Id.*

191. *Id.*

192. The Spanish words for general warehouses are *almacenes generales*.

193. *See* L.Q.S.P. art. 159.

### G. *Effects of a Bankruptcy Declaration*

As a consequence of the bankruptcy declaration, the bankrupt is denied the right of administration or dominium over the bankrupt estate.<sup>194</sup> The bankrupt's acts of administration or dominium in relation to his bankrupt estate represent actions which are void *vis-à-vis* the creditors, unless they benefit the creditors.<sup>195</sup>

The bankruptcy declaration also affects other legal proceedings of the bankrupt which are pending at the time of the bankruptcy declaration. All property that is currently the subject of legal proceedings against the bankrupt must be joined to the bankruptcy proceedings.<sup>196</sup> The only exceptions to this broad rule are proceedings where a final judgment has been delivered and those involving mortgage or pledge credits. All final judgments and those court proceedings involving mortgages and pledges are joined to the bankruptcy proceedings only for purposes of determining the priority of their payment.<sup>197</sup> Lastly, while the debts of the bankrupt generally cease to accrue interest from the date of the bankruptcy declaration, accrual of interest on mortgage and pledge credits does continue.<sup>198</sup>

The bankruptcy declaration also affects contracts to which the bankrupt is a party. Yet, the bankruptcy declaration's effect on the bankrupt's contracts does not mandate repudiation. Contracts, requiring partial or full performance at the time of the bankruptcy petition, may be performed by the trustee with the intervenor's prior favorable opinion and the judge's consent.<sup>199</sup> Further, the other contracting party may demand the trustee

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194. *Id.* art. 83.

195. *Id.* art. 116.

196. *Id.* art. 126.

197. *Id.* art. 127.

198. *Id.* art. 128-II. Mexican courts have applied article 132 by analogy to debts denominated in foreign currency. Article 132 provides that all obligations of the bankrupt need to be liquidated for the bankruptcy proceedings. *See* Judgment of Oct. 17, 1988, Segundo Tribunal Colegiado en Materia Civil del Primer Circuito, Amparo directo 1197/88, Segundo Tribunal Colegiado en Materia Civil del Primer Circuito, Informe 1988, p. 257, 17 de Octubre de 1988, Unanimidad de votos (reasoning by analogy that debts denominated in foreign currency are fixed in Mexican pesos at the rate of exchange applicable on the date of the declaration of bankruptcy).

199. L.Q.S.P. art. 139.

declare whether he will rescind or perform the contract.<sup>200</sup> The demanding party may even suspend performance of its obligations, without incurring liability, until the trustee either meets the bankrupt's obligations or guarantees its due performance.<sup>201</sup>

As a rule, contracts of deposit, contracts to open credit, and contracts of commission or agency must be rescinded by the bankruptcy unless the judge specifically authorizes the trustee, after a hearing with the intervenors, to assume the obligation.<sup>202</sup> The declaration of bankruptcy also suspends the operation of running accounts.<sup>203</sup>

In contrast, the declaration of bankruptcy will not rescind leases for real property in which the lessor is the bankrupt, absent mutual agreement.<sup>204</sup> Where the lessee is the bankrupt, however, the trustee is authorized to rescind the leases upon an indemnity payment, agreement of the parties, or judicial determination.<sup>205</sup>

### 1. Impact on Repurchase Contracts

The bankruptcy declaration also affects repurchase contracts. If the repurchasee<sup>206</sup> under a securities repurchase contract goes bankrupt, then on the maturity of the contract the trustee may deliver the securities and demand payment of the contract consideration.<sup>207</sup> The trustee's failure to do so enables the repurchaser<sup>208</sup> to assert a claim against the estate for the prior payment of the security documents, based on the agreed repurchase price.<sup>209</sup>

If the repurchaser is the bankrupt, then the trustee can pay simply the consideration and receive the documents.<sup>210</sup> If it does not do so, the repurchasee can deliver the documents and

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200. *Id.*

201. *Id.*

202. *Id.* art. 141.

203. *Id.* art. 142.

204. *Id.* art. 153.

205. *Id.*

206. The Spanish term for repurchasee is *reportador*.

207. L.Q.S.P. art. 150.

208. The Spanish word for repurchaser is *reportado*

209. L.Q.S.P. art. 150.

210. *Id.*

assert a claim, as any other creditor in the bankruptcy proceedings, equal to the amount of the consideration due.<sup>211</sup>

## 2. Effect on Work Contracts and Contracts for Personal Services

Personal service and work contracts are affected by the bankruptcy declaration to a lesser extent than other contracts. For example, contracts for personal services and for performance of particular work that benefit the bankrupt will not be rescinded because of the bankruptcy declaration.<sup>212</sup> In addition, the trustee may honor contracts requiring continued operation of the company, or contracts for the administration or liquidation of the bankrupt.<sup>213</sup>

### *H. Administrative Powers*

#### 1. Procedure to Use, Sell, and Liquidate Estate Property

The procedure for liquidating the bankruptcy estate's assets is designed to promote efficiency and speed. Once bankruptcy is declared, the judge or appropriate secretary carries out seizure of the assets, bank accounts, furniture, offices, books of account and other documents of the bankrupt company, and guards and seals the warehouses and premises,<sup>214</sup> with the exception of certain objects specified in article 185.<sup>215</sup> Subsequently, the trustee takes possession of the debtor's assets and prepares an inventory of them.<sup>216</sup> The trustee must act quickly and complete this inventory within ten days.<sup>217</sup> In addition, the trustee may only petition the court for a maximum extension of twenty days.<sup>218</sup> Last, once the declaration of bankruptcy is definitive and the creditors' claims are recognized, the trustee must move

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211. *Id.*; see also Credit Instr. & Operations Law arts. 259-66 (providing the general rules governing repurchase contracts).

212. L.Q.S.P. art. 154.

213. *Id.*

214. See *id.* art. 175.

215. *Id.* art. 185.

216. *Id.* art. 193. The trustee must commence the inventory of the bankrupt estate's assets within three days of the trustee's judicial appointment. *Id.* art. 187.

217. *Id.* art. 192.

218. *Id.* The trustee's failure to complete the inventory list within the allotted time may be grounds for the trustee's removal. *Id.*

without delay to sell off the bankrupt estate's assets.<sup>219</sup>

## 2. Business Operation During Liquidation

The trustee assumes enormous responsibility for business operations during liquidations. For example, the trustee must make all normal expenditures, collect all due credits from the seizure or those realized from business operations, and register all outstanding mortgages.<sup>220</sup> In addition, the trustee must broadly perform all acts necessary to protect and prevent harm to the rights and assets of the bankrupt estate.<sup>221</sup>

Upon the trustee's recommendation, the judge rules that the bankrupt company may or may not continue to operate.<sup>222</sup> Nevertheless, a bankrupt company's continued operations become mandatory under certain circumstances. The bankrupt company must continue operations, for example, where interruption to the bankrupt company's business would cause the creditors grave harm, or when the judge, together with the trustee and an expert, determines that the business is viable and its preservation is socially useful.<sup>223</sup> If the bankrupt company's operations continues, then it must also perform its contractual obligations.<sup>224</sup>

### I. Creditors and Claims

#### 1. Notice of Proceedings to Creditors

Creditors are well-informed during the bankruptcy process. Creditors are entitled to notice of the commencement of bankruptcy proceedings. Article 16 of the L.Q.S.P., for example, specifically mandates that creditors with known addresses be notified personally, by ordinary mail, or by telegram within fifteen days of the bankruptcy declaration's judgment. In addition, the trustee must publish, on three separate occasions, an extract from the bankruptcy declaration in the *Diario Oficial* and in two

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219. *Id.* art. 203.

220. *Id.* art. 198.

221. *Id.*

222. *Id.* art. 200.

223. *Id.* art. 201.

224. *Id.* art. 140.

major newspapers located where the bankruptcy is declared.<sup>225</sup> Further, the judge can order publication in locations where the bankrupt company has premises.<sup>226</sup> Creditors are deemed notified on the date of the last such publication.

As for the bankruptcy proceeding, creditors generally do not need notification of the trustee actions or those of the judge.<sup>227</sup> However, there are certain exceptions. The first exception requires notification of the convening of creditors' meeting.<sup>228</sup> The second exception affords discretionary notification where creditors appointed as intervenors were not present at the meeting appointing them.<sup>229</sup>

## 2. Submission of Claims to the Court

Creditors must file claims with the court to have their claims recognized.<sup>230</sup> A claim<sup>231</sup> includes any petition by an interested party to be recognized as a creditor of the bankrupt estate, of a particular class, and in relation to a particular amount.<sup>232</sup>

Claimants' petitions to the bankruptcy court must be in writing for their recognition.<sup>233</sup> They must also be accompanied by supporting documents with copies.<sup>234</sup> Last, the claim must comply with the requirements of article 255 of the C.P.-C.D.F.<sup>235</sup> Claims must specify the claimant's and the defendant's names and addresses, and include a succinct state-

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225. *Id.* art. 16.

226. *Id.*

227. *Id.* art. 27. The trustee is required, however, to report on the state of the bankruptcy every three months, including a detailed account of the trustee's actions. *Id.*

228. *Id.* art. 74.

229. *Id.* art. 63.

230. *See generally* L.Q.S.P. arts. 220-25.

231. The Spanish word for claim is *crédito*.

232. L.Q.S.P. arts. 220-25; *see also id.* art. 232; *see also generally id.* arts. 242-47.

233. *Id.* art. 221. Article 149 of the Fiscal Code, however, establishes that the Federal Treasury will not participate in bankruptcy or suspension of payments proceedings. Instead, the competent court must notify the Federal Treasury of the commencement of any such proceedings, and the Federal Treasury (through *Hacienda*) will administratively enforce its right to any pending tax claim. *See also generally* L.Q.S.P. art. 126-I.

234. L.Q.S.P. art. 221.

235. *Id.* art. 222.



ment of the factual and legal basis of the claim, its value, and its alleged rank and preference.<sup>236</sup>

Once the final publication of the bankruptcy judgment is published in the *Diario Oficial*, creditors have forty-five days to submit their credit claims for court review.<sup>237</sup> Creditors residing abroad, however, may receive an extension up to the date of the creditors' meeting, if the judge considers it advisable under the circumstances of the particular case.<sup>238</sup>

Creditors failing to submit their petitions within the specified deadline lose the priority they would have otherwise received.<sup>239</sup> Their claims are, therefore, reduced to those of common creditors.<sup>240</sup>

### 3. Claims Allowed or Disallowed

When the creditor presents its claim to the court, the judge passes the claim to the trustee to determine its amount and quality.<sup>241</sup> The trustee, in turn, passes the claim documentation on to the intervenor for a second determination of the claim.<sup>242</sup> If the trustee and the intervenor both decide that the documentation is insufficient to prove the claim's amount, priority, or preference, they must then issue an opinion in which they report these circumstances and request that the judge order presentation of the additional necessary evidence.<sup>243</sup>

Once all of the creditors' claims have been examined, the trustee must draw up a provisional list of creditors.<sup>244</sup> This list must be completed at least ten days before the creditors' meeting for the recognition of creditors' claims.<sup>245</sup>

Based on this list, the judge decides provisionally which creditors are entitled to vote at the creditors' meeting.<sup>246</sup> The claim holders and the bankrupt are then permitted to bring, in

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236. C.P.C.D.F. art. 255; L.Q.S.P. art. 222.

237. L.Q.S.P. art. 15-V.

238. *Id.* art. 223.

239. *Id.* art. 224.

240. *Id.*

241. *See id.* arts. 220, 226, 232-VI and VII.

242. *Id.* art. 227.

243. *Id.* art. 230.

244. *Id.* art. 233.

245. *Id.*

246. *Id.* art. 234.

writing before the judge, anything they consider relevant to defend their rights.<sup>247</sup> Finally, the judge sets a time and place for the creditors' meeting.<sup>248</sup>

The creditors' meeting is the forum for deciding the amount and priority of each claim, and the judge conclusively decides these claims within three days following the meeting.<sup>249</sup> The judge, however, may spend as many as twenty business days, counting from the date of that first meeting, listening to arguments related to disputed claims.<sup>250</sup>

The judge's broad reviewing power has some exceptions. Where a claim has been recognized by final judgment in a commercial proceeding, it is deemed accepted and recognized in bankruptcy proceedings.<sup>251</sup> Neither the creditors' meeting nor the judge in the bankruptcy proceeding will re-examine this final commercial judgment.<sup>252</sup>

The judge delivers a judgment, after conclusion of the creditors' meeting, dividing the claims into those recognized, those excluded, and those pending submission of additional proof.<sup>253</sup> The latter are finally allowed or disallowed in subsequent judgments within one month of the first judgment.<sup>254</sup> The bankrupt, the intervenor, and the creditors may appeal these judgments.<sup>255</sup>

#### 4. Priority of Claims

The L.Q.S.P.,<sup>256</sup> the Labor Law<sup>257</sup> and the Fiscal Code<sup>258</sup> generally establish six categories of priorities, so-called

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247. *Id.* art. 241.

248. *Id.* art. 26; *see id.* art. 242.

249. *See id.* art. 247.

250. *Id.* art. 246.

251. Amparo directo 2170/58, Guillermo Ruiz Vázquez y Coag., Sexta Epoca, Cuarta Parte, Vol. XXXII, 242. Mayoría de 3 votos, Apéndice al Semanario Judicial de la Federación, Segunda Parte, Salas y Tesis Comunes, Volumen V, México, 1989, 2477. It appears that to trigger this automatic acceptance and recognition certain requirements of proof and procedure must be established. *See id.*

252. *Id.*

253. L.Q.S.P. art. 247.

254. *Id.* art. 248.

255. *Id.* art. 249.

256. *See id.* arts. 261-64.

257. L.F.T. arts. 113-14.

258. C.F.F. art. 149.

"degrees,"<sup>259</sup> for creditors of the bankrupt. These are listed in descending order of preference.

First, *acreedores singularmente privilegiados*, or "exclusively privileged creditors," include business personnel, employees, or workers directly employed and paid by the bankrupt during the year immediately preceding the bankruptcy declaration.<sup>260</sup>

Second, *acreedores hipotecarios y prendarios*, or "secured creditors," include creditors under mortgage, pledge, and purchase finance agreements, who can recover their debt from the proceeds of the mortgaged or pledged property sale.<sup>261</sup> If there is more than one security interest in a property, creditors recover their debts according to the respective dates on which their security was filed.<sup>262</sup> The excess of proceeds which exceed the debt is applied to pay other creditors and, if the proceeds are insufficient, the mortgagee or pledgee is treated as a common creditor as far as the outstanding balance or deficiency.<sup>263</sup>

*Fisco federal* is the third category of creditor priority. The Federal Treasury under this category acts as a creditor for unpaid federal taxes.<sup>264</sup>

Fourth, *acreedores con privilegio especial*, or "creditors with special privilege," comprise all those creditors who, under the *Código de Comercio*, have some special privilege or right of retention. These kinds of creditors include commission agents,<sup>265</sup> merchandise vendors,<sup>266</sup> and carriers.<sup>267</sup>

*Acreedores comunes por operaciones mercantiles*,<sup>268</sup> or common creditors due to business transactions, enjoy fifth priority. The lowest, or sixth, priority creditor is the *acreedor común por derecho civil*,<sup>269</sup> the civil law common creditor.

259. The Spanish word for degrees is *grados*.

260. L.Q.S.P. arts. 261-I, 262-III.

261. See generally *id.* art. 263.

262. See *id.*

263. See generally *id.* arts. 263, 273; see also Cred. Instr. & Operations Law arts. 328 & 333; RODRÍGUEZ, *supra* note 142, at 282-83.

264. By virtue of article 269 of the Social Security Law (*Ley del Seguro Social*), pending social security credits shall have the same preference as federal taxes.

265. C.ÓD. COM. art. 306.

266. *Id.* art. 386.

267. C.C.D.F. art. 2662.

268. L.Q.S.P. art. 261-IV.

269. *Id.* art. 261-V. The law is silent as to the priority of credits secured by simple guarantees (*fianzas*). Consider, for example, the legal guarantee created by

As a general principle, creditor category (*graduación*) and creditor priority within that category (*prelación*), as provided by the law, determine payment order. Generally, creditors of the first through fourth priority categories<sup>270</sup> are repaid their credits in full. Assets to pay them are usually sufficient. However, where assets are insufficient, first priority category creditors are paid in full before category two creditors are paid, and so forth. Fifth and sixth priority creditors are always repaid a pro-rata reduced amount.

Creditors of the bankrupt estate, the trustee, and legal and other professionals involved in the estate's administration and conservation during the bankruptcy proceedings are paid before any of the bankrupt's creditors.<sup>271</sup> Notably, they are always paid in full.<sup>272</sup>

Trustees' fees may be as high as eight percent of every asset of the estate that is sold.<sup>273</sup> In contrast to the trustees' fees, the judge has discretion to determine the intervenor's fees.<sup>274</sup> The judge's decision turns on the complexity of the bankruptcy,

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the Financial Groups Law (FGL). A significant restriction is that no business of a controlled company may be transacted out of the holding company's offices. And, pursuant to article 28, the holding company of a financial group or "Fig" must enter into an agreement with each of its controlled companies pursuant to which, briefly stated, (i) the holding company will be severally and unlimitedly liable for the undertakings of its controlled companies in their ordinary course of business; (ii) the holding company will be responsible for each and every loss suffered by a controlled company; but (iii) none of the controlled companies shall answer for any loss suffered by a sister-controlled company or the holding company. FGL arts. 8 & 28. Presumably, creditors of financial groups subsidiaries can negotiate the terms of the guarantee of the holding company. The guarantee is considered an "accessory" agreement under Mexican law, not a unilateral act, and as such may be affected to the extent the "main" or guaranteed obligation is affected. To prevent having to wait for the finalization of bankruptcy proceedings and running the risk of a reduction of the value of the security which, unless otherwise agreed between the creditor and the guarantor, will be reduced in the same proportion the guaranteed obligation is in the bankruptcy proceedings. C.C.D.F. art. 2847 (certain agreements must be reached and waivers obtained). This complex subject exceeds the general scope of this work, but it is conceivable that grounds for direct legal action against the guarantor, concomitant to and independent from the bankruptcy proceedings, can be validly created.

270. Categories (1) to (4) comprise creditors holding debts which are: (1) exclusively privileged; (2) secured; (3) of the Federal Treasury; and (4) specially privileged.

271. L.Q.S.P. arts. 269, 270.

272. *Id.*

273. *Id.* art. 57.

274. *Id.* art. 70.

the number of creditors, and market practices.

### 5. Debt Set-off

In general, the bankrupt's credits cannot be used to set-off its debts. There are, however, exceptions. Where the estate's debts relate to the bankrupt's claims<sup>275</sup> set-off is possible. Set-off is also possible where it occurs because of a contractual set-off of a running account.<sup>276</sup> Finally, the shareholders of a corporation, and the partners of a limited liability company or of a joint venture are entitled to set-off their credits, but only for any remaining balance on previous contributions, as partners and stockholders, for which they are being credited.<sup>277</sup>

### 6. Discharging Claims and Debtors

The bankruptcy proceedings conclude when at least one of four conditions is satisfied. First, paying recognized creditors, either in full<sup>278</sup> or on a discounted basis,<sup>279</sup> concludes bankruptcy. Second, determining that there are insufficient funds in the bankrupt estate to pay creditors, even on a pro-rata basis,<sup>280</sup> necessarily concludes bankruptcy. Third, the proceedings end when only one of the creditors makes claims against the bankrupt estate.<sup>281</sup> Last, unanimous resolution of the creditors,<sup>282</sup> or agreement between the bankrupt and its creditors,<sup>283</sup> will terminate bankruptcy proceedings.

### 7. Distributions: Manner and Timing

Once a judgment is rendered after the creditors' meeting, the distribution process begins. After hearing the intervenor's

275. *Id.* art. 128-IV (a).

276. *Id.* art. 128-IV (b).

277. *Id.* art. 128-IV (c).

278. The Spanish phrase for payment in full is *pago íntegro*.

279. See L.Q.S.P. art. 274. The Spanish phrase for a payment on a discounted basis is *pago concursal*.

280. See generally L.Q.S.P. arts. 287, 288.

281. See *id.* art. 289.

282. *Id.* art. 292; see *id.* art. 287, 292. Pursuant to article 284 of the L.Q.S.P., those creditors who were not paid in full will maintain their individual rights against the bankrupt.

283. See L.Q.S.P. art. 296.

submission, the judge either approves or rejects the proposed distribution.<sup>284</sup> This process continues until the realizable assets near exhaustion, at which point the judge convenes a general meeting of recognized creditors.<sup>285</sup> At the end of each four-month period, starting from the last creditor recognition judgment, the trustee must present to the judge a statement of the current or cash assets and a statement of the creditors to be paid.<sup>286</sup>

For the final general meeting of recognized creditors, the trustee prepares final statements of account.<sup>287</sup> These final statements are useful because they help in distributing the remaining assets and winding up the bankruptcy estate. Nevertheless, distributing assets and winding up the estate can be a long process. The judge is obliged to give conditional or disputed creditors an additional four months to meet the requirements of their recognition,<sup>288</sup> and the bankruptcy will not be concluded while their claims for recognition remain under appeal and unresolved.<sup>289</sup> Finally, if additional assets are discovered

after winding up, the judge must also take measures appropriate for their sale and distribution.<sup>290</sup>

Except where specifically provided in international conventions and agreements, foreign bankruptcy declarations will only be recognized and given effect in Mexico when they are proved to comply with the formalities and preconditions for the bankruptcy declaration set forth in the L.Q.S.P.<sup>291</sup> That bankruptcy declaration then becomes governed by the L.Q.S.P., for purposes of giving effect to the declaration.<sup>292</sup>

### *J. Special Insolvencies*

The provisions of the L.Q.S.P. generally apply equally to special bankruptcies, except as provided in Title VII of the

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284. *Id.* art. 277.

285. *Id.* arts. 277, 278.

286. *Id.* art. 276.

287. *Id.* art. 278.

288. *Id.* art. 279.

289. *Id.* art. 280.

290. *Id.* art. 285.

291. *Id.* art. 14.

292. *Id.*

L.Q.S.P.<sup>293</sup> Title VII of the L.Q.S.P. contains special rules to regulate special bankruptcies. These special rules apply to bankruptcies of banks and auxiliary credit organizations,<sup>294</sup> insurance companies, bonding companies, governmental companies, and financial groups.<sup>295</sup> Those special rules relate to these various institutions in different ways.

### 1. Banks and Auxiliary Credit Organizations

Banks and auxiliary credit organizations, for example, may be declared bankrupt upon petition of the National Banking Commission (CNB).<sup>296</sup> This bankruptcy declaration will affect all of the respective bank's various departments.<sup>297</sup>

The L.Q.S.P. grants the CNB broad powers. The judge must appoint a trustee from the list of credit institutions compiled by the CNB.<sup>298</sup> The CNB has the right to propose the trustee's removal, provided that removal is for cause.<sup>299</sup> In addition, agreement proposals at the creditors' meeting must be submitted directly to the CNB for assessment.<sup>300</sup> Last, the judge is required to consider these proposals, and the CNB's assessment of them, when making a decree.<sup>301</sup>

The *Ley de Instituciones de Crédito*<sup>302</sup> also grants the CNB broad powers. Insofar as banks are concerned, article 138 of the

293. See RODRÍGUEZ, *supra* note 142, at 404-05.

294. The Spanish phrase for auxiliary credit organization(s) is *organizacion(es) auxiliar(es) de crédito*.

295. Banks are referred to as "credit institutions." There are only two categories of credit institutions: multiple banking institutions (*instituciones de banca múltiple*) and development banking institutions (*instituciones de banca de desarrollo*).

Pursuant to art. 3 of the *Ley General de Organizaciones y Actividades Auxiliares del Crédito* [General Law on Auxiliary Credit Organizations and Activities], auxiliary credit organizations are defined as warehousing companies, financial leasing companies, savings and loans associations, credit unions, and factoring companies. According to article 4, professional currency trading is considered to be an auxiliary credit activity.

296. L.Q.S.P. art. 430. CNB is the abbreviation for the *Comisión Nacional Bancaria*.

297. *Id.*

298. *Id.* art. 432. The list is published in the *Diario Oficial* at the end of each January. *Id.*

299. *Id.* art. 434; see also *id.* arts. 28 & 52 (limiting the right to remove to those cases where the trustee was not appointed according to article 28).

300. *Id.* art. 436.

301. *Id.*

302. Credit Institutions Law art. 138

Credit Institutions Law empowers the CNB to appoint an intervenor-manager<sup>303</sup> whenever it concludes that the irregularities found after an inspection "influence the stability or solvency" of a bank.<sup>304</sup> In these cases, articles 139-143 of the Credit Institutions Law also permit the intervenor-manager to automatically assume all authority from the respective bank's board of directors, and to use all means to manage the bank.

Beyond the CNB's influence, the bankruptcies of banks and auxiliary credit organizations also differ from other bankruptcies in their priority of claims. Article 437, for example, addresses the bankruptcy of a bank or an auxiliary credit organization and establishes the priority of claims as follows:<sup>305</sup>

I. Assets excluded from the estate.<sup>306</sup>

II. Creditors of the estate as a result of:<sup>307</sup>

(i) articles 113 and 114 of the Labor Law, employees or workers directly employed by the bankrupt in the year prior to the bankruptcy declaration; (ii) tax claims of the estate; (iii) creditors of the estate (as opposed to creditors of the bankrupt); and (iv) general expenses of the liquidation including trustees' fees;<sup>308</sup>

III. Creditors of credits of the bankrupt secured by real property or by pledge,<sup>309</sup>

IV. Privileged creditors such as: (i) creditors of savings deposits; (ii) creditors of demand and term deposits and bank checks; (iii) creditors of general payments;<sup>310</sup> and

V. Common creditors.

## 2. Insurance Companies

For the bankruptcy of insurance companies, the Secretary of

303. The Spanish word for intervenor-manager is *interventor-gerente*.

304. Credit Institutions Law art. 138 (stating- "[S]i esas irregularidades afectan la estabilidad o solvencia de aquellas . . . ." [If these irregularities affect the stability or solvency of [the banks]) (translated by author).

305. In Spanish, priority of claims is described as *graduación*.

306. L.Q.S.P. art. 437.

307. *Id.*

308. *Id.*

309. *Id.*

310. *Id.*



Finance and Public Credit (*Hacienda*)<sup>311</sup> has the same powers as the CNB *vis-à-vis* credit institutions.<sup>312</sup> The Secretary has broad powers to interpret, apply, and resolve all administrative aspects of the Insurance Institutions Law,<sup>313</sup> including bankruptcy actions.<sup>314</sup> Because the insured will be deemed a creditor with special privilege,<sup>315</sup> the judge must give preference to insurance companies to act as trustees.<sup>316</sup> In those cases in which *Hacienda* could petition for a bankruptcy declaration, *Hacienda* may opt, within one working day following notification, to either proceed to an "administrative liquidation" or petition for a declaration of bankruptcy.<sup>317</sup>

### 3. Public Corporations

Bankruptcy or suspension of payments of a public corporation involve special considerations. The public services that those corporations deliver must continue un-interrupted by the bankruptcy process.<sup>318</sup> In addition, the bankruptcy of a public

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311. In Spanish, *Secretaría de Hacienda y Crédito Público*.

312. L.Q.S.P. art. 443.

313. *Ley General de Instituciones y Sociedades Mutualistas de Seguros*.

314. See L.Q.S.P. arts. 430 & 443.

315. L.Q.S.P. art. 446.

316. *Id.* art. 447.

317. *Id.* art. 448.

318. L.Q.S.P. art. 450. The term "public corporation" is not commonly used in Mexico to refer to companies whose stock is publicly traded. Rather, a public corporation is one that offers services of such a nature that Mexico has an interest in its continuing operation for the benefit of the public at large. Examples of a public corporation are, pursuant to article 3 of the Organic Law of the Public Federal Administration (*Ley Orgánica de la Administración Pública Federal*), decentralized entities, parastate companies, and trust arrangements whose purpose is the fulfilment of a public goal. Each public corporation may be subject to special regulations, including bankruptcy regulations, to reflect the particular circumstances surrounding its operation.

On the other hand, "public corporations," as the term is defined in the U.S. legal system, are regulated by the Securities Market Law. Pursuant to article 41-II of the Securities Market Law, the National Securities Commission (*Comisión Nacional de Valores*) (CNV) shall have powers to inspect the operations transacted by securities issuers. Furthermore, article 41-VI also empowers the CNV to suspend trading of the shares of an issuer in a situation of insolvency, whether a bankruptcy or suspension of payments has been declared or not. Neither the L.Q.S.P. nor the Securities Market Law empowers the CNV to participate officially in insolvency proceedings relating to securities issuers. The CNV, however, does have the power to administratively intervene against financial intermediaries, such as brokerage houses, whose operations have endangered their solvency, stability, or liquidity. See Secur-

corporation always requires the public corporation to designate two of the members of the intervenors.<sup>319</sup> Where an administrative receivership is instituted, an administrative board of receivers will be appointed to replace the intervenor.<sup>320</sup> This board has strong-arm powers to impose, with the competent court's prior approval, payment agreements with the creditors of the bankrupt public corporation.<sup>321</sup>

*K. Personal Liability: Company Directors, Managers, Trustees, and Auxiliaries*

Company directors, managers, trustees, and auxiliaries may be held personally liable for certain types of bankruptcies.<sup>322</sup> The L.Q.S.P. classifies these bankruptcies as fortuitous, culpable, or fraudulent.<sup>323</sup>

A fortuitous bankruptcy is one in which the company, though managed properly, is unable to meet its payment obligations because of circumstances beyond the control of management.<sup>324</sup>

Culpable bankruptcies, in contrast, are those resulting from acts inconsistent with good management.<sup>325</sup> Acts inconsistent with good management include excessive and disproportionate personal expenses, expenses unrelated to the capital or operation of the corporation, or losses due to speculative investments, purchases, sales, or other operations to delay bankruptcy.<sup>326</sup> Where company accounts do not conform to respective legal requirements, the company does not declare bankruptcy within three days from cessation of payments, or the company fails to present the documents as and when required by the L.Q.S.P., a

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ities Market Law art. 41-VII and VIII.

319. See L.Q.S.P. art. 451. In Spanish, administrative receivership is called *incapacitación*. Article 451 in essence acknowledges the right of the corporation to name some of the members of the intervening body. *Id.* art. 451.

320. L.Q.S.P. art. 452.

321. *Id.* arts. 453, 454. The power to establish a payment agreement represents a deviation from the normal suspension of payments procedures.

322. See L.Q.S.P. arts. 95, 99, 101, 103.

323. *Id.* art. 91.

324. *Id.* art. 92.

325. *Id.* art. 93.

326. *Id.*

bankruptcy is *prima facie* culpable.<sup>327</sup>

A bankruptcy is *prima facie* fraudulent when the corporation deceitfully reduces its assets or increases its liabilities causing or aggravating the cessation of payments.<sup>328</sup> A bankruptcy is also classified as fraudulent when the books of account are altered, falsified, or destroyed.<sup>329</sup> A bankruptcy is also *prima facie* fraudulent if the entity favors for no legal reason a particular creditor, subsequent to the retroaction date, either by payment, guarantee, or preference.<sup>330</sup> Last, a bankruptcy is presumed to be fraudulent when the accounting books do not conclusively establish the entity's true financial position.<sup>331</sup>

The penalties for culpable and fraudulent bankruptcies are stiff. The penalty for causing a culpable bankruptcy, for example, is one to four years imprisonment.<sup>332</sup> A fraudulent bankruptcy can lead to five to ten years imprisonment and a fine of up to ten percent of the liabilities.<sup>333</sup> In addition, anyone assisting, co-operating in, or directly inducing the performance of acts causing a culpable or fraudulent bankruptcy will be punished with these same penalties.<sup>334</sup> Last, declaration of a corporation as culpable or fraudulent also means that the corporation's directors, managers or trustees, whose acts caused this kind of bankruptcy, will be held liable.<sup>335</sup>

#### IV. SUSPENSION OF PAYMENTS

The suspension of payments concept is derived from Spanish law and is found in various forms in Argentine, Italian, Brazilian, and French law.<sup>336</sup> Suspension of payments is designed to achieve the rehabilitation of the debtor. It provides a debt payment moratorium for commercial entities encountering diffi-

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327. *Id.* art. 94.

328. *Id.* art. 96.

329. *Id.*

330. *Id.*

331. *Id.* art. 98.

332. *Id.* art. 95.

333. *Id.* art. 99.

334. *Id.* art. 103; see also *id.* arts. 95, 99. The broad wording of this section suggests that it applies to both legal and natural persons. See *id.*

335. L.Q.S.P. art. 101.

336. RAÚL CERVANTES AHUMADA, DERECHO DE QUIEBRAS 26, 148 (1981).

culties paying their debts. In addition, the debtor is permitted to retain control over and, therefore, manage the entity's assets during this moratorium.<sup>337</sup> The debtor's control, however, is limited by the conditions of the suspension of payments' preventive agreement and the supervision of the court and trustee.

The norms and procedures applicable to bankruptcy proceedings also apply to suspension of payments to the extent they are consistent with the essence and character of suspension of payments proceedings.<sup>338</sup> The following section discusses only those elements of suspension of payments that are distinct from bankruptcy.

### A. *Commencing Suspension of Payments*

To commence a suspension of payments, the debtor must petition the bankruptcy court, and present all documentation normally required in a bankruptcy action to support the petition.<sup>339</sup> This documentation includes a proposed preventive agreement,<sup>340</sup> to be negotiated with the creditors,<sup>341</sup> a declaration by the Chamber of Commerce of the industry acknowledging the debtor's Chamber membership, and a declaration proposing a trustee or requesting *Hacienda* to appoint a bank as trustee.<sup>342</sup>

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337. Thus, the debtor maintains the control of his assets and is allowed to continue transacting "ordinary business" (*operaciones ordinarias*). See L.Q.S.P. art. 410; see also RODRÍGUEZ, *supra* note 142, at 370-75. Unusual acts, as compared to "ordinary business," requires court authorization.

338. L.Q.S.P. art. 429; see Competencia Civil 34/84, Tercera Sala de la Suprema Corte de Justicia de la Nación, Jueces Tercero de lo Civil del Distrito Federal y Segundo de Primera Instancia en Materia Civil de Zamora, Michoacan, 7 de Enero de 1987, Unanimidad de 5 votos; see also Judgment 299/91 of Aug. 8, 1991, Tribunal Colegiado en Materia Civil del Sexto Circuito, S.J.F., Octava Epoca, Tomo VIII, 282, Octubre de 1991.

339. L.Q.S.P. art. 395. As opposed to bankruptcy, only the debtor may petition the court for suspension of payments. Compare L.Q.S.P. art. 395 (stating that merchants may request suspension of payments) with L.Q.S.P. art. 5 (stating that a declaration of bankruptcy may be obtained if the merchant, creditors, or the District Attorney petition the court).

340. A proposed preventive agreement is a proposal by the debtor for a reduction of his payments, a restructure of payment, or both. See L.Q.S.P. art. 403.

341. See L.Q.S.P. art. 398.

342. See generally *id.* arts. 6, 7, 8; see also generally Credit Institutions Law arts. 47, 138. Pursuant to Credit Institutions Law art. 46-XXI, banks are authorized to act as bankruptcy trustees. Also, in comparison to the bankruptcy petition, the suspension of payments petition *must* be accompanied by a proposed preventive agreement.

A debtor's right to suspension of payments is not absolute. The debtor can be barred from requesting a suspension of payments if (i) it or its directors have been convicted of property or deceit-related crimes;<sup>343</sup> (ii) it has defaulted on a prior suspension of payments agreement;<sup>344</sup> (iii) it was previously declared bankrupt and not yet rehabilitated, unless the bankruptcy was concluded for lack of creditors or with the unanimous consent of the creditors;<sup>345</sup> (iv) it failed to produce all documents required by law;<sup>346</sup> (v) it presented its petition more than three days after the cessation of payments;<sup>347</sup> or (vi) it is an irregular mercantile corporation.<sup>348</sup>

### B. Parties to Suspension of Payments

#### 1. Fiduciaries

Debtors, trustees, and intervenors are parties to the suspension of payments because of their fiduciary responsibilities.

The debtor<sup>349</sup> is, in a sense, a fiduciary in that it is required to continue the ordinary administration of the company under the surveillance of the trustee.<sup>350</sup> In addition, the debtor must not act in ways that increase the company's liabilities or diminish the company's assets beyond its "ordinary management."<sup>351</sup> Moreover, the debtor's breach of its management obligations may lead to the judge's declaration of bankruptcy.<sup>352</sup>

The suspension of payments trustee generally has the same fiduciary obligations as trustees in bankruptcy proceedings. For example, the suspension of payments trustee must (i) prepare an inventory and correct the statement of assets and liabilities

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343. L.Q.S.P. art. 396. Similarly, *Código de Comercio* article 12 prohibits individuals who have been convicted of property or deceit-related crimes to engage in commerce.

344. L.Q.S.P. art. 396.

345. *Id.*

346. *Id.*

347. *Id.*

348. *Id.* (for example, a *de facto* corporation).

349. In Spanish, the debtor is called *deudor*. In practice, however, a debtor is also called *suspensio*, in the context of suspension of payments proceedings.

350. *Id.* art. 410.

351. *See id.* art. 411.

352. *Id.*

within fifteen days after appointment;<sup>353</sup> (ii) take charge of the funds, and supervise the accounts and the operations of the debtor, opposing any act prejudicial to the creditors;<sup>354</sup> (iii) report any irregularities of the debtor's account to the judge;<sup>355</sup> and (iv) furnish a report to the creditors, at least three days before the creditors' meeting, on the state of the business and the conduct of the debtor.<sup>356</sup>

Last, the intervenor is a party to the suspension of payments, representing creditor interest. The appointment of an intervenor is within the creditors' discretion. And, unlike a bankruptcy, the judge has no explicit power to appoint an intervenor.<sup>357</sup>

## 2. Committees of Creditors or Holders of Equity Interests

Like bankruptcy proceedings, the creditors of a company petitioning for suspension of payments must also meet to recognize claims and then to discuss, approve, or reject the proposed suspension of payments agreement.<sup>358</sup> The rules governing the recognition of claims are equivalent to those in bankruptcy.<sup>359</sup>

The creditors' voting rights governing the approval of preventive agreements are the same as those provided in bankruptcy.<sup>360</sup> The creditors must consent to the preventive agreement within three days from the date of admission of the lawsuit.<sup>361</sup> In practice, however, the courts often allow debtors more time to seek creditor approval because of the brevity of this period. In practice, to avoid an undesired bankruptcy declaration, preventive agreements are sometimes negotiated with the creditors before a suspension of payments is sought. If a proposed preventive agreement is rejected or the requisite majority of votes is not attained, the judge must declare bankruptcy.<sup>362</sup>

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353. *Id.* art. 416.

354. *Id.*

355. *Id.*

356. *Id.*

357. *Compare* L.Q.S.P. art. 417 *with* L.Q.S.P. art. 59.

358. *See id.* art. 407.

359. *Id.*

360. *See id.* art. 418.

361. *See id.* art. 402.

362. *Id.* art. 419.

### C. *Effect of Declaring Suspension of Payments*

For the duration of the proceedings, except in relation to salary debts or debts secured by real property,<sup>363</sup> no prior creditor is allowed to claim—and the debtor is not allowed to make—any debt payment.<sup>364</sup> All debt payment transactions are suspended. Further, all suits against the debtor demanding the performance of payment obligations are suspended.<sup>365</sup> In certain cases, however, actions related to the payment suspension can be undertaken.<sup>366</sup> These exceptions are limited to claims for payments of employment debts or debts guaranteed by real property.<sup>367</sup> Where final judgment has been rendered on the claim, it is joined to the suspension of payments proceedings.<sup>368</sup>

Solely for purposes of the preventive agreement, the debts of the debtor are treated as due.<sup>369</sup> Debts cease accruing interest from the date the suspension of payments is declared.<sup>370</sup> In contrast to article 15-III of the L.Q.S.P. where the trustee occupies the bankrupt assets as a consequence of a declaration of bankruptcy, a debtor under a suspension of payments declaration continues to possess and administer its assets.<sup>371</sup> Thus,

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363. *See id.* art. 409.

364. *Id.* 408.

365. *Id.*

366. *See* Judgment 392/91 of Sept. 18, 1991, Segundo Tribunal Colegiado en Materia Civil del Sexto Circuito, S.J.F., Octava Epoca, Tomo IX, 129-30, Marzo de 1992 (deciding that art. 126, which orders the joining of all pending legal proceedings against the bankrupt to the bankruptcy proceedings, is not applicable in suspension of payments proceedings).

367. *See* L.Q.S.P. art. 409; *see also* the Judgment 167/91 of Nov. 19, 1991, Primer Tribunal Colegiado en Materia Civil del Quinto Circuito, S.J.F., Octava Epoca, Tomo IX, 207-08, Marzo de 1992 (deciding that proceedings to enforce a mortgage credit, documented also in promissory notes, through expedited mercantile proceedings (*juicio ejecutivo mercantil*), would qualify as an exception to the principle and as such should not be suspended).

368. *See* the Judgment 867/91 of Aug. 8, 1991, Tercer Tribunal Colegiado en Materia Civil del Primer Circuito, S.J.F., Octava Epoca, Tomo VIII, 282-83, Octubre de 1991.

369. *Id.*; L.Q.S.P. art. 412.

370. *See* Judgment 853/90 of Dec. 6, 1990, Tercer Tribunal Colegiado en Materia Civil del Tercer Circuito, S.J.F., Octava Epoca, Tomo VII, 269-70, Abril de 1991 (determining that, as stipulated in article 128-II in relation to bankruptcies, interest ceases to accrue on the claims in suspension of payments proceedings).

371. *See* L.Q.S.P. art. 410.

the courts have treated the declaration to benefit the debtor.<sup>372</sup>

The suspension of payments declaration must contain the appointment of a suspension of payments trustee;<sup>373</sup> an authorization for the trustee to perform all relevant operations;<sup>374</sup> a notice to all creditors of commencement of the proceedings;<sup>375</sup> a call to convene a creditors' meeting;<sup>376</sup> and orders to register the judgment at the RPPC and to issue copies of the judgment to all parties privy to the proceedings.<sup>377</sup>

#### *D. Suspension of Payments Estate*

The same principles and procedures used to value the bankrupt estate are used to value the suspension of payments estate.<sup>378</sup> Similarly, the principles and procedures for separating creditor property from the bankrupt estate<sup>379</sup> apply to the separation of creditor property from a suspension of payments estate.<sup>380</sup>

#### *E. Administrative Powers*

Business operations continue during a suspension of payments. The debtor may continue to operate the business as usual. However, the debtor must comply with the terms of the suspension of payments agreement and acknowledge the supervision of the trustee and the court.<sup>381</sup>

The debtor must follow specific procedures for using or selling estate property. Unless a sale or use of estate property falls within the debtor's ordinary course of business, estate property

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372. See Judgment 471/88 of Feb. 27, 1988, Primer Tribunal Colegiado en Materia Civil del Primer Circuito, S.J.F., Octava Epoca, Tomo VIII, 312, Diciembre de 1991.

373. See L.Q.S.P. art. 405.

374. *Id.*

375. *Id.*

376. *Id.*

377. *Id.*

378. See *id.* art. 429.

379. See L.Q.S.P. art. 159-IV.

380. See Judgment 3210/90 of Nov. 28, 1990, Quinto Tribunal Colegiado en Materia Civil del Primer Circuito, S.J.F., Octava Epoca, Tomo VII, 485, enero de 1991.

381. L.Q.S.P. art. 410.



may only be used or sold by the debtor if the judge approves such sale or use on the grounds of necessity or urgency.<sup>382</sup> Absent this judicial approval, estate property sales or uses, *vis-à-vis* the existing creditors, will be annulled and the judge may declare the debtor's bankruptcy.<sup>383</sup>

The debtor's power to continue to carry out ordinary business arguably includes the power to borrow. While the L.Q.S.P. does not define "ordinary business," at least one renowned author has defined it as "that effected normally, in accordance with the nature and quality of the debtor's trade."<sup>384</sup> Thus, borrowing, in most cases, will require the trustee's non-objection, under articles 416-II, and the judge's approval under article 411.

#### F. Creditors and Claims

The rules governing submission, allowance, and priority of creditor claims are identical to those in bankruptcy cases.<sup>385</sup> Also identical are those rules regarding creditor notification of proceedings and approval of the proposed agreement,<sup>386</sup> appeals and submission of disputes to the court,<sup>387</sup> and the effects of the suspension of payments agreement approval.<sup>388</sup>

#### G. Officers, Directors, and Affiliates

The same penal sanctions that apply to bankruptcy cases apply to suspension of payments cases.<sup>389</sup> Officers, directors, and affiliates may bear personal liability. However, a criminal court's determination of fraud has no effect on a subsequently converted bankruptcy case.<sup>390</sup> In fact, should such a conversion occur, the bankruptcy court has authority to characterize the

382. *Id.* art. 411.

383. *Id.*

384. RODRÍGUEZ, *supra* note 142, at 393.

385. L.Q.S.P. arts. 407, 418.

386. *See id.* arts. 406, 421.

387. *Id.* art. 422.

388. *See id.* art. 423. Except in the case of suspension of payments, pending court actions are suspended rather than joined to the proceedings. *See* L.Q.S.P. art. 429; Judgment 392/91 of Sept. 18, 1991, Segundo Tribunal Colegiado en Materia Civil del Sexto Circuito, S.J.F. Octava Epoca, Tomo IX, 129-130, Marzo de 1992.

389. *See* L.Q.S.P. art. 427.

390. *Id.*

nature of the bankruptcy, as culpable, fortuitous, or fraudulent.<sup>391</sup>

#### *H. Suspension of Payments Preventive Agreement and Process*

Preventive agreement proposals are integral to the suspension of payments. Debtors must propose preventive agreements at the time they petition the courts for a suspension of payments declaration.<sup>392</sup> Arguably, the suspension of payments trustee, the creditors, and the intervenor may also propose an agreement.<sup>393</sup> Where the debtor is a corporation,<sup>394</sup> the corporation's Board of Directors or equivalent body must present the proposed agreement.<sup>395</sup> If the debtor's original proposal does not contain the elements required by law, then the judge may allow the debtor an additional three days to cure the defect.<sup>396</sup> After that time, the judge has the discretion to declare the estate bankrupt.<sup>397</sup>

Partners of the debtor and creditors must first give their preliminary acceptance<sup>398</sup> to the agreement.<sup>399</sup> Subsequently, the court must approve the agreement.<sup>400</sup> While there is no express deadline for the court's approval of this agreement, in practice, court review takes between twelve and thirty-six months, depending on the complexity of the debtor's business.

The preventive agreement's contents must comport with specific requirements. A proposed preventive agreement must contain at least all the elements that are required for a creditors' agreement for the winding up of a bankruptcy.<sup>401</sup> If the partners' consent cannot be obtained in cases of urgency, it

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391. See generally *id.* arts. 91-114.

392. *Id.* art. 398.

393. See *id.* arts. 302 and 316 (applicable to suspension of payments by virtue of article 429).

394. In Spanish, a corporation is referred to as *sociedad anónima* or *sociedad de responsabilidad limitada*.

395. L.Q.S.P. art. 300.

396. *Id.* art. 401.

397. *Id.*

398. The Spanish phrase for preliminary acceptance is *dar su consentimiento*.

399. See L.Q.S.P. art. 402.

400. See *id.* art. 420.

401. *Id.* art. 400.

can be obtained afterward.<sup>402</sup> Within certain legal limits, there is some flexibility for the preventive agreement to propose either a three-year maximum rescheduling of repayments or an offer to discharge the debts at a discount of up to sixty percent of the face value of the debt, or a combination thereof.<sup>403</sup>

### *I. Concluding Suspension of Payments*

A suspension of payments will cease to operate if, for any reason, the debtor is declared bankrupt.<sup>404</sup> Suspension of payments also ceases if the creditors' meeting approves a preventive agreement in which the debtor discharges the creditors' debts for a discounted amount and/or obtains a grace period to pay off its debts.<sup>405</sup> Last, improvement of the debtor's financial status, to the point that it can repay its debts as they become due,<sup>406</sup> also terminates the suspension of payments.

Suspension of payment proposals can involuntarily be converted to bankruptcy. The debtor seeking a suspension of payments or benefiting from a suspension of payments declaration will be declared bankrupt if it breaches any of the conditions listed in article 396. The debtor's failure to comply with the legal requirements set forth in the L.Q.S.P. for the preventive agreement proposal also triggers a bankruptcy declaration.<sup>407</sup> Further, a bankruptcy will be declared if, without the judge's consent, the debtor grants pledges or mortgages, or commits acts that exceed the ordinary administration of the company.<sup>408</sup> Last, suspension of payments will be converted to bankruptcy if the creditors reject or do not approve, by the requisite majority, the preventive agreement,<sup>409</sup> or if the judge does not approve the preventive agreement.<sup>410</sup>

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402. *Id.*

403. *See* L.Q.S.P. arts. 322, 403. The 60% discount is a five percent lower reduction than that which operates in bankruptcy proceedings. *See id.* arts. 317-20, 322.

404. *See* L.Q.S.P. arts. 396, 419 (discussing various ways a suspension of payments could cease and a declaration of bankruptcy declared).

405. *See* L.Q.S.P. art. 428.

406. *Id.*

407. *See id.* arts. 401, 420.

408. *See generally id.* arts. 411 & 420.

409. *Id.* art. 419.

410. *Id.* art. 420.

Any approved preventive agreement requires judicial approval. Once the judgment<sup>411</sup> approving the preventive agreement is signed, the suspension of payments concludes.<sup>412</sup>

Notwithstanding these two preceding procedures for concluding the suspension of payments, debtor rehabilitation may also trigger conclusion of the suspension of payments proceedings. If at any time after the declaration of suspension of payments and before the meeting for the recognition of creditors the debtor shows that he is able to perform his obligations, the judge may declare the suspension proceedings concluded. The debtor will then be excluded from applying for suspension of payments relief for a period of one year.<sup>413</sup>

### *J. Non-Judicial Reorganization*

Mexican law does not specifically provide for non-judicial reorganization. However, nothing would prevent a debtor from rescheduling its debts on a case-by-case basis prior to its cessation of payments.<sup>414</sup> The debtor and creditors can engage in workout agreements.<sup>415</sup>

## V. GENERAL INFORMATION

### *A. Multinational Insolvencies<sup>416</sup>*

Article 14 of the L.Q.S.P. provides for recognition of foreign bankruptcy judgments in Mexico. To be recognized and given

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411. The Spanish word for judgment is *sentencia*.

412. L.Q.S.P. arts. 347, 423.

413. L.Q.S.P. art. 428.

414. Note that there is no pending or proposed bankruptcy legislation despite the fact that the L.Q.S.P. has been only slightly amended once since its inception 50 years ago. Lender liability is not relevant in Mexico. For example, not even damages for defamation, economic, or other loss (*daño moral*) can be sought by the defendant from a plaintiff in a legal action on the basis of the claims presented in such legal action or the consequence thereof, even if the plaintiff is unsuccessful in the legal proceedings. *Jurisprudencia* 578, Apéndice al Semanario Judicial de la Federación, Segunda Parte, Salas y Tesis Comunes, Volumen III, México, 1989, p. 993.

415. See C.C.D.F. arts. 2944-63.

416. This section addresses recognition of foreign bankruptcy judgments as opposed to the broader concept of multinational insolvencies. Presently, there is no Mexican body of law concerning multinational insolvencies, either actual or developing. The primary reason for this void is Mexico's old close-mindedness toward participation in international trade in general and foreign investment in particular. For example Mexico only recently joined GATT. See LUIS M. DÍAZ GONZÁLEZ RUBIO, *GLO-BALIZACION DE LAS INVERSIONES EXTRANJERAS-NUEVOS ASPECTOS JURÍDICOS* 20 (1989).

effect in Mexico, foreign bankruptcies must comply with the formalities and preconditions for the declaration of bankruptcy set forth in the L.Q.S.P.<sup>417</sup> The foreign judgment is then subject to the L.Q.S.P. for purposes of giving effect to the bankruptcy declaration.<sup>418</sup> However, by virtue of Article 133 of the Mexican Constitution, ratified international treaties and conventions on bankruptcy prevail over the provisions of the L.Q.S.P. Therefore, foreign creditors must be cognizant of that when enforcing their claims. In addition, on submitting their claims, they must nominate an address in Mexico for serving notices.<sup>419</sup>

### *B. Tax Treatment of Losses in Insolvency Cases*

Whenever dealing with bankruptcy transactions, the tax treatment of losses is a significant issue. In general, creditors' losses as a result of the debtor's insolvency, either when the creditor is repaid a percentage of the original debt or not repaid at all, are tax deductible.<sup>420</sup> The Income Tax Law establishes that the loss can be deducted when "the practical impossibility of collection has become clear"<sup>421</sup> or, if applicable, when the respective statute of limitations expires.<sup>422</sup> Although the corporate debtor benefits from a suspension of payments, a percentage reduction of debt or forgiveness of its debt, the benefit is not taxable as such. Natural persons are taxed, however, on debts that are forgiven by the creditor or paid by third parties.<sup>423</sup>

### *C. Environmental Issues*

The Federal Environmental Protection Law (*Ley General del Equilibrio Ecológico y la Protección al Ambiente*) (LFPMA) provides, in article 194, the right for plaintiffs to petition the Minis-

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417. L.Q.S.P. art. 14.

418. *Id.*

419. *Id.* art. 238.

420. *Ley del Impuesto Sobre la Renta* [Income Tax Law] art. 24-XVII. Note that banks are subject to special rules. *Id.*

421. *Id.*

422. *Id.* art. 24-XVII.

423. *Id.* art. 133-I. There is no specific provision in the Income Tax Law on this issue as regards legal entities, and by virtue of arts. 2-I, & 5 of the Fiscal Code, this concept is not taxable.

try of Urban Development and the Environment (*Secretaría de Desarrollo Urbano y Ecología*) for technical judgments relating to a breach of the LFPMA. A tortfeasor's breach can then be used as evidence in proceedings against him.<sup>424</sup> However, the LFPMA does not impose that same liability for environmental damage on the debtor's lenders at insolvency.

## VI. CONCLUSION

In deciding whether to loan or to invest, creditors must emphasize the due perfection of their collateral. Otherwise, creditors are forced to fight among other creditors for the proceeds of a bankrupt's estate in the "class warfare" of an insolvency proceeding.

Mexico's bankruptcy statute clearly needs amending to bring it up to date, particularly in managing insolvency proceedings. The country's judicial system also needs reform to expedite the administration of justice. Finally, although Mexico has made important progress in the race towards better publicity of its court decisions, it still needs to make those decisions much more promptly available.

Nevertheless, it is reassuring for the lender or investor to know that Mexican laws can and will protect collateral before and during insolvency proceedings. Managing, rather than avoiding, risk must be the goal of lending or investing. Mexico's system provides the lender and the investor that requisite degree of certainty and meets the standards of the world's advanced legal systems.

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424. Currently, the Ministry of Social Development (*Secretaría de Desarrollo Social*).

**APPENDIX A**

## ABBREVIATIONS USED IN THE TEXT AND FOOTNOTES

<i>Abbreviation</i>	<i>Full Name</i>
Bonding Inst. Law	Nueva Ley Federal de Fianzas [New Federal Law of Bonding Institutions]
C.C.D.F.	CÓDIGO CIVIL PARA EL DISTRITO FEDERAL [CIVIL CODE FOR THE FEDERAL DISTRICT]
C.F.F.	CÓDIGO FISCAL DE LA FEDERACIÓN [FISCAL CODE OF THE FEDERATION]
CÓD. COM.	CÓDIGO DE COMERCIO [COMMERCIAL CODE]
C.P.C.D.F.	CÓDIGO DE PROCEDIMIENTOS CIVILES PARA EL DISTRITO FEDERAL [CIVIL PROCEDURE CODE FOR THE FEDERAL DISTRICT]
Credit Institutions Law	Ley de Instituciones de Crédito [Credit Institutions Law]

*Abbreviation**Full Name*

Credit Instr. & Operations  
Law

Ley General de Títulos y Operaciones de Crédito [General Law of Instruments and Operations of Credit]

Insurance Law

Ley General de Instituciones y Sociedades Mutualistas de Seguros [General Law of Insurance Institutions and Companies]

Investment Law

Ley para Promover la Inversión Mexicana y Regular la Inversión Extranjera [Law to Promote Mexican Investments and Regulate Foreign Investment]

L.F.P.C.

Ley Federal de Protección al Consumidor [Federal Law of Consumer Protection]

L.F.T.

Ley Federal de Trabajo [Federal Labor Law]

L.Q.S.P.

Ley de Quiebras y Suspensión de Pagos [Bankruptcy and Suspension of Payments Law]

Securities Market Law

Ley del Mercado de Valores [Securities Market Law]



*Abbreviation**Full Name*

RPPC

Registro Público de la Propiedad y de Comercio [Public Registry of Property and Commerce]