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**“MEXICO’S 2000 FINANCIAL LAWS AMENDMENTS:  
ON THE ROAD TO CERTAINTY”**

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This article is not intended to be comprehensive or to provide specific legal advice. It only enunciates the main amendments to the various statutes discussed herein.

**“MEXICO’S 2000 FINANCIAL LAWS AMENDMENTS:  
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**INTRODUCTION**

Mexico has once again amended various statutes in its search for transparency and expediency in debtor-creditor relations.<sup>1</sup> An important part of this effort is the Decree that was published in Mexico’s D.O. on May 23, 2000 (the “Decree”), which added 55 articles to and amended 4 articles of the General Law of Negotiable Instruments and Credit Transactions (Ley General de Títulos y Operaciones de Crédito) (“Credit Instr. & Operations Law”).<sup>2</sup>

The Decree also added a whole new section, Title Third Bis (Título Tercero Bis), which comprises 21 articles, and amended 9 articles of the Commercial Code (Código de Comercio) (“Commerce Code”), and added 2 articles to and amended 2 articles of the Credit Institutions Law (Ley de Instituciones de Crédito) (the “Banking Law”).

The thrust of the Decree was to bring more certainty to both creditors’ and debtors’ rights in general, with a specific emphasis on transactions involving the use of (i) the non-possessory pledge as collateral; and (ii) guaranty trusts. This article summarizes the Decree and elaborates on its most relevant substantive provisions.

**I. AMENDMENTS TO THE CREDIT INSTR. & OPERATIONS LAW**

**I.1 Enforcement of a Pledge**

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<sup>1</sup> Notably, the old Bankruptcy and Suspension of Payments Law (Ley de Quiebras y Suspensión de Pagos) was abrogated by a Decree that was published in the Federal Register (Diario Oficial de la Federación) (“D.O.”) of May 12, 2000, and replaced by a new statute, the Insolvency Law (Ley de Concursos Mercantiles).

<sup>2</sup> The Decree became effective on May 24, 2000 and its provisions shall not apply retroactively, unless otherwise agreed to by the parties to a contract.

The Decree amended Article 341 and other provisions of the Credit Instr. & Operations Law.

Enforcement of a pledge is now subject to the debtor's "reasonable defenses", including but not limited, to payment by the debtor.<sup>3</sup> In the past, the debtor's only statutory defense was payment. The amendment merely reflects well-established Mexican case law.

## I.2 Regulation of the Non-possessory Pledge

New articles 346-380 of the Credit Instr. & Operations Law regulate perfection and enforcement of the non-possessory pledge. The guaranteed amount can be determined upon creation of the pledge, or be determinable for its execution, and unless otherwise agreed to by the parties the pledge will cover ordinary and default interest as well as all execution expenses.<sup>4</sup> Provided that the assets subject to the non-possessory pledge can be divided without affecting their value and if permitted by their legal nature, the value of the pledge will be reduced pro rata following payment of each installment.<sup>5</sup>

In the event of the debtor's insolvency (concurso mercantil), credits guaranteed by means of a non-possessory pledge shall become due and payable and shall continue to accrue ordinary interest, up to the value of the pledge.<sup>6</sup> Furthermore, foreclosure of the pledge can be requested from the bankruptcy court, and the bankruptcy court must order the foreclosure "without any further proceedings".<sup>7</sup>

Any obligation can be guaranteed through a non-possessory pledge.<sup>8</sup> All kinds of rights and movable assets can be pledged, but no assets which have been pledged can be the object of another pledge or guaranty.<sup>9</sup> The pledged assets must be identified, except in the case where the debtor provides a non-possessory pledge on all of the movables that it uses to carry

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<sup>3</sup> See Credit Instr. & Operations Law art. 341.

<sup>4</sup> Id. art. 348.

<sup>5</sup> Id. art. 349.

<sup>6</sup> Id. art. 350.

<sup>7</sup> Id. art. 351.

<sup>8</sup> Id. art. 352.

out “its main activities”, in which case such movables may be identified “generically”.<sup>10</sup>

The following movables can be pledged: (i) the debtor’s rights and assets, including commercial names, trademarks and other rights; (ii) those whose legal nature is similar to the above-listed, which the debtor may acquire subsequent to the creation of the pledge; (iii) future products of the above-listed rights and assets, whether already accrued or not; (iv) goods produced with such rights or assets; and (v) the rights and assets which the debtor is entitled to receive, or actually receives, in payment for the sale of the above-listed rights and assets or as an indemnification in the case of damage or destruction thereof.<sup>11</sup>

Unless otherwise agreed to between the parties to a non-possessory pledge, the debtor in possession shall remain entitled to (i) use the pledged assets to manufacture goods, provided that their value is not impaired and the goods produced therewith become a part of the pledge; (ii) utilize the pledged assets and receive the products and benefits thereof; and (iii) sell the pledged assets “in the ordinary course of its business”, whereupon the pledge over such assets shall expire vis-à-vis bona fide third parties, although this right shall cease upon commencement of any enforcement proceedings against the debtor under Title Third Bis of the Commerce Code.<sup>12</sup> Whenever the pledged assets represent 80% or more of the debtor’s assets, the debtor shall be entitled to sell them in the ordinary course of business with the court’s or the creditor’s prior authorization, as the case may be. These concepts also apply

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<sup>9</sup> Id. art. 353.

<sup>10</sup> Id. art. 354.

<sup>11</sup> Id. art. 355.

<sup>12</sup> Id. art. 356. Conversely, bad faith shall be presumed to exist where the acquirer of the assets (i) is aware of the existence of the non-possessory pledge; and (ii) the terms and conditions of the purchase and sale transaction “depart in a significant manner” from market conditions prevailing at the time of the execution thereof, from the debtor’s general sales policies, or from “healthy” commercial usages and practices. Of course, no bad faith shall exist where the creditor’s prior consent shall have been obtained. See id. art. 373. Furthermore, the creditor’s prior written consent is required for the debtor to sell assets subject to a non-possessory pledge to any of the following individuals: (i) holders of the shares representing 5% or more of debtor’s capital stock; (ii) regular and alternate members of the debtor’s Board of Directors; (iii) the spouse and relatives by blood or affinity up to the second degree, or relatives-in-law, of any of the above-mentioned individuals or of the debtor’s should the debtor be an individual [instead of an entity]; and (iv) the debtor’s employees, officers and creditors. Failure by the creditor to respond within 10 days to a request by the debtor as described above shall be construed to mean its acceptance thereto. Sales made without the creditor’s consent shall be null and void and the creditor shall be entitled to recover the assets vis-à-vis the acquirer thereof. Moreover, the creditor may accelerate the credit in these cases if so agreed with the debtor. See id. art. 374.

mutatis mutandis to guaranty trust arrangements.<sup>13</sup>

In order to enable the creditor to keep track of the assets subject to the non-possessory pledge, the pledge contract must regulate, inter alia, (i) the location of the pledged assets; (ii) the “minimum consideration” which the debtor must obtain in exchange for the sale or transfer of any pledged assets; (iii) the use of the proceeds of each sale of pledged assets; and (iv) the information as to the sale, transfer or manufacture of such assets which the debtor shall provide to the creditor. Failure by the debtor to comply with the terms and conditions agreed to with respect to any of the above concepts shall give rise to acceleration of the credit guaranteed with the non-possessory pledge.<sup>14</sup>

The Credit Instr. & Operations Law provides for the creation of a non-possessory pledge on assets which are acquired with credits granted by new creditors, regardless of the existence of a previous non-possessory pledge.<sup>15</sup> Perfection of the new pledge in these cases requires a “precise identification” of the new collateral assets so as to enable the differentiation of the (new) assets from those which had already been pledged. The creditor holding a first priority pledge has a senior right to collect on its collateral, with the exception of assets acquired with resources of the second creditor upon which the second creditor shall have priority.<sup>16</sup>

Future obligations can be guaranteed with a non-possessory pledge, but the guaranty cannot be executed without the main obligation becoming due and payable.<sup>17</sup> The debtor is obligated to preserve the assets subject to the non-possessory pledge and to indemnify the creditor for losses and damages to such assets due to the debtor’s “fault or negligence”. The debtor must maintain, repair, manage and recover the pledged assets, and must utilize them as agreed upon with the creditor.<sup>18</sup> Further, the debtor must maintain and pay for insurance of the pledged assets, with the creditor being the beneficiary under the insurance policy. Payment by the insurance company shall be applied to reduce the amount of the main

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<sup>13</sup> Id. art. 402.

<sup>14</sup> Id. art. 357.

<sup>15</sup> Id. art. 358.

<sup>16</sup> See id.

<sup>17</sup> Id. art. 359.

<sup>18</sup> Id. art. 361. As regards guaranty trust agreements, see art. 405.

obligation.<sup>19</sup> These concepts also apply to guaranty trust arrangements.<sup>20</sup>

The debtor must give the creditors access to the premises where the pledged assets are located to enable verification of their physical condition.<sup>21</sup> In case of a reduction of the value of the pledged assets so that they are no longer sufficient to guaranty the principal amount and the interest of the credit, the debtor may deliver additional assets to restore the value of the pledge. Failure by the debtor to provide additional assets may give rise to acceleration of the credit.<sup>22</sup> The parties must designate a third-party expert (perito) who shall be responsible for assessing the value of the pledge for purposes of articles 361 and 362.<sup>23</sup> This expert may also be entrusted with the custody of the pledged assets.<sup>24</sup>

Upon full satisfaction of the principal amount, interest and other accessories of the debt, the creditor must release the pledge. Failure by the creditor to release the pledge shall give the debtor the right to recover losses and damages.<sup>25</sup> The pledge contract must be in writing and formalized before a Commercial Public Registrar (Corredor Público) or a Notary Public (Notario Público) when the value of the pledged assets is equal to or higher than the equivalent in pesos of 250,000 UDI's (Unidades de Inversión).<sup>26</sup> (These concepts also apply to guaranty trust agreements).<sup>27</sup> The formalities required to perfect a pledge, including recordation at the Public Registry of Commerce (Registro Público de Comercio) when applicable, must be observed to release it.<sup>28</sup>

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<sup>19</sup> Id. art. 360.

<sup>20</sup> Id. art. 403.

<sup>21</sup> Id. art. 362. As regards guaranty trust agreements, see art. 404.

<sup>22</sup> See id.

<sup>23</sup> Id. art. 363.

<sup>24</sup> See id.

<sup>25</sup> Id. art. 364.

<sup>26</sup> Id. art. 365. As of October 10, 2000 one UDI was equivalent to \$2.851969. Assuming an exchange rate of \$9.50 Mex. Cy. per U.S.\$1, 250,000 UDI's were the equivalent of approximately U.S.\$75,000 on such date.

<sup>27</sup> Id. arts. 407, 410.

<sup>28</sup> Id. arts. 365-66. The creation, amendment, assignment of rights, termination and any judicial resolution affecting a non-possessory pledge must be registered, when required, at the Public Registry of Commerce of the debtor's domicile or, as applicable, in the corresponding Special Registry. See id. art. 376. Officers of the Public Registry of Commerce shall refrain from refusing recordation of a non-possessory pledge (i) on the debtor's general assets when these are used by the debtor to carry out its main business activities as set forth in article 354; (see id. art. 377); or (ii) when the value thereof can be determined upon its execution, even if no ceiling was established as to the value of the security. See

Under Mexican law, classification (graduación) and priority within a class (prelación) determine the order of payment among creditors.

In general, the holder of a duly perfected non-possessory pledge has priority to collect on the collateral as of the date of recordation in the Public Registry of Commerce.<sup>29</sup> If its guaranty is recorded before the assets become part of a real property the object of another guaranty, the holder of the non-possessory pledge ranks higher than even a creditor under a mortgage agreement (garantía hipotecaria), a purchase finance agreement (garantía refaccionaria) or a trust agreement (garantía fiduciaria).<sup>30</sup> Furthermore, the creditor under a non-possessory pledge has priority over (i) unsecured credits; (ii) unrecorded secured credits; and (iii) unrecorded pre-existing judicial liens.<sup>31</sup> Failure to record a guaranty results in the guaranty being ranked based on the date of the execution of each contract.<sup>32</sup> The Credit Instr. & Operations Law expressly permits modification of the legal ranking of a non-possessory pledge by agreement of the parties thereto.<sup>33</sup> Such modification also requires recordation to become effective vis-à-vis third parties.<sup>34</sup>

The statute of limitations to enforce a non-possessory pledge is 3 years from the time the guaranteed obligation became due and payable.<sup>35</sup> The unauthorized sale or use (save for normal wear and tear) by the debtor of the assets subject to a non-possessory pledge, or its intentional causing of damage thereto, can give rise to penalties and even jail sanctions.<sup>36</sup>

Finally, the Credit Instr. & Operations Law creates a concept the validity of which will be undoubtedly challenged in court sooner rather than later: the creditor must agree in the pledge contract to relinquish its right to collect on the remainder of its credit where, in the event

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id. art. 378.

<sup>29</sup> Id. arts. 366-67.

<sup>30</sup> Id. art. 369. Actually, only employee-related obligations of the debtor rank higher than its obligations under a duly perfected and recorded non-possessory pledge. See id. art. 367.

<sup>31</sup> Id. art. 371.

<sup>32</sup> Id. art. 370.

<sup>33</sup> Id. art. 372.

<sup>34</sup> Id.

<sup>35</sup> Id. art. 375.

<sup>36</sup> Id. art. 380.

of enforcement of the non-possessory pledge, the proceeds of the sale of the pledged assets shall be insufficient to pay for the whole amount of the credit. This provision cannot be waived by the parties.<sup>37</sup> (These concepts also apply to guaranty trust agreements).<sup>38</sup>

### I.3 Regulation of the Guaranty Trust

Principles governing the non-possessory pledge are applicable to guaranty trusts to a great extent.<sup>39</sup> Differences between their regulation are a reflection of their varying legal nature. The summary below will avoid the repetition of concepts and will instead concentrate on their differences.

The Credit Instr. & Operations Law confirms a logical yet sometimes questioned principle: that the assets in trust (bienes fideicomitidos) are transferred to the trustee (institución fiduciaria) in the context of a guaranty, and not only in the context of a management, trust.<sup>40</sup> A guaranty trust agreement is created to guarantee performance of an obligation to the beneficiary (fideicomisario) thereunder as well as its payment preference.<sup>41</sup>

A guaranty trust can guarantee different obligations simultaneously or successively. Each creditor must notify the trustee within 10 days of the payment of its credit. Following such notification, the settlor (fideicomitente) may appoint a new beneficiary or terminate the trust agreement.<sup>42</sup>

The following entities can act as trustees, beneficiaries, and both as beneficiary and trustee in trust agreements involving a guaranty of their own credits.<sup>43</sup> (i) banks (instituciones de crédito); (ii) insurance companies (instituciones de seguros); (iii) bonding companies (instituciones de fianzas); (iv) limited-scope financial institutions (sociedades

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<sup>37</sup> Id. art. 379.

<sup>38</sup> Id. art. 412.

<sup>39</sup> See id. art. 414, which includes a list of the provisions of the Credit Instr. & Operations Law which apply to guaranty trust agreements even though they regulate specifically non-possessory pledges and trust agreements in general.

<sup>40</sup> See id. art. 395.

<sup>41</sup> Id.

<sup>42</sup> Id. art. 398.

financieras de objeto limitado); and (v) warehousing companies (almacenes generales de depósito).<sup>44</sup>

Trustees are liable for losses and damages caused to settlors arising from (i) their bad faith; or (ii) their acting ultra vires in the enforcement of the trust, i.e. beyond the scope of their powers as defined in the trust agreement or the law.<sup>45</sup>

Finally, the guaranty trust agreement must include at least the following provisions for purposes of articles 402, 404 and 405: (i) the location of the assets; (ii) a description of the asset inspections and the minimum accepted value of such assets, so as to avoid acceleration of the credit and the enforcement of the guaranty trust; (iii) the “minimum consideration” which the settlor must obtain in exchange for the sale or transfer of the assets; (iv) a description of the potential acquirers or transferees of the assets, as well as the use of the proceeds of the sale or transfer of the assets; (v) the information as to the sale, transfer or manufacture of the assets which the settlor shall provide to the trustee; (vi) the terms under which a third party expert (valuador) shall assess the value of the assets to measure the deterioration thereof, on the understanding that the valuation may be carried out based upon an index (such as the consumer price index) or another parameter mutually acceptable to the parties; and (vii) the terms under which assets will be released following their appreciation.<sup>46</sup>

Breach of any of the above provisions shall give rise to acceleration of the credit guaranteed with the guaranty trust.<sup>47</sup>

## **II. AMENDMENTS TO THE BANKING LAW**

### **II.1 Reference to Title Third Bis of the Commerce Code**

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<sup>43</sup> Id. art. 400.

<sup>44</sup> Id. art. 399.

<sup>45</sup> Id. art. 400.

<sup>46</sup> Id. art. 406.

<sup>47</sup> Id.

The Banking Law stipulates that, unless the parties to a trust agreement (fideicomiso) shall have established a conventional enforcement procedure, the provisions of Title Third Bis of the Commerce Code shall apply.<sup>48</sup> (Title Third Bis of the Commerce Code regulates the enforcement of non-possessory pledge agreements and guaranty trusts).

## II.2 Minimum Capital Requirements for Trustees

The Banking Law further requires that entities other than banks who wish to act as trustees obtain a specific authorization therefor. For these purposes, applicants must meet the “additional minimum capital” requirements set forth by the Ministry of Finance and Public Credit (Secretaría de Hacienda y Crédito Público)(“Hacienda”) through general rulings (disposiciones de carácter general). In order to set forth the amount of the “additional minimum capital” requirement, Hacienda shall get the opinion of (i) the National Banking and Securities Commission (Comisión Nacional Bancaria y de Valores) or the National Bonding and Insurance Commission (Comisión Nacional de Seguros y Fianzas), as applicable; and (ii) Mexico’s Central Bank (Banco de México)(“Banxico”). Hacienda shall grant the authorization requested “discretionarily”.<sup>49</sup>

The Banking Law further mandates the application of the provisions of its articles 79 and 80 to non-bank trustees.<sup>50</sup> The Banking Law also provides the National Banking and Securities Commission and the National Bonding and Insurance Commission with authority to suspend the operations during a period which shall not exceed 6 months, of trustees who shall have been ordered to pay an indemnification under article 411 of the Credit Instr. & Operations Law.<sup>51</sup>

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<sup>48</sup> See Banking Law art. 83.

<sup>49</sup> Id. art. 85 Bis.

<sup>50</sup> Id. Article 79 describes how banks must maintain the accounting records of the trust arrangements in which they act as trustees; article 80 sets forth the responsibility of banks as trustees as well as the functions of the “technical committee” in a trust agreement.

<sup>51</sup> Id. art. 85 bis 1. Article 411 sets forth the basis to calculate the indemnification which trustees must pay to settlors for losses or damages caused due to the trustees’ bad faith or acting ultra vires.

### III. AMENDMENTS TO THE COMMERCE CODE

#### III.1 General Purpose

As explained above, Title Third Bis offers a detailed set of rules for both the extra-judicial (out of court) and the judicial enforcement of non-possessory pledge agreements and guaranty trusts.<sup>52</sup> Arguably, nothing would prevent the parties to other types of agreements from incorporating the enforcement mechanism of Title Third Bis either by reference or by inserting the provisions thereof. The extra-judicial enforcement provisions apply to the extent the parties to a non-possessory pledge or guaranty trust agreement decide to observe them; nothing prevents them from resorting to the judicial enforcement provisions at will.<sup>53</sup>

#### III.2 Extra-judicial Enforcement Procedure<sup>54</sup>

This procedure is available to seek payment of credits that have become due and payable and to gain possession of assets subject to a non-possessory pledge or guaranty trust agreement, provided that there exists no disagreement as to (i) the fact that the credit has become due and payable; (ii) the credit amount; or (iii) the appropriateness of the delivery of possession of the assets.<sup>55</sup>

Valuation of the assets can be carried out by an expert designated by the parties prior to or after the execution of the agreement, or by any other means agreed to in writing by the parties.<sup>56</sup> At a minimum, the parties must set forth in the agreement the basis for the appointment of the valuation expert.<sup>57</sup>

The pledgee and the trustee can take possession of the assets in the terms of the non-possessory pledge or guaranty trust agreement, as the case may be, with the

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<sup>52</sup> See Commerce Code arts. 1414 bis-1414 bis 20.

<sup>53</sup> Id. art. 1414 bis 6.

<sup>54</sup> Id. arts. 1414 bis-1414 bis 6.

<sup>55</sup> Id. art. 1414 bis.

<sup>56</sup> Id. art. 1414 bis, section I.

<sup>57</sup> Id. art. 1414 bis, final para.

participation of a Commercial Public Registrar or a Notary Public, who shall prepare an inventory of the assets.<sup>58</sup> If possession of the assets is secured, these can be sold following the provisions of article 1414 bis 17, section II.<sup>59</sup>

An extra-judicial procedure must be terminated whenever (i) the debtor shall refuse to deliver the assets or to cover the credit amount;<sup>60</sup> or (ii) the parties shall have failed to reach an agreement on the terms of valuation of the assets or it shall become impossible to value the assets;<sup>61</sup> or (iii) in general, the pledgee or the trustee shall fail to obtain possession of the assets.<sup>62</sup> In all of these cases, the parties shall be entitled to seek the judicial enforcement of their guaranty.<sup>63</sup>

### III.3 Judicial Enforcement Procedure

Like an extra-judicial procedure, the judicial enforcement procedure is available to seek payment of credits that have become due and payable (crédito cierto, líquido y exigible) and/or possession of the assets subject to a duly formalized non-possessory pledge or guaranty trust agreement.<sup>64</sup>

Upon receiving a claim, the judge must order delivery of the assets to the creditor, who shall become a “judicial depository” (depositario judicial) of such assets during the proceedings.<sup>65</sup> The defendant can raise mostly defenses based on documentary evidence.<sup>66</sup> Other defenses are subject to strict terms and terms to avoid procrastination.<sup>67</sup> The court can use all “reasonable measures” (medidas conducentes) to bring a judicial enforcement procedure to an end, including (i) police aid; and (ii) temporary arrest (arresto administrativo).<sup>68</sup>

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<sup>58</sup> Id. art. 1414 bis 3.  
<sup>59</sup> Id. art. 1414 bis 4.  
<sup>60</sup> Id. art. 1414 bis 2, section I.  
<sup>61</sup> Id. art. 1414 bis 2, section II.  
<sup>62</sup> Id. art. 1414 bis 5.  
<sup>63</sup> Id.  
<sup>64</sup> Id. art. 1414 bis 7.  
<sup>65</sup> Id. art. 1414 bis 8.  
<sup>66</sup> Id. art. 1414 bis 10.  
<sup>67</sup> Id. arts. 1414 bis 10-1414 bis 16, 1414 bis 20.  
<sup>68</sup> Id. art. 1414 bis 9.

The assets must be valued in order to enforce the security.<sup>69</sup> If their value turns out to be equal to or lower than the credit amount as determined by the court, the pledgee or the trustee, as the case may be, shall be entitled to freely dispose of the assets and shall be considered to have relinquished its right to collect on the balance of its credit, if any.<sup>70</sup> However, if the value of the assets turns out to be higher than the credit amount as determined by the court, then the assets must be sold according to the specific rules included in Title Third Bis.<sup>71</sup> Within 5 days from completion of the sale the pledgee or the trustee, as the case may be, must deliver to the debtor any amount in excess of the amount of the credit, plus interest and execution expenses.<sup>72</sup> Breach of this obligation may result in stiff court-imposed penalties<sup>73</sup> and onerous interest payments to the plaintiff.<sup>74</sup>

Clearly, the thrust of Title Third Bis is to create expeditious enforcement procedures drawing from the experience of creditors both in court and out of court. Only time will enable us to judge the effectiveness of the provisions of Title Third Bis, the validity of some of which, as explained above, will in all likelihood be questioned on constitutional grounds.

SEMINAR-ABP

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<sup>69</sup> Id. art. 1414 bis 17, first para.

<sup>70</sup> Id. art. 1414 bis 17, section I.

<sup>71</sup> See art. 1414 bis 17, section II.

<sup>72</sup> Id. art. 1414 bis 17, section II, c).

<sup>73</sup> Id. art. 1414 bis 18.

<sup>74</sup> Id. art. 1414 bis 19. The interest rate which must be paid to the debtor in these cases is equal to two times the Mexican banks' cost of funding (costo de captación a plazo de pasivos denominados en moneda nacional), also known as "CCP", as published from time to time in the D.O. by Banxico.