

2011

International Secured Transactions and Insolvency

Susan Jaffe Roberts

Robin Phelan

Autumn Highsmith

Mattia Colonnelli de Gasperis

Maddalena Sala

See next page for additional authors

Recommended Citation

Susan Jaffe Roberts et al., *International Secured Transactions and Insolvency*, 45 INT'L L. 239 (2011)
<https://scholar.smu.edu/til/vol45/iss1/18>

This Article is brought to you for free and open access by the Law Journals at SMU Scholar. It has been accepted for inclusion in *International Lawyer* by an authorized administrator of SMU Scholar. For more information, please visit <http://digitalrepository.smu.edu>.

International Secured Transactions and Insolvency

Authors

Susan Jaffe Roberts, Robin Phelan, Autumn Highsmith, Mattia Colonnelli de Gasperis, Maddalena Sala, John E. Rogers, Ramiro Rangel, and Fernando Barrita

International Secured Transactions and Insolvency

SUSAN JAFFE ROBERTS, ROBIN PHELAN, AUTUMN HIGHSMITH, MATTIA COLONNELLI DE GASPERIS, MADDALENA SALA, JOHN E. ROGERS, RAMIRO RANGEL, AND FERNANDO BARRITA*

This article addresses developments in international secured transactions and insolvency during 2010. Although many developments took place around the world, because of space limitations this article is limited to developments in the United States, Italy, and Mexico.

I. Developments in the United States

A. CHAPTER 15 AND AVOIDANCE ACTIONS UNDER FOREIGN LAW

In a case of first impression, the U.S. Court of Appeals for the Fifth Circuit overruled the decisions of the U.S. Bankruptcy Court and the U.S. District Court for the Southern District of Mississippi and held that a Chapter 15 proceeding may be used to pursue foreign-law avoidance actions against defendants and assets in the United States.

* Susan Jaffe Roberts served as Editor of the Committee's 2010 year-in-review contribution. Ms. Roberts is a partner with the Bankruptcy Section at Whiteford, Taylor & Preston LLP (Baltimore, Maryland). Robin E. Phelan and Autumn Highsmith authored the section on Developments in the United States. Mr. Phelan is a partner with the Bankruptcy and Restructuring Section at Haynes and Boone LLP. Ms. Highsmith is an associate with the Bankruptcy and Restructuring Section at Haynes and Boone LLP. Mattia Colonnelli de Gasperis and Maddalena Sala of Colonnelli de Gasperis Studio Legale (Milan, Italy), authored the section on Developments in Italy. John E. Rogers, Ramiro Rangel, and Fernando Barrita authored the section on Developments in Mexico. Mr. Rogers is Of Counsel at Strasburger & Price LLP (New York, New York). Mr. Rangel is a partner and Mr. Barrita is an associate of Strasburger & Forastieri SC (Mexico City, Mexico). The authors gratefully acknowledge the helpful comments of Steve Roberts and John Dorsey of Strasburger & Price LLP and of Professor Alejandro Garro of Columbia Law School. The authors are, however, solely responsible for the contents of this article.

1. *Background*

Condor Insurance Ltd. (“Condor”) formerly operated an insurance and surety bond business in Nevis.¹ On November 27, 2006, one of Condor’s creditors requested that the Eastern Caribbean Supreme Court in the High Court of Justice of St. Christopher and Nevis, Nevis Circuit (“Nevis Court”) initiate a winding up proceeding (“Nevis Proceeding”) against Condor.² On May 18, 2007, the creditor’s winding up petition was granted, and Richard Fogerty and William Tacon were appointed as Joint Official Liquidators (“Liquidators”) by the Nevis Court.

On July 26, 2007, the Liquidators, as the foreign representative of Condor, filed a Chapter 15 Petition for Recognition of a Foreign Main Proceeding in the U.S. Bankruptcy Court for the Southern District of Mississippi (“Bankruptcy Court”) seeking recognition of the Nevis Proceeding. On August 21, 2007, the Bankruptcy Court entered its order recognizing the Nevis Proceeding as a foreign main proceeding pursuant to 11 U.S.C. § 1517.

After recognition, the Liquidators filed a complaint against Condor Guaranty, Inc. (CGI), Petroquest Resources, Inc., and other defendants (collectively, the “Defendants”) requesting relief for, among other things, the avoidance of fraudulent conveyances under Nevis law. Specifically, the Liquidators contended that over \$313 million in Condor’s assets were fraudulently transferred to or by the Defendants and that most of the transferred assets were located in the United States. The Liquidators alleged that the transfers were made to prevent creditors from recovering the value of the assets in the Nevis Proceeding.

CGI filed a motion to dismiss the complaint, in part, on the grounds that the Bankruptcy Court lacked subject matter jurisdiction. CGI argued that §§ 1521(a)(7) and 1523(a) of Title 11 of the United States Code (“Bankruptcy Code”) prohibited a foreign representative under Chapter 15 from bringing avoidance actions unless the foreign representative filed a bankruptcy case under either Chapter 7 or Chapter 11 of the Bankruptcy Code.³

2. *Applicable Law*

Bankruptcy Code § 1521(a)(7) provides that a bankruptcy court has the discretion to grant a foreign representative in a Chapter 15 proceeding relief available to a trustee “except for relief available under sections 522, 544, 545, 547, 548, 550, and 724(a).”⁴

Bankruptcy Code § 1523(a) provides that when a foreign proceeding has been recognized, “the foreign representative has standing in a case concerning the debtor pending under another chapter of this title to initiate actions under sections 522, 544, 545, 547, 548, 550, 553, and 724(a).”⁵

1. Nevis is an island in the Caribbean. Along with Saint Kitts, it forms the Federation of Saint Kitts and Nevis.

2. A “winding up proceeding” is similar to a Chapter 7 bankruptcy under U.S. law.

3. In this case, Condor was not eligible for relief under Chapters 7 or 11 because Condor was a foreign insurance company. Foreign insurance companies are not permitted to file Chapter 7 or Chapter 11 cases. See 11 U.S.C. §§ 109(b), (d) (2011).

4. 11 U.S.C. § 1521(a)(7) (2011).

5. § 1523(a).

The specific sections of the Bankruptcy Code referenced in §§ 1521(a)(7) and 1523(a) are those containing a trustee's "avoidance powers." These are the trustee's powers to avoid the transfer of debtor property that would deplete the debtor's estate at the expense of its creditors. Such powers, generally described, include (i) those addressing exempt property (§ 522); (ii) the "strong arm" power, which permits the trustee to act as a judicial lien creditor (§ 544); (iii) the power to avoid statutory liens (§ 545); (iv) the power to avoid transactions as "preferences" (§ 547); (v) the power to avoid fraudulent transfers (§ 548); and (vi) the power to avoid liens that secure claims for compensatory fine, penalty, forfeiture, or punitive damages (§ 724(a)). Bankruptcy Code § 550 contains the rules that govern the mechanics of avoidance actions.

The issue in *Condor* is whether the exceptions to the relief available to a foreign representative in Chapter 15 ancillary proceedings listed in Bankruptcy Code § 1521(a)(7) prohibit a foreign representative from bringing avoidance actions under applicable foreign law in the Chapter 15 proceeding.

The Liquidators argued that the plain language of Chapter 15 only prohibits foreign representatives from utilizing the avoidance provisions of the Bankruptcy Code when seeking avoidance of transfers. The Liquidators contended that Chapter 15 does not prohibit a foreign representative from bringing avoidance actions under foreign law.

The Defendants argued that reading Bankruptcy Code §§ 1521(a)(7) and 1523(a) together with the legislative history of both sections prohibit a foreign representative from bringing avoidance actions under either the Bankruptcy Code or foreign law without filing either a Chapter 7 or a Chapter 11 bankruptcy case.

3. *The Bankruptcy and District Court Decisions*

Both the Bankruptcy Court and the U.S. District Court for the Southern District of Mississippi ("District Court") interpreted Bankruptcy Code §§ 1521(a)(7) and 1523(a) to deny standing to the Liquidators to pursue avoidance actions based on Nevis law.

After considering the complimentary relationship between §§ 1521(a)(7) and 1523(a),⁶ the Bankruptcy Court concluded that "Chapter 15 was not designed to incorporate the law of the home court (here, Nevis) into the United States bankruptcy system" and granted CGI's motions to dismiss.⁷ The Bankruptcy Court adopted a portion of CGI's brief in support of the motion to dismiss that argued:

[T]he Liquidators improperly ask this Court to go beyond the parameters of Chapter 15 by using this Court as a de facto Nevis Court, interpreting and applying the substantive law of Nevis against a non-United States entity. The Liquidators cannot use this Court as a hub from which to launch international litigation under foreign avoidance law. If the Liquidators believe they have valid claims, those claims should be asserted elsewhere-not here.⁸

6. The Bankruptcy Court wrote that Bankruptcy Code § 1521(a)(7) delineates that a bankruptcy court does not have the power to provide relief in the form of avoidance powers to a foreign representative under Chapter 15; instead, Bankruptcy Code § 1523(a) affirmatively states that avoidance powers are available to a foreign representative if (and only if) those powers are exercised in a companion case under Chapters 7 or 11. *In re Condor Ins. Ltd.*, No. 07-51045 ERG, 2008 WL 285843, at *3 (Bankr. S.D. Miss. July 17, 2008).

7. *Id.*

8. *Id.*

The District Court affirmed the Bankruptcy Court's dismissal, concluding that the Bankruptcy Court had correctly interpreted §§ 1521(a)(7) and 1523(a).⁹ The District Court concluded that the plain language of Chapter 15 does not specifically address the use of avoidance powers under foreign law but that the legislative history of §§ 1521 and 1523(a) support the Bankruptcy Court's decision.¹⁰

The District Court primarily relied upon a House of Representatives report that provides:

The Model Law is not clear about whether it would grant standing in a recognized foreign proceeding if no full case were pending. This limitation [in § 1523] reflects concerns raised by the U.S. delegation during the UNCITRAL debates that a simple grant of standing to bring avoidance actions neglects to address very difficult choice of law and forum issues. This limited grant of standing in [§ 1523] does not create or establish any legal rights of avoidance nor does it create or imply any legal rules with respect to the choice of applicable law as to the avoidance of any transfer or obligation. The courts will determine the nature and extent of any such action and what national law may be applicable to such action.¹¹

The District Court concluded that §§ 1521(a)(7) and 1523(a) are intended to "exclude all of the avoidance powers specified, under either United States or foreign law, unless a Chapter 7 or 11 bankruptcy proceeding is instituted."¹²

The District Court went on to explain that the Liquidators' interpretation of § 1521(a)(7) "would conflict with Congress' expressed desire that courts make the choice of law determination in a full bankruptcy proceeding."¹³ The District Court echoed the Bankruptcy Court suggestion that the Liquidators seek avoidance of the challenged transfers in a Nevis court and then seek recognition of any Nevis judgment in the United States.¹⁴

4. *The Fifth Circuit Decision*

The U.S. Court of Appeals for the Fifth Circuit ("Fifth Circuit") reversed the decisions of the Bankruptcy and District Courts.¹⁵ The Fifth Circuit held that bankruptcy courts have authority to offer avoidance relief under foreign law in Chapter 15 ancillary proceedings.¹⁶

The Fifth Circuit explained that "[w]hile it is plain that relief under the listed sections [in § 1521(a)(7)] is excluded, the statute is silent regarding proceedings that apply foreign law, including any rights of avoidance such law may offer."¹⁷ The court referenced the

9. *Fogerty v. Condor Guaranty, Inc. (In re Condor Ins. Ltd. (In Official Liquidation))*, 411 B.R. 314, 316 (S.D. Miss. 2009).

10. *Id.*

11. *Id.*

12. *Id.* at 319.

13. *Id.*

14. *Id.* at 318.

15. *Fogerty v. Petroquest Res., Inc. (In re Condor Ins. Ltd. (In Official Liquidation))*, 601 F.3d 319, 320 (5th Cir. 2010).

16. *Id.*

17. *Id.* at 323.

maxim expressio unius est exclusio alterius (the mention of one thing within the statute implies the exclusion of another thing not so mentioned), and concluded that § 1521(a)(7) “provides for ‘any relief’ and excepts only actions under sections 522, 544, 545, 547, 548, and 724(a) of the Code and includes no other language suggesting that other relief might be excepted.”¹⁸ The court explained “[i]f Congress wished to bar all avoidance actions whatsoever their source, it could have stated so; it did not.”¹⁹

The Fifth Circuit rejected the lower courts’ interpretation of the legislative history of § 1521(a)(7), writing:

Congress did not intend to restrict the powers of the U.S. court to apply the law of the country where the main proceeding pends. Refusing to do so would lend a measure of protection to debtors to hide assets in the United States out of the reach of the foreign jurisdiction, forcing foreign representatives to initiate much more expansive proceedings to recover assets fraudulently conveyed, the scenario Chapter 15 was designed to prevent.²⁰

The Court also rejected the Bankruptcy and District Courts’ suggestion that the Liquidators should instead bring their claims in Nevis, explaining that full relief in Nevis might not be available if the Nevis courts cannot exercise jurisdiction over all of the Defendants.²¹

Additionally, the Fifth Circuit determined that its conclusion was consistent with prior case law under Bankruptcy Code § 304, the predecessor to Chapter 15.²² Indeed, the court reasoned that Chapter 15 might well have been a codification of case law under § 304 that held “avoidance actions under foreign law were permitted when foreign law applied and would provide for such relief.”²³ Finally, the court concluded that its holding would create settled expectations of the rules that will govern domestic businesses efforts in foreign territories.²⁴

5. Implications

As a result of the Fifth Circuit’s decision in *Condor*, assets transferred from the situs of a foreign main proceeding to the United States can be collected and distributed to creditors in the same manner as other assets. In the Fifth Circuit, this decision is a powerful tool for foreign representatives attempting to protect a foreign debtor’s assets in the United States.

The Bankruptcy Court, the District Court, and the Fifth Circuit did not address Bankruptcy Code § 544, one of the provisions listed in § 1521(a)(7), which provides that a bankruptcy trustee may avoid any transfer “that is voidable under applicable law” by a judgment creditor.²⁵ If “applicable law” under § 544(b) is interpreted by other circuits to

18. *Id.* at 324.

19. *Id.*

20. *Id.* at 327.

21. *Id.*

22. *Id.* at 328.

23. *Id.* at 329.

24. *Id.*

25. 11 U.S.C. § 544(b) (2011).

include foreign law, the question of whether § 1521(a)(7) bars foreign avoidance actions could be resolved differently. In short, the Fifth Circuit's decision in *Condor* will not be the last word on whether a foreign representative can pursue avoidance actions based on foreign law in a Chapter 15 ancillary proceeding.²⁶

II. Developments in Italy

A. ARRANGEMENTS WITH CREDITORS AND DEBT RESTRUCTURING AGREEMENTS

On May 31, 2010, the Government of Italy issued Law Decree no. 78 on "Urgent action on financial stabilization and economic competitiveness,"²⁷ converted to Law no. 122 of July 30, 2010.²⁸ Article 48 of the decree amends certain provisions of the Italian Bankruptcy Law²⁹ (IBL) applicable to cross-border and domestic insolvencies. The main goal of such amendments is to support and rescue companies in crisis by, among other things, enhancing the access to banks and shareholders' credit and liquidity in both the short and long terms, and to facilitate the restructuring and survival of companies in financial distress. Inter alia, foreign and domestic banks and financial institutions are encouraged to grant credit to companies in financial distress because, if such companies go bankrupt, the banks are protected by the fact that their credits are pre-deductible (i.e. they will not be a part of the *par condicio creditorum* and will be paid with top priority), and as a consequence they will have a very high chance of being paid in full.

1. Possibility of Pre-Deductible Credits Raised in Execution or by Reference to an Arrangement with Creditors or Debt Restructuring Agreement (New Article 82 quater IBL)

New Article 182 *quater* IBL, "Provisions on pre-deductible credits on debt restructuring agreements," establishes that the claims arising from loans made in any form by banks

26. The United States Bankruptcy Court for the Southern District of New York has questioned the District Court's reasoning, which suggests that it might reach the same conclusion as the Fifth Circuit if presented with the issue of whether a foreign representative in a Chapter 15 ancillary proceeding can bring avoidance actions under foreign law. See *In re Atlas Shipping A/S*, 404 B.R. 726, 743, 744 n.15 (Bankr. S.D.N.Y. 2009) ("While the parties relied extensively on *Condor* in briefing, the Court concludes that its reasoning is open to question . . . The *Condor* [district] court's conclusion that Congress intended to prevent a foreign representative from bringing avoidance actions based on foreign law is not supported by anything specifically in the legislative history. The [district] court also ignores cases decided under § 304."). In *Atlas*, the bankruptcy court also noted that no other court has addressed whether "applicable law" under § 544(b) includes foreign law. *Id.* at 744, n.16 (suggesting that a preference action under foreign law could still be brought even if § 544(b) is interpreted to include foreign law because preference actions under foreign law most likely do not depend on status as a judgment lien creditor).

27. Decreto Legge 31 maggio 2010, n. 78, in G.U. 30 luglio 2010, n. 176 (It.), available at <http://www.altalex.com/index.php?idnot=11219>.

28. Legge 30 luglio 2010, n. 122, in G.U. 30 luglio 2010, n. 176 (It.), available at http://www.urp.it/allegati/Legge_2010_122.pdf.

29. Regio Decreto 16 marzo 1942, n. 267, in G.U. 6 aprile 1942, n. 81 (It.), available at <http://www.altalex.com/index.php?idnot=2888>.

and financial institutions registered in the lists referred to in Article 106 and 107 of Legislative Decree of 1 September 1993 no. 385³⁰ under the execution of:

- an arrangement with creditors referred to in Article 160³¹ IBL and following, or
- a debt restructuring agreement approved pursuant to Article 182 *bis*,³² are pre-deductible under and for the purpose of Article 111 IBL.³³

Also included in this category are: claims arising from loans finalized in the arrangement with creditors or for funding under the plan of restructuring developed in the proceeding; funding from the company's shareholders (in derogation of Articles 2467 and 2497 *quinquies* of the Italian Civil Code), up to eighty percent of the amount; and the amounts owed to professionals for their work on these procedures, referred to in the third paragraph of Article 161³⁴ IBL and in the first paragraph of Article 182 *bis* IBL.

The above-mentioned creditors are excluded from voting and from the counting toward a majority for approval of the agreement pursuant to Article 177 IBL³⁵ and for calculation of the percentage of claims referred to in Article 182 *bis*, first and sixth paragraphs.³⁶

2. *Suspension Of Enforcement Measures And Protective Measures During The Negotiations To Conclude Debt Restructuring Agreements (New Article 182 bis IBL)*

New paragraph 6 of Article 182 *bis* IBL prohibits the commencement or continuance of precautionary measures or enforcement actions during the negotiations for an arrangement with creditors or for debt restructuring agreements, if:

- the entrepreneur has submitted a declaration confirming the presence of negotiations with creditors representing at least sixty percent of the overall claims; and
- the declaration is accompanied by a statement of an advisor, who meets the requirements of Article 67, ¶ 3(d) IBL³⁷ ensuring regular payment of creditors with whom negotiations are not in progress or who are unwilling to negotiate.

According to this new provision, companies in financial distress have an additional tool to overcome financial crisis and to reorganize their businesses.

III. Developments in Mexico

A. MEXICO'S NEW SECURED TRANSACTIONS REGISTRY OFFERS NEW OPPORTUNITIES FOR SECURED LENDING

Mexican companies have historically encountered difficulties in attracting secured lending from U.S. and other foreign banks, mainly because of concerns as to the reliability of Mexican laws governing secured transactions and of its systems for filing and perfecting security interests (*garantías reales*) in personal (movable) property or goods (*bienes muebles*).

30. Decreto Legislativo 1 Settembre 1993, n. 385, in G.U. 30 Settembre 1993, n. 230 (It.), available at <http://www.isaonline.it/s/gestione/show-main-frame.inc.php?url=/mag/DLgs385-1993.html>.

31. R.D. n. 267/1942 (It.).

32. *Id.*

33. *Id.*

34. *Id.*

35. *Id.*

36. *Id.*

37. *Id.*

Mexican banks have shared these concerns and have tended to rely on real property collateral in most of their secured lending. As a result, many Mexican companies whose primary assets are inventory, receivables, and equipment have lacked access to adequate financing on competitive terms.

In order to encourage lenders to finance the operations of Mexican borrowers, Mexico has enacted significant reforms of its secured transactions laws. Most recently, dramatic steps have been taken to improve its public registry system to make it easier to search for existing liens on a debtor's property and to perfect new security interests.

1. *Mexican Bankruptcy Considerations*

The importance to creditors of taking collateral security from Mexican debtors has arguably been increased by the Mexican Bankruptcy Law ("*Ley de Concursos Mercantiles*" or "LCM") enacted in 2000 and subsequently amended.³⁸ The LCM does not permit the "cram down" of secured creditors to the extent permitted under the U.S. Bankruptcy Code, which allows a debtor, under a reorganization plan, to pay a secured creditor less than its full claim if it is under-collateralized. The secured claim can be "crammed down" to the value of the collateral by paying under the plan, over time, the value of the collateral, with the remainder of the claim being treated as unsecured.³⁹

Under the LCM, on the other hand, a secured creditor may proceed with the enforcement of its collateral security if the reorganization plan does not provide for full payment of the secured debt.⁴⁰ This gives the secured creditor significant negotiating leverage in a restructuring under the LCM, and has implications not only for secured bank lending but also for Mexican corporate bond financings, as to which bond investors may have a strong argument based on the LCM to insist on collateral security. If an issuer must provide such collateral, for example to support a high-yield bond offering, it may be less costly for the issuer to provide collateral consisting of personal property than to mortgage its real property, partly because of high mortgage recording costs and the related notarial fees. In order to obtain the advantages of treatment as a secured creditor under the LCM, having personal property collateral is as effective as having real property collateral of comparable value.

2. *Like the United States Before the UCC*

Mexico has a bewildering variety of personal property security interests, including among others, the pledge (*prenda*), the industrial mortgage (*hipoteca industrial*), the specialized security interests tied to the *crédito refaccionario*, and the *crédito de habilitación y avío*, which brings to mind the personal property collateral devices (such as chattel mortgages and trust receipts) that were commonly used in the United States prior to the adoption of the Uniform Commercial Code. Although Mexico has had the advantage of a single commercial code (and other federal secured transactions laws) that apply to the entire country, rather than a system of separate state laws as in the United States, each of the thirty-two

38. *Ley de Concursos Mercantiles* [LCM] [Mexican Bankruptcy Law], as amended Diario Oficial de la Federación [DO], 12 de Mayo de 2000 (Mex.).

39. 11 U.S.C. § 1129(b)(2)(A) (2011).

40. See *Ley de Concursos Mercantiles* [LCM] [Mexican Bankruptcy Law], as amended, arts. 158, 160, Diario Oficial de la Federación [DO], 12 de Mayo de 2000 (Mex.).

states and the Federal District has its own civil code establishing a Public Registry system for real property deeds and mortgages (each such registry is a *Registro Público de la Propiedad*). Although personal property security filings are governed by the federal Commercial Code, they must be made in the commercial registry ("*Registro Público de Comercio*" or "RPC"), which is normally managed by a unit of the related State or municipal government, in the place of the debtor's domicile. Some of these locally managed commercial registries are less reliable than others, and significant delays are common in searching for existing liens and filing new security interests on collateral of companies domiciled in remote locations.

3. *The Non-possessory Pledge and the Guaranty Trust*

On the substantive side, Mexico has made significant progress since 2000 by amending the Mexican Commercial Code and the General Law of Credit Instruments and Transactions ("*Ley General de Títulos y Operaciones de Crédito*" or "LGTOC") to permit personal property security interests to be created more easily on a "floating lien" basis. A new type of non-possessory pledge called the *prenda sin transmisión de posesión* allows a debtor to pledge all of its inventory and receivables, for example, generically described (rather than described by reference to specific items), to a secured party without requiring that possession of the collateral be transferred to the secured party. This pledge can permit the debtor to sell the pledged collateral in the ordinary course of business without obtaining a case-by-case release from the secured party. And, it can automatically subject newly acquired property to the pledge without any further filing, which effectively results in a floating lien. A similar effect can be achieved through a guaranty trust (*fideicomiso de garantía*) with respect to the same or similar types of property, whereby title to the collateral is transferred to a Mexican trustee (typically a Mexican bank).⁴¹ Although these new devices resemble a security interest created in the United States under Article 9 of the UCC, lenders have remained reluctant to significantly expand their secured lending activities in Mexico because of ongoing concerns about their ability to perfect these security interests against third parties through the public registry system.

4. *UNCITRAL and the OAS Encourage Registry Reforms*

Recently, in an attempt to provide guidance for emerging market countries like Mexico that wish to improve access by borrowers to secured lending, the United Nations Commission on International Trade Law (UNCITRAL) has promoted reforms of the bankruptcy laws and secured transactions laws in such countries. Its 2008 Legislative Guide on Secured Transactions indicated the importance of a country having a "registry in which information about the potential existence of security rights in movable assets may be made public."⁴² In 2010, UNCITRAL decided to expand its work in this field by preparing a "model registry regulation," which is still in the process of preparation.

41. Published in the DO on May 23, 2000, with amendments published in the DO on June 13, 2003.

42. Legislative Guide on Secured Transactions of the UNCITRAL, GA Res. 63/121, U.N. GAOR, 63rd Sess., U.N. Doc. V.10-57126 (E) (Dec. 17, 2008).

The previous efforts of the Organization of American States (OAS) to adopt a Model Inter-American Law on Secured Transactions (“Model Law”)⁴³ appear to have influenced Mexico in its adoption of the non-possessory pledge concept. The OAS has also been tackling the registry issue. In October 2009, it held its Seventh Inter-American Conference on Private International Law, which approved Model Registry Regulations to “provide the legal foundation for implementing and operating the registry regime contemplated by the Model Law.”⁴⁴ Among other things, the Model Registry Regulations contemplate the adoption of electronic filing systems and acknowledge that most of their features were recommended in UNCITRAL’s 2008 Guide and included in the registry systems recently developed in some Latin American countries, including Mexico, as well as in the United States (the UCC), Canada (the Personal Property Security Act), and some European countries.

5. Mexico’s 2009 Commercial Code Amendments and Creation of the RUG

Mexico has been receptive to the objectives reflected by the UNCITRAL and OAS efforts. Not only did Mexico enact secured transactions law reforms in 2000 and in subsequent years to reflect many of the changes contemplated by the OAS’ Model Law, but Mexico’s initiatives with respect to public registry reforms have actually preceded the formal adoption of model rules by UNCITRAL and the OAS. In August 2009, a few months prior to the adoption of the OAS Model Registry Regulations, the Mexican Congress approved amendments to the federal Commercial Code that provide for the establishment of a Unified (or Sole) Registry of Movable Property Collateral (“*Registro Único de Garantías Mobiliarias*” or “RUG”).⁴⁵ The new Article 32 *bis* of the Code provides for the RUG (pronounced “roog”) to be a centralized registry for all types of security interests granted in favor of any creditor that carries out commercial activities (a *comerciante*) in personal property. The RUG will be a section of the PRC under the supervision of the Ministry of Economy (*Secretaría de Economía*), in which all filings are to be carried out electronically, through the RUG website, <http://www.rug.gob.mx>.

The stated congressional purpose of the RUG is to strengthen the system for personal property secured transactions “as an effective tool for access to credit.” Its main functions are to create a mechanism that allows public disclosure of security interests created on personal property and to establish priority rules for secured creditors. Filings through the RUG have immediate effect, without requiring any approval by any authority. Such filings can be made by financial institutions, public officials, public notaries (*notarios públicos*), or brokers (*corredores públicos*), and others authorized by the Ministry of Economy. Under Article 32 *bis* (4) of the amended Commercial Code, a debtor is generally deemed to have authorized any secured party creditor that is a *comerciante* to file evidence of the applicable security interest in the RUG. Article 32 *bis* (7) allows “any interested party” to request the

43. The Model Law was adopted on February 8, 2002, by the Sixth Inter-American Specialized Conference on Private International Law (known as “CIDIP-VI”, for its Spanish acronym). Organization of American States, CIDIP-VI, Final Act 3(f), OEA/Ser.K/XXI.6/ CIDIP-VI/doc.24/02 rev.3 (Mar. 5, 2002), available at <http://www.oas.org/dil/CIDIP-VI-finalact-Eng.htm>.

44. Approved by the Seventh Inter-American Specialized Conference on Private International Law (CIDIP-VII) at its second plenary session of October 9, 2009); quoted language appears in the Introduction.

45. Código de Comercio [CCo.] [Commercial Code], as amended Diario Oficial de la Federación [DO], 27 de Agosto de 2009 (Mex.).

issuance of a certification as to the filings that have been made in the RUG with respect to any debtor.

6. *New Registry Regulations*

On September 23, 2010, an executive decree was issued by Mexican President Felipe Calderón implementing the 2009 Commercial Code amendments by amending the Regulations governing the PRC to provide specifically for the inclusion of the RUG as a section of the overall PRC.⁴⁶ The amendments clarify how the RUG will operate through the electronic system called the Integrated System of Registry Procedures (“*Sistema Integral de Gestión Registral*” or “SIGER”) and the procedures to be followed for the use of the RUG by those who wish to (i) search it for the existence of existing security interests and (ii) perfect their own security interests as against third parties by filing notices. Anyone who registers with the RUG can initiate a search, but filings of security interests directly by an institutional creditor can only be done if the creditor entity has arranged to utilize an electronic signature for this purpose which satisfies the technical requirements contemplated by the Commercial Code.⁴⁷ Otherwise, the security interest must be filed on the creditor’s behalf by someone else authorized under the RUG to do so.

The provisions of the amended Regulations (“Amended Registry Regulations”) impose certain formalities which do not seem to be contemplated by the new Article 32 *bis* of the Commercial Code and may contravene the policy guidelines recommended by the OAS and UNCITRAL. For example, Article 10 of the Amended Registry Regulations provides for the RUG registrar or officer to verify that a filing has been properly made “in accordance with applicable legal and regulatory provisions,” which would seem to prevent the filing from becoming immediate and automatic, as provided in Article 32 *bis* (4) of the amended Commercial Code. Also, Article 10 *bis* of the Amended Registry Regulations specify that filings can only occur through a public authenticating officer (*fedatario*), i.e., a public notary (*notario público*) or broker (*corredor público*), although Article 30 *bis* seems to permit others, including financial entities, to make filings without using a *fedatario*. As a practical matter, until changes are made in Article 10 *bis* to allow filings to be made otherwise, it seems advisable to use a *fedatario* to carry out the filing. A number of law firms in Mexico employ *fedatarios*, so this should not be a significant impediment to the filing process or impose a significant additional cost. The use of a *fedatario* has the advantage of avoiding the requirement under Article 10 that the RUG registrar or officer verify the propriety of the filing; under Article 10 *bis* a filing by a *fedatario* has immediate effect.

7. *Preventive Filings*

Prior to the closing of a secured lending transaction, the proposed lender may wish to have the comfort that there will be no last-minute filings by other lenders of security interests that would have priority (based on time of filing) over any security interest to be filed to secure the transaction in favor of the proposed lender. To obtain such comfort, Articles 32 *bis* (5) of the Commercial Code amendments and 33 *bis* of the Amended Regis-

46. Código de Comercio [CCo.] [Commercial Code], as amended Diario Oficial de la Federación [DO], 23 de Septiembre de 2010 (Mex.).

47. *Id.*

try Regulations permit the proposed lender to make a filing prior to the scheduled closing, which will have the effect of preventing any other lender from making a filing that would have priority over the later definitive filing by the proposed lender of its own security interest. If the closing does not take place, the debtor need not seek removal of the preventive filing from the records of the RUG, because such filing would automatically cease to be effective after the passage of a specified period, normally two weeks.

8. *Information to be Provided in Filings through the RUG*

Article 33 *bis* (2) of the Amended Registry Regulations provides that the information that must be provided in the filing of the security interest will be (i) the name of the debtor or debtors granting the security interest, (ii) the name of the creditor or secured party, (iii) the type of security device utilized to create the security interest, (iv) the personal property securing the relevant obligations, (v) the secured obligations, (vi) the term or time frame during which the filing will be effective, and (vii) anything else contemplated by Article 33 of such regulations (i.e., anything else that may be required by the forms to be used in order to effect such filings, which are to be specified in a publication in the official Gazette ("*Diario Oficial*") of the Republic).

9. *Using the RUG*

As contemplated by the Amended Registry Regulations, to provide further guidance on using the RUG, the Ministry of Economy published a User's Guide ("*Guía de Usuario*") in Spanish providing additional guidance as to how the search and filing processes will operate.⁴⁸ The User's Guide shows how (i) a user can become registered with the RUG, (ii) searches can be performed, (iii) search certificates can be obtained, (iv) secured party creditors (whether organized or resident within or outside of Mexico) can be registered, and (v) the creditor's representatives can be registered in order to be entitled to submit filings on behalf of the creditor.

Mexican creditors can be registered online by including their Mexican tax ID numbers in the creditor information they provide. In the case of foreign creditors not having such numbers, the registration may be carried out at one of the designated offices of the Ministry or through a *fedatario*. Foreign creditors that wish to avoid delays at the closing of a secured loan may wish to become pre-registered before the closing. For cases involving multiple creditors, such as a syndicated loan, there is a separate procedure for entering the names of the additional creditors. As for the debtor, the filing form contemplated by the User's Guide mandates that it be filed electronically in such a way that the debtor's name is accompanied by an indication of whether the debtor is an individual or an entity and his or its nationality, registration file (*folio*) number and taxpayer ID or CURP number. A debtor that is an individual may be registered by a *fedatario* at the time of the filing of the security interest, but a debtor that is a company or other entity will have to have been registered in the PRC prior to the time of filing.

48. See *Guía del Usuario para el uso del sitio rug.gob.mx* [User Guide for Use of the rug.gob.mx Website], El Registro Único de Garantías Mobiliarias [Registry for Secured Transactions] (Mex.), <http://www.rug.gob.mx/Rug/resources/pdf/guia%20de%20usuario/Manual%20de%20Usuario%20RUG.pdf> (last visited Feb. 12, 2011).

According to the User's Guide, the filing of a security interest is to be effected by making entries in the electronic equivalent of a document akin to a UCC financing statement, which should specify:

- (i) the name and address of the person requesting the registration of the security interest;
- (ii) a description of the type of property subject to the security interest, such as "machinery and equipment" (the applicable type is to be selected from alternatives that appear on the screen);
- (iii) the type of security document under which the security interest was created, i.e. whether it was a non-possessory pledge, guaranty trust etc. (again, the selection is from the types indicated on the screen);
- (iv) the date of the relevant security agreement;
- (v) the maximum amount secured, specifying the applicable currency;
- (vi) a more detailed description of the property subject to the security interest;
- (vii) a description of the public deed issued before the *fedatario* which formalized the security agreement;
- (viii) a description of the agreement under which the secured obligation arose;
- (ix) optionally, any terms and conditions established by the documents; and
- (x) the period of time for which the filing is to remain effective.

The User's Guide provides examples of entries that are to be made in the online "financing statement," and indicates how the electronic signature is to be applied to the document in order to effect its filing.

The User's Guide includes similar instructions for related procedures, such as amendments, assignments, renewals, or reductions of the effective term of the filing; corrections of errors; cancellations; and "annotations" (*anotaciones*). The annotations might include information on any enforcement action with respect to the security interest, and would be made pursuant to instructions from a court or other authority. An annotation might result from a debtor challenging the propriety of the filing.

10. *Effect of the Reforms: Better than the UCC?*

The RUG is now the exclusive method in Mexico for perfecting security interests in inventory, receivables, equipment, and many other types of personal property; whether created through a possessory or non-possessory pledge, guaranty trust, or other device, the RUG supersedes all of the local public registries. However, security interests previously filed in the local registries will continue to be effective, so lenders must undertake searches as to any debtor in the locally-managed public registry responsible for such debtor's domicile until such time as the previously filed security interests are no longer effective (i.e., because they have been released or the related debt has been repaid) or otherwise satisfy themselves that no such filings have occurred (i.e., by obtaining representations and warranties from the debtor to this effect). Similar transition issues were encountered in the United States during the implementation of the UCC and its associated filing systems.

Two features are present in the Mexican situation that did not exist in the case of the adoption of the UCC. First, the RUG will be the sole registry in Mexico for filing security interests in personal property, unlike the separate filing systems in the fifty states of the

United States and in the District of Columbia and many local filing places such as the offices of County Clerks. Thus, the sometimes thorny question in the United States of where to file will not apply in Mexico. Secondly, the RUG is exclusively electronic, as opposed to the recordation systems in the United States, which initially relied entirely on paper filings and have only recently begun to transition to electronic systems, gradually, on a state-by-state basis.

It will still be necessary to comply with the relevant requirements for creating security interests, which in Mexico often requires that the security agreement or pledge agreement be formalized by the preparation by a *fedatario* of a formal deed (*escritura*). Instead of being recorded in the locally managed public registry, such deed should now be recorded in the RUG. Filings as to some types of collateral, such as vessels and aircraft, will continue to be made in specialized registries.

But with those exceptions, and despite some uncertainty created by the amended Regulations, the establishment of the RUG represents a huge step forward by Mexico in making secured lending an attractive option for borrowers and lenders alike.