

# RIGHTS AND PRIORITIES OF SECURED CREDITORS OF PERSONALTY IN MEXICO

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As Mexico develops economically and the purchasing power of the nation and its population expands, investment opportunities in that country will become increasingly attractive to United States businessmen. Before a foreign business moves part of its operations into Mexico, however, extensive study must be made of the legal rights and obligations the business will experience while operating there. For companies anticipating personal property credit transactions in Mexico, the system of creditors' rights under Mexican secured transactions law must be investigated.

The North American attorney studying creditors' rights and secured transactions in Mexico will find that Mexican law differs significantly from American law codified in the *Uniform Commercial Code* and the Bankruptcy Act. First, he will encounter highly systematized rules for determining priorities among competing creditors. The most important factor in determining priorities under these rules is the notice requirement—whether or not one creditor has perfected by registering his transaction so that subsequent creditors will have notice of it. The second most important factor in determining priorities will be decidedly strange to the United States attorney: priorities among

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The author wishes to express his sincere gratitude and thanks to Professor Boris Kozolchyk of the College of Law, University of Arizona, whose program in International and Comparative Law inspired this Article and without whose continuing help and expertise it would not have been possible. Others who counselled the author on specific points and whose contributions were taken with the greatest gratitude were Dr. Eugenio L. Revilla of the College of Law, University of Arizona, Professor Dale Furnish of the College of Law, Arizona State University, Lic. Gustavo J. Perez of Mexico City, Dr. Raul Cervantes Ahumada of Mexico City, and Lic. Erasmo Lozano Rocha of Cananea, Sonora, Mexico.

competing creditors are partially determined by the type of transaction in which each creditor is involved—whether or not, for example, the creditor is a mortgagee or conditional vendor. Additionally, the attorney will discover that a series of streamlined summary judicial proceedings are available to the creditor for enforcing his rights.

The practitioner will find little authority in Spanish language publications, and even less published in English, to help him understand this system. What authority he can find will often be contradictory and ultimately of little help. This Article is intended to provide a guide through the maze of Mexican law on creditors' rights in personal property transactions. The law governing installment sales, pledges, and chattel mortgages will be analyzed since these comprise the most used forms of credit transactions in Mexico. Consideration of each of these security devices will be subdivided into transactions falling under the *Código de Comercio* [Commercial Code]<sup>1</sup> and those governed by the more general *Código Civil para el Distrito* [Civil Code].<sup>2</sup> Additionally, the discussion of installment sales will distinguish between transactions where title passes immediately upon sale and those in which title is initially retained by the vendor.

#### INSTALLMENT SALES: CONDITIONAL SALES AND TITLE RETENTION CONTRACTS (COMPROVANTA: PACTO CON CLAUSULA RESCISORIA Y VENTA CON RESERVA DE LA PROPIEDAD)

Under the Mexican *Civil Code*, noncommercial installment sales may take the form of either a conditional sales agreement or a title retention contract (*venta con reserva de la propiedad*). In a conditional sale, title as well as possession passes to the buyer immediately upon sale.<sup>3</sup> In a title retention sale, title remains with the seller until payment is completed, even though the buyer obtains possession immediately.<sup>4</sup> Only when the buyer has completed his pay-

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1. C. COM. (Porrúa 1969).

2. C. CIV. DIST. Y TERR. FED. (Porrúa 1970) [CIVIL CODE FOR THE FEDERAL DISTRICT AND TERRITORIES]. In actuality each of the districts or states in Mexico has a civil code. Essentially, they are all similar to the civil code for the Federal District. Accordingly, this code will be used for illustrative purposes in this article.

3. *Código Civil para el Distrito y Territorios Federales* [Civil Code] article 2310 does not expressly stipulate that title as well as possession passes upon sale. Nevertheless, "transfer of title traditionally has been an essential element of a sale" in civil law countries. Warren, *Mexican Retail Instalment Sales Law: A Comparative Study*, 10 U.C.L.A.L. REV. 15, 19 (1962). Technically, title passes after the obligation and hence before possession. 4 ROJINA VILLEGAS, *COMPENDIO DE DERECHO CIVIL* 54-55 (3d ed. 1968). A comparison of articles 2310 and 2312 clearly indicates that title passes with the conditional sale contract. It is generally agreed that article 2312 provides for a special class of sales where the vendor retains title, with article 2310 applicable to the class where title is not retained. See Warren, *supra* at 19-20; Comment, *Security Interests in Movable Property in Mexico*, 4 TEX. INT'L L.F. 96, 108 (1968).

4. C. CIV. DIST. Y TERR. FED. art. 2312 (Porrúa 1970). Even where no rule ex-

ments does title vest in him. Both contracts may contain a rescissory clause (*pacto con cláusula rescisoria*). Under both types of transactions, the seller may seek his remedies upon the buyer's default, including rescission, when provided for in the contract, and reacquisition of possession and title.<sup>5</sup> There appears to be no requirement that the collateral in either type of sale be of a particular type such as consumer goods, equipment, or accounts. Instead, the sales agreements may govern either real (*bienes inmuebles*) or personal (*bienes muebles*) property, whether or not specifically identifiable.<sup>6</sup> The installment sales contract represents by far the largest percentage of buyer-seller transactions in Mexico.<sup>7</sup>

### *The Noncommercial Installment Creditor Against the Debtor*

The Mexican seller holding a valid installment sales agreement has rights in the transferred goods which are superior to those of the defaulting debtor, regardless of whether the agreement has been registered.<sup>8</sup> Some qualifications, however, pertain to situations where the goods are damaged or lost and where the buyer is disturbed in his possession by the seller.

In the conditional installment sale, where the collateral is in the seller's possession and is lost without the fault of either party through fortuitous events, the seller's obligation to deliver goods ceases unless otherwise agreed.<sup>9</sup> The *Civil Code* further provides that

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pressly provides for title retention contracts, as in the Mexican state of Oaxaca, such an agreement is valid if no law expressly prohibits it. Jaime Soriano Jiménez, XIX Semanario 6a 264 (A.D. 3392/56) (3a Sala 1959).

5. C. Civ. Dist. y TERR. FED. art. 2310 (Porruá 1970). Rescission upon default of payment (*pacto comisorio*) is legal in installment sale contracts, and the right to enter into such agreements may not be derogated by state law. Inmobiliaria Volcano S.A., XXXIX Semanario 6a 25 (A.D. 7765/58) (3a Sala 1960). For discussion of the *pacto comisorio*, see text & note 119 *infra*.

6. C. Civ. Dist. y TERR. FED. arts. 2310-12 (Porruá 1970). Notwithstanding the lack of limitation on property subject to sale by installment, sales of various types of property leave the vendor with differing rights against third parties. *Id.*

7. Cf. 4 ROJINA VILLEGAS, *supra* note 3, at 44-45. Most installment sales contracts are of the title retention type. Warren, *supra* note 3, at 19.

8. See C. Civ. Dist. y TERR. FED. arts. 2310-12 (Porruá 1970). The Mexican supreme court ruled in Isauro Herrera Ruiz, XIX Semanario 6a 264 (A.D. 7966/57) (3a Sala 1959), that a provision in the state of Veracruz' civil code making registration necessary to defeat third parties should not be construed to mean that registration was necessary to defeat the debtor himself. In Mexico, registration is merely declarative, not constitutive of a transaction. Carlos Laguna Govantes, XV Semanario 6a 263 (A.D. 3649/56) (3a Sala 1959); María Matamoros Vda. de Soria, XV Semanario 6a 275 (A.D. 103/57) (3a Sala 1959); Simón A. García, XIX Semanario 6a 215 (A.D. 6604/57) (3a Sala 1959); C. Civ. Dist. y TERR. FED. art. 3003 (Porruá 1970). See also UNIFORM COMMERCIAL CODE § 9-201. For an authoritative discussion of the concept of registration in Mexico, see Kozolchyk, *The Mexican Land Registry: A Comparative Evaluation*, 12 ARIZ. L. REV. 308 (1969).

9. C. Civ. Dist. y TERR. FED. art. 2017(V) (Porruá 1970). Although article 2017 uses the term "debtor," that term in civil law countries may mean—as it does here—one who is obligated to deliver a chattel. Warren, *supra* note 3, at 22.

Note that the seller will be presumed at fault if the goods are in his possession,

in such a case the "owner suffers the loss,"<sup>10</sup> the buyer being the owner in a conditional sale. Presumably, therefore, the buyer's duty to pay the contract price continues despite loss of the goods. The seller is required, however, to assign to the buyer all rights to indemnify arising from the loss.<sup>11</sup>

Where the goods are fortuitously lost while in the buyer's possession, no *Civil Code* provision specifically governs risk of loss. Arguably, however, the results are the same as when the goods are lost in the seller's possession. If the code places the onerous risk of loss on the buyer when the seller has possession, a *fortiori* the risk remains on the buyer when the goods are lost in his possession.

The *Civil Code* provisions governing risk of loss under conditional sales contracts probably do not apply to title retention contracts, since those provisions were enacted prior to the recognition of the retention contracts by the code.<sup>12</sup> Rather, under article 2315 of the code, the title retention buyer in possession of the goods is placed in the position of a lessee. Risk of loss is on the buyer, unless it is established that he was without fault, in which case the risk passes to the seller.<sup>13</sup> The obvious implication is that where goods are lost in the possession of the seller, with or without his fault, the risk of loss is on him.<sup>14</sup> Alternatively, if the risk of loss in retention sales is to be governed by the *Civil Code* provisions governing risk in conditional sales, the results as to allocating risk are the same as if a conditional sale were involved. This is because, despite the fact that title is in the seller in a retention sale, the Mexican supreme court has held that the buyer is a "conditional owner."<sup>15</sup>

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unless proved otherwise. *C. Civ. Distr. y Terr. Fed.* art. 2018 (Porrúa 1970). When goods in the possession of the seller are lost or destroyed through his fault, he is liable to the buyer for damages and losses and, at the buyer's request, may be required to deliver deteriorated goods with an abatement in price. *Id.* arts. 2017(I)-(II). When goods in the possession of the seller are lost through the buyer's fault, the seller's obligation to deliver ceases. *Id.* art. 2017(III). When goods in the possession of the seller are deteriorated through the buyer's fault, the buyer is obliged to receive the goods in their deteriorated condition. *Id.* art. 2017(IV).

10. *C. Civ. Distr. y Terr. Fed.* art. 2017(V) (Porrúa 1970). Sellers usually protect themselves by stipulating that the buyer bears the risk of loss. Warren, *supra* note 3, at 22-23.

11. *C. Civ. Distr. y Terr. Fed.* art. 2020 (Porrúa 1970).

12. Warren, *supra* note 3, at 21-22.

13. *C. Civ. Distr. y Terr. Fed.* art. 2468 (Porrúa 1970). See also Warren, *supra* note 3, at 22. Sellers usually protect themselves by stipulating that the buyer bears the risk of loss.

Note that the transfer of title is an element of all installment sales, whether conditional or title retention. 4 ROJINA VILLEGAS, *supra* note 3, at 104. Thus, article 2024 which provides for risk of loss where the giving of property does not imply the transfer of its ownership is inapplicable.

14. Cf. *C. Civ. Distr. y Terr. Fed.* art. 2018 (Porrúa 1970) (presenting seller at fault where goods are lost in his possession).

15. See Carlos Vales Cámara, XXXVIII Semanario 6a 69 (A.D. 2156/59) (3a Sala 1969); Felisa Maya, LXII Semanario 6a 87 (A.D. 3246/61) (3a Sala 1962). Note that

In addition to cases where the collateral is lost or damaged, the buyer will not be liable where the seller has disturbed the possession of the buyer. In this situation the buyer may withhold payments and demand assurances from the seller.<sup>16</sup> If the seller then attempts judicial action, the disturbance is a defense to the seller's threat of rescission for suspension of payments.

Where the buyer remains subject to the seller's rights, the seller has two basic remedies upon default. The seller may demand compliance,<sup>17</sup> essentially the concept of specific performance, and the seller also may receive indemnity for damages and losses.<sup>18</sup> Alternatively, the seller may rescind the agreement. Rescission for nonpayment may be accomplished in one of two ways: solely upon the seller's declaration where the agreement so provides or upon declaration and judgment of a court.<sup>19</sup> Where judicial rescission is required, if the seller accepts a late payment, the seller loses his right to rescind.<sup>20</sup> Once rescission occurs, the contract is void and both parties return to their precontract positions.<sup>21</sup>

To be fully restored to his precontract position, the seller must not only rescind his contract, but also must repossess the goods. Repossession by self-help is generally not permitted in Mexico.<sup>22</sup> Where judicial rescission is required, the seller must resort to the courts for re-possession. Even where rescission may occur immediately upon default without judicial action, the seller may be forced into the courts to regain possession of the goods.

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the buyer's position as a conditional owner is contrary to the status accorded him by article 2315.

16. C. CIV. DIST. Y TERR. FED. art. 2299 (Porrua 1970), *interpreted in* Carmen Salgado Rodriguez, VI Semanario 6a 101 (A.D. 7233/56) (3a Sala 1957).

17. C. CIV. DIST. Y TERR. FED. art. 1949 (Porrua 1970). *See* ROJINA VILLEGAS, *supra* note 3, at 140-41.

18. C. CIV. DIST. Y TERR. FED. arts. 1949, 2104-05, 2255, 2296(III) (Porrua 1970).

19. *See* Banco National de Crédito Ejidal S.A., CXXIII Semanario 5a 538 (A.D. 5061/52) (3a Sala 1955).

In regard to nonpayment, there is no delay in payment where the debtor attempts to make payments but is frustrated because seller has moved and has failed to notify debtor of his new address. Jardines del Pedregal de San Angel S.A., [1961] Informe 43 (A.D. 102/60) (3a Sala). Similarly, the Mexican supreme court has ruled that bills of exchange (*letras de cambio*) constitute merely a guarantee of payment and not payment itself under article 2310. Therefore, seller's possession of debtor's letters guaranteeing payment does not satisfy debtor's obligations, and the seller may rescind upon debtor's failure to make timely cash payments. María Encarnación Galíndez Vda. de Blancos, XIV Semanario 6a 123 (A.D. 5715/57) (3a Sala 1958).

20. Where the seller agrees to permit the debtor extra time to make payment, no rescissory action may be brought against the debtor. Marcelino Arellano Flores, XXXIII Semanario 6a 177 (A.D. 3730/59) (3a Sala 1960).

21. C. CIV. DIST. Y TERR. FED. art. 2311 (Porrua 1970).

22. Although self-help is generally against public policy in Mexico, Warren, *supra* note 3, at 42, in title retention contracts sellers probably may retake their collateral so long as they do not resort to criminal violence. *See* Kozolchyk, *Law and the Credit Structure in Latin America*, 7 VA. J. INT'L L. 1, 8 (1967).

The *Código de Procedimientos Civiles para el Distrito y Territorios Federales* [Code of Civil Procedure] provides for an "Executory Action" to enforce rescission aspects of conditional contracts containing a rescissory clause<sup>23</sup> and all title retention contracts.<sup>24</sup> Registration of the original agreement is necessary before the action may be brought.<sup>25</sup> Since the executory procedure provides the only expeditious device by which a volume creditor may obtain rescissory relief, registration of the contract becomes a necessity in order to obtain full protection against defaulting debtors.

The seller using the executory procedures finds himself in a very good position vis-à-vis the debtor-buyer. Once the seller notifies the buyer of his decision to declare default and retake the collateral, the buyer may contest the rescission or return the collateral.<sup>26</sup> Upon contestation by the buyer, the goods which are the subject of the dispute may be sequestered by the court.<sup>27</sup> If the goods no longer exist, other goods of the same value may be attached.<sup>28</sup> If the seller prevails in the action, he must deposit with the court the money he has received from the buyer's payments plus interest.<sup>29</sup> From this amount he may first deduct as indemnization an amount equal to the depreciation (*demérito*) of the goods.<sup>30</sup> This amount may be either specified in the contract or determined by the court,<sup>31</sup> although in either case it appears that experts must be consulted before the amount is fixed.<sup>32</sup> If the contract goods still exist, they must be delivered to the seller.<sup>33</sup> Whether or not the goods still exist, the buyer must pay, in

23. C. PRO. CIV. DIST. Y TERR. FED. arts. 443 *et seq.*, 464-67 (Porruá 1972) [CODE OF CIVIL PROCEDURE FOR THE FEDERAL DISTRICT AND TERRITORIES]. It should be noted that *Code of Civil Procedure* article 465 applies only to contracts of sale containing a "resolutorily condition" (*condición resolutoria*). Article 1940 of the *Civil Code* defines a resolutorily condition as a condition where "upon its occurrence it annuls the obligation and things return to their former status, as if the obligation has not existed." This definition clearly includes the installment sale contract where the buyer's default gives the seller a right to rescission or cancellation placing the parties in their former positions.

24. C. PRO. CIV. DIST. Y TERR. FED. art. 466 (Porruá 1972). *Id.* art. 467.

25. *Id.* art. 467.

26. *Id.* art. 464.

27. *Id.* art. 451.

28. *Id.* However, the debtor may avoid attachment by depositing cash sufficient to cover the debt. *Id.* art. 463.

29. C. CIV. DIST. Y TERR. FED. art. 2311 (Porruá 1970).

30. C. PRO. CIV. DIST. Y TERR. FED. art. 465 (Porruá 1972). Article 2311 of the *Civil Code* also provides that upon rescission the seller may require the buyer to pay the value of rent and indemnity for deterioration of the collateral as fixed by experts. This indemnity corresponds in time of payment and apparent purpose to the *demérito* mentioned in article 465 of the *Code of Civil Procedure*. Except for the fact that the indemnization is to be determined by experts, while the *demérito* is to be determined either in the contract or by the courts in their discretion, they appear to be the same charge. The Supreme Court of Mexico has stated that experts will aid in setting the amount of the depreciation, but the experts' exact role is not clear. Carlos Vales Cámaras, XXXVIII Semanario 6a 69 (A.D. 2156/59) (3a Sala 1960).

31. C. PRO. CIV. DIST. Y TERR. FED. art. 465 (Porruá 1972).

32. See text & note 30 *supra*.

33. C. CIV. DIST. Y TERR. FED. art. 2311 (Porruá 1970).

addition to depreciation, rental for the period the goods were held.<sup>34</sup> Since the contract is rescinded, the seller need not accept cash payment as an alternative to delivery.

### *The Noncommercial Installment Creditor Against Third-Party Creditors*

Anytime a Mexican debtor does not meet his financial obligations to a creditor, insolvency technically exists.<sup>35</sup> Only when insolvency exists will the unpaid creditors be compelled to compete formally with each other for payment, with the resulting chance that one or more will take a loss. Thus, the *Civil Code* rules for insolvency govern all cases involving noncommercial conflicts between creditors, a fact which is difficult to comprehend for United States attorneys who are not accustomed to applying their bankruptcy law to every such conflict.<sup>36</sup>

When insolvency occurs, the *Civil Code* provides for six categories of creditors. Of highest preference are, first, "Mortgage and Pledge Credits and Several Other Privileged Credits,"<sup>37</sup> and second, "Certain Preferred Creditors with Respect to Certain Property."<sup>38</sup> Following these creditors respectively in preference are creditors of the "First," "Second," "Third," and "Fourth" classes. "Privileged creditors" include tax lienors, mortgagees, and pledgees.<sup>39</sup> The "preferred" category includes creditors who have made sales on time to the defaulting debtor.<sup>40</sup> The lowest four classes may be broadly characterized as general or unsecured creditors.<sup>41</sup> It should be noted that the Mexican Constitution provides that materialmen's liens have priority over all other obligations in the event of receivership or bankruptcy.<sup>42</sup> The preference system established in the *Civil Code* is, of course, subject to this provision.

These statutory categorizations of transactions play a crucial role in determining creditors' priorities in insolvency. Priorities in con-

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34. *Id.* Although article 2315 states that the title retention buyer will be considered a lessee, the buyer assumes a lessee's position only for certain purposes. Carlos Vales Cámara, XXXVIII Semanario 6a 69 (A.D. 2156/59) (3a Sala 1960). The conditional buyer's payment of rent as prescribed by article 2311 indicates that to this extent, at least, he too is a lessee, even though under the conditional sale contract he already has title.

35. C. CIV. DIST. Y TERR. FED. art. 2965 (Porrúa 1970).

36. Under section 3 of the Bankruptcy Act, 11 U.S.C. § 21 (1970), bankruptcy can be declared for several reasons. None of these reasons is equivalent to the common default which constitutes bankruptcy in Mexico.

37. C. CIV. DIST. Y TERR. FED. arts. 2980-92 (Porrúa 1970).

38. *Id.* art. 2993.

39. *Id.* arts. 2980-81.

40. *Id.* art. 2993 (VIII).

41. *Id.* arts. 2994-98.

42. MEX. CONST. art. 123(A)(XXIII).

tested property will be determined according to the category into which each creditor's transaction falls. Thus, a creditor of the first, or "privileged," category always has priority in the contested goods over members of the second, or "preferred," category. This preference structure is not subject to attack by any figure equivalent to the trustee in bankruptcy found in the United States. Only if a Mexican creditor has secured a preference by some fraudulent act will his preference be voided.<sup>43</sup> Otherwise he need not worry about "gap creditors" or "hypothetical creditors."

1. *The Conditional Sales Vendor with a Registered Rescissory Clause.* The preference position of the conditional sales vendor with a registered rescissory clause is not entirely clear. His status will depend upon the effect registration of the rescissory clause has against third parties.

Upon rescission, the vendor is entitled to reacquire the goods sold.<sup>44</sup> It is clear under article 2310 of the *Civil Code* that where the clause has been registered, the vendor may reacquire against a subsequent purchaser. Specifically, that article provides that the clause "shall produce effects against third persons who have acquired the property in question, provided the clause of rescission was recorded in the public registry."<sup>45</sup> It is not clear, however, whether the phrase "persons who have acquired the property" (*adquirido*) includes secured parties, such as mortgagees, as well as mere purchasers. If secured parties are included, then the vendor also may reacquire directly against them without participating in insolvency proceedings.

If secured parties are not included within the phrase, the position of the vendor remains unclear. Article 2310, by failing to mention secured parties, may be construed by negative implication as providing that registered rescissory clauses are only effective against subsequent purchasers. In this case the vendor with a registered rescissory clause would have only the rights of an unregistered conditional vendor as against secured third parties.<sup>46</sup> On the other hand, article 2310 does not expressly preclude effect against secured third parties and therefore need not be read as precluding its applicability to such parties. Moreover, articles 2311, 3002, and 3003, when read together, seem to contemplate that registered rescissory clauses are effective against subsequent third-party creditors secured by the vendor's

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43. C. CIV. DISTR. Y TERR. FED. arts. 2971(III), 2979 (Porrúa 1970).

44. *Id.* art. 2311.

45. *Id.* art. 2310.

46. See text & notes 49-54 *infra*.

goods.<sup>47</sup> Thus, despite the possible contrary application of 2310, the vendor with a registered rescissory clause may still be permitted to reacquire against secured third parties without participating in insolvency proceedings.<sup>48</sup>

2. *Conditional Vendors Without Registered Rescissory Clauses.* Conditional vendors without rescissory clauses and conditional vendors with unregistered rescissory clauses fall within the second, or "preferred," category of preferences. This is evident from the wording of *Civil Code* article 2993 which describes the second category.<sup>49</sup> As a member of the second highest category of creditors, the conditional vendor's priority rights are clearly defined.<sup>50</sup> To share in the disposition of the debtor's assets he must participate in insolvency proceedings in which the general creditors agree to a division of the assets not secured to mortgagees and pledgees, members of the higher "privileged" category.<sup>51</sup> He will be paid that percentage of the total assets specified in the agreement unless he decides to contest the agreement in court.<sup>52</sup> So long as he makes his claim within 60 days after maturity of the debt, however, the conditional vendor will not lose his preference among the general creditors or other creditors of his category to an amount equal to the proceeds from the property he sold to the debtor.<sup>53</sup> This preference, of course, will be valueless to the extent the property has been mortgaged or pledged.<sup>54</sup>

3. *The Registered Title Retention Vendor.*<sup>55</sup> It is not clear

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47. Article 2311 requires restoration of the goods to the vendor upon rescission without qualification. Articles 3002 and 3003 contemplate that only registered documents may produce effects against third parties.

48. Note that this construction of the effect of a registered rescissory clause in a conditional sale is consistent with the apparent consequence of a registered title retention stipulation in a title retention sale. See text & notes 55-57 *infra*. An inconsistent construction would exalt form over substance. In both the registered title retention and registered conditional sale cases, third parties are given constructive notice. Beyond that, the difference is purely procedural. In one case, notice is given of a right to rescind, in the other, of a retention of title.

49. C. CIV. DIST. Y TERR. FED. art. 2993 (Porrua 1970), states in part:

With the value of the property here mentioned, the following shall be paid with preference:

... VIII. Credits arising from the price of property sold and not paid, with the value of the same, if the creditor makes his claim within sixty days . . . after maturity, if the sale was on time.

Accord, ROJINA VILLEGAS, *supra* note 3, at 139.

50. C. CIV. DIST. Y TERR. FED. arts. 2964-79 (Porrua 1970).

51. *Id.* art. 2969. It is illegal to make private deals with the debtor after insolvency has been declared. *Id.* art. 2968.

52. *Id.* art. 2970.

53. *Id.* arts. 2967, 2993(VIII).

54. Moreover, article 2993(VIII) provides that the vendor will lose his right to payment from the proceeds of this property if it becomes immovable prior to insolvency.

55. *Civil Code* article 2312 provides that the title retention vendor, like the conditional sales vendor, may not register transactions involving "unidentifiable" or intangible personal property. Specifically, that article provides that such property shall be governed by article 2310(III), which states that transactions in such goods may not be

whether the title retention vendor is a member of the second preference category or whether, due to his retention of title, his goods never enter insolvency proceedings. The wording of the insolvency laws, which place sales on time in the second category,<sup>56</sup> suggests that the title retention vendor also is included in that category. On the other hand, the title retention seller does not retain merely a right to rescind his contract as does the conditional sales vendor. Instead, he retains title in the collateral itself, an interest equal to or greater than the rights of "privileged" creditors such as mortgagees or pledgees. Since the goods are not assets of the debtor, they probably may be entirely excluded from insolvency proceedings.

Due to the nature of the title retention sale, the vendor has the same preference rights in his collateral whether he is a member of the second category or whether his goods are exempt from insolvency entirely. Since the vendor retains title, his property cannot be subjected to the vendee's tax liabilities nor may they be pledged or mortgaged by the vendee.<sup>57</sup> Thus, there can be no member of either the "privileged" or "preferred" category who have a security interest in the vendor's goods. Accordingly, the registered title retention vendor has rights superior to all general creditors and creditors of the first and second categories.

4. *The Unregistered Title Retention Vendor.* Like the conditional vendor, the title retention vendor who fails to register will suffer adverse consequences. According to *Civil Code* article 2312, if the title retention vendor is unregistered, his attempt to retain title is not effective against third parties.<sup>58</sup> Consequently, if registration does not occur

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registered and that third-party *purchasers* in good faith will be unaffected by *rescissory* clauses. But article 2312, unlike article 2310(III), applies to all third parties rather than solely purchasers, and title retention clauses rather than rescissory clauses. Thus, the provisions of article 2310(III), read in the light of article 2312, must be taken to mean that title retention clauses incapable of registration will leave unaffected all third parties acting in good faith. Therefore, in referring to the rights of the registered title retention vendor, this Article also will be referring to the rights of the unregistered title retention vendor dealing in intangibles as against third parties acting in bad faith. Where a third party has acted in good faith, the title retention vendor's rights will be the same as those of the unregistered conditional sales vendor. *See* text & note 58 *infra*. It should be noted that at least for third-party purchasers, good faith will be difficult, if not impossible, to establish. *See* text & note 214 *infra*.

56. C. CIV. DIST. Y TERR. FED. art. 2993(VIII) (Porrua 1970).

57. *Id.* arts. 2856, 2868, 2906. In Mexico, one cannot claim to be a bona fide encumbrancer until he has checked the public registry to determine that the other party has title. *See* discussion note 213 *infra*. Since the vendee cannot record title which he does not have, there could never be a bona fide mortgagee or pledgee to challenge the rights of the vendor, whether or not the vendor has registered. In United States law, the location of title is irrelevant to creation of a security interest. *See* UNIFORM COMMERCIAL CODE §§ 9-112, -202.

58. C. CIV. DIST. Y TERR. FED. art. 2312 (Porrua 1970). Where the collateral is intangible goods, however, even the unregistered transaction will be effective against good faith creditors. *Id.* *See* discussion note 55 *supra*. Therefore, in speaking of the rights of the unregistered title retention vendor, the discussion in this section is not in-

cur, the title retention vendor has the status of an unregistered conditional vendor as against third parties. As such, he drops from a position of unassailable priority in the goods to a position as a member of the second priority category, like all other unregistered conditional vendors.

### *Rights Against Third-Party Purchasers*

Where the goods are of a type by which registration can protect the seller against third parties,<sup>59</sup> the installment vendor's registration will give him rights over any third-party purchasers.<sup>60</sup> Where registration does not occur, however, the installment vendor's rights against third-party purchasers are not so simply stated.

Generally, where a creditor does not register his transaction, it has no effect against third-party purchasers, and the collateral is lost.<sup>61</sup> This is not always true, however. For example, the unregistered installment vendor may defeat the interests of a third-party purchaser when the second transaction renders the original vendee insolvent.<sup>62</sup> If both the debtor and the third party have knowledge of the debtor's impending insolvency, the transaction will be in bad faith and therefore void,<sup>63</sup> even if the second sale is for a valuable consideration. If the transaction was gratuitous, it will automatically be void if it results in the debtor's insolvency,<sup>64</sup> unless the third party has possession of the collateral.<sup>65</sup> In the latter case, the third party must act in bad faith, that is, with knowledge of the debtor's insolvency,<sup>66</sup> before the transaction may be voided.<sup>67</sup> Annulment of the transaction may be avoided by the debtor satisfying his debt to the vendor<sup>68</sup> or by payment or guarantee of payment to the vendor by the third party.<sup>69</sup> Otherwise, the third party will be required to return the collateral to the debtor<sup>70</sup> along with payment for any loss caused if

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tended to include the rights of the vendor where the collateral is intangible and the third party has acted in good faith. Such a transaction gives the vendor the same rights as a registered vendor. These rights are discussed in text & notes 55-57 *supra*.

59. C. CIV. DIST. Y TERR. FED. art. 2310(III) (Porrua 1970), states that where the collateral is personal property which is not indubitably identifiable registration may have no effect against third parties. On the other hand, a transaction involving such collateral is automatically effective against bad faith third-party purchasers. *Id.*

60. *Id.* arts. 2310-12, 3002-03.

61. *Id.* art. 2310.

62. *Id.* art. 2163. Under this article, insolvency means that assets are less than liabilities. *Id.* art. 2166. The burden falls on the debtor to prove his solvency. *Id.* art. 2178.

63. *Id.* arts. 2164, 2166.

64. *Id.* art. 2165.

65. *Id.* art. 2167.

66. *Id.* art. 2166.

67. *Id.* art. 2167.

68. *Id.* art. 2174.

69. *Id.* art. 2176.

70. *Id.* art. 2168.

he acquired in bad faith.<sup>71</sup>

## COMMERCIAL INSTALLMENT SALES (LA COMPRAVENTA MERCANTIL)

Commercial installment sales are governed by the *Commercial Code* of Mexico, except that where that code is silent on a matter the *Civil Code* will apply.<sup>72</sup> An installment sale will be commercial in nature if it is made as a part of trade or exchange.<sup>73</sup> In addition, the *Commercial Code* states that its provisions apply to purchases and sales of "mercantile" property,<sup>74</sup> while the civil code of the local state applies to the purchase and sale of personality. The *Commercial Code* indicates that in determining what is "mercantile" or "commercial" one must consider the nature of the transaction,<sup>75</sup> the parties' commercial intent,<sup>76</sup> their intent to resell upon purchase,<sup>77</sup> the nature of the goods,<sup>78</sup> and the status of the parties.<sup>79</sup> Where these factors do not clearly identify the transaction as commercial or civil, the transaction is referred to as "mixed" (*acto de naturaleza mercantil condicionada*).<sup>80</sup> Authorities disagree as to whether these mixed transactions will be governed by the substantive law of the *Commercial Code* or the *Civil Code*.<sup>81</sup> Regardless of how this issue is ultimately resolved,<sup>82</sup> creditors' priorities under the *Commercial Code* require consideration.

### *The Commercial Installment Creditor Against the Debtor*

Both conditional sale and title retention contracts are provided

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71. *Id.* art. 2169.

72. C. COM. art. 2 (Porrúa 1969). In actuality, the civil code of the state in which the transaction occurred will apply, but the *Civil Code* of the Federal District will be used for illustrative purposes. See discussion note 3 *supra*.

73. C. COM. art. 371 (Porrúa 1969). The English words "trade and exchange" are used here as a translation of the Spanish "traficar."

74. *Id.*

75. *Id.* art. 75, sets forth a lengthy, but nonexclusive list of "commercial transactions."

76. *Id.* art. 75(I).

77. 4 ROJINA VILLEGAS, *supra* note 3, at 60.

78. C. COM. art. 75(III) (Porrúa 1969).

79. There is a presumption that transactions between businessmen are commercial in nature. 4 ROJINA VILLEGAS, *supra* note 3, at 61; see C. COM. arts. 4, 51 (Porrúa 1969). *But see id.* art. 76.

80. MANTILLA MOLINA, DERECHO MERCANTIL 51 (11th ed. 1968).

81. C. COM. art. 1050 (Porrúa 1969), states that the procedural rules of the *Commercial Code* will govern such transactions, at least where the plaintiff is the party who performed the commercial act. Normally, a vendor such as a department store will be the plaintiff. Thus, the *Commercial Code* will usually govern.

82. Warren, *supra* note 3, at 56, argues that "the more sound view is that since a retail buyer is committing a civil act when he purchases goods, his rights should be entirely governed by the . . . [Civil Code]." Superficially, this view is consistent with the unilateral act doctrine—where the transaction is "mixed," the code governing the defendant should apply. Since the retail buyer is the defendant in most cases, the *Civil Code* governing him will govern the whole transaction. C. CIV. DIST. Y TERR. FED. art. 1050 (Porrúa 1970). The latter view, however, will not always require the same result as the former. Where the buyer institutes an action for breach against the seller, the second view would require application of the *Commercial Code*, but the first view would support application of the *Civil Code*.

for in the *Commercial Code*, although the vendor's right to retain title must be inferred from a provision that an agreement is subject to all lawful stipulations expressed in a contract.<sup>84</sup> The commercial or mercantile installment contract automatically includes the right to rescind upon default, but both parties have this right, not just the vendor.<sup>85</sup> Thus, the vendor is protected against the buyer's default in commercial transactions just as he is in noncommercial transactions.

There are two methods in addition to rescission through which the commercial installment vendor may enforce his rights and settle disputes with the buyer. First, where the dispute concerns the quality of the collateral or conformity of the collateral to advertising, two arbitrators will be named by the contracting parties to settle the disagreement. If these two arbitrators cannot settle the dispute, a third will be appointed.<sup>86</sup> Second, where the vendor desires to foreclose the debt, he may use the "Executory Proceeding."<sup>87</sup> In this proceeding, the debtor has 3 days to present defenses to execution on the attached property.<sup>88</sup> This property may include not only the original collateral but other property of the buyer.<sup>89</sup> If the buyer fails to present defenses, the attached items may be levied upon.<sup>90</sup> In any case, a judgment must follow within 1 week of the original attachment.<sup>91</sup> If, however, the defendant presents evidence, he may have 15 additional days to prove his defense.<sup>92</sup> If the goods are auctioned, the vendor may purchase them at the price for which similar goods were last auctioned so long as no other bidder appears.<sup>93</sup> Apparently, this procedure, as well as other procedures pertaining to the sale, may be changed by agreement of the parties.<sup>94</sup>

The *Commercial Code* does not parallel the *Civil Code* in allo-

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83. See generally C. COM. arts. 371 *et seq.* (Porrúa 1969).

84. *Id.* art. 372. One may only assume that the title retention provision is lawful under the *Commercial Code* since it is nowhere prohibited, and it is permitted under the *Civil Code*.

85. C. COM. art. 376 (Porrúa 1969).

86. *Id.* art. 373.

87. *Id.* arts. 1391-414. Article 1391(VII) states that Executory Proceedings may be used when the action is based upon "invoices, *current accounts* and all other commercial contracts signed and judicially acknowledged by the debtor." (Emphasis added.)

88. *Id.* art. 1399.

89. The creditor may attach property sufficient to satisfy his debt in the following order:

- I. The merchandise sold;
- II. Credits of easy and speedy collection, sufficient to satisfy the creditor;
- III. Other personality of the debtor;
- IV. Realty
- V. Other rights and actions held by the debtor.

*Id.* art 1395.

90. *Id.* art. 1404.

91. *Id.* art. 1407.

92. *Id.* art. 1405.

93. *Id.* art. 1412.

94. *Id.* art. 1413.

cating the risk of loss between buyer and seller. The *Commercial Code* unequivocally places the risk of loss on the buyer once the goods have been delivered to him.<sup>95</sup> Presumably, the installment vendee remains liable to the vendor for any balance remaining to be paid on goods lost or destroyed. If the loss occurs prior to delivery, the vendor bears the loss of the goods and bargain.<sup>96</sup> In this case, presumably, the installment vendor must return any sums already paid by the vendee. Of course, if the loss is due to the negligence of some identifiable party, he will be liable to the contracting party required to bear the loss.<sup>97</sup>

### *Rights Against Third-Party Creditors*

As with the risk of loss, the commercial installment vendor does not fare exactly as does the noncommercial vendor against third parties. To see this, some digression into the Mexican law of commercial creditors' priorities will be necessary. First, any commercial vendor who has possession of the goods at time of default will have priority over all other creditors.<sup>98</sup> Therefore, there is a great advantage in selling goods on lay-away. In all other cases, however, the debtor's creditors must compete according to the timing and quality of their interests in the collateral, as governed by the *Le de Quiebras y Suspensión de Pagos* [Commercial Bankruptcy Law].<sup>99</sup> That law provides for five classes of creditors: (1) singularly privileged creditors, (2) mortgagees (*hipotecarios*), (3) creditors with a special privilege, (4) common commercial creditors, and (5) common civil creditors. The first class, singularly privileged creditors, comprises the debtor's funeral and last medical expenses and employee creditors.<sup>100</sup> The second consists solely of mortgagees.<sup>101</sup> Creditors who "under the *Commercial Code* or special laws have a special privilege or right of retention"<sup>102</sup> constitute the third class. Like the mercantile pledgee, the installment creditor falls into this class since he holds a special

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95. *Id.* art. 377.

96. *Id.*

97. *Id.*

98. *Id.* art. 386.

99. LEY DE QUIEBRAS Y DE SUSPENSIÓN DE PAGOS (Porruá 1969) [LAW OF COMMERCIAL BANKRUPTCY AND SUSPENSION OF PAYMENTS]. For a general outline of commercial bankruptcy in Mexico, see GENERAL SECRETARIAT, ORGANIZATION OF AMERICAN STATES, A STATEMENT OF THE GENERAL LAWS OF MEXICO IN MATTERS AFFECTING BUSINESS 56-62 (4th ed. 1970) [hereinafter cited as O.A.S.]. Bankruptcy occurs not only when the debtor's assets are less than his liabilities, as in the United States, but also when he fails to make payments consistent with his financial obligations. See *Ley de Quiebras y de Suspensión de Pagos* article 2, for a list of situations in which the debtor will be presumed unable to meet his obligations.

100. LEY DE QUIEBRAS Y DE SUSPENSIÓN DE PAGOS art. 262 (Porruá 1969).

101. *Id.* art. 263.

102. *Id.* art. 264.

privilege, the right of rescission, and since he is granted this right under the *Commercial Code*.<sup>103</sup>

As a member of the third class of creditors, the installment creditor has rights inferior to the singularly privileged creditors and registered mortgagees. This means that the installment creditor will receive no satisfaction whatsoever from the debtor's assets until all members of the classes above him have been fully satisfied.<sup>104</sup> Additionally, any persons who have incurred expenses for administration or conservation of any of the debtor's assets will have rights to the proceeds arising from the bankruptcy sale or distribution of these assets which are superior even to the rights of the singularly privileged creditors.<sup>105</sup> On the other hand, the registered installment creditor has rights superior to all general creditors, either commercial<sup>106</sup> or noncommercial.<sup>107</sup> Of course, if the installment creditor fails to register and does not retain possession of the collateral, his transaction will be ineffective against third parties,<sup>108</sup> and he will participate in bankruptcy only as a common creditor of one of the lowest classes.

Among themselves, the rights of members of the third preference class, including the installment creditor, are determined according to three principles. If the transaction is subject to registration, the creditor's priority in the debtor's estate will be established by the date of registration.<sup>109</sup> If the transaction is not subject to registration, the creditor takes by date of his transaction.<sup>110</sup> Anytime any of the creditors are secured by the same property, however, they share pro rata, without regard to dates,<sup>111</sup> and to the exclusion of all creditors of the third or lower classes not secured by the object.

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103. One authority has interpreted *hipotecarios* of the second class to mean all secured creditors, which would include title retention vendors. Comment, *supra* note 3, at 144. Materials published by both the Organization of American States and the National Association of Credit Management, however, translate *hipotecarios* to mean solely mortgagees. O.A.S., *supra* note 99, at 61; 3 NATIONAL ASSOCIATIONS OF CREDIT MANAGEMENT, DIGEST OF COMMERCIAL LAWS OF THE WORLD ch. 15, at 27 (1971). Not only do the latter two authorities appear more experienced in this area of the law, but their translation seems consistent with the wording *Ley de Quiebras y de Suspensión de Pagos* article 264.

104. LEY DE QUIEBRAS Y DE SUSPENSIÓN DE PAGOS art. 269 (Porrua 1969).

105. *Id.* arts. 269-70.

106. *Id.* art. 266.

107. *Id.* art. 267.

108. C. COM. art. 26. If the creditor's transaction is commercial in nature, see text & notes 72-81 *supra*, the creditor will probably be placed in the class just under that of the "creditors with a special privilege." Otherwise, the transaction will be civil in nature and the creditor will become a member of the next and last class, the "common creditors under the civil law."

109. LEY DE QUIEBRAS Y DE SUSPENSIÓN DE PAGOS art. 265 (Porrua 1969) (referring to art. 263).

110. *Id.* art. 265.

111. *Id.* Whether this provision applies only to transactions not subject to registration or to all transactions in the third class is not clear. The article could be interpreted

To state priority rights in another way, installment creditors retain a preferential interest in their own collateral just as do mortgagees.<sup>112</sup> Thus, in the absence of unsatisfied claims by creditors of higher classes, installment creditors take first rights in their collateral unless other secured creditors of their class, such as pledgees, are also competing for an interest in the same property. In this event, the creditors share pro rata in the collateral's proceeds. To the extent that the installment creditor's debt is not satisfied, however, he has equal rights with all other creditors of his class to look to the balance of the debtor's assets before members of any lower class.<sup>113</sup>

### *Rights Against Third-Party Purchasers*

The *Commercial Code* does not alter the relative preference positions established by the *Civil Code* for original vendors and subsequent purchasers.<sup>114</sup> As noted, however, under commercial law the original vendor will retain an absolute preference in collateral in his possession. Thus, an unregistered installment vendor in possession could defeat a third-party purchaser.

### **THE PLEDGE (LA PRENDA)**

There are two types of pledges in Mexico, the traditional pledge (*prenda*) and the mercantile pledge (*prenda mercantil*). The former is derived from the ancient Roman pledge (*pignus*) and is treated in the *Civil Code*. The latter, provided for in the *Ley General de Títulos y Operaciones de Crédito* [*General Law of Instruments and*

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so that the only creditors who share pro rata in the proceeds are those competing for an interest in the same collateral and whose contracts are not subject to registration. This interpretation would mean that members of the third class whose contracts are subject to registration would continue to take priority by date of registration even when competing for the same collateral. This seems most consistent with that portion of the article which provides that members of the third class whose transactions are subject to registration take as do mortgagees: by date of registration only, with no provision for priorities. *See id.* art. 263. Such a reading, however, creates unjustifiable distinctions for purposes of determining priorities. The party who registers serves no better notice of his interest than does the pledgee, for example, who possesses the collateral but is not required to register. Thus, any distinction as to determining priorities is unjustified. Moreover, if creditors other than those subject to registration shared pro rata while other creditors participated by date of registration, the provision would be glaringly deficient in failing to provide which group participated first in the collateral by which they are all secured.

112. *Id.* art. 265 (referring to art. 263).

113. *Id.* art. 269. See C. COM. art. 386 (Porrua 1969), which provides that an installment creditor in possession of the goods has an absolute priority in them.

114. See text & notes 59-71 *supra*. The only difference between commercial and noncommercial preferences in this area is in the rules used. *Commercial Code* article 26 corresponds exactly to *Civil Code* article 3003. The *Commercial Code* does not contain any other applicable rules on this matter, and it is therefore necessary to apply the *Civil Code* to determine preferences against purchasers. C. COM. art. 2 (Porrua 1969).

*Credit Operations]*,<sup>115</sup> was developed to provide a more practical means of securing pledges' interests in commercial transactions. Due to significant differences between the two, the traditional pledge will be considered separately in this section. The commercial pledge will be discussed in the following section.

### *Rights Against the Debtor*

The *Civil Code* defines the traditional pledge as a "property right over movable alienable goods (*muebles*) for the purpose of guaranteeing the performance of an obligation and its priority of payment."<sup>116</sup> The basic provisions for the pledge are found in articles 2856 through 2892 of the *Civil Code*. Under these provisions, a pledge is effectuated by either actual or constructive delivery<sup>117</sup> and a written agreement of pledge.<sup>118</sup>

Where the two basic requirements of a pledge are satisfied, the creditor will have sufficient rights to bind the debtor and to seek remedies against him in the pledged collateral. In the event the debtor defaults on his payments, "the creditor may demand and the judge shall decree the sale of the pledged object at public auction . . ."<sup>119</sup> If collateral cannot be sold at public auction,<sup>120</sup> it is given

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115. LEY GENERAL DE TÍTULOS Y OPERACIONES DE CRÉDITO (Porruá 1969) [GENERAL LAW OF INSTRUMENTS AND CREDIT OPERATIONS].

116. C. CIV. DIST. Y TERR. FED. art. 2856 (Porruá 1970). The pledge has been defined as:

an accessory contract by virtue of which the debtor or a third person delivers to the creditor a specific and alienable thing to guarantee the performance of a separate principal obligation, giving the creditor a contingent right of sale and priority of payment in the event of breach of the principal obligation by the debtor. If the principal obligation is performed the creditor must return the object.

4 ROJINA VILLEGRAS, *supra* note 3, at 456-57.

117. C. CIV. DIST. Y TERR. FED. art. 2858 (Porruá 1970). Constructive delivery may occur in two ways: "when the creditor and the debtor agree that it remain in possession of a third person [known in the United States as a warehousing agreement], or when it remains in possession of the debtor himself because he so stipulated with the creditor or the law expressly so provides." *Id.* art. 2859. The latter type of constructive delivery is called "pledge without dispossession" (*prenda sin disposición*). This type of arrangement is permitted only in noncommercial pledges. See text & notes 160-61 *infra*. The "pledge without dispossession" is conceptually similar, but administratively superior to the chattel mortgage because of its simplified procedural aspects. See text & notes 181-83 *infra*.

118. C. CIV. DIST. Y TERR. FED. art. 2860 (Porruá 1970). Registration is never required for mere constitution of a pledge in Mexico, although it may be required to make the pledge effective against third parties. *Id.* arts. 2859-60; see Alejo Roberto Pérez, XLIII Semanario 6a 78 (A.D. 5438/60) (3a Sala 1961); Simón A. García, XIX Semanario 6a 215 (A.D. 6604/57) (3a Sala 1959); Carlos Lagunas Govantes, XV Semanario 6a 263 (A.D. 3649/56) (3a Sala 1959); María Matamaros Vda. de Soria, XV Semanario 6a 275 (A.D. 103/57) (3a Sala 1959).

119. C. CIV. DIST. Y TERR. FED. art. 2881 (Porruá 1970). See also *id.* art. 2887. These provisions apply the general rule that the *pacto comisorio* (a right to nonjudicial rescission of the contract by the creditor upon the debtor's default, resulting in the creditor keeping the pledged object) is illegal in pledge arrangements. José Montano Oceguera, [1961] Informe 21 (A.D. 3571/60) (3a Sala); see 3 G. CABANALLAS DICCIONARIO

to the creditor for two-thirds of the legal bid.<sup>121</sup> The debtor, however, may agree that upon default the creditor may keep the collateral at a price determined at the time of maturity of the debt<sup>122</sup> or that the pledged item may be sold extrajudicially.<sup>123</sup> The creditor will not be permitted to contract to keep the pledged item without some sort of payment for it.<sup>124</sup> Regardless of which of the foregoing procedures is used, the debt due must be reduced by any proceeds earned from the collateral and received by the creditor while pledged, since these proceeds belong to the debtor.<sup>125</sup>

The creditor often does not obtain the full value of his debt from the sale of the collateral. First, the sale of the object may not yield proceeds sufficient to satisfy the debt. Second, the *Civil Code* recognizes that the creditor or the constructive holder of the collateral will have administrative expenses which may be deducted from the proceeds of the collateral before the balance is applied against the principal debt. In the event that sale of the collateral does not satisfy the debt, the pledgee may sue the debtor for the balance.<sup>126</sup>

Where the pledged collateral is lost or deteriorates without the creditor's fault,<sup>127</sup> he has the right to demand from the debtor another pledge or immediate payment of the debt, even though the debt has not matured.<sup>128</sup> The creditor is not required to accept replacement collateral or a security bond, and he may, in his discretion, rescind the contract entirely.<sup>129</sup> If the collateral is insured, the law requires the insurance company, upon notice of loss or deterioration, to pay the creditor all amounts due him until the insurance coverage is exhausted.<sup>130</sup> Any loss of deterioration of the collateral caused by

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DE DERECHO USUAL 9 (1954). Such an agreement, however, is legal in installment sales. See discussion note 5 *supra*.

120. C. CIV. DIST. Y TERR. FED. art. 2881 (Porrúa 1970). Relief through attachment or levy may be obtained through summary proceedings (*juicio ejecutivo*), C. PRO. CIV. DIST. Y TERR. FED. arts. 443 *et seq.* (Porrúa 1972), unless issues arise related to the manner in which the agreement was constituted or created. Gerber, *Secured Credit Devices in Latin America: A Comparison of Argentina, Brazil, and Mexico*, 23 U. MIAMI L. REV. 677, 686 (1969), citing R. FERNANDEZ, DE LA HIPOTECA, LA PRENDA, Y DEMÁS PRIVILEGIOS 171 (1941).

121. C. CIV. DIST. Y TERR. FED. art. 2882 (Porrúa 1970). The term "legal bid" apparently refers to the judicially determined fair value of the merchandise.

122. *Id.* art. 2883. This provision should be distinguished from the *pacto comisorio*, see discussion note 119 *supra*, since the creditor must pay for the collateral to keep it and since the price determination occurs only *after* default.

123. C. CIV. DIST. Y TERR. FED. art. 2884 (Porrúa 1970).

124. *Id.* art. 2887.

125. *Id.* art. 2880.

126. *See id.* art. 2886.

127. The creditor is required "[t]o preserve the pledged article as if it were his own . . . ." *Id.* art. 2876(I). If the creditor meets this standard of care, he will not be liable for loss or damages to the collateral. *Id.* arts. 2877-78.

128. *Id.* art. 2873(IV).

129. *Id.* art. 2875.

130. LEY SOBRE EL CONTRATO DE SEGURO art. 109 (Porrúa 1969) [LAW OF INSURANCE CONTRACTS].

the creditor's lack of care<sup>131</sup> will be at his expense.<sup>132</sup> Where the creditor fails to exercise care, the debtor may, if the contract so stipulates, demand that the collateral be deposited with a third-party bailee or that the creditor "give security to return it in the condition in which he received it."<sup>133</sup> Thus, upon the debtor's demand, the creditor may not merely restore the collateral but must provide the debtor with assurance that the collateral will be restored. The creditor may tender cash to the debtor, pledge an object to the debtor as security, or deposit cash or other collateral with a third party.

### *Rights Against Third-Party Creditors*

1. *Where the Pledgee Has Registered.* The pledgee must perfect his interest against third parties by registering or annotating in a public document the date of the pledge if the pledged object either remains in the hands of the debtor or is delivered to a third party.<sup>134</sup> If the creditor takes actual possession of the collateral, registration of the transaction is not necessary in order to perfect.<sup>135</sup> Where the pledgee has properly registered, his rights against third parties are very strong. The pledgee shares the highest of the *Civil Code* preference categories with the mortgagee.<sup>136</sup> Hence the pledgee need not participate with the "preferred" and the general creditors in the insolvency proceedings but may take direct action to obtain compensation from his collateral.<sup>137</sup> Only the government, as a tax lienor, will have a higher preference to the proceeds of his collateral.<sup>138</sup>

Among competing mortgagees and pledgees, preference priorities are determined by the recording date for mortgages and by the transaction dates for pledges.<sup>139</sup> Thus, a pledge takes priority whenever it is created before the mortgage, provided the date of the pledge is properly registered.<sup>140</sup> Whenever parties disagree about their preferences, summary court proceedings may be taken under the *Code of Civil Procedure* to adjudicate priority rights.<sup>141</sup>

Where the debtor retains possession of the collateral, the pledge without dispossession (*la prenda sin disposición*), other creditors are

131. See discussion note 127 *supra*.

132. C. CIV. DIST. Y TERR. FED. art. 2876(I) (Porrúa 1970).

133. *Id.* art. 2877.

134. *Id.* arts. 2859-60. See Gerber, *supra* note 120, at 684.

135. See C. CIV. DIST. Y TERR. FED. art. 2859 (Porrúa 1970).

136. *Id.* arts. 2981 *et seq.* See text accompanying notes 35-43 *supra*.

137. C. CIV. DIST. Y TERR. FED. art. 2981 (Porrúa 1970).

138. *Id.* art. 2980.

139. *Id.* arts. 2982, 2985(IV).

140. *Id.* arts. 2859, 2860. Registration of the date of the pledge is not required if the date is recorded in a "public instrument, or in some other authentic manner." *Id.* art. 2860.

141. C. PRO. CIV. DIST. Y TERR. FED. art. 430(XVIII) (Porrúa 1972).

unlikely to have notice of the pledge. Apparently for this reason, the pledgee who leaves possession with the debtor must always register his transaction to preserve his position among other pledgees and mortgagees. Yet, probably due to an oversight in the *Civil Code* caused by the relatively recent provision permitting a pledgor to retain possession, the registered pledgee's priority is established as of the date of the pledge rather than date of registration.<sup>142</sup> Nevertheless, the code clearly seems to intend that the notice be a primary factor in determining priorities among members of the highest category of creditors. This is evident since, where possible, priorities are established in accordance with the date of constructive notice of the pledge.<sup>143</sup> The *Civil Code* should be modified to recognize that where the debtor retains the collateral other creditors do not have constructive notice of the pledge transaction. This may be accomplished by providing that the pledge without dispossession is effective against third parties only from the time of registration.

Where the registered pledgee loses priority to another member of his category, the balance of the proceeds may not be sufficient to satisfy his debt. In that case, the pledgee may sue as a member of the "third class" of creditors to obtain the balance due on his debt.<sup>144</sup>

2. *Where the Pledgee Has Not Registered.* Where the pledgee has failed to register his transaction when required by law, it has no effect against third parties.<sup>145</sup> In that case the pledgee loses his status as a member of the first category of creditors. Although his position is not entirely clear, it appears that he participates in the insolvency proceedings only as a general creditor. If his transaction appears in a public instrument or other authentic document,<sup>146</sup> he may may participate as a member of the "third class," the second lowest group of creditors.<sup>147</sup> If only a private document were used, he will be cast into the "fourth class," the last category of creditors.<sup>148</sup> He

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142. C. CIV. DIST. Y TERR. FED. 2985(IV) (Porrúa 1970).

143. *See id.* arts. 2857, 2860 (requiring registration to make the pledge effective against third parties, who thereby have constructive notice of the transaction).

144. *Id.* art. 2983.

145. Registration is required where the collateral is crops or other anticipated proceeds from land, *id.* art. 2857, when the collateral remains in the possession of the debtor, *id.* art. 2859, or when the collateral is a credit document. *Id.* art. 2861. In addition, no "pledge shall take effect against third persons if the date is not proved by a registry, a public instrument, or in some other authentic manner." *Id.* art. 2860.

146. *Id.* art. 2860. It is not the purpose of this Article to attempt to define what constitutes an "authentic" document. However, an "authentic" document appears to mean one that is "authenticated" by an official and is not strictly private in nature. Cf. Kozolchyk, *supra* note 8, at 321. Such documents would include those executed before a notary public and those issued by courts or administrative boards.

147. C. CIV. DIST. Y TERR. FED. art. 2996 (Porrúa 1970).

148. *Id.* art. 2992.

will share with members of his appropriate category in the debtor's property that remains after all other creditors have been satisfied according to the agreement resulting from the insolvency proceedings. Among themselves, members of a category shall be paid according to the date of their documents, if such date appears in an indubitable manner. In any other case, they shall be paid pro rata.<sup>149</sup>

### *Rights Against Third-Party Purchasers*

If the debtor alienates either right of title or possession of pledged collateral to a third party, the third party cannot demand delivery without first paying the amount of the debtor's obligation, along with interest and expenses.<sup>150</sup> This provision helps guarantee to the creditor that the debtor at all times will have sufficient assets to satisfy the debt. There is, however, no guarantee that the debtor in possession of collateral will demand such payment from the third party or that the debtor will preserve any amount paid by the third party until the debt matures.

If the debtor cannot pay, the creditor's remedy, if any, is against the third party holding the collateral, provided that the pledgee has properly perfected his interest against third parties. As noted, the pledgee must perfect by taking actual or constructive possession of the collateral or by registering his transaction when the debtor retains possession.<sup>151</sup> Additionally, the pledgee is always required to register the date of his transaction or to document that date by public instrument in order to establish his priority in the collateral.<sup>152</sup> Where the pledgee has failed to properly perfect, he will find himself defeated by the third-party purchaser. Even if the pledgee plans to take possession, if a third party purchases before possession is obtained, the intervening purchase will defeat the pledgee's interest in the collateral.<sup>153</sup> The only exception to this rule is when the sale to a third party results in the pledgor's insolvency, then the creditor will be able to defeat the third party.<sup>154</sup>

### **THE MERCANTILE PLEDGE (LA PRENDA MERCANTIL)**

It is often difficult to determine whether a pledge is commercial or noncommercial in nature. If the pledge is commercial, it will be called a mercantile pledge and will be governed by the *Gen-*

149. *Id.* art. 2977.

150. *Id.* art. 2879.

151. *Id.* art. 2859.

152. *Id.* art. 2860.

153. *Id.* art. 2872.

154. See text & note 64 *supra*.

eral *Law of Instruments and Credit Operations*,<sup>155</sup> rather than by the *Civil Code*. Although the *General Law of Instruments and Credit Operations* does not indicate when a pledge is commercial, its predecessor enactment, title 11 of the *Commercial Code of 1887*, stated that a pledge was a mercantile act when it guaranteed an act of commerce.<sup>156</sup> Transactions which are considered acts of commerce are specified in article 75 of the present *Commercial Code*. Thus, pledges which guarantee these transactions are mercantile pledges subject to the provisions of the *General Law of Instruments and Credit Operations*. With this notion of the meaning of mercantile pledge, it is possible to discuss the credit preferences held by the mercantile pledgee.

### *Rights Against the Debtor*

It should be clear from previous discussion that generally a secured creditor in Mexico, whether registered or not, will have better rights in the collateral than will the defaulting debtor. Although this rule usually applies to mercantile pledges,<sup>157</sup> there are two instances in which registration is required for the pledge to become binding even on the original parties. Registration is necessary where the collateral is an instrument (*título nominativo*) which is of a type required by law or contract to be registered.<sup>158</sup> Registration also is required where there is a credit transaction for the operating or financing of equipment (*contratos de crédito refaccionario o de habilitación o avío*).<sup>159</sup> In these instances, the creditor must register in order to acquire any rights in the collateral as against the debtor. In addition to these registration requirements, the *General Law of Instruments and Credit Operations* also requires actual delivery of the collateral to the creditor of a third party,<sup>160</sup> eliminating the advantages of the pledge without dis-

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155. LEY GENERAL DE TÍTULOS Y OPERACIONES DE CRÉDITO arts. 334-45 (Porruá 1969).

156. C. Com. art. 605 (1887). The definition found in the *Commercial Code of 1887* is accepted by contemporary Mexican authority. See MANTILLA MOLINA, *supra* note 80, at 68.

157. See LEY GENERAL DE TÍTULOS Y OPERACIONES DE CRÉDITO arts. 334(III), (VIII) (Porruá 1969) (prescribing the requisites for a pledge and therefore its effectiveness between parties, without requiring registration).

158. *Id.* art. 334(II) (referring to art. 24).

159. *Id.* art. 334(VII). *Los contratos de crédito refaccionario y de habilitación o avío* are special forms of credit provided for in article 326. For a description of such transactions, see Gerber, *supra* note 120, at 701-03.

160. Banco Comercial Mexicano, [1956] Bol. Info. Jud. 671 (A.D. 475/56) (3a Sala); Oscar Torres, CXIII Semanario 5a 943 (A.D. 1105/43) (3a Sala 1952); LEY GENERAL DE TÍTULOS Y OPERACIONES DE CRÉDITO art. 334 (Porruá 1969).

A pledge of warehoused goods may be made by pledging the warehouseman's certificate of deposit. A pledge certificate (*bono de prenda*) may also be issued by the warehouseman and, if it is, will be required along with the certificate of deposit to obtain the collateral from the warehouseman. If bearer instruments are pledged, they will be

possession.<sup>161</sup>

The *General Law of Instrument and Credit Operations* has several provisions directly relating to the creditor's rights over the debtor. First, proceeds derived from the collateral during the pledge arrangement and received by the creditor belong to the debtor and must be credited towards payment of the debt unless otherwise agreed.<sup>162</sup> Second, when the goods pledged are fungible goods or instruments, the creditor's rights in those items continues even though other goods or instruments of the same kind are substituted.<sup>163</sup> Thus, with fungible collateral the creditor may maintain his priority under a warehousing agreement or any other agreement constituting a floating lien. Moreover, there is some authority that this floating lien will be valid while the collateral is in the hands of a third party<sup>164</sup> or while the debtor has possession if the creditor has access to the storage area.<sup>165</sup> Thus, in this limited situation a pledge without dispossession may exist in Mexican commercial law.

The mercantile pledge protects the creditor's interest in two ways. First, where the value of the collateral falls below the value of the debt plus 20 percent, the creditor has the right to petition the court for permission to sell the collateral.<sup>166</sup> The debtor may oppose this sale by pledging new collateral which brings the aggregate value of the collateral to 120 percent of the debt level.<sup>167</sup> Alternatively, the debtor may decide to pay the entire amount due, thus terminating the pledge arrangement.<sup>168</sup> Second, where the debtor defaults upon maturity of the debt, the creditor also may petition for sale. The debtor may oppose this sale only by completing the required payments.<sup>169</sup>

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endorsed to the creditor but will be endorsed as being *en garantía* or *en prenda* (either a guarantee of payment or the actual pledge), thereby protecting the debtor from fraudulent assignment of the instrument. LEY GENERAL DE TÍTULOS Y OPERACIONES DE CRÉDITO art. 36 (Porruá 1969). If registered shares are pledged, they must not only be endorsed but the pledge must be noted in the company's register. H. WRIGHT, FOREIGN ENTERPRISE IN MEXICO 320 (1971).

161. See discussion note 117 *supra*; H. WRIGHT, *supra* note 160, at 318.

162. LEY GENERAL DE TÍTULOS Y OPERACIONES DE CRÉDITO art. 338 (Porruá 1969).

163. *Id.* art. 335; *see id.* art. 343 (providing for substitution where a pledged instrument or shares mature and are converted to cash). The latter provision permits the creditor to keep all cash proceeds until the principal debt matures. At that time he must pay any excess to the debtor.

The Spanish word "fungibles" means consumable, fungible, or expendable in English. L. ROBB, DICTIONARY OF LEGAL TERMS: SPANISH-ENGLISH AND ENGLISH-SPANISH 60 (5th ed. 1973).

164. LEY GENERAL DE TÍTULOS Y OPERACIONES DE CRÉDITO art. 334(IV) (Porruá 1969). *But see* discussion accompanying note 160 *supra* (indicating that a commercial pledge requires actual rather than merely constructive delivery).

165. LEY GENERAL DE TÍTULOS Y OPERACIONES DE CRÉDITO art. 334(V) (Porruá 1969).

166. *Id.* art. 340.

167. *Id.* art. 342.

168. *Id.*

169. *Id.* art. 341.

As an alternative to petitioning for sale, the seller may seek a written agreement from the debtor which makes the creditor the owner of the collateral.<sup>170</sup>

### *The Pledgee Against Third-Party Creditors*

Where the mercantile pledgee is compelled to compete with any third parties for shares in the defaulting debtor's assets, the commercial preference rules, as found in the Mexican bankruptcy law, will govern priorities among the parties. Of the five preference classes existing under these commercial bankruptcy provisions,<sup>171</sup> the mercantile pledgee is clearly a member of the third class. Like the installment creditor, the mercantile pledgee has a special privilege under the rules of the *General Laws on Instruments and Credit Operations*. The pledgee's membership in this class gives him rights inferior not only to singularly privileged creditors holding rights to payment of certain final debts of the debtor but also to mortgagees. This is a significant change from *Civil Code* provisions which provide that mortgagees and pledgees are equal members of the same preference class.<sup>172</sup> In addition, all pledgees take their share of the debtor's assets only after payment of administrative or maintenance costs on any of debtor's assets.<sup>173</sup>

The pledgee's rights against members of his own class are the same as those already described for the installment creditor.<sup>174</sup> If the pledgee is the only party claiming rights in his collateral, he alone will have the right to satisfaction of his debt from the proceeds of the collateral. If other parties secured in that collateral are competing for the proceeds from it, however, the pledgee will share pro rata with these parties. Where his debt is not satisfied in this way, he retains the right to compete with members of his own class, on the basis of the date of his registration or transaction, for payment from the other assets of the debtor before payment to any lower classes. Finally, since actual deposit or delivery of the collateral is necessary to create a valid commercial pledge,<sup>175</sup> a pledge which is effective between the pledgor and pledgee will always be effective against third parties. This is because such parties will always have notice by vir-

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170. *Id.* art. 344.

171. LEY DE QUIEBRAS Y DE SUSPENSIÓN DE PAGOS art. 261 (Porrúa 1969).

172. Compare C. CIV. DIST. Y TERR. FED. arts. 2980-92 (Porrúa 1970), with LEY DE QUIEBRAS Y DE SUSPENSIÓN DE PAGOS art. 261 (Porrúa 1969).

173. See LEY DE QUIEBRAS Y DE SUSPENSIÓN DE PAGOS art. 264 (Porrúa 1969).

174. See text & notes 72-114 *supra*.

175. C. COM. art. 334 (Porrúa 1969). Note that registration is also required to validate a pledge of certain instruments or a pledge securing credit for the operating or financing of equipment. See text & notes 158-61 *supra*.

tue of pledgee's actual or constructive possession. Thus, the commercial pledgee need never fear losing his preference status.

### *The Pledgee Against Third-Party Purchasers*

As noted, where a mercantile pledge is effective between pledgor and pledgee, it also will be effective against all third parties.<sup>176</sup> Thus, the creditor with a valid mercantile pledge will have an interest in the collateral which is superior to that of any subsequent third-party purchaser. Otherwise, the pledge contract will be null and void for lack of proper constitution,<sup>177</sup> and the pledgee will be defeated by the third-party purchaser.

### **NONCOMMERCIAL CHATTEL MORTGAGE (HIPOTECA SOBRE BIENES MUEBLES)**

The *Civil Code of 1884* limited application of the mortgage concept to immovables or real property.<sup>178</sup> The word *inmuebles*, literally meaning immovables, is not, however, used to define mortgages in the present code.<sup>179</sup> It is generally agreed that this obvious change in the definition of mortgage means that the mortgage concept has been expanded in Mexico to include the chattel mortgage.<sup>180</sup>

The role of the noncommercial chattel mortgage in Mexican commercial transactions remains ill-defined. It is conceptually identical to the pledge without dispossession (*prenda sin disposición*).<sup>181</sup> Yet greater formalities and controls exist under the mortgage than govern the pledge.<sup>182</sup> Thus, the chattel mortgage is a less desirable form of security than the pledge.<sup>183</sup>

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176. See text accompanying note 175 *supra*.

177. See LEY GENERAL DE TÍTULOS Y OPERACIONES DE CRÉDITO art. 334 (Porrúa 1969).

178. C. Civ. Dist. y Terr. Fed. art. 1823 (1884).

179. C. Civ. Dist. y TERR. FED. art. 2893 (Porrúa 1970), provides: "Mortgage is a guaranty in rem constituted on property which is not delivered to the creditor, and giving the latter the right, in case of nonfulfillment of the guaranteed obligation, to be paid with the value of such property, in the degree of preference established by law."

180. 4 ROJINA VILLEGAS, *supra* note 3, at 353; Gerber, *supra* note 120, at 699. But see ROJINA VILLEGAS, *supra* note 3, at 356 ("The mortgage is a real right which is constituted over determined goods, generally of the immovable (real property) type . . . " (emphasis added)); H. WRIGHT, *supra* note 160, at 314, 316 (acknowledging that chattel mortgages are legal but not often used and suggesting the reason for disuse is that the chattel mortgage cannot be recorded). For discussion of the nonrecordability of chattel mortgages, see note 199 *infra*.

181. For discussion of the *prenda sin disposición*, see Gerber, *supra* note 120, at 690; Kozolchyk, *supra* note 22, at 7; text preceding note 142 *supra*.

182. "There are . . . greater formalities and controls upon the mortgage device, such as special registration and foreclosure procedures, which in most circumstances would make it less desirable than the pledge." Gerber, *supra* note 120, at 699. Another disadvantage of the chattel mortgage, as opposed to the pledge, is that the mortgagee often cannot obtain an interest in the proceeds of the collateral. See text & notes 190-93 *infra*.

183. See discussion note 180 *supra*.

### *The Chattel Mortgagee Against the Debtor*

Whether or not his transaction has been registered, the chattel mortgagee has the right to be paid with the sale proceeds of the mortgaged property when the debtor defaults on his payments.<sup>184</sup> To obtain sale of the collateral, however, the creditor must bring a summary judicial action.<sup>185</sup> This requirement is consistent with Mexico's general policy against self-help.<sup>186</sup> The mortgage action has generally the same characteristics as the already described summary action available to installment creditors.<sup>187</sup> If he is so motivated, the creditor may bid for the collateral at the judicial sale or, if no other bidders appear, may be granted ownership of the collateral by adjudication.<sup>188</sup> Alternatively, the parties may agree in their contract that there be no judicial sale and that the creditor be adjudicated owner of the collateral at a price set by the parties. The price, however, may not be set until after maturity of the mortgage debt.<sup>189</sup> If the debtor expressly agrees, the mortgagee may have as additional security two types of proceeds from his collateral:<sup>190</sup> (1) the industrial proceeds of the property mortgaged provided they are produced before the creditor demands payment of the debt,<sup>191</sup> and (2) the rents due and unpaid at the time when fulfillment of the guaranteed obligation is demanded.<sup>192</sup> Where the collateral is insured and then damaged, the mortgagee is automatically entitled to any insurance proceeds and a continued security interest in the remaining property.<sup>193</sup>

A limitation on the creditor's rights against the debtor operates where several properties are mortgaged to secure a single debt. In such a case, the parties must determine the portion of the debt to which each item of property is subject. As that portion of the debt secured

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184. C. CIV. DIST. Y TERR. FED. art. 2893 (Porrua 1970); C. PRO. CIV. DIST. Y TERR. FED. art. 469 (Porrua 1972). Registration generally has only declarative, not constitutive, effect in a transaction. *See* discussion note 8 *supra*.

185. C. PRO. CIV. DIST. Y TERR. FED. art. 468 (Porrua 1972). The *pacto comisorio*, under which a creditor has the right to keep the collateral without court adjudication, is illegal in mortgage arrangements. José Montano Oceguera, [1961] *Informe 21* (A.D. 3571/60) (3a Sala).

186. *See* text & note 22 *supra*.

187. *See* C. PRO. CIV. DIST. Y TERR. FED. arts. 468-88 (Porrua 1972); text & notes 23-28 *supra*.

Moreover, it is clear that in such an action the mortgagee need prove only that the mortgage exists and that he has the right to satisfaction of his debt; the burden of proving completion of payments is on the debtor. Esparanza Soto Rueda, *XXXVI Semanario 6a 98* (A.D. 7146/58) (3a Sala 1960).

188. C. CIV. DIST. Y TERR. FED. art. 2916 (Porrua 1970).

189. *Id.*

190. A mortgage does not automatically extend to fruits of the collateral. *See id.* arts. 2895-96.

191. *Id.* art. 2897. This class would seem to include proceeds from the use of mortgaged goods as they are enhanced or changed through manufacture.

192. *Id.*

193. *Id.* art. 2910.

by any given property is paid, that property must be released from the mortgage.<sup>194</sup> This process may place the creditor in a dangerous position where the value of any of the mortgaged property decreases substantially, since in this situation the chattel mortgagee has no right to demand additional collateral to secure the debt.<sup>195</sup> Consequently, the debtor may satisfy his mortgage on all but those properties which have suffered the greatest decrease in value and then default, leaving the creditor with worthless properties from which to satisfy his debt.

### *The Chattel Mortgagee Against Third-Party Creditors*

The *Civil Code* states that for a chattel mortgage to be effective against third parties<sup>196</sup> it must be registered.<sup>197</sup> With the exception of liens<sup>198</sup> and various administrative and maintenance expenses,<sup>199</sup> the insolvency provisions of the *Civil Code* give the registered mortgagee, along with the pledgee, the highest priority rights among all of the creditors of the defaulting debtor.<sup>200</sup>

Generally, the mortgagee will have priority in his collateral over other mortgagees or pledgees according to the date of registration of his transaction.<sup>201</sup> Two qualifications, however, apply. Where the mortgage secures a future advance or is dependent upon the occurrence of a recorded condition precedent (*condición suspensiva*),<sup>202</sup> it will be effective against third parties from the date of its registration only if the future advance or condition precedent in fact occurs.<sup>203</sup>

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194. *Id.* art. 2912.

195. *Id.* art. 2907, grants this right only to mortgagees of real property.

196. Assignees or successors in interest (*causahabientes*) are not third parties within the meaning of the code. Pablo Sukis, LXVIII Semanario 6a. 71 (A.D. 736/58) (3a Sala 1962); Jorge Mucino, XXVIII Semanario 6a 111 (Q. 37/58) (3a Sala 1959).

197. C. CIV. DISTR. Y TERR. FED. art. 2919 (Porrua 1970). It has been suggested, however, that chattel mortgages may not be registered because article 3002 does not specifically state that mortgages may be registered. See H. WRIGHT, *supra* note 160, at 316. Nevertheless, other authorities indicate that chattel mortgages may now be created under the general mortgage provisions of the *Civil Code* and clearly imply that chattel mortgages may be recorded. See discussion note 180 *supra*. Their views seem correct. If it is true that chattel mortgages are governed by the general mortgage provisions of the *Civil Code*, it requires a mortgage to be recorded to be effective against third persons, C. CIV. DISTR. Y TERR. FED. art. 2919 (Porrua 1970), and chattel mortgages should be recordable under the same provisions.

198. C. CIV. DISTR. Y TERR. FED. art. 2988 (Porrua 1970).

199. *Id.* art. 2985(IV).

200. *Id.* arts. 2981-92.

201. *Id.* art. 2982. The various mortgagees may enter into an agreement (*concurso*) among themselves to determine how the proceeds of the collateral are to be divided among them. They cannot, however, be compelled to do so, and any mortgagee who does not join such an agreement is not bound by it. Chávez Hayhoe Salvador, LXIII Semanario 5a 2789 (A. Civ. en Rev. 378/39) (3a Sala 1940).

202. A *condición suspensiva* exists where "the existence of the obligation depends on its occurrence." C. CIV. DIST. Y TERR. FED. art. 1939 (Porrua 1970).

203. *Id.* art. 2921.

Where the mortgage terminates upon occurrence of a condition subsequent (*condición resolutoria*),<sup>204</sup> the mortgage will lose its effect against third parties when the occurrence of the condition is recorded.<sup>205</sup>

If the registered mortgagee cannot satisfy his debt out of the mortgaged collateral, he has two alternatives. First, he may sue for the balance due after sale of the collateral, although he is reduced to the "third class," the second to last category, of preferences when he takes such action.<sup>206</sup> Second, he may surrender his priority in the proceeds from his collateral and join in the insolvency agreement of the general creditors, maintaining, however, his first priority to payment in the pro rata distribution agreed to by the general creditors.<sup>207</sup> This alternative may be advantageous where several other mortgagees or pledgees have a priority in the collateral which would preclude significant satisfaction of the creditor's debt if he attempted to enforce his own rights in the collateral.

Where the mortgagee has failed to register, his transaction will have no effect against third parties,<sup>208</sup> and the mortgagee loses his status as a member of the first category of creditors. Although his position is not entirely clear, it appears that he will participate in the insolvency proceedings in the same manner as the unregistered pledgee.<sup>209</sup>

### *The Chattel Mortgagee Against Third-Party Purchasers*

Where the mortgage transaction is registered, it is effective against third parties.<sup>210</sup> These third parties include purchasers, who always take subject to the registered mortgage<sup>211</sup> and who therefore may be defeated by the mortgagee to the extent of his interest in the collateral.<sup>212</sup> Where the mortgage is not registered, however, the mortgagee does not fare as well. Generally, his mortgage has no effect against the third-party purchaser who acts in good faith.<sup>213</sup>

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204. See discussion note 23 *supra*.

205. C. CIV. DIST. Y TERR. FED. art. 2922 (Porruá 1970). For the *Civil Code's* definition of *condición resolutoria*, see article 1940, discussed in note 23 *supra*.

206. C. CIV. DIST. Y TERR. FED. art. 2983 (Porruá 1970).

207. *Id.* art. 2973.

208. *Id.* art. 2919.

209. See text & notes 146-49 *supra*.

210. C. CIV. DIST. Y TERR. FED. art. 2919 (Porruá 1970).

211. *Id.* art. 2894.

212. One who holds property subject to a mortgage in Mexico is ultimately, though not primarily, "liable" on it, *see* L. ROBB, DICTIONARY OF LEGAL TERMS: SPANISH-ENGLISH AND ENGLISH-SPANISH 115 (5th ed. 1973), or "obligated" on it. *See* 3 G. CABANELLAS, *supra* note 119, at 630-31.

213. The *Civil Code* presumes good faith in an installment sale agreement. Clotilde Pérez Prado de Negreto, [1961] Bol. Info. Jud. 606 (A.D. 2592/59) (3a Sala). At

Upon default by the debtor, the unregistered mortgagee will have no recourse but to join in the insolvency proceedings in the same manner as an unregistered pledgee. The mortgagee will be able to defeat the interest of a third-party purchaser only where the purchase renders the debtor insolvent, and even then only in certain circumstances.<sup>214</sup>

### THE COMMERCIAL CHATTEL MORTGAGE

#### *The Commercial Chattel Mortgagee Against the Debtor*

The commercial laws of Mexico do not make specific provision for the chattel mortgage. Nevertheless, article 2 of the *Commercial Code* allows application of the *Civil Code* as determinative of commercial matters where no commercial provisions conflict.<sup>215</sup> Thus, where a mortgage qualifies as a commercial transaction,<sup>216</sup> the *Civil Code* provisions discussed above will govern much of the agreement. Consequently, a commercial chattel mortgagee will fare against his debtor as would a civil chattel mortgagee. An important question which cannot be answered, however, is what procedures are available for the commercial chattel mortgagee to enforce his rights against the mortgagor. Arguably, the mortgagee may use the procedures set forth in the *Civil Code*.<sup>217</sup> Alternatively, the mortgagee may be entitled to bring an ordinary commercial action<sup>218</sup> or an "Executory Proceeding," such as that used with commercial installment contracts.<sup>219</sup>

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least in the context of a sale and purchase, to act in good faith one must have checked the public registry, have found no defect in the vendor's title, and have no actual knowledge of any defect. *Sucesión Miguel Capistrán*, CXXVI Semanario 5a 412 (A.D. 3735/54) (3a Sala 1955). The defects of title for which the buyer will be held responsible include not only defects in the seller's immediate title but also defects in the titles of his predecessors in interest. *Guillermo Francisco Macias*, CXXX Semanario 5a 234 (A.D. 5169/55) (3a Sala 1956). Finally, the third party must not have knowledge that his purchase will render his vendor insolvent, an act which constitutes a fraud on the vendor's creditors. *C. Civ. Dist. y TERR. FED.* arts. 2163 *et seq.* (Porruá 1970). *Guillermo Saldívar*, [1955] *Informe 46* (A.D. 2748/52) (3a Sala) (purchase of real property, but the principle appears applicable to personal property transactions as well, since it is arguable that the requirement of checking the registry to be in good faith would apply to any third party).

214. See text & notes 62-71 *supra*.

215. C. COM. art. 2 (Porruá 1969).

216. *Id.* art. 75, provides a list of transactions which, for purposes of determining which code applies, are considered commercial in nature. The chattel mortgage transaction, under proper circumstances, could be included in a number of the listed categories. See, e.g., *id.* art. 75(VIII) (undertakings for factories and manufacturing); *id.* art. 75(XIV) (banking operations); *id.* art. 75(XXI) (obligations between merchants and bankers which are not essentially civil in nature).

217. See text & notes 184-185 *supra*.

218. C. COM. arts. 1377-90 (Porruá 1969).

219. *Id.* arts. 1391-414; see text & notes 87-94 *supra*.

### *The Commercial Chattel Mortgagee Against Third Parties*

While the commercial chattel mortgage is governed by the *Civil Code* when the only parties involved are the debtor and creditor, the applicable law changes when third parties are involved and the debtor is a merchant. In that case, the commercial bankruptcy law provides the applicable rules of priority. Under this law, the mortgagee is the sole member of the second class of creditors.<sup>220</sup> Registration is a prerequisite to his membership in this class.<sup>221</sup> His rights to repayment from the proceeds of the collateral are subject only to the preferences held by funeral and last medical expenses and employee creditors.<sup>222</sup> Additionally, his rights are subject to the rights of persons who have incurred administrative or maintenance costs in caring for the assets of the debtor.<sup>223</sup>

Among themselves, mortgagees' have priority rights, including claims in the same collateral, determined according to the registration dates of their transactions.<sup>224</sup> The registered mortgagee's rights against lower classes of creditors are absolute. He must be satisfied first from the proceeds of his collateral and then from the rest of the debtor's assets before members of the next lower class may be paid.<sup>225</sup> He apparently is not compelled, as is the mortgagee under the *Civil Code*, to seek any balance due on his debt by suing as a member of a lower class.<sup>226</sup> On the other hand, the provisions of the commercial bankruptcy law do not provide a preference position for mortgagees who have not registered.<sup>227</sup> Thus, the unregistered mortgagee partic-

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220. See text accompanying notes 100-03 *supra*.

221. While the *Commercial Code* provides the rules of priority, whether a chattel mortgage transaction is valid against third parties at all is controlled by the *Civil Code*. See C. COM. art. 2 (Porrúa 1969). Article 2919 requires registration of chattel mortgages for effect against third parties. Note, moreover, that priorities among commercial mortgages are determined according to their dates of registration, *LEY DE QUIEBRAS Y DE SUSPENSIÓN DE PAGOS* art. 263 (Porrúa 1969), thereby implying registration is a prerequisite to priority.

222. *LEY DE QUIEBRAS Y DE SUSPENSIÓN DE PAGOS* art. 262 (Porrúa 1969). It is not entirely clear why the mortgagee is favored over other secured parties, such as the pledgee. One possible reason is the extra formality and diligence required of the chattel mortgagee in setting up his transaction. See text & note 182 *supra*. Another possible reason is that the mortgage not only is one of the most basic and oldest security devices, see Gerber, *supra* note 120, at 680, but also is generally associated with real rather than personal property. Thus, the priority of the security device is commensurate with the importance of the property normally utilized as collateral.

223. *LEY DE QUIEBRAS Y DE SUSPENSIÓN DE PAGOS* art. 262 (Porrúa 1969).

224. *Id.* art. 263.

225. *Id.* art. 269.

226. Although *Ley de Quiebras y de Suspensión de Pagos* article 263 provides only that the mortgagee will have absolute rights in his collateral, article 269 provides that no class of creditors will be allowed to share in the distribution of the debtor's assets until all the members of the higher classes have been completely paid. This indicates that where the mortgagee's debt is not satisfied by his collateral, he will have the right to take the balance due from the rest of the debtor's assets.

227. Cf. *LEY DE QUIEBRAS Y DE SUSPENSIÓN DE PAGOS* art. 263 (Porrúa 1969). Note also that the *Civil Code*, which governs commercial chattel mortgages in the ab-

ipates in bankruptcy only as a member of one of the lowest classes. This interpretation of the preference system under the *Commercial Code* is consistent with the scheme under the *Civil Code*.<sup>228</sup>

### *The Commercial Chattel Mortgagee Against Third-Party Purchasers*

The mortgagee's rights against third-party purchasers in commercial law are governed by the *Civil Code* since the *Commercial Code* is silent on this matter.<sup>229</sup> Thus, under commercial law, the mortgagee fares the same against third-party purchasers as the mortgagee under the *Civil Code*.<sup>230</sup>

### CONCLUSION

A review of creditors' rights and preference systems in Mexican secured transactions law has identified several major considerations which may control creditor conflicts. First, it is evident that in general a creditor will not fare well against other creditors if he has failed to give adequate notice of his transaction. Second, the type of transaction into which each creditor has entered is important in determining creditors' rights among one another. For example, a commercial mortgagee may have better rights in collateral than a pledgee or installment creditor merely because he holds by mortgage rather than a pledge or installment credit. Finally, the procedures available for enforcement of creditors' rights are for the most part efficient and simple.

While the above statements are generally true, they are subject to multitudes of exceptions. In addition, there are other elements of the law of creditors' rights which are not subject to generalization, such as the effect of damage to the collateral. These exceptions and additional elements create havoc for the foreigner who is considering doing business in Mexico. This Article has attempted to grapple with a sufficient number of the problems in this field to substantially aid the reader in attempting to research and resolve his particular legal problem. Used as a foundation for further labors, it is hoped that a basis has been established for making the law of creditors' rights in Mexico appear less formidable.

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sence of applicable *Commercial Code* provisions, requires mortgages to be registered to be effective against third parties. C. CIV. DIST. Y TERR. FED. art. 2919 (Porrúa 1970).

228. See text accompanying notes 208-09 *supra*.

229. C. COM. art. 2 (Porrúa 1969).

230. See text & notes 211-14 *supra*.

