Uniform Commercial Code Law Journal

Vol. 36, No. 4 **Spring 2004**

Mat #40083930

Vol. 36 #4, Uniform Commercial Code Law Journal (USPS 0647-740), (ISSN 0041-672X) is published quarterly by WEST GROUP, 610 Opperman Drive, P.O. Box 64833, St. Paul, MN 55164-1801. Subscription price: $235. Periodicals postage paid at St. Paul, MN.

Postmaster: Send address changes to Uniform Commercial Code Law Journal, P.O. Box 64526, St. Paul, MN 55164-0526.

We welcome the submission of material to be considered for publication, including articles, essays, decisions, or other items of interest to attorneys and others professionally interested in commercial law. The utmost care will be given to material submitted, although we cannot accept responsibility for unsolicited manuscripts. One copy of the manuscript (double spaced, including endnotes), along with a diskette containing the material in electronic format, should be mailed to each of the following:

LOUIS DEL DUCA Associate Dean,
Advanced Legal Education and
Professor of Law
The Dickinson School of Law
150 South College Street
Carlisle, PA 17013-2899

AARON MICHEAU, Managing Editor
Uniform Commercial Code Law Journal
West, a Thomson business
50 Broad Street
Rochester, NY 14694

A Practical Point-by-Point Comparison of Secured Transactions Law in the United States and Mexico

ALEJANDRO LÓPEZ-VELARDE AND JOHN M. WILSON

ABOUT THE AUTHORS:

Alejandro López-Velarde is a Partner, López-Velarde Heftye y Soria, S.C., Mexico City. John M. Wilson is the Legal Advisor for Private International Law, Organization of American States, Washington, D.C. and consultant, López-Velarde Heftye y Soria, S.C. The authors wish to dedicate this Article to Lic. Francisco Ciscomani Freaner and Lic. Ricardo de la Rosa Guzman, whose foresight, leadership and dedication have made secured transactions reform possible in Mexico. The authors also wish to thank Maria Gutierrez for her invaluable assistance in the comparative research for this work. Errors and omissions are the sole responsibility of the authors.

I. INTRODUCTION

Mexico's ongoing market reforms have opened the financial service sector of the economy to foreigners, creating new investment opportunities in the country. However, for every successful transaction, there is a greater number that never gets off the ground. Compared to the United States, where businesses have access to abundant and inexpensive credit, Mexican businesses are hard-pressed to finance their economic activities. Many viable businesses are not able to obtain credit, and the few that do must pay very high interest rates. According to many observers, this discrepancy in the credit market—a lack of credit produced by an outdated secured transactions framework—is the most important reason many transactions flounder.

In an attempt to alleviate this credit shortage, lawmakers have undertaken the modernization of Mexican secured transactions law, producing several reform efforts. The most significant of these reforms led to the adoption of a new Secured Transactions Law (STL), composed of two reforms to Mexican substantive law and a separate reform to Mexican registry law. The first of these reforms, principally amending the General Law of Credit Instruments and Operations, the Commercial Code, and the Law of Credit Institutions, was enacted on May 23, 2000.[1] The second reform, which added further amendments to these same laws, was enacted on June 13, 2003.[2] The registry reform component of the STL, which is contained in a wider commercial law reform, created a Commercial Registry Law enacted on May 29, 2000.[3] The final component of the STL reform is a separate Registry Regulation enacted on October 24, 2003.[4]Together with previously existing legal figures,

---

[1] Decree that amends, adds, and repeals several provisions of the General Law of Credit Instruments and Operations (Ley General de Títulos y Operaciones de Crédito published in D.O. Aug. 27, 1932) [hereinafter LGTOC]; the Commercial Code; and the Law of Credit Institutions (Decreto por el que se reforman, adicionan y derogan diversas disposiciones de la Ley General de Títulos y Operaciones de Crédito, del Código de Comercio y de la Ley de Instituciones de Crédito), published in the Diario Oficial [hereinafter cited as "D.O."], May 23, 2000 [hereinafter "STL 2000"].

[2] Decree that amends, adds, and repeals several provisions of the General Law of Credit Instruments and Operations; the Commercial Code; the Law of Credit Institutions; the Securities Market Law, the General Law of Mutual Institutions; the Law of Federal Bonding Companies; and the General Law of Organizations and Activities Ancillary to Credit (Decreto por el que se reforman, adicionan y derogan diversas disposiciones de la Ley General de Títulos y Operaciones de Crédito, del Código de Comercio, de la Ley de instituciones de Crédito, de la Ley del Mercado de valores, de la Ley General de Instituciones y Sociedades Mutualistas de Seguros, de la Ley Federal de instituciones de Fianzas y de la Ley General de Organizaciones y Actividades Auxiliares del Crédito) [hereinafter "STL 2003" jointly cited with "STL 2000" as "STL"] published in D.O. June 13, 2003.

[3] Decree that amends, adds, and repeals several provisions of the Civil Code for the Federal District in Common Matters and for the entire country on Federal Matters, the Federal Civil Procedure Code, the Commercial Code and the Federal Consumer Protection Law (Decreto por el que se reforman y adicionan diversas disposiciones del Código Civil para el Distrito Federal en Materia Común y para toda la República en Materia Federal, del Código Federal de Procedimientos Civiles, del Código de Comercio y de la Ley Federal de Protección al Consumidor), published in D.O. May 29, 2000 [hereinafter, Comercial Registry Law].

[4] Reglamento del Registro Público de Comercio, published in D.O. Oct. 24, 2003 [hereinafter, Registry Regulation].

the STL reforms shape the current legal framework for secured transactions in Mexico.

The purpose of these new laws, amendments, and regulations is to create a new credit market for Mexican businesses by providing the legal certainty and flexibility necessary for creditors to lend in Mexico. However, it is still unclear how well these reforms accomplish this goal and how well they resolve extensive weaknesses under the previous legal framework.

This article attempts to shed some light on these issues, and the overall effectiveness of Mexico's new system, by providing a point-by-point comparison with the legal principles and concepts of the secured financing system of the United States under Revised Article 9 of the Uniform Commercial Code.[5]

II. POINTS OF COMPARISON

Secured transactions reform, whether in the U.S. under Revised Article 9 or in Mexico under the new STL, generally centers around eight legal principles or concepts. These principles are:

(1) scope and uniformity of the security mechanism;

(2) inclusion of after-acquired property as collateral;

(3) inclusion of proceeds as collateral;

(4) inclusion of future advances as part of the secured obligation;

(5) protection of debtors via purchase money security;

(6) protection of third parties via ordinary course buyer exception;

(7) protection of creditors via effective enforcement methods; and

(8) notice of security interests via modern registry systems.

Uniformity: In very general terms, a secured financing system must reduce a creditor's risk and exposure by reducing the economic and legal uncertainty in a transaction. One of the most common causes of legal uncertainty is the multiplicity of confusing or

---

[5] Uniform Commercial Code, Revised Article 9, Secured Transactions (2000 Revision), effective July 1, 2001 [hereinafter U.C.C. Rev. Art. 9].

competing security mechanisms. Before the advent of Article 9, several legal devices used to create security interests characterized U.S. law. Deciding which legal device was more suited to a given transaction was difficult. Mistakes in the determination were common and costly. Article 9 eliminated this uncertainty by replacing all existing devices with the creation of a single, unitary device: the 'security interest.' Latin-American legal systems, including Mexico, have not taken this important step. Instead, these systems remain plagued by multiple security devices, creating a system proven to be highly inefficient. Often, devices are based on legal concepts that undermine the security provided by others. Other devices are governed by different perfection rules that ignore the priority scheme that regulates others. Still others allow the creditor to retain title to collateral thus creating secret liens.

After-Acquired Property: Another central feature of secured transactions law is the automatic extension of a security interest from the original encumbered collateral to property acquired by the debtor after the creation of the security agreement. This feature allows extension of security interests to replacement collateral when the original is replaced, such as in inventory or credit-line financing.

Proceeds: Modern secured financing also requires that debtors retain possession of the collateral and dispose of the collateral pursuant to the terms of the security agreement. Consequently, any statute must include the extension of a security interest to proceeds upon sale, exchange, collection, or other disposition of collateral. The proceeds concept allows a security interest to continue in the collateral notwithstanding a sale or other transformation.

Future Advances: Modern secured transactions law allows the parties to secure debts (obligations) obtained for funds advanced after the creation or perfection of a security interest. This feature allows a creditor to extend (and a debtor to receive) future funds without sacrificing the creditor's priority with relation to the collateral used to secure the original and future extension of funds.

Purchase Money Mechanism: The practice of giving priority to secured creditors in a debtor's after-acquired property and proceeds can tie a debtor with future credit needs, to an individual secured creditor. Consequently, a debtor's ability to receive credit from other sources is limited. A Purchase Money Security Interest (PMSI), another central feature of secured transactions laws, alleviates this problem by creating an exception to the principle of first-in-time, first-in-right, allowing a party second-in-time to become first-in-right. If a debtor is able to procure additional financing for a new line of goods, notwithstanding the prior interest, the PMSI provides a new creditor with protection over previous secured creditors with respect to the financed goods.

Buyers in Ordinary Course: Another tenet of secured transactions law is that purchases in ordinary course of business must be free of any security interest created by a seller. This rule must operate even if the parties perfected the security interest prior to sale and even if the buyer knows of the existence of the security interest. This exception, essential to consumer confidence, shield consumers who purchase goods from a retailer/secured debtor's inventory from secured party's right to repossess the goods in case of default.

Notice and Registration: Reform efforts must also ensure that secured financing systems provide notice of encumbered collateral to third parties. If notice is not provided, or is ineffective, subsequent purchasers or lenders may believe that debtor's goods are free of encumbrances. Failure to make available notice may lead unwary third parties to purchase or lend against the collateral. The most effective method for providing notice is filing of a registration form. Filing a registration form allows secured parties to perfect their security interests and gain priority over competing claimants.

Effective Enforcement: In case of a debtor default, secured financing systems must allow for quick and effective methods of execution on the collateral. Any secured financing system must consider the possibility of extra-judicial enforcement when possible in order to ensure that creditors have the means to repossess the collateral to satisfy an outstanding deficiency on a loan.

The following sections describe the method in which U.C.C. Revised Article 9 implements these legal principles into a modern comprehensive statute and compares the operation of its rule with those recently enacted by the Mexican Legislative and Executive Branches.

III. UNIFORMITY

Secured financing in most countries outside the United States and Canada is characterized by multiple mechanisms and practices for the taking of security. The legal characteristics of these mechanisms (including perfection and notice) can vary greatly, creating a complicated network of laws and practices that often conflict with one another. An over-arching goal of all secured financing statutes, therefore, should be to include all transactions that attempt to use movable assets as security for a loan into a single legal framework, comprised of a single security mechanism, and a single notice and priority system. This rule should apply to all existing mechanisms, whether or not they are considered formal security interests under present laws; as long as a transaction intends to create an interest in personal property in favor of a creditor/seller as protection against default, it should be included in a comprehensive and uniform system.

Prior to the enactment of U.C.C. Article 9, secured financing in the U.S. was also characterized by multiple competing legal mechanisms used for securing a loan. Article 9 replaced these mechanisms with a single, uniform mechanism called a security interest, which increased legal certainty by eliminating competing devices. In order to create a properly functioning asset-based lending system, Mexican law must replicate this result by replacing all movable goods devices (such as pledges, chattel mortgages, title retention devices, agricultural credits, consignments, leases, trusts, banking mechanisms, and production guarantees) into a single and uniform system.

A. REVISED ARTICLE 9

One of the most important aspects of Article 9 is that it applies *only* to consensual liens, regardless of their form.[6] That is to say, Article 9 applies to every transaction where the parties intend to create a security interest, regardless of the mechanism or practice employed by the parties.[7]

---

[6] U.C.C. Rev. Art. 9 § 109(a)(1). Article 9 applies to every transaction that creates a contractual security interest in movable goods.

[7] Uniform Commercial Code [hereinafter U.C.C.] Art. 1 § 201(37) definition of a security interest; U.C.C. Rev. Art. 9 § 109 description of transactions to which Article 9 does and does not apply.

The U.C.C. defines the term security interest as "an interest in personal property... which secures payment or performance of an obligation."[8]

Revised Article 9 makes reference to this definition in setting the scope of the secured transactions concept. Revised Article 9 provides that the single and uniform mechanism created by Article 9 applies to all transactions, regardless of their form, if they create a security interest in movable goods by contract.[9]

In sum, the goal of Article 9 is to incorporate every secured transaction into a single security mechanism. This rule applies as long as a security mechanism creates an interest in personal property in favor of a creditor/seller as protection against default. Under Revised Article 9, this rule includes all previously existing security mechanisms, including pledges, title retention devices, chattel mortgages, etc.

Article 9 also covers transactions that are not typical security interests. These include consignment arrangements, financial leases, and sale of accounts.[10] As a result, Article 9 applies to some transactions that would not (or should not) fall within its scope. However, these transactions are included due to their commercial characteristics, which are very similar to those of security interests, making this types of transactions oftentimes indistinguishable from secured transactions. Of greatest importance to the application of this rule is the fact that the party in possession of the goods is not the true owner. Consequently, this separation of ownership and possession can lead to confusion by third parties who rely on possession as indicia of ownership.

Consignments

Under Revised Article 9, a security interest covers the interest of a consignor because this party retains legal title to the goods on

---

[8] U.C.C. Art. 1 § 201(37). "Security interest" means an interest in personal property or fixtures that secures payment or performance of an obligation.

[9] U.C.C. Rev. Art. 9 § 109 (a) states that:

This article applies to: (1) any transaction, regardless of its form, that creates a security interest in personal property or fixtures by contract; (2) an agricultural lien; (3) a sale of an account, chattel paper, payment intangible, or promissory note; (4) a consignment; (5) a security interest arising under Section 2-401, 2-505, 2-711(3), or 2A-508(5), to the extent provided in Section 9-110; and (6) a security interest arising under Section 4-210 or 5-118.

[10] U.C.C. Rev. Art. 9 § 109.

consignment while the consignee retains possession. Revised Article 9, however, reduces the importance of title in defining the application of this system.[11]

On this issue, Pre-revision Article 9 differentiated between *true* consignments and *security* consignments.[12] Under that statute, true consignments were considered sales or returns while security consignments were considered security interests. Revised Article 9 simply includes all consignments (whether *true* consignments or *security* consignments) within the scope of Article 9.[13]

Leases

The U.C.C. and Revised Article 9 also make a distinction between *true* leases and *security* leases.[14] The rationale behind this rule is that a lease, like a consignment, also separates ownership (or title) from possession. As a result, this device may be used to disguise a security interest.

Characteristics of a lease, including its term, the lifespan of the goods, and a lessee's option to purchase at the end of the lease term, may be used to determine whether a lease is being used, not as a lease, but as a security interest. If that is the case, then Revised Article 9 will apply to that transaction regardless of what the parties call it.

Accounts and Promissory Notes

Revised Article 9 also applies to a sale of an account, chattel paper, payment intangible, or promissory note.[15] Even though these types of transactions are not security interests *per se*—they are actual sales between two parties—they are included under the definition of security interest.[16] The reason these transactions fall within the scope of Article 9 is that there is little difference between the

---

[11] U.C.C. Rev. Art. 9 § 202 states as follows: Except as otherwise provided with respect to consignments or sales of accounts, chattel paper, payment intangibles, or promissory notes, the provisions of this article with regard to rights, obligations, and remedies apply whether title to collateral is in the secured party or the debtor.

[12] U.C.C. Rev. Art. 9 § 102(a)(20) defining consignment.

[13] U.C.C. Rev. Art. 9 § 109(a)(4), establishing the application of these rules to a consignment.

[14] U.C.C. Art. 1 § 201(37).

[15] U.C.C. Rev. Art. 9 § 109(a)(3).

[16] U.C.C. Art. 1 § 201(37).

sale of these types of goods and the taking of security in them. This is especially true if the sale allows recourse against the seller. For example, assigned or factored accounts are difficult to distinguish from security interests in accounts because these goods have no physical manifestation that might indicate the party in possession of the accounts. In order to avoid possible uncertainty, Revised Article 9 covers most of these types of payment intangibles.

Judicial Liens

Finally, it should be noted that Revised Article 9 does not apply to liens that come into existence by operation of law or other nonconsensual method.[17] There are some exceptions, however, including agricultural liens.[18]

In summary, Article 9 eliminates all previously existing security mechanisms, replacing them with a single device: a legal mechanism referred to as a security interest. All transactions that give a party an interest in goods in case of default, regardless of their name or form, are deemed a security interest for purposes of Article 9. As a result, parties must comply with Article 9 in order to have rights against the debtor and recover the collateral in case of default. Additionally, commercial efficiency makes it necessary for Article 9 to cover other transactions that do not create security interests. In most cases, the rationale behind this inclusion is to eliminate the ostensible ownership problem, where a party in possession of goods may not be the true and complete owner of such goods as in the case with consignments, leases, and sales of payment intangibles.

B. MEXICAN LAW

Unlike Article 9, current Mexican law does not provide a uniform system with a single security mechanism. Instead, Mexican law creates a piecemeal system of multiple competing devices

---

[17] U.C.C. Rev. Art. 9 § 109 (d) establishes the inapplicability of Article 9. Sub paragraph (2) further establishes that Article 9 does not apply to liens, with the exception of Agricultural Liens.

[18] Rev. Art. 9 §102(a)(5) defines agricultural liens as statutorily created lien over farm products. Unlike Revised Article 9, pre-revision Article 9 [hereinafter "U.C.C. Prerevision Article 9"] did not include agricultural liens in its application. Unlike Pre-revision Article 9, Revised Article 9 § 333 also provides a rule for dealing with priority disputes between parties who hold Article 9 security interests and those who hold liens arising by operation of law.

used for secured financing. There is little coordination between these devices. As a result, uncoordinated competing devices can undermine the operation of the system as a whole.

Pre-STL

Secured financing in Mexico resembled the U.S. system before the enactment of U.C.C. Article 9. The Mexican system is composed of what some scholars refer to as a “crazy-quilt” of varying devices. Conditional sales contracts, pledges of various types, chattel mortgages of various types, universal liens, production credits, financial leases, specialized banking mechanisms, warehouse receipts, pledge receipts, book-entry deposits, etc., are all used in Mexico for secured financing. All of these devices are constant reminders of those replaced by Article 9 since the 1950s.[19]

The problem of multiple security devices is compounded by the lack of uniformity in perfection and notice rules. Each security device provides for a different method for perfection of the security interest and a different method for providing notice of that interest to third parties. This makes it difficult for a prospective creditor to know whether a debtor’s assets have been previously encumbered.

New STL

The new STL, as enacted in 2000[20] or amended in 2003,[21] does not alleviate this problem. On the contrary, the STL simply adds two more devices to the mix. These new devices are the non-possessory pledge[22] and the guarantee trust.[23]

Prior to the enactment of the STL, Mexican lawmakers worked on a number of reform proposals, most of which also dodged the

---

[19] Article 9 substituted the unending web of secured financing mechanisms developed through ingenious commercial and legal practice with one basic security device and one body of law. See Victor Levine, *Secured Loans,* 1946 A.B.A. Sec. Leg. Ed. Prac. L. Inst. 1-30, defining a vast array of pre-article 9 security devices, including the pledge, chattel mortgage, conditional sale, trust receipt, guaranty, etc. See also Grant Gilmore, *Security Interests in Personal Property* at 5-250 (1965).

[20] STL 2000.

[21] STL 2003.

[22] STL 2000, Article 1 reforming Article 346 of the LGTOC; STL 2003, Article 1 also reforming Article 346 of the LGTOC.

[23] STL 2000, Article 1 reforming Articles 383, 392 and 395-414 of the LGTOC; STL 2003, Article 1 reforming Articles 381-387 and 392-407 of the LGTOC.

issue of replacing current mechanisms with a unitary device.[24] In particular, lawmakers recognize that pledge and title retention devices enjoy strong traditions and are firmly entrenched in civil law systems throughout Latin America. As a result, there is an implicit recognition that replacing these devices or even incorporating them into a single security scheme is a difficult task.

Instead of directly proposing the elimination of these various devices (a move many consider too radical), some lawmakers believe these devices may be phased out. Lawmakers base this belief on that hope that if they provide a better security mechanism, parties to a transaction will stop using older, less-flexible devices. As a result, these previous mechanism will fall into disuse, making their future removal or incorporation in to a single system more politically feasible.

There are several problems with this belief. First, current mechanisms undermine secured transactions under the new STL. Second, many current mechanisms create secret liens, making it difficult for a secured party to determine if potential debtor's assets are encumbered. Finally, bankruptcy laws do not reconcile priorities between the various Mexican mechanisms, making it difficult for a secured party to determine its priority position in case of default or insolvency.

Pledge

Unlike other current devices, most pledge mechanisms under Mexican law do not seriously undermine the issue of uniformity under the STL. The reason is that most Mexican pledge devices require the delivery of the collateral to the secured party or a third party depository.[25] Consequently, any subsequent creditor would have notice that specific goods serve as collateral for a loan by simply noting the party in possession. There is one type of pledge, however, that can create great uncertainty to asset-based lending. Bailment pledges under the LGTOC are interpreted by most lawyers to allow the creditor to retain constructive possession of the

[24] Previous secured transactions projects included draft proposals at the Ministries of Economy (Secretaría de Comercio y Fomento Industrial, currently Secretaría de Economía) and Foreign Relations (Secretaría de Relaciones Exteriores), and the Mexican Association of Notaries (Asociación Mexicana del Notariado). Projects on file with the authors.

[25] LGTOC, Article 334.

collateral while the debtor retains actual possession and control.[26] This pledge is one of the few that does not require that the debtor deliver possession of the collateral to the secured party. This pledge also does not require registration and so creates a secret lien that makes it difficult for subsequent parties to have notice of the true status of the goods. The secret operation of this device can severely undermine the operation of security interests under the STL.

Title Retention

Title retention devices (including conditional sales contracts, reservation of title, and reversionary interests) also count with storied traditions in civil law systems and are difficult for lawmakers to replace or incorportate into a uniform system. These devices are based on traditional civil law notions of ownership, where ownership is represented by title to the property: the holder of the title is the owner of the goods. These notions are largely incompatible with modern secured financing law, which places less emphasis on the notion of title and greater emphasis on the rights to possession of the collateral.[27]

Consignments and Leases

Mexican practice permits the use of leases and consignments as security interests. Unlike Revised Article 9, Mexican practice does not distinguish between "true" leases or consignments and "security" leases or consignments. In these cases, Mexican law places form over substance. Any transaction denoted as a "lease" or "consignment," regardless of whether it actually intends to create a security interest, will be considered a lease or consignment under present law. Leases and consignments do not require registration. If used as security devices, these transactions create secret liens detrimental to the overall success of the STL.

Accounts and Payment Intangibles

Finally, the new STL does not cover assignment or factoring of accounts. As previously noted, assignment and factoring can involve the sale or transfer between two parties. However, there is

---

[26] LGTOC, Article 334 (iv).

[27] See U.C.C. Rev. Art. 9 § 202, Title to Collateral Immaterial, which states that Article 9 applies whether title to the collateral is deemed to reside with the secured party or with the debtor.

little difference between the sale of accounts and the taking of a security interest in accounts, especially if the sale allows recourse against the seller. Consequently, the new STL makes it difficult to properly take a security interest in these types of goods without extensive background research or extensive risks.

As we have seen, the new Mexican STL did not create a unitary security device, nor did it incorporate transactions that function like secured transactions and thus should be included into a uniform notice and priority system. Consequently, any lender considering the use of the new STL must be very careful of two things: first, to ensure that any transactions it may be contemplating do not fall in conflict with current, competing devices; and second, to ensure that a debtor's goods at the time of the loan are not previously encumbered.

IV. AFTER-ACQUIRED PROPERTY

Any properly functioning secured financing system must allow a security interest to cover property acquired by the debtor after the creation of the security agreement and after the registration of the security interest. This feature is essential to preserve a creditor's interest when the collateral is replaced in ordinary course of business and when a creditor extends a line of credit.

This after-acquired property feature places special requirements on a secured financing system. For example, a secured creditor can only anticipate the general category or the types of assets that the debtor may acquire in the future. Consequently, the secured financing system must allow for general collateral descriptions in both the security agreement and the registration form, even when specific descriptions are possible.

A. REVISED ARTICLE 9

Article 9 allows for security interests in various types of future assets, including after-acquired property, as collateral for a loan.[28] However, this is a practice that until the mid-1950s was difficult

---

[28] U.C.C. Pre-revision Art. 9 § 204(1) and U.C.C. Rev. Art. 9 § 204(a). Article 9 allows a security agreement to provide for security interests in after-acquired collateral. Consumer goods and commercial tort claims, however, are excluded. "A security interest does not attach under a term constituting an after-acquired property clause to: (1) Consumer goods, other than an accession when given as additional security, unless the debtor acquires rights in them within 10 days after the secured party gives value; or (2) A commercial tort claim." U.C.C. Rev. Art. 9 § 204(b).

even in the United States and continues to present difficulties with regard to the collateral and descriptions thereof.

Description

As mentioned before, a legal framework that permits security interests over future assets, including after-acquired property, must also permit the use of general collateral descriptions. By definition, after-acquired property will not exist until after the security interest is created and perfected (typically by registration). As a result, the particular details of the goods cannot be known in advance, making it difficult for a creditor to provide a precise description of the future property in the security agreement and registration.

All properly functioning secured financing systems, including U.C.C. Article 9, thus allow the parties to describe future collateral in general/generic fashion in both the security agreement and registration form.

However, general/generic descriptions may cover transactions over presently existing collateral as well as those covering present and future collateral. Consequently, Article 9 adds an additional description requirement to ensure that it is the intent of the parties to cover future goods. Consider the word "equipment" which would qualify as a general/generic description. The problem with this description is that since it is general enough to encompass both present and future equipment, it is not possible to determine the intent of the parties based on that description alone. This can be especially problematic if the parties intend a security interest to cover only present equipment.

Although Revised Article 9 does not provide a specific rule for the description of after-acquired property, it does state that a description is sufficient, whether or not it is specific, if it reasonably identifies the collateral.[29] As a result, one way to alleviate the problem of unintentionally encumbering future assets is to require additional language to ensure that a description actually intends to do so. An acceptable description, for example, could state the it a security interest covers "equipment, now existing and after-acquired." Such description would not only comply with the Article

[29] U.C.C. Rev. Art. 9 § 203(b)(3)(A). See also U.C.C. Rev. Art. 9 § 108 (a).

9 standard of reasonably identifying the collateral, but would also solve the problem concerning the parties' intent.[30]

Pre-revision Article 9 permitted super-generic descriptions, such as "all the debtors assets" "all the debtor's personal property" and the like. Revised Article 9 does away with this practice, with regard to the security agreement, stating that these types of descriptions are not considered to reasonably identify the collateral and are thus invalid.[31] Registration rules, however, provide greater flexibility on this point.[32]

Floating Lien

Security interests in after acquired property also made another Article 9 innovation possible, that of permitting a 'floating lien.' Under this concept, both the collateral and secured obligation fluctuate. To allow this practice, Revised Article 9 allows two things. First, it allows for security interests in after-acquired property and proceeds (discussed in section V below). Second, it allows using the collateral to secured present and future obligations (future advances, discussed in section VI below). Together, these features provide flexibility to enable the debtor to obtain a fluctuating line of present and future funds by creating a security interest over a fluctuating fund of present and future collateral. This practice is essential for several modern financing practices, including inventory financing and accounts financing.

In sum, Revised Article 9 provides a framework that encumbers property acquired by the debtor after creation and perfection of the security interest, including after-acquired property. Many transactions cannot take place without after-acquired property features. These include transactions where the original collateral will be re-

---

[30] U.C.C. Rev. Art. 9 § 108. A description of personal property is sufficient, whether or not it is specific, if it reasonable identifies what is described. Art. 9 § 108 (a). This rule also states that a description reasonably identifies the collateral if it identifies it by specific listing, category, quantity, computational or allocational formula or procedure, or any other method, if the identity of the collateral is objectively determinable. U.C.C. Rev. Art. 9 § 108 (b).

[31] U.C.C. Rev. Art. 9 § 108 (c). According to Official Comment 2, § 108 (c) simply follows prevailing case law by adopting the view that, with regard to the security agreement, super-generic descriptions are insufficient.

[32] U.C.C. Rev. Art. 9 § 504 states that a financing statement (registration form) does reasonable identify the collateral is it "covers all assets or all personal property." These issues are discussed in greater detail in Section IX of this Article.

placed or transformed during the course of the security interest and where a lender extends a secured line of credit used to purchase future goods.

B. MEXICAN LAW

Unlike the great majority of security devices before its adoption, the STL represents a huge step forward by permitting security interests in after-acquired property. This new law provides two new devices for the taking of security in future collateral: the pledge without transmission of possession (non-possessory pledge)[33] and the guarantee trust.[34]

Collateral

The STL states that security interests under these two devices may cover all types of rights and movable property.[35] Even though this provision does not expressly permit security interests in "future goods," it do not prohibit it either. In addition, the LGTOC further provides that a non-possessory pledge may cover goods and rights in the patrimony of the debtor at the moment at which the non-possessory pledge is created, as well as goods of equal or similar nature to these that the debtor acquires after the creation of the pledge.[36] Although the effect of the requirement that future goods must be of equal or similar nature is not clear, this rule is a departure from previous Mexican law, which limited security interests on future goods.[37]

---

[33] STL amendments LGTOC Articles 346-380. [Hereinafter STL amendments to the LGTOC are cited simply as STL].

[34] STL, Arts. 383-414.

[35] STL, Art. 353 with respect to the non-possessory pledge and Art. 401 with respect to the guarantee trust.

[36] STL, Art. 355. The STL states as follows: A pledge without transmission of possession may be created over the following movable goods: (I) Those goods and rights in the patrimony of the debtor at the moment at which the pledge without transmission of possession is created, including commercial names, trademarks and other rights; (II) Goods of equal or similar nature to those mentioned in the section above, that the debtor acquires in a date after the creation of the pledge without transmission of possession.

[37] The primary type of security interest in after-acquired property permitted under old Mexican law was under the Avio and Refaccionario production credits, which covered fruits directly attributable to a farming or production process. LGTOC, Art. 327. Even then, Mexican law placed several limitations on the operation of a security interest over these future goods. LGTOC, Art. 327.

Description

As we have seen, in order for a security interest to cover future goods, the legal system must permit for general/generic descriptions of the collateral. The new STL has some provisions allowing for general/generic descriptions. However, these provisions provide unclear rules and could contain several important limitations. Creditors, hence, should pay close attention to those cases in which general/generic descriptions are permitted.

The first rule contained in the STL states that all collateral *must* be identified.[38] The STL goes on to state that, in cases where the debtor creates a non-possessory pledge over all the movable goods used in its preponderant activity, the collateral *may* be identified in generic fashion.[39]

Although there is little experience on this point and no case law precedent, these provisions may complicate security interests in after-acquired property and proceeds, unless the parties agree to create a security interest over all goods used in the debtor's preponderant activity.[40]

Further complicating things is that the STL, although requiring that encumbered property be "identified," does not spell out how to do so and, aside from the exception mentioned above, does not state that it may be identified in general or generic fashion.

This omission may be complicated further by the legislative history and negotiations of the text. One day before the Congress passed the new STL in 2000, this provision read as follows:

> *The encumbered property must be* <u>identified in specific manner</u>, *except in the case where the debtor creates a pledge without transmission of possession in favor of its creditor over all the movable goods used in its preponderant activity, in which case these may be identified in generic fashion.*

---

[38] STL, Art. 354.

[39] STL, Art. 354.

[40] The STL does not contain a definition of the term "preponderant activity". From the context of the drafting process and the negotiations of the text, it appears likely that the term is similar to the concept of ordinary course of business under U.S. law. However, only case law and doctrine will further clarify the meaning of this term under Mexican law.

Under this version, general/generic collateral descriptions were limited exclusively to blanket/universal liens. Mexican lawmakers realized that retaining the specificity requirement would severely limit security interests in future property (after-acquired and proceeds), as well as in inventory, equipment, accounts receivable, fungible goods, etc. As a result, the words "in specific manner" (or the Spanish, *"de forma pormenorizada"*) were removed before the final bill was sent for a vote.

However, simply removing the words "in specific manner," without tailoring the remainder of Article 354 (or other Articles in the STL), produces its own set of concerns. First, Article 354 reads poorly. In essence, this provision read as follows: property *must be identified*, unless the parties create a universal lien, in which case the property *may be identified in generic fashion*.

The original wording provided a distinction that read as follows: property *must be identified in specific manner*, unless the parties create a universal lien, in which case such property *may be identified in generic fashion*. Although the new wording attempts to do away with the distinction, the sentence structure was not changed. As a result, it can be argued that the distinction was preserved. On one hand, security interests in property require "descriptions." On the other, security interests in universal goods permit "generic descriptions." Consequently, it is possible that a Mexican court can interpret that permitting generic descriptions in the latter case may exclude them in the former.

This rule becomes further complicated under the guarantee trust provisions of STL and may encounter another limitation in the description of the collateral. The applicable rule for the trust simply states that movable goods encumbered by a guarantee trust must be specified pursuant to Article 354.[41]

The concept that the collateral must be "specified" may create further complications and creates an effect that may have been inadvertent. Although this may be a question of semantics, using the word "specified" brings this Article one step closer to previous rules and case law. Previous law used the word "specify," "specificity," and "specified" to clarify the description requirements. It is not clear whether this difference in language produces further reason for concern. However, creditors should be aware that a Mexi-

41 STL, Art. 408.

can court could interpret Article 408 to require that goods be described with "specificity."

Additionally, the Commercial Code requires that the collateral be described with specificity prior to an enforcement action.[42] These types of requirements are difficult given that, as we mentioned, future and fungible goods cannot be described in detail. Additionally, a creditor may not know the true extent of collateral existing at the time of enforcement. The fact that other provisions retain this specificity wording may create problems in the operation of the STL.

As mentioned, Mexican law prior to the STL did not permit the registration of security interests that described collateral in general/generic fashion. As a result, registry officials rejected all documents containing general/generic collateral descriptions. To end this practice, the STL now removes the duty of registry officials to reject such security interests. That provision states as follows:

> Registry Officials must abstain from suspending or refusing the registration of a security interest over movable goods, the *identification* of which takes place in *generic* manner and which correspond to the preponderant activity of the debtor, under the terms of Article 354 of the LGTOC.[43]

This provision does away with a long-standing civil law requirement and practice that the asset-base be well-defined and described. However, again, this provision carries over the flaw contained in Article 354 regarding the specificity of the descriptions.

As mentioned earlier, previous Mexican law permitted security interests in future goods in only a couple of mechanisms (e.g. production credits and industrial mortgages). Additionally, these rules required that future assets be traceable to the original asset-base; that is to say that future goods be directly attributable to goods in the original collateral pool. Secured lenders, however, are usually reluctant to rely on an ability to trace a particular asset that exists today back to the originally encumbered collateral.

---

[42] Código de Comercio (Commercial Code), published in D.O. Sept. 15, 1889, amended several times, Art. 1414 bis 3.

[43] LGTOC, Art. 377.

It is clear that the STL takes several important steps to allow the creation of security interests in after-acquired property. In doing so, it has remedied one of the long-standing flaws with Mexican legislation in this area. It is unclear, however, whether these attempts go far enough. In the meantime, creditors should keep in mind that Mexican courts may continue to favor specific descriptions and require tracing of future collateral.

V. PROCEEDS

Another central feature of effective secured transactions laws is that they allow security interests to include proceeds—a second type of future collateral. Proceeds include any property received upon sale, exchange, collection, or other disposition of the collateral. That is to say, proceeds allow a creditor to encumber future generations of collateral after the original collateral is disposed of or changed in some way during the debtors use of the collateral. Many modern lending practices, including inventory financing, would not be possible without this feature.

A. REVISED ARTICLE 9

Like with after acquired property, Article 9 allows for security interests in proceeds as collateral for a loan.[44] Under Article 9, a secured creditor's rights to proceeds after the disposition of collateral attaches to identifiable proceeds.[45] Similarly, a security interest in such proceeds is perfected automatically if the security interest in the originally encumbered collateral was perfected correctly.[46]

Definition

Pre-revision and revised Article 9 define proceeds in similar terms: proceeds include whatever is received upon sale, exchange, collection or other disposition of the originally encumbered collateral or its subsequent proceeds.[47] Although proceeds under Pre-revision Article 9 included insurance payable and payments or other distributions made with respect to investment collateral,[48] Revised

---

[44] U.C.C. Rev. Art. 9 § 315(a)(2) and § 203(f).
[45] U.C.C. Rev. Art. 9 § 315(a)(2) and § 203(f).
[46] U.C.C. Rev. Art. 9 § 315(c).
[47] U.C.C. Pre-Revision Article 9 § 306 (1) and Rev. Art. 9 § 102(a)(64).
[48] U.C.C. Pre-Revision Article 9 § 306 (1).

Article 9 adds to this definition by including any rights arising out of collateral, any property collected or distributed on account of collateral, and any claims arising out of loss or other interference with the use of collateral as well as defects or damage to the collateral.[49] Like Pre-Revision Article 9, proceeds under Revised Article 9 continue to include insurance payable for loss, defects and other damage to the value of the collateral.[50]

General Rule

Pre-revision and Revised Article 9 follow a similar rules: for a security interest in proceeds to be valid, creditors must identify proceeds as collateral subject to their security interests at the time of perfection.[51] The basic rule establishes that a security interest continues in collateral notwithstanding sale, lease, license, exchange, or other disposition, if it attaches to identifiable proceeds of the original collateral, unless the creditor authorized the disposition free of encumbrances.[52] Revised Article 9 also adds new rules concerning security interests in deposit accounts and agricultural liens.[53] Finally, it is worthwhile to note that Revised Article 9 extends the period for automatic perfection discussed above from 10 days to 20 days.[54]

Commingled Goods

As discussed above, security interest in proceeds require that proceeds be identifiable. Ordinarily, this means that proceeds must be traceable to the originally encumbered collateral. This tracing

---

[49] U.C.C. Rev. Art. 9 § 102(a)(64). The right to claim proceeds for the loss, nonconformity or interference with collateral, and defects, infringement or damage to collateral, is limited to the extent of the value of the collateral. Rev. Art. 9 § 102(a)(64)(D).

[50] U.C.C. Rev. Art. 9 § 102. Revised Article 9 formally defines proceeds as (a) whatever is acquired upon sale, lease, license, exchange, or other disposition of collateral; (b) whatever is collected on, or distributed on account of, collateral;(c) rights arising out of collateral;(d) to the extent of the value of the collateral, claims arising out of the loss, nonconformity, or interference with the use of, defects or infringement of rights in, or damage to the collateral; and (e) To the extent of the value of collateral and to the extent payable to the debtor or the secured party, insurance payable by reason of the loss or nonconformity of, defects in, or damage to the collateral.

[51] U.C.C. Pre-Revision Article 9 § 306 (1) and Rev. Art. 9 § 102(a)(64).

[52] U.C.C. Rev. Art. 9 § 315. This rule applies equally to agricultural liens.

[53] U.C.C. Rev. Art. 9 § 315.

[54] U.C.C. Rev. Art. 9 § 315(d). See Official Comment 4 concerning the extension of the period for automatic perfection.

can be difficult under even the best of circumstances, which is the reason many creditors would rely on after-acquired property clauses to cover future goods rather than rely exclusively on the extension of the security interest to proceeds. The problem, however, is even more complicated when the proceeds are commingled with other goods that are not traceable to the originally encumbered goods.[55]

As a result of the difficulties inherent to separating proceeds that are part of a mass of goods that includes non-proceeds, Article 9 places some limitations on the operation of its primary rule. In general, Article 9 provides that a security interest does not exist in commingled goods as such.[56] However, a security interest may attach to a product or mass that results when goods become commingled.[57] In such cases, if a security interest in collateral is perfected before the collateral becomes commingled goods, the security interest over the commingled mass is also perfected.[58]

Cash Proceeds

Like commingled proceeds, cash proceeds can present special problems. Money, checks, deposit accounts and other similar payment instruments are all included under the definition of cash proceeds under Article 9.[59] Non-cash proceeds are simply defined as proceeds other than cash proceeds.[60]

Because of the specialized nature of cash as a bearer instrument, it can be difficult to establish with certainty that cash is directly attributable to the sale or other disposition of encumbered collateral. This problem can be exponentially magnified when cash proceeds are commingled with non-cash cash proceeds in an account. Article 9 recognizes the limitations of its scope with regard to issue and establishes that proceeds that are commingled with other property will be considered proceeds if they are iden-

---

[55] U.C.C. Rev. Art. 9 § 336(a). Revised Article 9 defines commingled goods as goods that are physically united with other goods in such a manner that their identity is lost in a product or mass

[56] U.C.C. Rev. Art. 9 § 336(a).

[57] U.C.C. Rev. Art. 9 § 336(b).

[58] U.C.C. Rev. Art. 9 § 336(d).

[59] U.C.C. Rev. Art. 9 § 102(a)(9).

[60] U.C.C. Rev. Art. 9 § 102(a)(58).

tifiable and traceable by a method of tracing permitted under law other than Article 9.[61]

B. MEXICAN LAW

The new STL does not distinguish between after-acquired property and proceeds where collateral descriptions are concerned. Consequently, the analysis contained in section IV (B) above applies equally here. The primary issue, as stated in before, is the type of general/generic descriptions allowed by the STL.

Pre-STL

Most security devices under previous Mexican law required delivery of the collateral to the secured party. Those devices that allowed the debtor to retain possession of the collateral did not allow the debtor to make use or dispose of the collateral in any way. The debtor was a mere depository for the goods. Under these rules, the concept of proceeds would be nonexistent.

New STL

The new STL expressly allows the debtor to use, and in some cases dispose of, collateral, thereby overturning previous law.[62] The STL states that a debtor, unless otherwise agreed, has the right to make use of the collateral, as well as to combine it with other goods and employ it in manufacturing.[63] In addition, proceeds produced from this use will automatically become part of the collateral pool used to secure a security interest.[64] The STL does contain one limitation, requiring that the value of the collateral is not diminished after use or disposition.[65]

Like Article 9, in order to allow the debtor to use the collateral, the STL allows the creation of a non-possessory pledge over mov-

---

[61] Proceeds that are commingled with other property are identifiable proceeds: (1) If the proceeds are goods, to the extent provided by Section 9-336; and (2) If the proceeds are not goods, to the extent that the secured party identifies the proceeds by a method of tracing, including application of equitable principles, that is permitted under law other than this article with respect to commingled property of the type involved. U.C.C. Rev. Art. 9 § 315(b).

[62] STL, Art. 356 concerning the non-possessory pledge and Art. 402 concerning the guarantee trust.

[63] STL, Arts. 356 and 402.

[64] STL, Section (I).

[65] STL, Section (I).

able goods that the debtor intends to use or dispose in some manner. However, unlike Article 9, which permits proceeds over all categories of goods, the new STL separates proceeds into three different types of goods created by such use or disposition.

First, the STL provides that this pledge may be cover proceeds that are goods obtained as future fruits or products of the original collateral.[66] This provision permits a security interest in agricultural proceeds, similar to production credits used under previous Mexican law.[67] Second, this pledge may cover goods that result from the physical transformation of the original collateral.[68] This rule permits security interests in the manufacturing process, which turn from raw materials to finished products inventory. Finally, this pledge may cover goods or receivables that a debtor received or has a right to receive in payment for the sale of the collateral.[69] This rule permits a security interest in the proceeds of the sale of the original collateral, such as in the sale of inventory. Like Article 9, this latter category includes the right to receive indemnity or insurance proceeds for the loss of or damage to the collateral.[70]

Together, these three provisions attempt to span all types of transactions that may require of security interests in proceeds. It is not clear what purpose is served by the STL's tri-partite approach. However, there does not appear to be any serious limitation in the application of this rule.

VI. FUTURE ADVANCES

In addition to allowing security interests to attach to future collateral as discussed above, another important feature of a modern secured financing system is to permit collateral to serve as security

---

[66] "A pledge without transmission of possession may be created over the following movable goods: … (iii) the goods that derive as future fruits or products, pending or present, of the original collateral." STL, Art. 355(iii).

[67] LGTOC, Art. 327.

[68] "A pledge without transmission of possession may be created over the following movable goods: … (iv) the goods that result from the process of transformation of the original collateral." STL, Art. 355 (iv).

[69] "A pledge without transmission of possession may be created over the following movable goods: … (v) the goods or rights that a debtor receives or has a right to receive, in payment for the sale to third parties of the encumbered collateral or as indemnity in case of loss or damage to such goods." STL, Art. 355 (v).

[70] STL, Art. 355.

for future obligations—commonly referred to as future advances—or fund disbursements made after creation and perfection of a security interest. To accomplish this, a law must permit a creditor to take a security interest that secures not only an original extension of credit but later or future obligations as well. Additionally, the amount or composition of the secured debts must be allowed to vary and include fluctuating amounts.

Together with after-acquired property and proceeds features, securing future advances is necessary to create a "floating lien," one of the most innovative practices permitted by modern secured financing statutes, where both the collateral pool and secured obligation can fluctuate.

A. REVISED ARTICLE 9

Both Pre-Revision and Revised Article 9 allow collateral to serve as security for future advances.[71] However, many of the problems discussed with regard to the taking of security in future collateral are also present when using collateral to secure future obligations.[72] For example, like with collateral, a security interest that covers future obligations poses special problems with regard to the description of that obligation.

Future advances can stem from a contractual obligation, such as in a line of credit available to the secured debtor. They can also stem from commercial realities of a particular transaction, where for example a growing debtor requires future disbursement of funds for a new line of goods. Article 9 contemplates both circumstances.

The general rule under Revised Article 9 establishes that a security agreement may provide that collateral secures future advances, whether or not the advances or value are given pursuant to commitment.[73] As such, both obligatory and optional types of future advances are covered by the statute, and collateral that secures an original disbursement of funds will also secure a later disbursement of funds or future advance.

In order for a security interest to extend to future advances, however, Article 9 requires that the security agreement contem-

---

[71] U.C.C. Rev. Art. 9 § 204(c); U.C.C. Pre-revision Art. 9 § 204(3).

[72] See sections IV and V supra.

[73] U.C.C. Rev. Art. 9 § 204(c).

plate this possibility.[74] Hence, secured creditors that intent to provide future advances secured with the original collateral pool should include a specific clause in the security agreement.[75]

Revised Article 9 also provides a special set of rules dealing with the priority of advances made by the secured creditor after a third party acquires an interest in the collateral.[76] Generally speaking, the time when an advance is made plays no role in determining priorities among conflicting security interests.[77] With regard to lien and judgment creditors, Article 9 establishes that the secured creditor has priority to the extent of future advances made regardless of when they were made, if the advance was obligatory in nature and entered into without knowledge of the intervening judgment.[78]

Under these rules, Article 9 allows for the securing of future advances contemplated or not contemplated at the time of the original agreement or at the original disbursement of funds. Although future advances may be provided for from the outset, the parties are free to negotiate later disbursements and enter into a new agreement to secure them. In addition, the parties may agree that a new advance be secured with the original collateral. If this is the case, no changes to the original registration are needed, and the new advance will have the same priority as the original. However, if the new advance is secured by new or different collateral, the parties must file a new financing statement.

B. MEXICAN LAW

As discussed above, Mexican law requires specific descriptions for secured property collateral.[79] Similarly, Mexican law requires specific descriptions for secured obligations. Consequently, Mexi-

---

[74] Official Comment 5, U.C.C. Rev. Art. 9 § 204(c). Under subsection (c) collateral may secure future as well as past or present advances if the security agreement so provides.

[75] See U.C.C. Rev. Art. 9 § 204(c).

[76] U.C.C. Rev. Art. 9 § 323.

[77] U.C.C. Rev. Art. 9 § 323(a).

[78] U.C.C. Rev. Art. 9 § 323(b) states that a security interest is subordinate to the rights of a person that becomes a lien creditor while the security interest is perfected only to the extent that it secures advances made more than 45 days after the person becomes a lien creditor unless the advance is made: (1) Without knowledge of the lien; or (2) Pursuant to a commitment entered into without knowledge of the lien.

[79] See sections IV and V supra.

can law provides little support for the registration of future and open-ended obligations. Secured parties are typically required instead to indicate the specific amount of the secured debt in order to perfect their security interests.

The STL attempts to do away with specificity requirements for secured obligations, expressly permitting security interests over future advances. On this issue, the STL provides some flexibility by allowing the secured obligation to be a sum that is determined or determinable at the time of creation of the security interest.[80] In the latter case, the STL requires that the sum be determined at the time of its enforcement.[81]

The STL expressly states that a non-possessory pledge can secure future obligations.[82] In addition, the STL further states that a security agreement does not have to contain a specific loan amount. Instead, the security agreement may provide a formula for determining the amount due at the time of default. This amount will be considered the secured obligation and may include future advances.

The STL further provides that the creditor may not enforce a security interest covering a future advance unless value was given under the formula contemplated in the security agreement. In this regard, the STL states that security interests that cover future advances cannot be enforced unless the principle obligation actually becomes payable.[83]

As described above, registry officials currently deny registration of security interests that provide general/generic descriptions of the collateral.[84] Likewise, registry officials will deny the registration of a security interest that does not provide a specific description of the secured obligation. As a result, the STL provides specific instructions to registry officials that this practice must be discontinued. This specific rule states that when dealing with secured obligations the amount of which may not be determined at the mo-

[80] STL, Art. 348.
[81] STL, Art. 348.
[82] STL, Art. 359.
[83] STL, Art. 359.
[84] See section IV B discussion of Description.

ment of registration, registration will proceed even when the total or maximum secured amount has not been provided.[85]

Once again, the STL goes against the grain of the previous legal framework, which rejects future advances. The previous system would consider any future advance as a new obligation, requiring new and separate creation and perfection actions. Consequently, the STL and current law come into direct conflict on this issue. To reduce potential frictions, creditors should draft future advance clauses that are mindful of traditional rules, which, if ignored, may prove costly in litigation.

Finally, future advances depend greatly on the secured party's ability to pre-register a registration form or financing statement that can cover future disbursements and loans. The ability to add new credit extensions to an initial security agreement and to modify the original loan terms also hinge on pre-registration. Typically, civil law requires that a security agreement pre-date registration of a credit or advance. Although it is possible that the new system will permit pre-registration practices, the STL does not expressly reverse this outcome. In addition, the new registry regulation does not address this issue.[86] Consequently, the result concerning pre-registration is not yet clear.

VII. PURCHASE MONEY SECURITY INTEREST

As discussed in sections IV and V above, a creditor's security interest can cover a debtor's after-acquired property and proceeds. Granting these two rights to the creditor, however, can create a security interest over all of the debtor's present and future goods. Broad liens of this type can place the debtor at a competitive disadvantage. As a debtor cannot provide unencumbered collateral for future loans, a debtor that has encumbered its after-acquired property and proceeds can be tied to credit stemming from a single source. The purchase money security interest (PMSI) alleviates this problem by creating an exception to the principle of first-in-time, first-in-right (prior tempore prior iure). This device allows a subsequent future creditor that provides specific purchase money to become first-in-right with regard to specific items or categories of collateral. In most cases, this priority rule stands irrespective of

[85] STL, Art. 378.

[86] Registry Regulation.

previous security interests that mention those types of goods as collateral. This special priority is given to the purchase money party to encourage the infusion of new assets and credit into the debtor's business.

A PMSI covers goods obtained on credit from the seller or obtained with funds provided by a creditor. In turn, these goods secure the total or partial payment of the purchase price. The main reason for the PMSI mechanism is that the debtor needs protection from a secured creditor who is unwilling or unable to provide additional funds. If a debtor is able to procure financing for a new line of goods, notwithstanding the prior interest, the PMSI will provide a new creditor with protection over previous secured creditors with respect to the financed goods. Although this action provides a security interest to the subsequent creditor, it does not affect the priority of the previous secured creditor with respect to previous goods.[87]

A. REVISED ARTICLE 9

Purchase money security interests receive special treatment under both Pre-revision and Revised Article 9, which generally translates into special priority vis-à-vis third parties. The general PMSI priority rule provides that a perfected PMSI has priority over a

---

[87] The following example illustrates the function of a Purchase Money Security Interest. Debtor (D), an agricultural enterprise, needs $1,000,000 (one million USD) to finance the purchase of agricultural equipment (including planting and seeding units, irrigation systems and combine tractors) needed for its annual production cycle. Creditor One (C1) makes a loan to D for that amount at a rate of 8 % interest. C1 takes a security interest over all of D's farming equipment, present and after-acquired, and perfects by filing at the proper registry location. During harvest time (nine months into the loan), D requires the purchase of an extra combine tractor at the price of $200,000. Under the terms of the loan, D can go to C1 and request the additional funds for the combine at the contract rate. Once purchased, C1's security interest would automatically cover the new combine. D, however, attempts to purchase and finance the tractor through Joe Moose Agricultural Equipment Company (JM), which is running a promotion for 0 % financing on its combines. During preliminary dealings, JM checks the local registry and discovers C1's security interest over all of D's present and future agricultural equipment, including combines. As a result, JM would be forced to take a junior priority over the combine if it chooses to sell on credit to D. In all likelihood, however, JM would refuse to take a second priority position over the combine and D would lose the finance savings of purchasing directly from JM. The Purchase Money Security feature alleviates this problem by allowing JM to take a PMSI over the single tractor financed by JM. This device then allows JM to become the first-priority creditor with regard to that one item of collateral, irrespective of C1's earlier security interest over all future combines. C1's security interest is otherwise unaffected by this transaction.

conflicting security interests in the same goods, if the purchase money security interest is perfected within 20 days of the debtor taking possession of the collateral.[88]

The innovative feature of the PMSI priority rule is that it provides an exception to the general Article 9 first-in-time priority rule.[89] A common situation in which this special priority feature operates concerns disputes between a non-purchase money security interest and purchase money security interests in the same collateral. The general rule in this case is that a purchase money security interest in collateral has priority over a non-purchase money security interest in the same collateral if the purchase money security interest is perfected when the debtor receives possession of collateral or within 20 days thereafter.[90] This rule operates regardless of when the previous non-PMSI security interest was created or perfected. In addition, this special priority rule also applies to proceeds of the purchase money collateral.[91]

Inventory PMSI

Although the Article 9 rule may seem straight forward, it is important to note that purchase money security interests in inventory can serve to mislead a preexisting creditor with a security interest in the debtor's inventory. As a result of the special concerns created by this type of transaction, Article 9 provides several important differences to the basic priority rule applicable to purchase money security interests in non-inventory goods.[92]

---

[88] U.C.C. Rev. Art. 9 § 324 (a).

[89] U.C.C. Rev. Art. 9 § 324 (a) provides and exception for inventory and livestock.

[90] "(a) Except as otherwise provided in subsection (g), a perfected purchase-money security interest in goods other than inventory or livestock has priority over a conflicting security interests in the same goods, and, except as otherwise provided in Section 9-327, a perfected security interest in its identifiable proceeds also has priority, if the purchase money security interest is perfected when the debtor receives possession of the collateral or within 20 days thereafter." U.C.C. Rev. Art. 9 § 324.

[91] For a more detailed description of the Article 9 rules concerning proceeds, see section V above.

[92] U.C.C. Rev. Art. 9 § 324:

(b) Subject to subsection (c) and except as otherwise provided in subsection (g), a perfected purchase-money security interest in inventory has priority over a conflicting security interest in the same inventory, has priority over a conflicting security interest in chattel paper or an instrument constituting proceeds of the inventory and in proceeds of the chattel paper, if so provided in Section 9-330, and, except as otherwise provided in Section 9-327, also has priority in identifi-

Under Revised Article 9, a purchase money security interest in inventory has priority over a non-purchase money security interest in the same type of inventory *only* if the former creditor notifies the latter that it has acquired or expects to acquire a purchase money security interest in the debtor's inventory. [93] Such notice must contain a valid description of the inventory covered or to be covered by the PMSI. The reasoning behind this requirement is that the preexisting non-purchase money creditor may rely on the additional inventory to make an extension of additional credit or other concession to the debtor. As a result, the non-PMSI creditor should receive notification that the new and additional inventory is encumbered by a PMSI in order to avoid making advances against these goods, which are of course encumbered by a subsequent purchase money creditor.

Another important difference Revised Article 9 makes for purchase money security interests in inventory is that it does not provide the 20-day window for perfection of a PMSI over non-inventory collateral mentioned above. When it comes to purchase money security interests in inventory, Revised Article 9 requires that the PMSI be perfected at the time the debtor takes possession of the collateral or before.[94]

---

able cash proceeds of the inventory to the extent the identifiable cash proceeds are received on or before the delivery of the inventory to a buyer, if:

(1) Purchase-money security interest is perfected when the debtor receives possession of the inventory;

(2) Purchase-money secured party sends an authenticated notification to the holder of the conflicting security interest;

(3) Holder of the conflicting security interest receives notification within five years before the debtor receives possession of inventory; and

(4) Notification states that the person sending notification has or expects to acquire a purchase-money security interest in inventory of the debtor and describes the inventory.

(c) Subsections (b)(2) through (4) apply only if the holder of the conflicting security interest had filed a financing statement covering the same types of inventory:

(1) If the purchase-money security interest is perfected by filing, before the date of the filing; or

(2) If the purchase-money security interest is temporarily perfected without filing or possession under Section 9-312(f), before the beginning of the 20-day period thereunder.

[93] U.C.C. Rev. Art. 9 § 324(b)(2), (b)(4), and (c).

[94] U.C.C. Rev. Art. 9 § 324(b)(1).

A third important limitation imposed by Article 9 on purchase money security interests in inventory concerns claims over the proceeds of the inventory.[95] Generally speaking, the Article 9 priority over proceeds is much more limited when dealing with a PMSI. In most cases, A PMSI creditor would have PMSI priority only to identifiable cash proceeds.[96]

Unlike Pre-revision Article 9, Revised Article 9 also deals with three specialized types of conflicts in the PMSI context: conflicts between non-PMSI vs. PMSI in livestock;[97] conflicts between non-PMSI vs. PMSI in software;[98] and conflicts between competing PMSIs.[99]

---

[95] U.C.C. Rev. Art. 9 § 324(b).

[96] U.C.C. Rev. Art. 9 § 330.

[97] U.C.C. Rev. Art. 9 § 324:

(d): Subject to subsection (e) and except as otherwise provided in subsection (g), a perfected purchase-money security interest in livestock that are farm products has priority over a conflicting security interest in the same livestock, and, except as otherwise provided in Section 9-327, a perfected security interest in their identifiable proceeds and identifiable products in their unmanufactured state also has priority, if:

(1) Purchase-money security interest is perfected when the debtor receives possession of the livestock;

(2) Purchase-money secured party sends an authenticated notification to the holder of the conflicting security interest;

(3) Holder of the conflicting security interest receives the notification within six months before the debtor receives possession of the livestock; and

(4) Notification states that the person sending the notification has or expects to acquire a purchase-money security interest in livestock of the debtor and describes the livestock.

(e) Subsections (d)(2) through (4) apply only if the holder of the conflicting security interest had filed a financing statement covering the same types of livestock:

(1) If the purchase-money security interest is perfected by filing, before the date of the filing; or

(2) If the purchase-money security interest is temporarily perfected without filing or possession under Section 9-312(f), before the beginning of the 20-day period thereunder.

[98] U.C.C. Rev. Art. 9 § 324 (f) Except as otherwise provided in subsection (g), a perfected purchase-money security interest in software has priority over a conflicting security interest in the same collateral, and, except as otherwise provided in Section 9-327, a perfected security interest in its identifiable proceeds also has priority, to the extent that the purchase-money security interest in the goods in which the software was acquired for use has priority in the goods and proceeds of the goods under this section.

B. MEXICAN LAW

Although not referred to expressly as a Purchase Money Security Interest, the new STL provides a mechanism to protect debtors who have created security interests in their present and future property. Like the PMSI, this feature allows debtors to obtain purchase money credit for additional goods, irrespective of prior security interests.[100]

The STL provides in part that debtors who previously encumbered their present and future movable collateral can grant a security interest to new creditors over specific items of collateral acquired with the funds granted by the new creditor.[101] The STL handles priority by allowing the first creditor to continue having payment preference over the movable goods encumbered by its security interest and creates a first-in-time exception for goods specifically acquired by the debtor with funds from the new creditor.[102] This latter creditor will take payment preference over the specifically acquired movable goods encumbered by its security interest.[103]

---

[99] U.C.C. Rev. Art. 9 § 324(g):

(g) If more than one security interest qualifies for priority in the same collateral under subsection (a), (b), (d), or (f):

(1) A security interest securing an obligation incurred as all or part of the price of the collateral has priority over a security interest securing an obligation incurred for value given to enable the debtor to acquire rights in or the use of collateral; and

(2) In all other cases, Section 9-322(a) applies to the qualifying security interests.

[100] STL, Art. 358 states as follows:

> Irrespective of the fact that a debtor may have created a pledge without transmission of possession over all of the movable goods it uses in the realization of its preponderant activities, the debtor may grant a security interest to other creditors over the goods that it acquires with the proceeds of a credit granted by these new creditors.
>
> In this case, the first creditor will continue having priority in the payment of its credit over all of the movable goods that the debtor encumbered in its favor, in front of any other creditor, with the exception that the goods acquired by the debtor, with the resources provided by the new creditor, may serve as collateral for this latter creditor and may secure the priority in the payment with respect to any other creditor of the debtor, including the first creditor.

[101] "Application of this device applies exclusively for security interests using a pledge without transmission of possession." STL, Art. 358.

[102] STL, Art. 358.

[103] STL, Art. 358.

Like Article 9, the purchase money provisions of the STL require that a purchase money security interest be an enabling credit. That is to say that credit funds must enable the debtor to obtain the goods that will serve as collateral. Unlike Article 9, however, the STL places limitations on the types and amounts of collateral that can exist prior to the operation of the purchase money exception. The STL states that a new creditor can obtain a security interest in purchase money collateral even when a previous security interest exists over all of the movable goods that the debtor uses in the realization of its preponderant activities.[104]

This rule raises two further questions. First, under the wording of the statute, it appears that the debtor must encumber all of its movable property before using the purchase money feature. It is not clear from this wording what is meant by all of the debtor's movable property, that is to say whether this requirement includes all present and future types of tangible, intangible, and payment property. It is further unclear as to what determination must be made to ensure all property has been encumbered before the purchase money feature is available or whether it is the obligation of the creditor or the debtor to make that determination. Finally, the outcome of a purchase money credit issued prior to all property being encumbered is also unclear. The statue provides little guidance for the courts on these issues.

The second question raised by the statute stems from the requirement that all the encumbered movable goods be used in the debtor's "preponderant activity." The statute does not define this term. However, the term is used throughout the statute in ways similar to the Article 9 concept of the ordinary course of business.[105] Again, as was the case with the requirement that all goods be encumbered, the STL does not provide clear guidelines to determine the practical application of this requirement that limits the manner in which collateral can be used by the debtor.

---

[104] STL, Art. 358. The original wording in Spanish states as follows:

> No obstante que el deudor dé en prenda sin transmisión de posesión a su acreedor todos los bienes muebles que utilice para la realización de sus actividades preponderantes, el deudor podrá dar en garantía a otros acreedores, en los términos previstos en esta Sección Séptima, los bienes que adquiera con los recursos del crédito que le otorguen los nuevos acreedores.

[105] See, infra, section VIII B describing the concept of Ordinary Course of Business under the New Mexican Secured Transactions Law.

What is clear, however, is that both these limitations (neither of which exists under Article 9) can function as considerable barriers to various types of transactions. The STL makes a policy choice on this issue that is opposite to that of Article 9, placing greater importance on protecting the original creditor and its security interest than in protecting the debtor and its ability to obtain new credit.

Title Retention as PMSI

Before the advent of the STL, Mexican law used title retention devices as PMSI mechanisms. The STL continues to allow this practice whereby creditors can retain title to collateral in both non-purchase money and purchase money cases. Title retention—a legal figure in which the debtor has possession of the property and the creditor has legal title or ownership—is used primarily if not exclusively as PMSI. The most common use is the conditional sales contract in which a debtor acquires goods on credit.[106] To secure the payment of the purchase price, the seller (or creditor) retains the title to the property. Considering that the debtor is not the possessor of legal title to the new goods, such collateral could not become encumbered by a previous security interest over the debtor's property. Consequently, debtors that previously encumbered their present and future property can use this device as a PMSI security interest to finance new collateral.

Description Specificity

Like many figures under Mexican law, the PMSI features of both the STL and previous title retention devices require that collateral be specifically identifiable. The STL provides that the purchase money exception applies exclusively with specifically identifiable movable goods.[107] As a result, PMSI financing functions well with property that can be individually identified (e.g. equipment and machinery), but less well with property that can only be

[106] Código Civil Federal, (Federal Civil Code), published in the D.O. May 26, 1928, amended on May 29, 2000, Arts. 2310-2312.

[107] STL, Art. 358, paragraph two, states in full that: "The [purchase money] exception contained in this Article will continue exclusively when dealing with movable goods that can be identified with complete precision and that can be distinguished from the rest of the movable goods that the debtor may have given in pledge to the first secured creditor."

described in general/generic fashion (e.g. inventory, fungible goods, etc.).

Commingling of Goods

The STL also contains a rule that states that purchase money credit cannot be used to obtain goods similar to those given in security to a previous creditor. Specifically, the STL states that movable goods subject to a PMSI must be distinguished from the rest of the movable goods that the debtor may have encumbered in favor of a previous secured creditor.[108]

The reasoning behind this limitation is to avoid confusion concerning the commingling of collateral. However, the language requiring that goods must "be distinguished" from other collateral can lead to confusion. For example, would a tractor combine manufactured by Joe Moose be distinguishable from a similar tractor manufactured by John Deere? Or are all tractors such that they are indistinguishable from each other? The statute does not provide clear guidelines for making this determination, potentially leaving room for litigation in the future. Although it is unclear how this provision will operate, it is important to note that the STL again places greater importance in protecting the original secured party than in allowing the debtor to obtain purchase money credit.

Inventory PMSI

Except for its strict rules on the specificity of collateral, the STL does not contain specific rules for purchase money inventory.[109] With few exceptions, such as cars and other big-ticket items, inventory cannot be described with specificity. Even in those cases in which the inventory can be described specifically, practical concerns render such descriptions inoperable. Consequently, this requirement hinders PMSI financing for inventory and the STL does not do enough to avoid potential problems between inventory creditors and purchase money creditors with an interest in inventory.

These problems are compounded when the inventory is sold, generating proceeds, an issue that is also not properly addressed by

---

[108] STL, Art. 358, paragraph two, states in full that: "The [purchase money] exception contained in this Article will continue exclusively when dealing with movable goods that can be identified with complete precision and that can bedistinguished from the rest of the movable goods that the debtor may have given in pledge to the first secured creditor."

[109] See section IV B discussion of Description.

the STL. Unlike Article 9, which resolves the priority conflict over proceeds by limiting the proceeds stemming from the sale of purchase money inventory, the STL does nothing.[110] Moreover, unlike Article 9, the STL does not require that a purchase money creditor notify a previous inventory creditor concerning purchase money additions to the collateral pool. As we have seen, this practice is necessary to help an inventory financier to avoid making future disbursements of funds based on collateral that does not secure the original loan. The STL does not provide any guidance on these issues, which can cause problems for Mexican courts.

Judicial Creditors

Another impediment to secured financing under Mexican law is the long-standing priority of labor liens over all types of secured loans. In this regard, the Mexican Civil Code establishes that, in the case of insolvency, labor liens will have priority over secured loans. The anti-creditor effect of this rule makes most creditors even more hesitant to lend to a debtor that may fall into insolvency or activate labor liens. The new STL creates an exception to this rule with regard to enabling credits, such as purchase money security interests. Here, the STL states that when the goods subject to a security interest are acquired with the proceeds of a secured credit, a creditors priority will prevail over the privilege corresponding to the labor liens and creditors.[111]

---

[110] Revised article 9 regulates competing claims over the proceeds of inventory, by limiting a PMSI priority in proceeds to identifiable cash proceeds. See discussion of priority in section VII B.

[111] STL, Art. 367 states as follows:

> Creditors secured with a pledge without transmission of possession will receive the principle and interest of their credits from the proceeds of the goods given as collateral for those security interests, with absolute exclusion of all other creditors of the debtor.
>
> The foregoing provision does not affect the preferences that according to Mexican law correspond to labor liens against the debtor.
>
> In every case, levies for labor debts that cover goods in possession of the debtor must take place exclusively over those goods that cover the balance of the corresponding labor lien.
>
> When the goods subject to a security interest have been acquired directly with the proceeds of a secured credit, the priority established in this article, in reference to

VIII. BUYER IN THE ORDINARY COURSE

An important objective in inventory financing is the protection of those who buy items of collateral from the debtor in the ordinary course of the debtor's business. Such buyers must take free of a security interest created by the seller. This rule should apply even when a secured creditor is perfected and when the buyer knows of the existence of the security interest. In general, this rule creates an exception to the secured party's in rem right to follow the collateral into the hands of whoever acquires it from the debtor.

A. REVISED ARTICLE 9

The U.C.C. defines a buyer in ordinary course of business (BIOC) as a person that buys goods in good faith, without knowledge that the sale violates the rights of another person in the goods, and in the ordinary course from a person in the business of selling goods of the kind purchased.[112] It should be noted, though, that a buyer from a pawnbroker cannot be a buyer in the ordinary course.[113] The U.C.C. goes on to state that a buyer in ordinary course of business may be a buyer for cash, by exchange of other property, or on secured or unsecured credit, and may acquire goods or documents of title under a pre-existing contract for sale.

This definitional rule, however, does make two exclusions: bulk transfers and sales in total or partial satisfaction of a debt. To this effect, U.C.C. Article 1 states that a person that acquires goods in a transfer in bulk or as security for, or in total or partial satisfaction of, a money debt is not a buyer in ordinary course of business.[114] Finally, it should also be noted that only a buyer that takes possession of the goods or has a right to recover the goods from the seller can qualify as a buyer in ordinary course of business.

This definition can be divided into three principal requirements necessary for a person to qualify as a BIOC. First, the buyer must buy from a seller who is in the business of selling the types of

---

the mentioned goods, will prevail over the privilege corresponding to the creditors mentioned in the second paragraph of this provision.

[112] U.C.C. Art. 1 § 201(9). In addition, a person buys goods in the ordinary course if the sale to the person comports with the usual or customary practices in the kind of business in which the seller is engaged or with the seller's own usual or customary practices.

[113] Art. 1 § 201.

[114] U.C.C. Art. 1 § 201(9).

goods acquired. Second, the buyer cannot buy a bulk quantity of the seller's goods. And third, the buyer must give new value (cash or indebtedness) for the acquisition. If these conditions are met, a buyer would generally take free of a security interest created by the person from whom the buyer buys the goods. This would be true even though a properly and timely perfected security interest may exist over the collateral.

The general rule under Pre-revision and Revised Article 9 establishes that if a buyer qualifies as a BIOC, such buyer takes free of a security interest created by its seller. This would be true even if the security interest had been perfected and the buyer had known of its existence.[115]

Buyers of consumer goods can also qualify for protection under the Article 9 concept of the buyer in the ordinary course. Here, the exception provides that a buyer of goods from a person who used or bought the goods for use primarily for personal, family, or household purposes takes free of a security interest, even if it us perfected.[116] However, for this rule to apply the buyer has to buy with the following conditions:

(1) without knowledge of the security interest;

(2) for value;

(3) primarily for the buyer's personal, family, or household purposes; and

(4) before the filing of a financing statement covering the goods.[117]

B. MEXICAN LAW

Like Revised Article 9, the STL attempts to provide protection to ordinary course buyers by terminating a creditor's right to repossess goods sold in the debtor's "preponderant" activity. The STL states that the debtor has the right, unless otherwise agreed, to sell encumbered inventory in the ordinary course of its preponderant activity. In this case, the effects of the security interest and

---

[115] However, subsection (a) does not provide BIOC protection to a person buying farm products from a person engaged in farming operations. U.C.C. Rev. Art. 9 § 320(a). See also U.C.C. Pre-revision Art. 9 § 307(1).

[116] U.C.C. Rev. Art. 9 § 320(b).

[117] U.C.C. Rev. Art. 9 § 320(b).

creditor's rights of persecution over the collateral terminate in relation to parties who acquire in good faith. In return, the secured creditor will receive a security interest in the goods or rights that the debtor receives or has a right to receive in payment for the sale of such goods.[118]

This rule encourages buyers to buy from merchants without concern for acquiring encumbered property. However, as seen under Article 9, modern secured financing statutes require three basic conditions for the proper operation of a rule to protect ordinary course buyers while ensuring the proper functioning of the underlying security interest. Those conditions include the following: (1) the seller must be in the business of selling the type of goods acquired; (2) the buyer must give new value for the goods acquired; and (3) the buyer may not acquire in bulk or acquire a disproportionately large quantity of the seller's inventory. The STL provides a rule directly on point with regard to condition number one but is completely silent with regard to conditions two and three.

The first condition requires that the seller be in the business of selling the type of goods acquired by the buyer. In other words, a secured party's right to the collateral will terminate only if the debtor is in the business of selling the types of goods disposed of. To illustrate, a jeweler is in the business of selling jewelry and not in the business of selling equipment (glass cabinets or safes). Consequently, a person who buys a safe or a glass cabinet from a jeweler would not qualify as an ordinary course buyer.

The new STL may cause interpretation problems with regard to this condition. Instead of using the words "in the ordinary course of business," Article 356(III) states "in the ordinary course of its preponderant activity." This language is not equivalent. Whereas the Article 9 rule allows for a fact-based inquiry into the business activities of the debtor, the STL rule may require a determination based on activities as described in debtor's bylaws or articles of incorporation. That is to say, if a jeweler's articles of incorporation state that it may sell glass cabinets and safes (regardless of whether the debtor is in fact in the business of selling such goods), then this

---

[118] STL, Art. 356 (III) states that the debtor has the right to sell the encumbered goods, in the ordinary course of its preponderant activity, in which case the effects of the security interest and rights of persecution will terminate in relation to parties who acquire in good faith, providing in pledge the goods or rights that the debtor receives or has a right to receive in payment for the sale of such goods.

sale may be considered to be in the "course of its preponderant activity"—the legal basis ordained in the debtor's charter. As a result, the STL may protect a buyer who obtained the cabinets and safes, even though this buyer should be subject to the security interest.

The second condition requires that ordinary course buyers give new value for the purchased goods. The argument can be made that this requirement is implied in any sale. After all, a buyer, by definition, must pay for the goods. However, the STL does not include express reference to this rule. As a result, the new law may allow a secured debtor to sell collateral to a buyer (previous creditor) in payment for a previous debt. This result would allow the parties to circumvent the objective of a secured transaction—to give first-in-time priority to the secured creditor—thereby severely undermining the operation of the STL.

The third condition regulates the volume of goods purchased. Again, the STL is silent in this regard. The general rule of thumb for determining an ordinary course sale is that the quantity of goods purchased must be for the buyer's own use or the buyer is acting as a normal consumer. Under an ideal system, a buyer who purchases a disproportionately large quantity of the debtor's inventory would not qualify as an ordinary course buyer and thus could not obtain protection from a secured creditor. The new law, in contrast, can be used to protect a buyer who purchases a secured party's entire collateral base, as long as the sale was in the debtor's preponderant activity. This rule also undermines the policy objectives of ordinary course buyer protection. As a result, creditors must be very careful to ensure their transactions are not open to abuses by debtors and buyers in the ordinary course.

In addition, the STL requires compliance with several specific instructions not required under Article 9. These instructions dictate the type of buyers to which the debtor may sell collateral in the ordinary course, the location at which the collateral must be kept, and the minimum sale price acceptable for ordinary course sales.

To this effect, the STL requires the security agreement to contain the following instructions for these types of sales:

(1) the location at which the encumbered goods will be located;

(2) the minimum that the debtor must receive for the sale;

(3) the characteristics or categories of persons to which the debtor may sell;

(4) the manner in which cash, goods, or rights received in payment are handled; and

(5) the information that the debtor must deliver to the creditor concerning the transformation, sale, or transfer of the mentioned goods.[119]

A violation of any of these provisions gives rise to an accelerated default of the security interest. In addition, a creditor may terminate a debtor's right to sell in the ordinary course by giving notice of the creditor's intention to begin enforcement actions against the debtor.[120]

Previous Mexican law allowed debtors to retain possession of the collateral in very few instances. In the few instances in which Mexican law permitted debtors to retain possession, the law did not allow them to dispose of the collateral in any form. As a result, Mexican lawmakers feared that debtors might abuse this right. The objective of Article 356 is to limit the debtor's discretion in this regard.

IX. REGISTRATION NOTICE

Modern secured transactions create a setting in which property in possession of one party may serve as security in a favor of a different party. For such a system to operate correctly, it must notify third parties of circumstances where possession is not indicative of complete ownership. If proper notice is not provided, subsequent parties (both purchasers or lenders) may believe that a debtor's goods are free of encumbrances. Absent this notice, third parties may purchase or lend against the collateral.

The most effective method for providing notice is filing/registering a registration form (financing statement) at a legislatively established location. Under modern secured transactions statutes, creditors must comply with notice/registration requirements in order to obtain priority over competing claimants (purchaser or subsequent creditors). Perfection of a security interest is the term given when a creditor complies with the notice requirements, and the debtor acquires rights to the collateral. Failure to perfect a security interest exposes the creditor's right to competing claims. Although

[119] STL, Art. 357.
[120] STL, Art. 357.

it should be noted that registration is not the sole method for perfection, it is the most common method.

A. REVISED ARTICLE 9

The primary purpose behind Article 9 is to ensure that a secured creditor receives priority over collateral serving as security for a loan, vis-à-vis third parties. In order to accomplish this goal, Article 9 generally establishes priority at the time of perfection. Perfection, in turn, is the step taken by the secured creditor to put the world on notice that a debtor's collateral is encumbered by a security interest. Once notice is given to all third parties, a secured creditor can be assured of a reliable priority over the collateral.

Registration Document

Although there are some exceptions, the main method for perfection of an Article 9 security interest is the registration of a one-page form.[121] This form, typically called a financing statement or a "U.C.C. 1," is a one-page registration form that contains information to provide the requisite notice to third parties of the creditor's security interest in the collateral. Under Article 9, the registration form requires only sufficient information to put third parties on notice. To this effect, a properly registered financing statement is valid if it provides the name of the debtor, the name of the secured party, and a description of the collateral covered by the security interest.[122]

The information contained in the financing statement communicates only preliminary notice to third parties. Since, as we have mentioned, a financing statement must contain only the name of the debtor and the secured party, as well as a description of the col-

[121] U.C.C. Rev. Art. 9 § 310 (b). However, Article 9 also provides that the registration of a financing statement is not necessary to perfect a security interest: perfected under Section 9-308(d), (e), (f), or (g); perfected under Section 9-309 when it attaches; in property subject to a statute, regulation, or treaty described in Section 9-311(a); in goods in possession of a bailee which is perfected under Section 9-312(d)(1) or (2); in certificated securities, documents, goods, or instruments which is perfected without filing or possession under Section 9-312(e), (f), or (g); in collateral in the secured party's possession under Section 9-313; in a certificated security which is perfected by delivery of the security certificate to the secured party under Section 9-313; in a deposit account, electronic chattel paper, investment property, or a letter-of-credit right which is perfected by control under Section 9-314; in proceeds which is perfected under Section 9-315; or that is perfected under Section 9-316.

[122] U.C.C. Rev. Art. 9 § 502(a)(1)-(3).

lateral serving as security for the loan, third parties must inquire further to discover particular details of any existing security interest.[123] That is to say, once a third party has received preliminary notice of a security interest, the onus is on this party to conduct a further inquiry to obtain further details concerning that transaction.

Although registration rules are generally similar under Pre-revision and Revised Article 9, it should be noted that Revised Article 9 makes two important changes to the registration form. The first change is that the new statute does not require the secured party's address. [124] The second change is that Revised Article 9 also eliminated the need for the debtor's signature.[125] The first change appears to be recognition that sufficient notice is provided without further details concerning the secured creditor, while the second change is recognition that the elimination of signatures facilitates electronic filing.[126]

Article 9 also contains additional filing requirements for specialized types of collateral. For example, when dealing with security interests in collateral incorporated into real estate, Article 9 requires notice in the real estate records, referred to as a fixture filing.[127] This specialized registration play two roles. First it protects the secured creditor from a preexisting mortgage creditor whose mortgage may otherwise glom-on to the personal property collateral. Second, the registration provides notice to the mortgage lender that goods subject to an Article 9 security interest have been or will be incorporated into the real property subject to its mortgage.

---

[123] U.C.C. Rev. Art. 9 § 502.

[124] U.C.C. Pre-Revision Art. 9 § 402(1) stated that, to be sufficient, a security interest required the address of the secured party from which information concerning the security interest could be obtained. This provision also required the mailing address for the secured debtor.

[125] Under the rationale that the secured debtor was the only adversely affected party, Pre-revision Article 9 required only the debtor's signature. U.C.C. Pre-Revision Art. 9 § 402(1). However, it should be noted that Pre-revision Article 9 allowed the signature of the secured creditor in lieu of that of the debtor in certain circumstances. U.C.C. Pre-Revision Art. 9 § 402(2).

[126] It should be noted, however, that despite the elimination of signatures from the registration form, only filings duly authorized by the debtor can take place. U.C.C. Rev. Art. 9 § 509(a) establishes that a person may file a financing statement only if the debtor authorizes the filing in an authenticated record.

[127] The special requirements for a fixture filing also apply to filings covering as extracted collateral, such as minerals and timber. U.C.C. Rev. Art. 9 § 502(b).

Unlike Pre-revision Article 9, which allowed each state to have its own registration form, Revised Article 9 attempts to create a national standardized form.[128] Although Revised Article 9 does not expressly require that all states move away from the use of local variations of the "UCC 1," it does encourage this result. In addition, Revised Article 9 requires all state registries to accept the standard form when it is presented and sets limits on state registries concerning when them may accept or reject a filing.[129] As a result, Article 9 ensures that a registry officer will not reject the national form if it contains the required information.

Finally, it is important to note that Revised Article 9, like Pre-Revision Article 9 establishes that a financing statement that contains flaws but that otherwise substantially complies with its requirements will nonetheless be effective.[130]

Registration Timing

The timing of a registration is another critical element in the perfection process. As mentioned before, the primary purpose behind Article 9 is to ensure that a secured creditor receives priority against third parties. This priority, in turn, is determined by the principle of first-in-time, first-in-right. That is to say, the creditor that registers its security interest first will have priority over subsequent parties. As a result, creditors have a big incentive to register their security interests as quickly as possible.

In recognition of this motive, Article 9 is designed to allow registration to take place as early as possible. In effect, Article 9 does not require even the existence of a security agreement in order for registration to take place, requiring simply that the debtor have authorized the registration.[131] This practice, referred to as pre-registration, is necessary to secure future advances and to fix a creditor's priority.[132]

The operative timing component under the Article 9 registration process is the communication of the form to the registry.[133] A creditor's priority will generally commence once the registration form

---

[128] U.C.C. Rev. Art. 9 § 521.
[129] U.C.C. Rev. Art. 9 §§ 520 and 519(h).
[130] U.C.C. Rev. Art. 9 § 506.
[131] U.C.C. Rev. Art. 9 § 502(d).
[132] See supra sections VI (A) and (B).

has been presented (or communicated) to the registry, and the registration fee has been paid, and the document accepted. In short, this provision establishes that priority is governed by the time a registration form is properly presented or accepted for filing.

Considering the potential dangers of any delay between the time of communication or presentation of a record and the time in which it becomes available for consultation by third parties, Revised Article 9 allows a registry to perform registration functions pursuant to that office's internal rules. However, Article 9 requires that all records presented for registration must appear for consultation by third parties no later than two business days after the registry receives the record in question.[134]

Registration Location

The final component in the Article 9 registration process is the determination of the proper place in which to register the security interest. To do so, however, a creditor must first determine the proper U.S. state in which the registration must take place. Once the creditor has figured out the state, the creditor must then determine the proper registration location within the state. Pre-revision Article 9 provided comprehensive rules to determine the proper state and location of the registration.[135] Revised Article 9 attempts to simplify this process by establishing that the law of the location of the debtor determines the location of the registration.[136] In simple terms, Revised Article 9 requires registration in the central registry for the state in which the debtor is located.

Revised Article 9 also changes rules under Pre-revision Article 9 for establishing the location for registration within a given state. Under the previous statute, registration depended on three alternatives and whether the collateral required local or central filing—local filing took place at a local county registry while central filing took place at a single statewide level, generally at the Office of the Secretary of State in the capitol.[137] However, Revised Article 9

---

[133] U.C.C. Rev. Art. 9 § 516(a) states that a communication of a record to a filing office and tender of the filing fee or acceptance of the record by the filing office constitutes filing.

[134] U.C.C. Rev. Art. 9 § 519(h).

[135] U.C.C. Pre-revision Art. 9 § 103.

[136] U.C.C. Rev. Art. 9 § 301.

[137] U.C.C. Pre-revision Art. 9 § 401(1).

limits the operation of local filing, making central filing the norm.[138]

Again, as a central rule, the registration location under Revised Article 9 is the designated central registry of the debtor's location. However, this statute continues to require a local county-level registration for security interests in fixtures, extracted collateral, and timber to be cut.

B. MEXICAN LAW

The new Mexican Secured Transactions Law, as described in the sections above, provides general registration rules. However, this collection of statutes does not contain a comprehensive registration system. For this purpose, the Mexican Legislature enacted a Commercial Registry Law (CRL) on May 29, 2000,[139] and the Mexican Executive Branch enacted a Commercial Registry Regulation on October 24, 2003.[140] The CRL, relatively short in scope and length, was part of a larger electronic commerce bill, the main purpose of which was to create a federal database of commercial registry records, currently located at the state level. The main purpose of the CRL regulation was to provide the basis for an electronic registration system for the registry of commerce. A secondary purpose of these instruments was to install an electronic information program to regulate electronic communications between the states a newly created federal database.

Historically, the Public Registry of Commerce contains very few records of security interests over personal property. Records contained in these registries almost exclusively center on business entities and include articles of incorporation, bylaws, powers of attorney, etc. As a result, before the enactment of the STL and CRL, the registry laws and rules provided little guidance for perfection/registration of security interests in personal property.

As with Article 9, the following sections analyze the CRL and the registry regulation by examining the three most important ele-

---

[138] U.C.C. Rev. Art. 9 § 501. For cases in which local filing is still necessary, Revised Article 9 requires registration only in local real estate records, rather than both real estate and personal property records as required by previous law.

[139] Commercial Registry Law, published in D.O. May 29, 2000, www.siger.gob.mx/legismerc/electron.html.

[140] Registry Regulation, published in D.O. Oct. 24, 2003, www.siger.gob.mx/siger/RRPC18.htm.

ments: 1) registration document; 2) registration timing; and 3) registration location.

Registration Document

Traditional Mexican registration law requires the registration of transactional documents, a practice deeply rooted in all civil law systems. With secured transactions, this rule required that creditors file the entire security agreement or agreements. The CRL, however, moves away from document filing, toward the filing of registration forms similar in many ways to the UCC 1 financing statements under Article 9.[141]

The importance of this advance cannot be understated. Several modern secured transactions practices, including securing future advances, floating liens, lines of credit, etc., would not be possible under a transactional filing system. Copies of the pre-codified forms have been published in the Official Gazette.[142] Forms M-21, M-35, and M-36 provide for the registration of security interests using the devices provided for in the STL.[143]

Although these forms represent a significant advance in registry practices in Mexico, they require much more information than a financing statement under Revised Article 9, which simply requires the identification of the debtor, the creditor, and the collateral.[144] These forms contain 23 data-fields. Among other requirements, the forms generally provide for registration of the following information:

(1) identification of the debtor (name, address, and representative);

(2) identification of the creditor (name, address, and representative);

---

[141] The new system uses pre-codified forms for the various registration requirements. Commercial Registry Law, Art. 21 (bis); Registry Regulation, Art. 2.

[142] Acuerdo que establece las formas para llevar a Cabo las Inscripciones en el Registro Público de Comercio (Decree establishing the forms necessary to carry out registration in the Public Registry of Commerce) [hereinafter Registry Forms], published in D.O. Sept. 18, 2000.

[143] Registry Forms. The various forms used under the new CRL maybe downloaded at the following address maintained by the Mexican Ministry of Economy: www.siger.gob.mx/siger/fp.htm

[144] See supra Section IX: Revised Article 9.

(3) folio number assigned by the registry (including volume number, book number, and page number);

(4) identification of the public official before which the transaction is brokered;

(5) description of the collateral; and

(6) description of the secured obligation (including payment terms.[145]

Registration Timing

Under the STL, registration is the exclusive method for perfection of a security interest. Article 366 of the STL establishes that a security interest is effective against third parties from the *date* of its registration.[146] In a very similar rule, Art 368 of the STL states that a security interest has priority from the *moment* of its registration.[147] An additional priority rule provides that a secured creditor will receive the principle and interest of his credits from the proceeds of the collateral with absolute exclusion of all other creditors of the debtor.[148]

There is no clear reason why the STL contains two such similar, nearly repetitive (or perhaps conflicting) priority rules. Article 366 states that the creditor will receive priority from the date of registration. Article 368, on the other hand, states that a creditor will receive priority from the moment of registration.

Although it is likely that these provisions intended to embody the same rule, the difference can be of some importance in cases where competing security interests are filed on different hours of the same day. The disparate language in these two provisions may cause confusion and may produce litigation at a future point. What is clear, however, is that a creditor must register its security interest to obtain priority. As under Article 9, the earlier the registration takes place, the better.

---

[145] Registry Forms, published in D.O. Sept. 18, 2000.

[146] Referring specifically to the Pledge without Transmission of Possession, this Article provides the following: The pledge without transmission of possession will be effective against third parties from the date of its registration in the registry. STL, Art. 366.

[147] Also referring to the pledge without transmission of possession provides the following: a pledge without transmission of possession will have the priority referred to in the Article 367 from the moment of is registration. STL, Art 368.

[148] STL, Art. 367.

Registration Location

With regard to the place of registration, the STL follows a rule similar that of Revised Article 9, requiring that registration take place at the debtor's domicile. Under the STL, the creation, modification, termination, assignment, and any judicial resolutions over a security interest must be registered in the Public Registry of Commerce for the location in which the debtor is domiciled.[149] For specialized types of collateral (e.g. real property fixtures), the STL also requires a special registration.[150]

The rule under the STL thus requires that registration take place at the state level—like the U.S., Mexico is a federalist system of government composed of states. Historically, however, state registry systems have been plagued by lack of uniformity and other problems. As a result, the CRL creates a new centralized database to coordinate and safeguard information. This database, housed in the offices of the Ministry of Economy in Mexico City, will contain a copy of all state registrations and will have the following function: to capture, maintain, safeguard, disseminate, reproduce, verify, administer, and transmit registry information.[151] To achieve this result, the Ministry of Economy has entered into Cooperation and Coordination Agreements with thirty one of Mexico's thirty two states.[152] Based on these agreements, the CRL requires that

---

[149] STL, Art. 376.

[150] STL, Art. 376.

[151] Registry Regulation, Art. 4; Commercial Registry Law, Art. 20.

[152] Coordination and Cooperation agreements, subscribed between the Ministry of Economy and each of the Mexican States. Coordination and Cooperation Agreement between the Ministry of Economy and the State of Aguascalientes, published in D.O., July 31, 2001; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Baja California, published in the D.O., July 2, 2002; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Baja California Sur, published in D.O., March 29, 2002; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Campeche, published in D.O., July 7, 2002; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Chiapas, published in D.O., December 28, 1999; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Chihuahua, published in the D.O., December 2002; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Coahuila, published in D.O., December 21, 2000; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Colima, published in D.O., November 24, 2000 and August 20, 1998; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Durango, published in the D.O., October 6, 2000; Coordination and Cooper-

each state provide a copy of all security interests filed in that state. The transmission of this information is accomplished electronically via secure means. The Ministry of Economy provides the technology and training to allow the states to use the federal database. This system preserves the local nature of the current registry framework while linking registry locations within a state to a statewide database of records and, in turn, to a federal database that contains all nationwide registrations.[153]

---

ation Agreement between the Ministry of Economy and the State of Guanajuato, published in D.O., September 25, 2001; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Guerrero, published in the D.O., November 17, 1999; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Hidalgo, published in D.O., November 2002; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Jalisco, published in D.O., October 4, 2000 and July 7, 1998; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Mexico, published in D.O., December 6, 2000 and December 5, 1998; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Michoacan, published in D.O., December 2002; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Morelos, published in D.O., December 6, 2000; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Nayarit, published in D.O., July 31, 2001; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Nuevo Leon, published in D.O., April 7, 1998; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Puebla, published in D.O., September 19, 2001; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Oaxaca, published in D.O., August 7, 2001; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Queretaro, published in D.O., May 18, 2001; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Quintana Roo, published in D.O., December 21, 2000 and July 16, 1998; Coordination and Cooperation Agreement between the Ministry of Economy and the State of San Luis Potosi, published in D.O., April 23, 1998; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Sinaloa, published in D.O., October 7, 1999; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Sonora published in D.O., April 19, 2002; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Tabasco, published in D.O., March 31, 1998; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Tamaulipas, published in D.O., April 30, 2002; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Tlaxcala, published in D.O., October 31, 2000; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Veracruz, published in D.O., February 7, 2002; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Yucatan, published in D.O., November 19, 2001; Coordination and Cooperation Agreement between the Ministry of Economy and the State of Zacatecas, published in D.O., October 30, 2001.The only State that has not entered into a Cooperation and Coordination Agreement with the Ministry is Mexico City.

[153] Registry Regulation, Art. 4. The Ministry of Economy maintains a website with up to date information of the centralized registry system at www.siger.gob.mx.

X. ENFORCEMENT

The final element of all modern secured financing statutes is a quick and effective enforcement mechanism. The most efficient systems allow creditors to repossess collateral without court intervention; those systems in which extra-judicial remedies are not possible must provide other summary procedures. In addition, a modern statute must provide flexibility in the method in which repossessed collateral is disposed. Finally, a modern statute should provide special enforcement procedures for all types of receivables.

A. REVISED ARTICLE 9

Under both Pre-revision and Revised Article 9, a secured creditor has two main concerns upon default by a secured debtor.[154] Given that Article 9 security interests are typically non-possessory in nature, the creditor's first concern is to recover possession of the collateral from the hands of the defaulting debtor.[155] Once the collateral has been seized, the second concern is to sell or dispose of the collateral in a manner that maximizes its value in satisfying the outstanding debt obligation. Finally, it should be noted that a creditor also has the option of forgoing the Article 9 enforcement process altogether if it prefers to enforce against a defaulting debtor pursuant to agreement or via the use of an ordinary judicial process.[156]

Repossession

Under both Pre-revision and Revised Article 9, a secured creditor can repossess the collateral upon default, without any judicial intervention whatsoever, by using a figure known as "self-help."[157] In order to protect the debtor from a creditor's abuse or from untenable or dangerous circumstances, Article 9 limits a creditor's right to use self-help procedures if there is a breach of the peace

---

[154] U.C.C. Rev. Art. 9 § 601.

[155] U.C.C. Rev. Art. 9 § 601(a)(1). A secured creditor may reduce a claim to judgment, foreclose, or otherwise enforce the claim, security interest, or agricultural lien by any available judicial procedure. U.C.C. Rev. Art. 9 § 601(a)(1).

[156] U.C.C. Rev. Art. 9 § 601(a) After default, a secured party has the rights provided by Article 9 as well as those provided by agreement of the parties. U.C.C. Rev. Art. 9 § 601(c). Rights with regard to enforceability are also cumulative and can be exercised simultaneously.

[157] U.C.C. Rev. Art. 9 § 609.

during the repossession process.[158] If such breach exists, judicial intervention is necessary.[159] Alternatively, Article 9 allows the parties to agree that the debtor, upon default, shall deliver the collateral to the secured creditor.[160] In certain cases, Article 9 also allows a creditor to dispose of collateral directly from the debtor's premises without the need to recover or transport the goods to a creditor's location.[161]

In addition to limitations on self-help repossession, Article 9 includes other provisions to protect debtors from potentially abusive enforcement practices. First, Article 9 requires that parties agree to enforcement procedures in the security agreement while limiting the enforcement actions a creditor may alter by agreement.[162] Article 9 also carefully sets forth the responsibilities of the creditor once this party has repossessed the collateral.[163]

In further recognition that a flexible repossession process can lead to potential abuses, Article 9 provides other important controls to guard against abusive enforcement practices. In this regard, Article 9 provides remedies to the debtor if a creditor fails to comply with Article 9.[164] These remedies may include statutory damages for a creditor's failure to comply with its duties while in possession or control of the collateral,[165] failure to comply with its duties to notify account debtors of an assignment,[166] failure to comply with its requirement to provide an accounting of collateral

158 U.C.C. Rev. Art. 9 § 609(b).

159 U.C.C. Rev. Art. 9 § 609.

160 U.C.C. Rev. Art. 9 § 609(c). If the secured creditor and debtor agree, a creditor may require the debtor to assemble the collateral and make it available to the creditor at a place designated by this party, which is reasonable convenient to both parties.

161 U.C.C. Rev. Art. 9 § 609(a)(2).

162 U.C.C. Rev. Art. 9 § 601(a).

163 U.C.C. Rev. Art. 9 § 601(b). A creditor in possession or control of the collateral under Article 9 §§ 104, 105, 106 or 107, has the rights and duties provided in § 207. U.C.C. Rev. Art. 9 § 207 establishes that a creditor shall use reasonable care in the custody and preservation of the collateral in its possession. In case of chattel paper or an instrument, reasonable care includes taking the necessary steps to preserve rights against prior parties, unless otherwise agreed.

164 U.C.C. Rev. Art. 9 § 625.

165 U.C.C. Rev. Art. 9 § 208.

166 U.C.C. Rev. Art. 9 § 209.

or account,[167] failure to provide an explanation concerning the disposition of the collateral,[168] or failure to provide a waiver of deficiency in consumer transactions.[169]

The most important safeguard against abusive enforcement practices, however, comes not from the Uniform Commercial Code or Article 9, but from U.S. civil responsibility tort law. In cases of extreme abuse, including wrongful repossession or repossession despite a breach of the peace, a debtor may sue the creditor under tort law and receive punitive damages.[170]

Finally, it should be noted that repossession is not necessary with regard to some types of security interests. An obvious example is when the collateral is already in the possession of the creditor, in a traditional pledge, or in the hands of a third party. Another less obvious example is when collateral does not have a tangible physical manifestation, such as accounts and other receivables. Article 9 contains special enforcement rules to accommodate these special situations.[171]

Disposition

Once the collateral is in the creditor's possession, Pre-revision and Revised Article 9 provide two options for the disposition thereof. Under the first option, the creditor may dispose of the repossessed collateral and apply the proceeds to the secured obligation.[172] Under the second, the creditor may keep the collateral in satisfaction of the outstanding obligation.[173]

---

[167] U.C.C. Rev. Art. 9 § 210.

[168] U.C.C. Rev. Art. 9 § 616(b)(1).

[169] U.C.C. Rev. Art. 9 § 616(b)(2).

[170] A creditor may comply with Article 9 yet still be subject to tort actions if this party's behavior during the repossession and or disposition process gravely oversteps the boundaries or the law. In such cases, a creditor's potential liability is limited only by the nature and number of tort actions available under the applicable jurisdiction and may include trespass, assault, battery and conversion of property. See James J. White and Robert Summers, *Uniform Commercial Code*, at § 26-13, West Publishing Co. (1972).

[171] U.C.C. Rev. Art. 9 § 607.

[172] U.C.C. Rev. Art. 9 §§ 608 and 610. After default, a creditor may sell, lease, license, or otherwise dispose of any or all of the collateral in its present condition or following any commercially reasonable preparation or processing.

[173] U.C.C. Rev. Art. 9 §§ 620 and 622.

As with repossession, disposition of the collateral may also take place without judicial intervention. In fact, Article 9 places only two limitations on the disposition of the collateral. The first limitation is that disposition of the collateral must take place in a "commercially reasonable" manner.[174] The second limitation is that the creditor must notify all concerned parties of the disposition.[175]

Once the disposition has taken place, Article 9 sets out the manner in which to apply the proceeds of the disposition.[176] First in line are the reasonable expenses incurred in the collection and enforcement process, including attorney fees to the extent provided for in the agreement and not prohibited by law.[177] Second in line is the outstanding amount of the secured obligation.[178] And, the previous two items have been settled, third are other obligations secured by subordinate security interests or liens over the collateral.[179] If there is a surplus after payment of items one through three, the debtor has the right to those funds.[180]

Conversely, if the proceeds of the disposition are insufficient to cover items one and two above, Article 9 provides that a creditor has the right pursue the debtor for any deficiency.[181] Article 9 also provides specific rules on how to calculate the amount.[182]

Finally, a creditor may also retain the collateral in partial or

---

[174] U.C.C. Rev. Art. 9 §§ 610. Every aspect of a disposition of collateral, including the method, manner, time, place, and other terms must be commercially reasonable. If commercially reasonable, a secured party may dispose of the collateral by public or private proceedings, by one or more contracts, as a unit or in parcels, and at any time and on any terms. U.C.C. Rev. Art. 9 §§ 610(b).

[175] U.C.C. Rev. Art. 9 § 611. A creditor that disposes of collateral is required to send a reasonable authenticated notification of the disposition to the debtor, any secondary obligor, and other persons that have provided notice of an interest in the collateral. U.C.C. Rev. Art. 9 § 611(b)-(c).

[176] U.C.C. Rev. Art. 9 § 608.

[177] U.C.C. Rev. Art. 9 § 608(a)(1). See also U.C.C. Rev. Art. 9 § 615.

[178] U.C.C. Rev. Art. 9 § 608(a)(2).

[179] U.C.C. Rev. Art. 9 § 608(a)(3). This provision, however, requires that the junior lien-holder provide the creditor with an authenticated demand for proceeds before distribution of the proceeds is complete.

[180] U.C.C. Rev. Art. 9 §§ 608(a)(4), 615 and 626.

[181] U.C.C. Rev. Art. 9 §§ 608(a)(4) and 615.

[182] U.C.C. Rev. Art. 9 §§ 615 and 616.

complete satisfaction of the debt.[183] The debtor, however, must consent to the acceptance, and any parties that may be adversely affected may present an objection.[184] Before the acceptance or other disposition, affected parties may also redeem the collateral from the creditor by paying the outstanding amount of the secured obligation and other collection fees.[185]

B. MEXICAN LAW

In recognition that collateral has value only if it can be repossessed quickly and inexpensively and then sold as close to market prices as possible, the STL provides an extra-judicial enforcement remedy whereby a creditor can repossess collateral without court intervention. The STL also reduces court intervention in the disposition of collateral. In cases where extra-judicial remedies are not available, the STL attempts to create a quicker and more cost-effective process than previous law. The overall success of the STL in accomplishing these enforcement goals will be fundamental to the overall success of asset-based lending in Mexico.

Repossession

In contrast to enforcement under previous Mexican law, the STL creates an extra-judicial mechanism to obtain possession of collateral subject to a security interest.[186] Use of this figure provides greater incentives to lending but is subject to several important limitations. First, the procedure is permissive, requiring express statement in the security agreement.[187] Second, there must be no controversy regarding the overdue nature of the loan. Third, there must be no controversy regarding the amount that is overdue. Finally, there must be no controversy regarding the delivery of the collateral.[188]

---

[183] U.C.C. Rev. Art. 9 §§ 620 and 622. A creditor may accept collateral in full or partial satisfaction of the secured obligation of the debtor consents to the acceptance and other parties with an interest in the collateral do not object.

[184] U.C.C. Rev. Art. 9 §§ 620 and 622.

[185] U.C.C. Rev. Art. 9 § 623.

[186] "[This extra-judicial method] may be used for the payment of overdue credits and to obtain the possession of the goods subject to a security interest, so long as there are no controversies regarding the overdue nature of the credit, the delinquent amount, and the delivery of the mentioned goods." STL, reforming Commercial Code, Art. 1414 (bis).

[187] STL, Art. 1414 (bis 3).

[188] STL, Art. 1414 (bis).

Although there is no doctrine or precedent to determine the meaning of the "no controversy" requirement, this wording may be interpreted as requiring full agreement of the parties concerning several issues central to the enforcement process—default itself may be an issue that requires the debtor's agreement under this rule. If this is the case, a debtor's objection to the cause of default (or to the amount of the obligation) may be enough to limit the practical application of the STL's extra-judicial remedy.

Other requirements may also limit the effect of the extra-judicial mechanism. The first step in the STL process, for example, requires that the creditor send a formal request to the debtor for delivery of the collateral.[189] This request, which must be delivered to the debtor via public fiduciary, provides both notice and opportunity for a debtor to claim discrepancies (cause for default, amount overdue, or other loan formalities) that can be used to stop repossession.[190]

Even a creditor that overcomes these initial limitations may encounter other difficulties. For example, the STL also provides for the automatic termination of the extra-judicial process in the following circumstances: the debtor opposes the material delivery of the goods; the debtor objects to the payment of the corresponding loan; the parties have not agreed to the requirements of the law; and the terms of the security agreement and enforcement procedure are impossible to fulfill.[191]

Advantages or disadvantages aside, it is clear that the STL process does not operate with the flexibility of self-help remedies under Article 9.[192] Extra-judicial repossession under the STL seems to require the debtor's knowledge and possibly involvement and consent.[193] Article 9, on the other hand, allow creditors to repossess collateral without the consent, presence, or even knowledge of a defaulting debtor. Article 9 simply requires the absence of a breach of the peace, which in most cases translates to the absence of an objection by the party in possession of the collateral.[194]

---

[189] STL, 1414 (bis 1).

[190] Under Mexican Law, Public Notaries, Public Brokers and Court Officials can act as public fiduciaries. STL, 1414 (bis 1).

[191] STL, Art. 1414 (bis 2).

[192] Article 9 simply requires that repossession take place without a breach of the peace. U.C.C. Rev. Art. 9 § 609(b).

[193] STL, Art. 1414 (bis 1).

[194] STL, Art. 1414 (bis 1). See also supra section X (A).

As a result, enforcement rules—breach of the peace under U.S. law and voluntary consent under Mexican law—operate in a similar fashion in cases where a debtor has knowledge of repossession. The main difference between the two, however, is that Article 9 allows the repossession to take place without the debtor's knowledge, which is not possible under the STL.

The practical effect of these limitations is not clear at this early stage. What is clear, however, is that use of a court-free repossession mechanism will require utmost care in both drafting a security agreement containing an extra-judicial enforcement clause and in employing the STL remedy upon default.

Summary Procedure

For those cases in which extra-judicial repossession is suspended or unavailable, the STL provides a summary judicial procedure that reduces enforcement timetables and legal formalities required under previous law.

This summary procedure requires that the creditor present a motion for repossession before the corresponding court, which must be accompanied by a copy of the security agreement and a statement of the delinquent amount.[195] Once these requirements are met, the court must act under the strictest guidelines to admit the motion and render a decision within two days.[196] In its decision,

---

[195] When the creditor is a licensed financial institution, the statement must be certified pursuant to accepted rules and practices. STL, Art. 1414 (bis 8).

[196] STL, Art. 1414 (bis 8), as translated, states as follows:

> Once the creditor presents a motion, accompanied by the respective security agreement and the determination of the delinquent amount formulated by the creditor, and annexing the certification of the delinquent amount when the creditor is a financial institution, the judge under strict interpretation, if he finds that the mentioned requirements are fulfilled, in a term no to exceed two days, will admit the motion and will render a decision in form requiring payment from the debtor and, if payment is not received, requiring the delivery to the plaintiff of the material possession of the goods serving as collateral mentioned in the agreement. In this latter case, the creditor will gain the character of judicial depository and must inform the judge concerning the place in which the goods will be held until they are disposed.
>
> In the same act by which the debtor is required to make payment, the judge will conduct service of process to the debtor, in case the debtor does not pay or deliver possession of the collateral to the creditor, in order to appear to contest a lawsuit within five days and to present any of the defenses provided by law.

the court must require full payment from the debtor. If payment is not received, the court must require immediate delivery of the collateral to the creditor.[197]

The STL also shortens the enforcement procedure by allowing the court to provide service of process to the debtor in the same act requiring payment of delivery of the collateral to the secured party. No additional service is required.[198] If the debtor does not pay or deliver possession of the collateral, the debtor must appear before the court within five days to contest the enforcement action.[199]

This procedure departs significantly from previous law. Whereas, before, a motion to judicially repossess the collateral could take months (or even years), the STL procedure requires the court to deliver a motion for payment or repossession to the debtor within two days from the time in which the creditor files. In this motion, the debtor must pay the outstanding loan amount or deliver the collateral to the secured creditor. If the debtor does not comply with either of these requirements, the debtor is given five days to present any defenses to the motions.

This procedure drastically cuts the time needed to recover the collateral. However, the procedure is not as effective as the extra-judicial process. In the best case, a creditor can expect to receive possession of the collateral in five days. Such a time period can be relatively long when dealing with some types of movable goods and can cause potential problems. For example, collateral can be moved from one location to another, payment instruments can expire, perishable collateral can spoil, etc. Furthermore, the STL does not clearly establish how and in what timeframe the process concludes. Finally, the courts, accustomed to operating under significant delays, have not been put to the test and may fall short in keeping up with the time requirements of the STL. Consequently, only time will tell how efficiently the new enforcement framework will operate in practice.

Disposition

Once the creditor obtains possession of the collateral, whether it is by court intervention or extra-judicial means, the STL allows the parties to proceed to the disposition of the collateral and provides

---

197 STL, Art. 1414.
198 STL, Art. 1414.
199 STL, Art. 1414.

rules for this process to take place.[200] Before disposition is permitted, however, the STL requires that goods be inventoried before a public fiduciary, a potentially cumbersome requirement that does not exist under Article 9.[201]

The disposition process under the STL is also much less flexible than under Article 9. Article 9, for example, allows for various types of disposition so long as they are commercially reasonable.[202] In most cases, this means that the market determines the value of the collateral.[203] By contrast, the STL requires that the parties either agree to a method for assigning value to the collateral or assign an evaluator to determine such value.[204]

Once the value of the collateral has been determined, the STL allows for disposition of the collateral, which must take place by judicial sale or before a public fiduciary.[205] Although this sale process is common under Mexican law, questions arise concerning these requirements. For example, the STL does not establish what happens if the amount of the evaluation is greater than the amount obtained at the sale. Given that judicial sales typically generate low sale prices, this is another issue that may generate litigation under the STL.

---

[200] Once the goods are delivered to the trustee or secured creditor, this party will have the character of judicial depository until the disposition is carried out. STL, Art. 1414 (bis 4) and (bis 1).

[201] Article 1414 (bis 3) provides that the secured party may obtain possession of the collateral, if it was so stipulated expressly in the corresponding security agreement. This act must take place before a public fiduciary who will create a corresponding act and render a detailed inventory of the collateral.

[202] U.C.C. Rev. Art. 9 § 627.

[203] U.C.C. Rev. Art. 9 § 627. Article 9 states that a disposition is commercially reasonable if it is made in the usual manner on a recognized market, is made at the price current in any recognized market at the time of the disposition, or is otherwise made in conformity with reasonable commercial practices.

[204] STL, Article 1414 (bis). Under the STL, the value of the collateral can be determined by: (i) an evaluator designated by the parties in the security agreement, or (ii) other procedure agreed to in writing by the parties. The STL also states that the parties must establish, in the security agreement, the basis for designating an authorized person, different from the creditor, to conduct an evaluation of the collateral, in case such evaluation cannot be conducted under the subsections of this Article. STL, Article 1414 (bis). This paragraph states that the security agreement must provide a contingency method for conducting evaluations when such evaluations cannot proceed under subsections (i) and (ii). However, this provision does not clarify the conditions that would lead to the inoperability of subsections (i) and (ii). STL, Article 1414 (bis).

[205] STL, Art. 1414 (bis 17).

Deficiencies

The STL, as enacted in 2000, prohibited a creditor from suing a debtor for any deficiency when the sale of the collateral produced less than the outstanding amount of the loan.[206] In such cases, the STL 2000 disregarded the judicial sale requirement altogether, forcing the creditor to strictly foreclose on the collateral as the exclusive remedy if elected. Ostensibly, once strict foreclosure takes place, the creditor may dispose of the collateral in any way he deems fit. However, this flexibility comes at a great price.

The old STL had little impact on asset-based lending in Mexico after its enactment in May 2000. This provision was a large part of its lack of success, as lenders were unwilling to enter the Mexican market with this enforcement limitation.[207]

The new STL completely repeals these rules in what many lawmakers and legal practitioners feel is the most important contribution of the 2003 modifications.[208]

XI. CONCLUSION

Scarcity and the high cost of commercial credit have been among the most significant economic problems facing Mexico during the past decade. Conversely, inexpensive and abundant credit has been one of the catalysts behind a dynamic U.S. economy during most of that same period and an important factor in the economic recovery of the last year. An important reason for this divergence is the state of the legal framework for secured transactions. Whereas in the United States, UCC Article 9 creates a flexi-

---

[206] STL 2000, Arts. 379, 412, and 1414 (bis 17). These provisions stated as follows:

The parties must stipulate in the security agreement that if the proceeds of the sale of the collateral do not suffice to cover the total amount of the secured obligations charged to the debtor, this party will become liberated from covering the resulting differences, considering extinguished the rights of the creditor to demand the deficiencies. This provision cannot be waived.

[207] This rule provided no incentive for the secured debtor to preserve the value of the collateral or to cooperate with the timeframe of an enforcement procedure—even when failure to cooperate was detrimental to the value of the collateral, especially concerning perishable collateral. Recognizing this problem, the Old STL provided penal sanctions (including prison terms from 1 to 12 years) for parties that intentionally committed an act that reduced the value of the collateral. Although the threat of this type of sanction can force a debtor to cooperate during enforcement proceedings, it is unlikely that the threat of prison terms will translate into reduced deficiencies. Realistically, it was also possible that Mexican courts would refuse to enforce these types of sanctions.

[208] See STL 2003, Art. 2, derogating Articles 379 and 412 of the LGTOC.

ble system that provides great legal and economic certainty, the Mexican secured transactions system is beset with legalistic formalities and provides little assurances to either party in case of default.

To improve the state of Mexican law and alleviate this credit shortage, lawmakers enacted a new Secured Transactions Law in May 2000, revised it in June 2003, and complimented it with new registry rules later that same year.

These new laws and regulations present a noticeable improvement over the previous legal framework. To illustrate the great advances of the new laws, it is simply necessary to recall the eight legal principles upon which modern secured transactions are based (uniformity, after-acquired property, proceeds, future advances, purchase money security interests, buyer in the ordinary course of business, effective enforcement, and registry systems). The STL contains seven of the eight; the one omission is the need for uniformity. Under the previous legal framework, the production credit—then the most UCC-like security mechanism—contained only four of the eight. Typical security mechanisms provided fewer and some only one.

The new law creates an improved system that allows secured parties to encumber present and future goods, secure present and future obligations, that protects debtors and buyers and provides notice to third parties. In addition, this new system also creates a summary enforcement procedure. Not to detract from its many accomplishments, though, it is necessary to point out that the new law is also characterized by several problems. This analysis has pointed out only the most noteworthy.

As it stands, the new law creates a framework that is infinitely more hospitable to modern secured transactions than that which it replaces. Creditors must be extremely careful, however, not to fall into one of the many noted shortcomings. If the text of the law is revised again (as some lawmakers continue to discuss), this new system will provide the legal certainty and flexibility necessary to create a new credit market throughout Mexico, one that opens new business opportunities and resolves current financing needs.