

1997

MEXICAN BANKRUPTCY LAW: THE LEGAL EFFECTS OF BANKRUPTCY AND SUSPENSION OF PAYMENTS

Eduardo R. Martinez

Follow this and additional works at: [https://digitalcommons.nyls.edu/
journal_of_international_and_comparative_law](https://digitalcommons.nyls.edu/journal_of_international_and_comparative_law)



Part of the [Law Commons](#)

Recommended Citation

Martinez, Eduardo R. (1997) "MEXICAN BANKRUPTCY LAW: THE LEGAL EFFECTS OF BANKRUPTCY AND SUSPENSION OF PAYMENTS," *NYLS Journal of International and Comparative Law*. Vol. 17 : No. 2 , Article 11.

Available at: [https://digitalcommons.nyls.edu/journal_of_international_and_comparative_law/vol17/iss2/
11](https://digitalcommons.nyls.edu/journal_of_international_and_comparative_law/vol17/iss2/11)

This Article is brought to you for free and open access by DigitalCommons@NYLS. It has been accepted for inclusion in NYLS Journal of International and Comparative Law by an authorized editor of DigitalCommons@NYLS.

MEXICAN BANKRUPTCY LAW: THE LEGAL EFFECTS OF BANKRUPTCY AND SUSPENSION OF PAYMENTS

*Eduardo R. Martinez**

I. INTRODUCTION

From a legal stand point, bankruptcy is not a fact, but a legal status which exists until it is judicially declared by a competent judge; it has judicial effects and consequences when it has been recognized as such.

The Bankruptcy and Suspension of Payment Law, *Ley de Quiebras y Suspensión de Pagos*, establishes that the merchant who ceases in the payment of its obligations may be declared bankrupt.¹ In order to declare a merchant bankrupt, it is required that the merchant has ceased in the payment of its obligations. The concept of “cessation of payments” should not be misinterpreted with the one of “insolvency”; the latter is an economic status that cannot be estimated externally but only through the examination of the merchant’s books. Our legal regulations establish a series of presumptions of cessation of payments, or facts of bankruptcy, whose presence permits a court to declare the bankruptcy of a merchant without analyzing its insolvency.

In our criteria there are three types of presumptions for recognizing the cessation of payments: a) the economic ones, such as a general breach by the merchant when it fails to pay its matured and due obligations, or when there are no assets (or insufficient assets) to secure the payment of due obligations; b) the ones deriving from the merchant’s own acts, such as its hiding or absence without leaving a legal representative in charge of the

* Eduardo Rodriguez Martinez is a member of the law firm of Santamarina y Steta, S.C. in Mexico City, where he represents Mexican and foreign companies in international business, with an emphasis on financial matters. He has been a member of the faculty of Universidad Iberoamericana, Universidad Intercontinental, and Escuela Libre de Derecho in Mexico City. Mr. Martinez has authored several articles on commercial and administrative law for publication in the Law School of Universidad Iberoamericana’s “JURIDICA.” Mr. Martinez graduated from Universidad Iberoamericana School of Law in Mexico City. He is a member of the Mexican bar’s “Ilustre y Nacional Colegio de Abogados de México.”

1. LEY DE QUIEBRAS Y SUSPENSIÓN DE PAGOS [L.Q.S.P.] [Law of Bankruptcy and Suspension of Payments] art. 1 (Mex.), *translated in* DOING BUSINESS IN MEXICO app. 8, A.8-3 (Andrea Bonime-Blanc, Esq. & William E. Mooz, Jr., Esq. eds., 1996).

corporation who may fulfill its obligations, the closing of the corporation's premises or the nonexistence of the principal place of business, or the performance of ruinous, fraudulent or fictitious acceptances to avoid its obligations; and c) the ones resulting from procedural acts, such as the merchant's request for a declaration of bankruptcy, its unsuccessful request for the suspension of payments benefit, or the failure to meet its obligations in a suspension of payments.²

Based on the principle that bankruptcy is a harmful institution for the debtor due to the total loss of its property, harmful for the creditors due to the uncertainty of recovering their pro-rata share of the debtor's property, and harmful for the community due to the loss of a work resource, our legislation tends to restrict the cases that declare bankruptcy by establishing a preventive institution that is the suspension of payments.

With small exceptions, the bankruptcy and the suspension of payment proceedings are absolutely parallel institutions in their presumptions, as well as their juridical and economic structures and consequences.

In view of the beneficial characteristics granted to a debtor by the suspension of payments, it avoids some painful and harmful consequences of bankruptcy. In fact, the suspended party does not lose the management of its property.³ Furthermore, during the suspension of payments proceedings, the suspended party obtains the right of a moratorium in all its payments until the execution of a preventive agreement, and afterwards, only if agreed to by the creditors.⁴ Finally, the restrictions on the bankrupt's capacity are not produced because suspension of payments is an institution that permits the suspended party to readjust its economic status through a moratorium of payment and a final arrangement for the payment of its credits. This prevents bankruptcy and produces the continuation of the corporation.

In order for a merchant to obtain the benefit of suspension of payments it is necessary to meet certain requirements. For example, the merchant may not have been convicted of any crimes against property, or be a party to an unfulfilled agreement of suspension of payments. In addition, the lack of filing documents such as accounting books, balances, list of debtors and creditors or the failure to report the benefit of suspension within the three days following the day of insolvency may disqualify a merchant.⁵

2. *See id.*

3. *Id.* art. 410.

4. *Id.* arts. 398, 408.

5. *Id.* art. 396.

A merchant's request for suspension must be accompanied by a draft of a preventive agreement which must contain an offer to creditors for the payment of their claims.⁶ Generally, the effects of a suspension of payments are the following:

(1) so long as the proceedings remain pending, no debt arising before the start of the proceedings may be claimed against the suspended party, and the suspended party may not pay any claim;⁷

(2) the statute of limitations on all contracts or negotiable instruments is suspended; therefore such statute of limitations does not start or run against the suspended party until the preventive agreement is approved or bankruptcy is declared;⁸

(3) in order to make a claim effective, there is no legal obligation for the creditors to file notice of the suspended party's default on negotiable instruments, however, there is such an obligation for creditors who demand payment from endorser of the claim;⁹

(4) all judicial proceedings to enforce or fulfill an obligation of the suspended party are stayed, except for the ones which seek assets that are not the property of the suspended party, indebtedness due to workers, alimony or secured indebtedness;¹⁰

(5) the main benefits of suspension of payments is that the merchant keeps the management of its assets, and the ordinary operations of the corporation continues under the receiver's vigilance; there is no intervention in the merchant's accounting and correspondence, no assets are taken out of his control, and the merchant is not subject to an action which seeks to remove him from his place of business;¹¹

6. L.Q.S.P. art. 398, translated in *DOING BUSINESS IN MEXICO*, *supra* note 1, at A.8-83.

7. *Id.* art. 408.

8. *Id.*

9. See generally LEY DE TÍTULOS Y OPERACIONES DE CRÉDITO [L.T.O.C.] [Law of Negotiable Instruments and Credit Operations] (Mex.), translated in *DOING BUSINESS IN MEXICO*, *supra* note 1, at A.5-3.

10. *Id.* art. 409.

11. *Id.* arts. 409, 410.

(6) when acting under the receiver's vigilance, all those acts which exceed the ordinary management of the merchant's business, such as the creation of mortgages or pledges, must be authorized by the judge in order to be valid, binding and not subject to nullity;¹² and

(7) in these proceedings, the appointment of an intervenor is optional for the creditors, and the judge does not perform any appointments.¹³

The agreement of payment, which the suspended may propose to the creditors, may contain releases of up to 50% of the amount of the claim and /or adjournments of up to two years.¹⁴

The proceedings of suspension of payment conclude by the fulfillment of the agreement executed. During the fixed term for the execution or fulfillment of the agreement, the receiver continues to supervise the debtor's acts to ensure the faithful fulfillment of the agreement.¹⁵

II. LEGAL EFFECTS OF BANKRUPTCY

Bankruptcy creates a special judicial status of limitation for exercising rights, and a merchant is prevented from performing acts of domain or administration with respect to assets comprising the estate.¹⁶ Merchants or their representatives must remain in their place of business; they cannot disappear from the place of the proceedings without leaving an attorney sufficiently instructed.¹⁷ The chief officer of the postal service, telegraph and similar entities are ordered to deliver all correspondence sent to the merchant's offices directly to the trustee, and then the trustee must return to the merchant any items that do not relate to the bankruptcy proceedings.¹⁸

The merchant declared bankrupt may have criminal liability. For such purposes, there are three kinds of bankruptcies (1) accidental bankruptcies,

12. L.Q.S.P. art. 411, *translated in* DOING BUSINESS IN MEXICO, *supra* note 1, at A.8-85; *see also id.* art. 26.

13. L.Q.S.P. art. 417, *translated in* DOING BUSINESS IN MEXICO, *supra* note 1, at A.8-85.

14. *Id.* arts. 403, 318, 319.

15. *Id.* arts. 423, 424, 365.

16. *Id.* art. 83.

17. *Id.* art. 87.

18. L.Q.S.P. art. 85, *translated in* DOING BUSINESS IN MEXICO, *supra* note 1, at A.8-26.

(2) culpable bankruptcies and (3) fraudulent bankruptcies.¹⁹

Accidental bankruptcy occurs when the merchant suffers a sudden misfortune which is not related to prudent management, and which provokes the status of cessation of payments.²⁰

A culpable or guilty bankruptcy is caused by acts against good management principles, such as excessive and oversized personal domestic expenses, excess losses in games, bets and stock market operations, purchases, sales or operations delaying the bankruptcy, excessive expenses not related to capital investments, and similar movements and circumstances of the company.²¹

Fraudulent bankruptcy occurs when the merchant fraudulently dismisses its assets or increases its debts in such a way as to cause or exacerbate the cessation of payments. In addition, fraudulent bankruptcy may occur if the merchant conceals its financial status by improper record-keeping, or by altering or failing to keep record books.²²

The declaration of bankruptcy by itself does not trigger criminal responsibility of the bankrupt; it arises only when the existence of a guilty or fraudulent bankruptcy is proven.²³ In addition, criminal responsibility for bankruptcy crimes may be placed upon the merchant, the legal representative, directors, administrators or liquidators.²⁴ Furthermore, criminal responsibility may arise from complicity by the auxiliaries or assistants of the bankrupt in previous and later agreements, or from direct induction.²⁵ If, however, a spouse, the consanguineous or akin ascendant of the bankrupt, without consent, takes away or hides assets belonging to the estate, they are not considered partners in the crime of guilty or fraudulent bankruptcy, rather, they are guilty of robbery.²⁶

As to its assets, the bankrupt is deprived from the administration and possession of its assets; the bankrupt may not manage or dispose of them, because they are the property of the estate which will be used to pay the creditors.²⁷ Nevertheless, the assets or rights related strictly to the person

19. *Id.* art. 91.

20. *Id.* art. 92.

21. *Id.* art. 93.

22. *Id.* art. 94.

23. *Id.* arts. 95, 99.

24. L.Q.S.P. art. 101, *translated in* DOING BUSINESS IN MEXICO, *supra* note 1, at A.8-29.

25. *Id.* art. 103.

26. *Id.* art. 105.

27. *Id.* arts. 116, 83.

remain excluded; these include the rights to assets belonging to another, which are not transferable, earnings from personal activities, the rights inherent to the person, such as intellectual capacity or artistic qualities, and assets comprising the estate of the family.²⁸

Once the bankruptcy loses the management and the power to sell its assets, the acts of management and disposition performed on same after declaration of bankruptcy do not produce any effect to the creditors.

In relation to the bankruptcy proceedings, any actions and suits pursued and followed by the bankrupt, and those pursued and followed against it which relate to the estate are continued by the receiver with the participation of the bankrupt.²⁹ All the actions and proceedings which concern the estate are consolidated with the bankruptcy proceeding, and continued before the competent judge of bankruptcy; other proceedings in which the final resolution has already been pronounced and notified, or those which derive from secured claims are consolidated for purposes of classification and payment only if there has been a writ of execution.³⁰

Once bankruptcy is declared, the bankrupt's pending obligations become due.³¹ This is true because the concession of a creditor to a bankrupt's repayment term involves the faithful capacity to comply, and the declaration of bankruptcy is a circumstance that warrants a loss of that confidence. The bankrupt's debts cease to accrue interest against the estate from the moment of the declaration of bankruptcy, except that interest accrues on secured claims up to the amount of the security, and the claims of bondholders are computed by the bond's issuance value less any amount paid by amortization or reimbursements.³²

The bankrupt's debts to a creditor may not be offset.³³ Claims against the estate cannot be offset against the estate's claim against a creditor because the creditor will be able to collect 100% of its claim, and this would be preferential treatment.

With respect to joint obligations involving the bankruptcy of one or more joint debtors, the creditor has the right to obtain from each estate the amount corresponding to its pro-rata share until its claim is extinguished.³⁴

28. *Id.* art. 115.

29. *Id.* art. 122.

30. L.Q.S.P. art. 126, translated in *DOING BUSINESS IN MEXICO*, *supra* note 1, at A.8-33.

31. *Id.* art. 128.

32. *Id.*

33. *Id.*

34. *Id.* art. 135.

That is, the creditor may demand in the bankruptcy proceeding of each bankrupt a part of its claim up to the total amount due.

With respect to pending bilateral contracts, bankruptcy by itself does not prevent the pending execution of bilateral contracts; nevertheless such contracts shall be fulfilled by the receiver after prior approval by the judge.³⁵ Therefore, the right to ask for the termination of the contracts remains subordinated to the receiver's right to comply with them. Furthermore, the contracting non-bankrupt party may suspend the execution of the contract until it is guaranteed by the bankrupt.³⁶

Notwithstanding the foregoing, there are certain specific contracts, such as deposit contracts, the extension of credit, and commissions which are extinguished by the simple declaration of bankruptcy, because said contracts assume a special faithful relationship from the bankrupt party.³⁷

In general, bankruptcy has repercussions on the acquired assets by the non-bankrupt spouse during the marriage. It is presumed that a bankrupt spouse owns the assets which the non-bankrupt spouse acquired during the marriage within five years prior to the date of the declaration of bankruptcy.³⁸ This presumption grants the non-bankrupt spouse an opportunity to prove that these assets were acquired by means outside the bankrupt spouse's estate, either because they are of his or her exclusive ownership, or that they were owned before marriage.³⁹ On the other hand, if a non-bankrupt spouse has claims against the bankrupt spouse, it is presumed that those have been paid. Therefore, the non-bankrupt spouse has no claim against the estate.⁴⁰

In the case of joint ownership of property by husband and wife, all assets owned by such remain included in the estate, and the non-bankrupt spouse may ask for termination of the joint ownership of property and the separation of what belongs to him or her.⁴¹

The acts performed before the declaration of bankruptcy are subject to a special regime. They have validity in principal because at the moment that the debtor performed them, he was owner and had complete capacity of management and disposal. Nevertheless, some acts may be voided in

35. *Id.* art. 139.

36. L.Q.S.P. art. 139, translated in *DOING BUSINESS IN MEXICO*, *supra* note 1, at A.8-36.

37. *Id.* art. 141.

38. *Id.* art. 163.

39. *Id.*

40. *Id.* art. 164.

41. *See id.* art. 165.

a special proceeding which may be commenced by any creditor when it is demonstrated that such acts were performed with the object to harm the creditors or benefit some of them specially.⁴²

The law establishes that fraudulent or gratuitous transfers which benefit only certain creditors, such as due debts paid in kind or the creation of security interests, may be set aside if any of them are performed during the retroactive period of bankruptcy.⁴³ The retroactive date of bankruptcy is fixed by the judge in accordance with his or her criterion after reviewing the bankrupt's acts and determining when the merchant ceased in the payment of its obligations.⁴⁴

Once the retroactive date is fixed, it is understood that on such date, the bankrupt entered into cessation of payments; thus, the bankrupt was deprived of disposing and managing its assets, and any action or operation occurring after the retroactive date which harmed a creditor may be reviewed and refuted by the judge.⁴⁵

After bankruptcy is declared, there is the possibility that the estate possesses merchandise or negotiable instruments which are not the property of the estate. In this case, our law grants to their proprietors specific actions to recover the assets held by the bankruptcy estate.⁴⁶

In addition, other actions may be commenced in several cases where the necessity of separation is proven. Some of these special cases recognized by the law include real estate sold to the debtor but not yet paid in full, the movable property purchased but not yet paid in full, the assets which are in possession of the bankrupt by deposit, management, lease, usufruct, trust or consignment, and security pledged upon a public instrument or based upon a broker's warranty.⁴⁷

The bankruptcy proceedings may be concluded in any of the following situations: the debtor pay all of its obligations in full;⁴⁸ the debtor has insufficient assets to proceed with the bankruptcy administration;⁴⁹ the

42. L.Q.S.P. art. 168, *translated in DOING BUSINESS IN MEXICO, supra* note 1, at A.8-44.

43. *Id.* art. 169.

44. *Id.* arts. 15, 6.

45. *Id.* art. 170.

46. *Id.* art. 158.

47. *Id.* art. 159.

48. L.Q.S.P. art. 274, *translated in DOING BUSINESS IN MEXICO, supra* note 1, at A.8-64.

49. *Id.* art. 287.

creditors fail to attend the meeting of creditors;⁵⁰ the creditors unanimously agree to terminate the proceedings;⁵¹ or the creditors consent to a payment agreement which is approved by the judge.⁵²

50. *Id.* art. 289.

51. *Id.* art. 289.

52. *Id.* arts. 296-379.

