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Separation of Trust Assets Under Mexican Bankruptcy Law

By Francisco Javier Garibay Guemez*

In this article, the author analyzes the intricate process of separating assets that have been transferred to a guarantee trust by a settlor who later faces insolvency. Toward that end, the author delves into the judicial decision rendered by the Second Collegiate Court in Civil Matters of the Seventh Circuit, as it pertains to the resolution of the Amparo Directo *188/2021 case. According to the author, this decision, in direct contradiction to fundamental legal principles, inaccurately negates the validity of the separation of assets transferred to a guarantee trust. Significantly, the author adds, this decision is marked by substantial deficiencies in its reasoning and a lack of theft foundation and justification. The author concludes that, consequently, it not only breaches established legal norms but also significantly influences doctrine and legal practice.*

I. INTRODUCTION

In Mexico, the trust has emerged as an indispensable legal tool, playing a pivotal role in reshaping the nation's financial terrain and enhancing access to financing. This transformation is in large part a response to the ripple effects of globalization, which has reconfigured the global market economy, especially within the financial and capital markets sectors. Such shifts have fostered capital movement across borders, leading to the normalization of financing patterns. Consequently, a plethora of methods for obtaining credit and investment has emerged, each tailored to the unique requirements of creditors and debtors. This ebb and flow of financing supply and demand is largely dictated by the risk and profitability associated with the assets in play. A pivotal aspect to consider here is the "country risk," which bears directly on profitability. This risk is intertwined with the solidity of a nation's legal framework and its institutional integrity.

In this global backdrop, legal constructs that aid investors in mitigating debtor insolvency risks have gained significant traction. The trust serves as a testament to this trend. Operating on the "bankruptcy remoteness" principle, this mechanism aims to segregate a debtor's assets, ensuring their accessibility during insolvency and shielding them from potential claims by other creditors. Employing trusts in credit transactions brings forth benefits such as risk

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dispersion and optimized asset management. Furthermore, they bolster investor confidence by guaranteeing investment safety, thereby ushering in attractive financial terms and heightened operational structure flexibility. Cumulatively, this tactic not only safeguards investors but also propels credit accessibility and invigorates the broader economy.

In the quest to lure investments, numerous countries are striving to create a legally certain structure, preserving financial stability, and implementing regulatory reforms. By integrating itself into global financial markets to augment capital inflow, Mexico has underscored its dedication to bolstering legal security and buttressing commercial and financial entities. This dedication is epitomized by the financial reform of 2014. Yet, it is imperative to emphasize that the consistent and precise interpretation and enforcement of laws are foundational to the efficacy of such endeavors.

Judicial missteps can profoundly reverberate within both financial and legal spheres. The ruling by the Second Collegiate Court in Civil Matters of the Seventh Circuit is illustrative of this. This ruling has sparked discussions on the validity of the trust's property separation actions concerning assets related to the bankruptcy estate. A parallel can be drawn to the judgment passed by the Third Collegiate Court in Civil Matters of the First Circuit on May 28, 2015. While that decision explores the trust's legal implications and the protection it affords in financial and business endeavors, its nuances will not be addressed here. The emphasis of the resolution moves away from property separation, instead probing the implications of the insolvency declaration (*Concurso*) and the use of interim measures (*medidas cautelares*) within the *Concurso* process – topics that fall outside the scope of this paper.

Therefore, this article focuses on the decision rendered by the Second Collegiate Court in Civil Matters of the Seventh Circuit (hereinafter, the Court) concerning the direct amparo trial 188/2021.[1] It is important to note that although this verdict is not binding (as it does not form *jurisprudencia*),[2]

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[1] The "amparo process" in Mexican law is a constitutional check that assesses acts of authority and court decisions for potential violations of rights in the Constitution. It can challenge final decisions, especially if rights are violated during their proceedings or within the decision itself. The amparo against judgments in civil or commercial cases (*amparo directo*) is filed before Collegiate Courts, initiated only by the aggrieved party. Generally, all standard appeals must be exhausted before resorting to an amparo, which starts with an initial claim brief. Following this, the authority has a period to respond, then evidence is presented, closing arguments made, and a final hearing concludes with the issuance of a judgment.

[2] In Mexico, "*jurisprudencia*" or binding court precedents are established through three primary mechanisms:
(i) Court Precedent by Confirmation or Reiteration, established when the collegiate circuit courts

it presents several deficiencies that have the potential to undermine Mexico's financial structures. Such vulnerabilities could, in turn, erode investor confidence and elevate credit costs in Mexico by increasing default risks and intensifying the expense of securing credit.

II. BANKRUPTCY ESTATE AND SEPARATION RIGHT

Article 4, Section V of the Mexican Insolvency Law (*Ley de Concursos Mercantiles*, hereinafter, the Bankruptcy Law) provides a definition of the "bankruptcy estate". It characterizes this estate as "the aggregate of the insolvent debtor's assets and rights, excluding specific assets outlined in this Law, upon which recognized creditors and other valid claimants may enforce their claims."

However, it is worth noting that the classification of assets and rights exempted from the bankruptcy estate is not solely confined to those "expressly excluded" as per the Bankruptcy Law. As an illustration, Article 71 of the Bankruptcy Law permits the exclusion of assets from the bankruptcy estate if they align with circumstances akin to those explicitly laid out in that article (analyzed below). Additionally, according to Antonio Brunetti, Joaquin Rodriguez y Rodriguez, and Jorge Barrera Graf, the bankruptcy estate also excludes the following:[3]

a. *Assets Excluded by their Inherent Character:* This category includes assets such as:
   - (i) Personal rights.
   - (ii) Rights over assets owned by third parties.
   - (iii) Assets lacking an exchange value.
   - (iv) Proprietary rights intrinsic to the debtor that arise due to their personal status.

b. *Assets Excluded because of its Stipulated Function*: This group encompasses assets rendered inalienable due to their legal purpose, such as

unanimously uphold the same criteria in five consecutive decisions without any contrary ruling in between;

(ii) Court Precedent by Contradiction, aiming to resolve and unify contradictory court opinions, necessitating the report of such contradictions and confirmation of substantive differences in interpretations; and

(iii) Mandatory Court Precedent, which are the rationales underpinning decisions made by the Supreme Court of Justice, especially when such decisions are determined by a majority of at least eight votes.

[3] Barrera Graf, J. (1998). *El Desapoderamiento en la Quiebra* (1a ed.). Ediciones Mar, pp. 127-152.

family assets (*patrimonio de familia*).[4]

c. *Assets Excluded for Public Interest Reasons*: Here, we find assets that the law designates as unattachable, examples being alimony, wages, salaries, and pensions.

d. *Assets Excluded Due to Possessory Privilege*: These are assets owned by the bankrupt debtor but have been designated as collateral for credit – either in the form of a pledge (*prenda*) or a retention right (*derecho de retención*).

As delineated above, the bankruptcy estate encompasses all debtor's assets, save for those specifically exempted due to their inherent character, stipulated function, or for reasons rooted in the public interest. This inclusion persists regardless of the asset's geographical location – whether within national borders or abroad – and irrespective of the debtor's possession or control over them at the commencement of bankruptcy proceedings.

The assets under discussion include both tangible and intangible forms. It is imperative to underscore that the bankruptcy estate is not exclusively constituted by assets within the debtor's immediate control. Similarly, not every asset under the debtor's control is automatically deemed part of the bankruptcy estate. The Bankruptcy Law provides clear provisions to:

(i) Incorporate assets that intrinsically pertain to the bankruptcy estate (integrative measures).

(ii) Isolate or exclude assets that should remain untouched by the bankruptcy proceedings (disintegrative measures).

Integrative measures encompass those related to the fulfillment of outstanding obligations in favor of the debtor, the exercise of third-party ownership rights, claims by the bankruptcy estate, and, significantly, the set of actions classified as revocation actions. The latter aim to restore assets or rights to the debtor's estate that were previously transferred out, by rendering the transfer act unenforceable against the bankruptcy estate.[5]

Regarding revocation or annulment actions, these are detailed in Title III, Chapter VI of the Bankruptcy Law, which addresses acts of creditor fraud. They are designed to counteract detrimental actions undertaken by the debtor prior

[4] Article 723 of the Federal Civil Code: The following are considered as family assets:
I. The family residence;
II. In certain instances, a cultivable plot of land.

[5] Rodriguez and Rodriguez, J. (1951). *La Separación de Bienes en la Quiebra* (1a ed.). Universidad Nacional Autónoma de México, p. 16.

to the initiation of the bankruptcy process. Such actions might involve concealing assets, orchestrating sham transactions, unduly favoring specific creditors, or diminishing the value of the debtor's assets. The objective of these provisions is to ensure fairness among creditors and to maximize the assets available for distribution, in alignment with the credit priorities and hierarchy set forth in the law.[6]

According to Article 70 of the Bankruptcy Law, assets in the debtor's custody that are distinguishable and haven't been transferred pursuant to a final and irrevocable legal title can be reclaimed by their rightful titleholders. Hence, the criteria essential for the validity of separatory action can be enumerated as follows:

- The assets must be under the debtor's control at the point when *Concurso* is declared.[7]
- The assets in question need to be individually identified.
- No transfer of these assets to the debtor should have occurred pursuant to a final and irrevocable legal title.
- The claimant must validate their rightful ownership of these assets or rights. In the absence of such proof, ownership is assumed to lie with the debtor.[8]

III. SEPARATION OF TRUST ASSETS

The aforementioned criteria serve as the foundational rules for asset separation. However, Article 71 of the Bankruptcy Law offers a descriptive list

[6] Bankruptcy Law on fraudulent conveyance is focused on overturning past transactions to which the insolvent debtor was a party or which involved the debtor's assets whose consummation is found to be prejudicial to the debtor (i.e., a reduction to the net value of its property). The retroactive period is the period that begins 270 days prior to the Concurso declaration. Such a period may be extended to an earlier date by the judge, at the request of the conciliator (*conciliador*), the receiver (*síndico*), the conservators (*interventores*) or any creditor, provided that (i) the facts invoked by the abovementioned persons fall within any of the circumstances set forth in Articles 114 to 117 of the Bankruptcy Law (providing the relevant documentation); (ii) the requested extension date does not exceed three years prior to the bankruptcy declaration; and (iii) the request is filed before the issuance of the debt recognition, priority, and ranking ruling (*sentencia de reconocimiento, graduación y prelación de créditos).*

[7] Article 790 of the Federal Civil Code defines possession as the *de facto* power over a certain asset, and includes not only assets over which the debtor has physical possession, but also assets over which the debtor has primary possession (e.g., the debtor shall be deemed to be in possession of an asset even if the debtor has leased it out to a third person). See Rodriguez and Rodriguez, op. cit., p. 61.

[8] Art. 798 of the Federal Civil Code.

of scenarios where a separation action can be initiated. Essentially, these situations can be categorized into three groups:

- Assets subject to recovery;
- Assets subject to quasi recovery; and
- Assets subject to a restitution duty.

a. Assets Subject to Recovery

This category pertains to assets that stand central to a recovery action. Within the framework of Mexican law, a recovery action is an in rem action wherein the rightful owner pursues the restitution of an asset, inclusive of its yields and accessions, from an unauthorized possessor. Its primary aim is to enable the rightful owner to regain possession of an asset from which said rightful owner has been improperly dispossessed.

b. Assets Subject to Quasi Recovery (*Vindicatio Utilis*)

In the realm of bankruptcy law, certain assets are enveloped by intricate legal scenarios. This typically occurs when a rightful owner's title is affected by a legal transaction – consider, for instance, the sale of a piece of real estate. When a debtor defaults due to unpaid sums, or when the necessary registration of the transaction is neglected, the law permits claims on such assets. This specific category encompasses:

1. Realty sold to the debtor, provided that the purchase price has not been paid in full and the sale has not been recorded with the Public Registry of Property.
2. Unpaid chattel sold to the debtor in a spot market transaction.
3. Unpaid assets (realty and chattel) under contracts with a recorded default resolution clause.
4. Securities issued to the debtor's benefit or endorsed over to the debtor in payment of sales made on behalf of third parties.[9]

Furthermore, for political and tax collection purposes, the Bankruptcy Law incorporates, within this category, any contributions the debtor might have withheld, accumulated, or relayed on behalf of tax authorities. Such inclusion contravenes the foundational principle that assets should be individually identified to be eligible for a separatory action.

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[9] Sepulveda, E. (2011). *Mexican Legal Framework of Business Insolvency* (1st ed.). White & Case, p. 49.

c. Assets Subject to a Restitution Duty

This category comprises assets that, while in the debtor's possession, are not inherently their own due to pre-existing contractual arrangements. Such contracts might dictate the return or transfer of these assets to their legitimate titleholder under specific conditions. As outlined by the Bankruptcy Law, assets falling under this designation include:

1. Assets held under deposit, lease, usufruct, or those taken for administration or consignment, if commercial insolvency (*Concurso*) is declared before the buyer indicates a desire to claim said goods, or if the stipulated window for such expression of intent remains open.
2. Assets associated with transactions such as purchasing, selling, transit, delivery, or collection commissions.
3. Assets meant to be delivered to a specific person, on behalf of a third party, or to meet obligations at the debtor's domicile.
4. In instances where a bill of exchange influences the credit associated with a shipment, the rightful holder may petition for its segregation.
5. Proceeds in the debtor's ledger from sales transacted on behalf of another, wherein the claimant might concurrently request the assignment of the correlated credit entitlement.
6. Assets transferred to a trust.

Therefore, assets falling under the ambit of quasi recovery are those which, due to certain unfulfilled formalities or substantive conditions – such as comprehensive registration or full payment – may be retrieved by the original or aggrieved party. This principle echoes constructs like "*pacto comisorio tácito*" and the "*exceptio non rite adimpleti contractus*." Its core objective is to shield the party that has complied, ensuring that the debtor satisfies pivotal obligations, such as complete payment, prior to the affirmation of a complete ownership transition.

On the other hand, assets that carry a restitution duty are those temporarily under the debtor's custody, premised on previous or implicit agreements of return, contingent upon meeting specified stipulations. This paradigm is anchored in the notion of "temporary possession" coupled with the intrinsic obligation to revert the asset to its rightful possessor.

To elaborate, while assets subject to quasi recovery pertain to certain unmet requirements for a lawful transfer of ownership, those with a restitution duty focus sharply on the debtor's capacity as an interim custodian of the asset, underlined by the acknowledgment that such an asset is not legally theirs through any formal transaction.

This brings us to a salient query surrounding guarantee trust agreements. When a debtor, in the role of a settlor, transfers assets to a trustee, prescribing specific rules concerning the asset's deployment and ultimate destination, does this scenario constitute a quasi-recovery right in favor of the settlor or a restitution obligation in favor of the true owner, who is the trustee? This article asserts that it embodies a restitution obligation on the part of the debtor. This perspective is underpinned not only by the Bankruptcy Law but also by the fact that, once a trust is set up and the transition of asset ownership to the trustee is perfected, the debtor lacks the grounds to invoke any unfulfilled conditions to argue for a reverse quasi recovery of trust assets to the bankruptcy estate, contrary to what the Court has ruled. But before we delve deeper, we must examine the Court's analysis and its justifications for deeming the fiduciary institution's separation action for trust assets in a guarantee trust as impermissible.

IV. DECISION OF THE COURT IN *AMPARO DIRECTO* 188/2021

a. Background of the Case

To fully grasp the Court's resolution, it is crucial to succinctly lay out the case's background:

1. A financial entity acting as trustee under a trust agreement (hereinafter, the Claimant) filed a separation action of certain assets from the bankruptcy estate before the Fifth District Court of Veracruz (hereinafter, the Bankruptcy Court). This action was predicated upon a guarantee trust agreement with a right of reversion, which the debtor (now declared bankrupt) entered into with the Claimant. Under this agreement, aiming to secure the payment of various loans to the first-place beneficiary under the trust, the debtor, as the settlor, transferred several assets to the trust as collateral.
2. In response to the separation claim, the receiver (*síndico*)[10] submitted its reply, opposing to the separation of the assets from the bankruptcy estate.
3. On August 28, 2018, the Bankruptcy Court issued a decision declaring the separation claim pertaining to the assets described in the lawsuit as inadmissible.

[10] Under the Bankruptcy Law, the receiver, who may or may not be the conciliator, is responsible for taking possession of the bankrupt business. If the debtor is declared to be in the liquidation stage (*en quiebra*), or if no restructuring plan is agreed upon during the conciliation stage, the receiver will proceed with the sale of assets, among other duties.

4. Displeased with the aforementioned resolution, the Claimant lodged an appeal. But, in a decision dated February 9, 2021, the Bankruptcy Court found the appeal unfounded, upholding the previous resolution.
5. On February 8, 2021, the Claimant was notified of the Bankruptcy Court's verdict. In response, on March 2 of the same year, the Claimant filed an Amparo claim against the Bankruptcy Court's resolution.
6. The competent authority forwarded the case files to the Common Correspondence Office of the Court, which were received on March 23, 2021. The Court then reviewed the Amparo lawsuit, and the file was sent to the presiding judge for the formulation of the final resolution. This resolution denied the protective order to the Claimant.

b. Judicial Interpretation of the Asset Separation Right

The Court's examination of asset separation within the context of the *Concurso* process revealed that Article 70 of the Bankruptcy Law addresses more than the debtor's simple possession of assets without a final and irrevocable transfer. Delving deeper, the Court inferred that in order to separate assets from the bankruptcy estate, such assets should have been transferred to the Claimant under a definitive and irrevocable legal title. Drawing on the *a contrario sensu* interpretation of Article 70 and emphasizing the tenets of business conservation and safeguarding the bankruptcy estate's interests, the Court concluded that the right to separate assets only stands when the transfer to the Claimant is both definitive and irrevocable.

Additionally, the Court examined Article 71 of the Bankruptcy Law, outlining the assets that can be excluded from the bankruptcy estate when their cost remains unpaid in full. The Court discerned that the separation right is inapplicable in scenarios where the buyer has either completed or secured the total payment, or when objections arise from the receiver (*síndico*) or the conciliator (*conciliador*).[11] According to the Court, this understanding has its roots in Articles 93 and 96 of the Bankruptcy Law.

Central to its findings, the Court highlighted that the separation right, in instances of debtor default, comes into play exclusively when the debtor has outstanding payments, and neither the receiver (*síndico*) nor the conciliator

[11] Under the Bankruptcy Law, once a debtor has been declared in Concurso, a conciliator is appointed. This conciliator's responsibilities include mediating between the debtor and creditors to achieve a mutual reorganization plan, submitting a list of claims for court approval, and, in rare circumstances, seeking the debtor's removal from business management.

(*conciliador*) contests this on behalf of the estate. Conversely, "if the Claimant seeks this right due to outstanding debts, it stands to reason that the debtor is equally entitled to retain assets which, though transferable, remain unpaid." Hence, the Court determined that "transferring the debtor's assets to the trust didn't represent a final and irrevocable legal title. This stance aligns with the overarching public interest in preserving businesses, as stipulated in Article 1 of the Bankruptcy Law."

Drawing on fundamental tenets like business preservation, process efficiency, speed, transparency, and good faith, the Court cites multiple sections within the Bankruptcy Law intended to protect the bankruptcy estate. More specifically, these sections counteract or neutralize actions to shield both the debtor and its creditors. In its review, the Court:

- Points to Title Three, Chapter VI of the Bankruptcy Law, which treats certain transactions between the debtor and third parties – such as gifts or debt forgiveness – as null. These transactions lack mutual benefit and consequently deplete the debtor's assets.
- References Articles 91 and 92 of the Bankruptcy Law, which state that the declaration of *Concurso* does not affect the provisions of an executory contract or those tied to assets over which the debtor maintains managerial or dispositional control. Importantly, the debtor remains obligated by these contracts unless the bankruptcy conciliator (or receiver) deems them counter to the estate's best interests.
- Notes that Article 100 of the Bankruptcy Law confirms that credit agreements persist unless the conciliator (or receiver) views termination as beneficial. Similarly, personal obligations or credit relationships hold unless seen as harmful to the bankruptcy estate by the conciliator or receiver.
- Highlights Article 87, which stipulates that any provision of an agreement that sets modifications that worsen the contractual terms for a debtor as a result of the filing of a petition for, or the declaration of, Concurso, shall be deemed not included therein.

From these sections, the Court determines that while the conciliator or receiver doesn't have jurisdiction over the validity of executory contracts, they can challenge the debtor's contractual relationships if they negatively affect the bankruptcy estate.

Conclusively, the Court argues that the Bankruptcy Law "strives to resolve uncertainties regarding a debtor's commitments after the declaration of Concurso. By addressing these concerns, the law primarily serves the bankruptcy estate, aligning with Article 2 of the Law, without causing undue strain on creditors in the contractual context."

Finally, when analyzing Bankruptcy Law sections related to fraudulent conveyance – which harm the bankruptcy estate and are, therefore, deemed void – the Court finds parallels with situations where a receiver or conciliator steps in to prevent contracts that are detrimental to the estate. Based on this understanding, the Court concludes that the right to separate assets does not apply when either the payments have not been made or, though paid for, the services or goods have not been delivered. In both scenarios, if they pertain to the estate's assets, such assets should not be segregated from the bankruptcy estate. Instead, these matters should be resolved through credit acknowledgment, ensuring that the bankruptcy estate remains unaffected, as stipulated in Article 114 of the Bankruptcy Law.

c. Court's Decision in *Amparo* 188/2021

In its detailed review of the case, the Court draws attention to several pivotal aspects of the trust agreement. While the agreement required the debtor to transfer asset ownership to the fiduciary institution, serving as trustee, to primarily secure payment obligations under the credit agreement, the second clause made it clear that this transfer did not equate to a transfer for tax purposes, as outlined in Article 14, Section V, of the Federal Tax Code. This distinction was premised on the settlor's retention of the assets' reversionary rights.[12]

Moreover, the Twentieth Clause enumerated specific events of default by the settlor. These included actions that jeopardize any of the collateral agreements or those that potentially render the debtor akin to a state of insolvency, bankruptcy, *Concurso*, reorganization, liquidation, suspension of payments or debt relief, including the appointment of officials such as a receiver, trustee, liquidator, *síndico*, *conciliador*, administrator, custodian, conservator, or any comparable figure over either the debtor or a substantial part of its assets.

Furthermore, the Thirteenth Clause elucidated the trust's enforcement mechanism designed to safeguard credit obligation repayments. It affirmed that any residual assets, after such enforcement, would devolve back to the settlor.

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[12] Article 14: The term 'alienation of assets' is understood as:
I to IV. . . .
V. Transactions executed through a trust, under the following circumstances:
a) When the settlor designates, or commits to designate, a trust beneficiary other than himself/herself, provided that the settlor does not retain the right to reacquire the assets from the trustee.
b) When the settlor forfeits the right to reacquire the trustee's assets, in instances where such a right had been previously reserved.

In its judgment, the Court referenced Article 386 of the General Law of Negotiable Instruments and Credit Transactions (*Ley General de Títulos y Operaciones de Crédito*, or LGTOC). This provision emphasizes that trust assets must be allocated exclusively for their designated purpose. Furthermore, Article 393 of the LGTOC stipulates that, unless otherwise provided, assets or rights held by the trustee revert to the settlor upon the trust's termination. Article 405 clarifies that claims grounded on a guarantee trust become time-barred after three years. After this period, the right to enforce them ceases, and the trust assets' ownership returns to the settlor.

In light of these contractual provisions and statutory guidelines, the Court determined that the transfer of assets to the trust was neither definitive nor irrevocable. Consequently, the trust assets cannot be isolated from the bankruptcy estate. This is because, according to the Court, ownership of the trust assets should revert to the bankruptcy estate in line with the principles of good faith and fundamental tenets of bankruptcy proceedings.

The Court, in substantiating its decision, points to Article 386 of the LGTOC, emphasizing that trust ownership does not automatically grant the right to profit or benefit from the trust assets. The trustee may not use, profit from or dispose of the trust assets, as these rights typically rest with the beneficiary of the trust. Moreover, the scope of fiduciary ownership is strictly defined by the trust agreement. Consequently, the trustee can only enforce the trust and liquidate assets within the trust when guaranteed obligations set forth in the agreement are breached by the settlor. Any remaining proceeds will revert to the settlor. In instances where the trust terminates, or the enforcement claim is statute-barred, the assets revert in favor of the settlor. Hence, the Court determines that such constructs do not denote a definitive and irrevocable transfer of assets eligible for separation from the bankruptcy estate. Instead, it illustrates a temporary influence on asset allocation, contingent upon fulfilling the contract's obligations.

In essence, the trustee can assume ownership of the trust assets only upon breach of guaranteed obligations, which would allow the trustee to carry out trust enforcement actions and liquidate the trust assets to satisfy those obligations. However, pursuant to Article 65 of the Bankruptcy Law, the enforcement of the trust and the liquidation of trust assets with the resultant fulfillment of obligations by the trustee becomes infeasible once *Concurso* is declared. The debtor's assets and rights then receive protection from seizure, barring labor-related exceptions specified in the Bankruptcy Law.

Elaborating further, the Court contends that if, at the time of Concurso declaration, the debtor is not in default regarding obligations backed by trust assets containing a reversion clause, such assets should revert to the settlor, adhering to principles of good faith and efficiency. Consequently, the remaining debts should be deemed terminated under Article 88, Section I, of the Bankruptcy Law but remain recoverable through credit acknowledgment.

To fortify its stance, the Court cites the following articles from the Bankruptcy Law:

- Article 86: The declaration of Concurso does not affect the provisions of an executory contract, unless the conciliator rejects it on grounds that rejection is in the best interest of the estate.
- Article 88, Section I: Upon the declaration of *Concurso*, all claims against the debtor shall become due.
- Article 100: A debtor's declaration of Concurso doesn't automatically terminate credit agreements unless the conciliator deems it appropriate and in the best interests of the bankruptcy estate.
- Article 105: Upon the declaration of *Concurso*, debts and credits are set off or allotted for payment, especially those arising from specific financial contracts. They can be invoked as due based on respective contracts or the Bankruptcy Law, regardless of their current state.

The Court discerns a prevailing legal trajectory from the cited articles: "post Concurso declaration, outstanding credit balances become payable through credit acknowledgment. Even if the debtor's obligations under the credit agreement are accelerated upon the Concurso declaration, they remain enforceable per liquidation (Quiebra) provisions 229 to 236. This acknowledgment and the subsequent alteration in payment method align with the assumption that both secured obligations and those under trusts are managed in accordance with these rules."

The Court concludes that for guarantee trusts with a "reversion clause," if the guaranteed obligation remains undefaulted and a *Concurso* is initiated, the reversion rights should be triggered, leading to the fulfillment of credit obligations through the debt acknowledgement.

V. CRITICAL EXAMINATION OF THE COURT'S RESOLUTION

a. Flawed Interpretation Concerning the Reversion of Trust Assets

Upon analyzing the Court's reasoning, it becomes clear that assets transferred to a guarantee trust with a reversionary right were not viewed by the court as being subject to a restitution duty as clearly outlined in subsection (e) of Section VII of Article 71 of the Bankruptcy Law. Instead, the Court believed that such assets should revert to the debtor. Advancing the notion of an inverse quasi-recovery action in favor of the settlor, the Court reasoned that the declaration of *Concurso*, coupled with the subsequent acceleration of the debtor's obligations under the credit agreement, renders these obligations enforceable under provisions pertaining to payments to acknowledged creditors during the liquidation phase (*etapa de quiebra*) of the bankruptcy process, especially in the absence of an approved restructuring plan. This view underscores the transformative effect of the *Concurso* declaration and the acknowledgment of debt on the initial repayment terms.

However, there is a discernible gap in the Court's reasoning. The Court fails to connect its primary assertions to a consistent and legally sound conclusion. It seems to embark on an unwarranted logical stretch, culminating in an inaccurate judgment. To clarify, the trust agreement's terms stipulate that assets revert to the settlor only after the payment obligations to the recognized creditor have been met. A mere declaration of *Concurso*, the early acceleration of the credit agreement with trust-guaranteed obligations, and the debt acknowledgement do not equate to satisfying these guaranteed payment obligations. Consequently, asset reversion ought to be deferred until all such commitments are fully met (i.e., the recognized creditor has been paid in full).

The Court's misstep stems from its logical formulation. Although it confidently asserts its major premise – that a declaration of *Concurso* and credit acknowledgment alters the initial payment framework – it omits a crucial minor premise. The Court doesn't offer a legal basis to explain the process by which trust-held assets revert to the bankruptcy estate without first settling debts to the recognized creditor. This omission undermines its final judgment on asset reversion to the bankruptcy estate.

In a different scenario, should a restructuring plan gain approval to write off 80% of the outstanding credit balance – binding the recognized creditor[13] pursuant to Article 158 of the Bankruptcy Law – the subsequent payment of the remaining 20% to this creditor would be considered a full payment due to the cramdown effect of the bankruptcy plan. Under these circumstances, the rationale leading to the assertion that asset reversion to the trust is appropriate becomes legally and logically robust.[14] However, if no such agreement is in

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[13] The recognized creditor possesses top tier beneficiary rights over the trust.

[14] However, please note that some legal experts argue that beneficiaries of guaranty trusts might qualify as creditors with a special privilege. This stems from the view that obligations backed by such trusts should be recognized as claims with this privilege, allowing a preferential collection right against the trust property over standard unsecured creditors. Under the

place, bankruptcy proceedings naturally continue in a liquidation phase (*etapa de quiebra*).

Article 3 of the Bankruptcy Law articulates the core objective of the liquidation phase: the liquidation of the debtor's assets – whether that encompasses the entire business, specific production units, or individual assets – with the aim of settling debts with recognized creditors. Given this directive, it stands to reason that only after the assets are liquidated and payments made to the recognized creditors, should there be any contemplation of reversing the trust assets back to the settlor. To suggest otherwise is akin to the age-old idiom of "putting the cart before the horse." Such a suggestion lacks backing within the Bankruptcy Law, its supplementary laws like the Commercial Code, or other relevant legislations, including the LGTOC and the Federal Civil Code.

Thus, asset reversion remains inactive until the guaranteed obligation is fully paid. If, after liquidating assets, payments still remain due, Article 235 of the Bankruptcy Law prescribes that, following the termination of the bankruptcy process, creditors still holding unpaid balances retain the right to pursue legal remedies against the debtor for those amounts. This includes the creditor's right to initiate legal action for trust enforcement in line with Article 1414 bis 17 of the Commercial Code, which provides:

(i) If the collateral assets are equivalent in value to the determined debt, the debt is considered settled, allowing the plaintiff unfettered access to the assets.

(ii) If the assets' value is less than the debt's assessed amount, the plaintiff can use the assets without restriction but also maintains the right to pursue the remaining debt through other legal means.

(iii) Only when the assets' value exceeds the determined debt does the plaintiff need to return the excess to the defendant after settling the principal debt, accumulated interest, and expenses.

In summary, the trust assets' reversion to the settlor only takes place after the creditor's claims are fulfilled. Moreover, in cases where the debtor fails to meet obligations and there's a subsequent legal enforcement of the trust, the debtor shouldn't expect any surplus unless the value of the asset surpasses the amount owed.

b. Misapplication of Legal Tenets

The Court's reference to principles like transcendence, procedural efficiency, promptness, transparency, and good faith is, at its core, ambiguous. The Court's

Bankruptcy Law, payments in a reorganization plan should first address these privileged creditors who haven't agreed to such restructuring plan.

rationale does not successfully forge a tangible connection between these tenets and the foundational arguments shaping its decision. Moreover, there's a noticeable absence in the Court's reasoning on how these principles guided its final judgment.

The Court's reliance on the principle of business preservation appears misplaced. Notably, Article 3 of the Bankruptcy Law emphasizes the importance of business preservation only during the conciliation phase (*etapa de conciliación*), a period dedicated to reaching agreements with acknowledged creditors. However, once the process advances to the liquidation phase (*etapa de quiebra*), the operational core of the business effectively comes to an end. While Article 197 of the Bankruptcy Law instructs the receiver (*síndico*) to explore the continuation of business operations and, where feasible, to sell all debtor's assets and rights as a going concern, the primary objective is not necessarily the preservation of the business. Instead, the main concern is to maximize the proceeds from asset disposals for the creditor's advantage.

c. Erroneous Interpretations and Unwarranted Ambiguity in the Bankruptcy Law

The Court's reference to the principle of business preservation – deemed irrelevant in this context – lacks a well-grounded reasoning when interpreting Article 70 of the Bankruptcy Law, straying from its explicit language.

The essential role of law is to offer clarity and consistency. To uphold this mission, interpretations should align faithfully with the statute, particularly when its directives are straightforward. Article 70 of the Bankruptcy Law articulates precise guidelines for separating assets under the debtor's possession. However, seeking to widen the scope, the Court resorts to an *a contrario* reading, leading to unnecessary ambiguity and misalignment with the original legislative intent.

The *a contrario sensu* approach seeks meaning from what is left unsaid, rather than from clearly spelled out provisions. While occasionally useful, applying this method necessitates careful judgment, especially when the law is explicit. Given that Article 70 candidly outlines the criteria for asset separation during bankruptcy, any *a contrario* reading feels both redundant and misplaced.

By leaning on this interpretative method, the Court imposes conditions not present in the Bankruptcy Law. Such insertions complicate the application of the law, diverging from its inherent purpose and potentially leading to uneven verdicts – a distinct departure from principles of legal consistency and certainty.

It is important to recognize that the *a contrario* method is not a foremost tool in legal interpretation. It should act as a fallback, applied only when primary methods prove ineffective.[15] Here, the Court's reliance on this technique seems less about clarifying the law and more about shaping its enforcement, jeopardizing the Bankruptcy Law's integrity and predictability.

Moreover, Article 71 of the Bankruptcy Law unambiguously specifies that assets transferred to a trust can be separated from the bankruptcy estate. The Court's undue preoccupation with specific trust intricacies clouds this clear provision. By giving undue weight to the settlor's reversion right, the Court conflates the reversion of assets with trust irrevocability – evidencing a clear misunderstanding of both concepts.

While Article 71 does not differentiate between trust types (i.e., guaranty trust, administration trusts or source of payment trusts) or list specific provisions or considerations for asset separation, the Court oversteps its bounds by introducing such distinctions – needlessly complicating matters and even citing Articles 93 and 96 of the Bankruptcy Law, which hold no relevance to trusts or asset separation.

Persisting with its *a contrario* interpretation, the Court suggests that the separation action applies only under certain conditions, a departure from the clear guidelines in Article 71. Such a stance not only obfuscates comprehension but also implies that assets tied to trusts can only be separated from the bankruptcy estate if the settlor waives its reversion right. This interpretation is not just logically unsound but jeopardizes the legal standing of countless credit transactions in our legal landscape.

Lastly, the attempt to associate this reading with the public interest in preserving businesses, as articulated in Article 1 of the Bankruptcy Law, appears to be an endeavor aimed at providing a moral or justifiable underpinning to the Court's rationale. However, this is misguided: the principle of business preservation should not serve as a means to curtail or modify the explicit

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[15] See: DISTRICT JUDGE: INVOCATION OF LEGAL PRECEPTS USING *A CONTRARIO* READING FOR SUPPORTING RESOLUTIONS. In the event that a District Judge, when delivering a judgment, finds the absence of a specific regulation governing the case under consideration, they can appropriately turn to the "argument *a contrario*" principle to address the contentious matter. This action aligns with the principle of the hermeneutic plenitude of the legal framework, as stipulated in Article 18 of the Federal Civil Code. The "argument *a contrario*" serves as one of the several techniques for integrating legal norms, enabling the filling of gaps in legislation. Notably, this technique specifies that if a norm establishes a restrictive solution concerning the addressed case, it logically implies that unmentioned scenarios must be subjected to an opposing resolution. Consequently, this approach stands as a legally sound course of action. Tribunales Colegiados de Circuito. (2006). Tesis aislada III.2o.C.18 K. In Semanario Judicial de la Federación y su Gaceta, Ninth Period, Common Matter, Vol. XXIII (p. 1827). Digital registration: 175910.

provisions outlined in other sections of the Bankruptcy Law – especially not within the context of the liquidation phase (where there is no business to be preserved).

d. Inappropriate Conflation of Creditor Fraud Provisions and Asset Separation Actions

The Court frequently cites Title III, Chapter VI of the Bankruptcy Law, which pertains to fraudulent conveyance. However, it stops short of clarifying the connection between these provisions and the action for separating assets transferred to a trust. To reiterate, the main thrust of Title III, Chapter VI is to safeguard creditors from any malicious conduct by the debtor, recognized by the Bankruptcy Law as acts committed in bad faith. The goal of such reinstatement actions is to balance the scales within the debtor's assets, ensuring that no action unjustly diminishes their value or favors specific creditors.[16]

Conversely, the central contention of the present case pertains to the exercise of asset separation rights, striving to affirm and safeguard third-party ownership rights over assets that, while in the debtor's possession, do not rightfully belong to it. This right is less about the debtor's financial behaviors and more about justly protecting third-party assets.

It is manifestly clear that revocation actions and the right to separate assets have unique legal objectives and inherently differ. Given their clearly divergent aims, it is curious that the Court sought to rely on provisions from Title III, Chapter VI while considering the nature and requirements for separating assets held in trust. This approach obfuscates distinct legal goals and inappropriately merges separate legal frameworks.

Moreover, by analogously employing provisions related to creditor fraud to hinder the asset separation action, the Court commits a significant interpretative mistake, resulting in an amalgamation of concepts and ultimately issuing a ruling that lacks precision, jeopardizing both legal clarity and certainty.

Exacerbating this oversight, the Court offers no rationale for invoking provisions from Title III, Chapter VI, especially in the absence of evidence or

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[16] Per se fraudulent transactions are those that a company carries out before the bankruptcy declaration, intentionally defrauding creditors if the third party that participated in the transaction had prior knowledge of such fraud. Pursuant to Article 113 of the Bankruptcy Law, all per se fraudulent transactions are avoidable, regardless of the time when they were carried out. On the other hand, the other types of transactions subject to avoidance (cases of constructive fraud, objective preferences, and subjective preferences) are avoidable only if they are carried out within the retroactive period.

an assertion that the assets in contention were deceptively transferred to the trust to defraud creditors. As the case records clearly demonstrate, both the credit agreement's execution and the asset transfer to the trust occurred outside the stipulated look-back period (*periodo de retroacción*).

e. Conflating Asset Separation with Trust Enforcement

A significant oversight by the Court is its assertion that the debtor's partial compliance to obligations tied to the trust assets nullifies the trustee's right to file a separation claim. While it might be tenable to argue that a debtor's partial compliance could impede the foreclosure of assets used as collateral, it is intellectually untenable to infer that such partial compliance (or lack of breach) ipso facto precludes the separation of assets - not encompassed within the bankruptcy estate – from the debtor's estate or precipitates their reintegration into the bankruptcy estate.

The Court's analysis blurs the distinction between the outcomes of a separation action and the ramifications of enforcing a guaranty trust – two distinct matters. Notably, the declaration of *Concurso*, which pauses any asset seizure or stays any enforcement proceedings during the conciliation stage, doesn't contradict the legal premise of a separation action.

Regrettably, the Court appears to misconstrue the quintessential purpose of separation: asserting that assets transferred to a trust should remain insulated from, and not be subsumed within, the bankruptcy estate. While in certain scenarios, the separation action might result in the transference of the asset to the Claimant, it could also signify a mere affirmation of proprietary rights, thereby retaining the asset under the immediate control of the debtor (or the receiver).

The Court's flawed reasoning, suggesting that the debtor's adherence to obligations backed by trust assets is grounds for denying a separation action, raises concerns. Even more problematic is the Court's application of this erroneous logic to argue for the reversion of trust assets to the bankruptcy estate. This overlooks the fact that the bankruptcy estate lacks legitimate claim over those assets. Incorporating those assets into the bankruptcy estate would amount to an unwarranted seizure or improper asset appropriation that does not rightfully belong to the debtor.

f. Trust Property Misconception and the Misrepresentation of Separation Action

The Court's reliance on the notion that trust property (*propiedad fiduciaria*) does not grant the trustee complete rights to benefit from the trust assets reveals a significant misapprehension. This not only obscures the fundamental nature and objectives of trust property but also misconstrues the true purpose of separation actions in bankruptcy contexts.

Neither Article 70 nor Article 71 of the Bankruptcy Law explicitly mandates that a titleholder possess rights equivalent to those outlined in the Federal Civil Code to use and benefit from the assets. This absence highlights the Bankruptcy Law's aim to separate assets based on titleholder status, rather than a conventional civil law definition of "full ownership". The choice of the term "titleholders" in Article 70, instead of "owners," reinforces this reading. The Court, by introducing this additional criterion, goes far beyond the express language of the law, overstepping its interpretative limits.

As detailed in Article 381 of the LGTOC, a trust is crafted to create a distinct and earmarked asset pool. This pool stands entirely autonomous, separate from the personal assets of parties involved in the trust agreement. The primary objective of a trust is to insulate certain assets. Whether these assets can be conventionally utilized or not remains irrelevant to its core nature or objective.

By either neglecting or misunderstanding this intrinsic aspect of trust property, the Court has exposed its flawed grasp on the structure and purpose of the guaranty trust. Its perspective, which hinges more on the practical enjoyment of assets rather than the establishment of an independent asset pool, misrepresents the legislative intent and could jeopardize credit accessibility in our country.

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