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Contracting Pitfalls 1

Warning: Be very careful with the way you construct the jurisdiction clause if your contract is subject to Mexican law.
Antonio Vázquez

Our Firm has extensive experience in the litigation of breaches of contract before the Mexican Courts, (particularly in the aviation industry)¹. Generally in these disputes there are two parties: One of Mexican nationality with domicile in Mexico and a foreign counterpart doing business in Mexico, but with domicile in another country. As a consequence, it is very common in this kind of legal procedure that judges from either country may be competent to hear the dispute, so it is very important to construct your jurisdiction clause so that it is very clear as which court will have jurisdiction in case of a dispute.

The suggestions contained in this brief document are based on our practical experience of litigating jurisdiction clauses that were badly constructed. The immediate consequence of these mistakes is a very difficult litigation process, not in the legal dispute itself, but in the discussion of the legality of the appointment agreed by the parties in the jurisdiction clause. Sometimes the problem is so important that the original intention of the parties on appointing a Mexican judge to hear the procedure may be voided based on the illegality of the jurisdiction clause. If your jurisdiction clause does not comply with certain rules, this clause will have a great chance of being declared void and as a consequence, the competent judge will be appointed through a judicial judgement, based not in the agreement of the parties, but in the applicable legal provisions.

¹ In the last few years, the members of our Firm have been involved in the repossession of more than 30 aircraft that were leased by Mexican lessees. 80% of the mentioned cases were ordered by Mexican Courts. We have a success rate of the 100% in these kind of cases.



In the next paragraphs you will find very easy rules that you must follow, and take into account when you construct a jurisdiction clause, so as to be sure that the appointment of the judge will be valid in Mexico. The following suggestions are based on two main premises: 1) The existence of one Mexican party (with its domicile in Mexico) and another foreign party with domicile outside of Mexico, and 2) That the main obligations contained in the contract will be carried out in Mexico.

Applicable law to the contract

As a general rule, the applicable law to the contract will be the one that the parties agreed to. However, if the parties agreed to a foreign law jurisdiction, but appoint a Mexican judge to hear the case, then the law applicable to the appointment will be the Mexican law ONLY for the specific matter in litigation².

If the parties do not agree on a specific applicable law, then I consider that the Mexican law may be applicable, considering that the domicile of one of the parties is in Mexico, and that the main obligations of the contract will be carried out in Mexico.

Mexican Rules applicable to the jurisdiction clause

The Commerce Code contains the rules applicable to the jurisdiction clause. This Code provides the following basic rules.



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FIRST RULE: The parties must have the legal authority to designate a competent Court in case of a dispute.

This rule seems to be clear; however you should be very careful, because the Code contains also various requirements to ensure the validity of the jurisdiction clause. If one of the following requirements is not observed, then the jurisdiction clause will not be valid:

The parties must make an express waiver of the jurisdiction that according to their respective domicile would be the applicable one. For example: If the other party to the contract is a Mexican Company and the parties appoint a foreign Court in case of controversy, but the Mexican party does not include an express waiver of the applicable Mexican jurisdiction then you will have a potential risk of a future dispute based on the voiding of the jurisdiction clause (Do not forget that the main obligations of the contract will be carried out in Mexico).

² According to the Civil Federal Code, the Mexican Courts may apply foreign law.





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As you can see, the parties must clearly appoint one specific Court that in case of controversy will hear the case and the appointment must refer to one Court exclusively, and specify the exclusion of any other court or jurisdiction...

If the parties do not appoint a specific Court, the appointment will not be valid. For example the following is an invalid clause: *"The parties agree that it will be competent court in the place the aircraft are physically based during the performance of the contract..."* The parties MUST appoint a specific Court from the three criteria listed above (domicile of one of the parties, place of compliance of the obligation or place at which the assets are placed).

SECOND RULE: The parties do not appoint a specific judge. As a consequence, the Mexican Legal provisions will apply to determine the competent judge.



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It is very important to know these rules, or to be well advised at the moment of choosing or constructing your jurisdiction clause, in order to have the legal security that the Court agreed by the parties will be the one to actually hear the dispute.

In following editions of this newsletter, we will discuss our experience with the Mexican courts on hearing these kinds of disputes.



The Mexican Senate has ratified the Cape Town Convention. A great start.

Mario Molina

On April 27, 2006 the Mexican Senate ratified the Cape Town Convention¹ and the Protocol of the aircraft equipment signed by the Federal Government.

With the agreement to this Convention and Protocol some of the benefits of the aircraft equipment financing will start to flow into our country. The Cape Town Convention represents an ideal mechanism to reduce the price of the international financing of modern aircraft, and for Mexico it represents as well a golden opportunity to commence to build a new reputation in the aircraft leasing business around the world.

Two months ago, an aircraft lessor, who faced the default of a Mexican client, would have to fight the termination of the lease contract before a Mexican court in order to gain the repossession of his aircraft. This would be fraught with all the disadvantages that a litigation procedure can bring, but mostly, with the inevitable detriment of its property. After that, once the lessor obtained the effective possession of the aircraft, then in order to achieve de-registration, he would then have had to walk an even more devious path. Today the panorama is a lot more encouraging.

The Convention provides an international legal regime for the creation, perfection and priority of security, title retention and leasing interests in aircraft equipment, railway rolling stock and space assets, which will be underpinned by an International Registry. It has been estimate that such a regime could save very large sums of money annually in financing charges and open up to developing countries access to finance at reasonable cost.



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² The Convention on International Interests in Mobile Equipment and its Aircraft Equipment Protocol were concluded at Cape Town in November 2001. The Convention is one of the most ambitious and imaginative private commercial law Conventions ever have been concluded. Hitherto, interests in mobile equipment of high unit value regularly crossing national boundaries have been exposed to the risk and uncertainty created by differences in national laws governing security and related interests. The Convention provides an international legal regime for the creation, perfection and priority of security, title retention and leasing interests in aircraft equipment, railway rolling stock and space assets, which will be underpinned by an International Registry. It has been estimate that such a regime could save very large sums of money annually in financing charges and open up to developing countries access to finance at reasonable cost.



The Cape Town Convention and its Protocol on Aircraft Equipment have two main objectives:

- a. To facilitate the acquisition and financing of aeronautic equipment of high value, by means of the creation of international guarantees that are recognized by the signatory states;
- b. To provide to the creditor with the basic defense mechanism in case of default or insolvency of the debtor.

Therefore, the Convention establishes a list of concrete mechanisms directed firstly to the creation of an International Registry for Aircraft and equipment; and secondly, for effective legal action against defaulting lessees or debtors in aircraft lease or purchase contracts.

It is in this specific instance that we find some discrepancy with the local aviation law of Mexico. The Cape Town Convention and Protocol establishes that the owner of the aircraft is able to choose from two main different lines of action once the default appears. Either to obtain de-registration or repossession. According to the Mexican Aviation Law, the solicitor handling the de-registration process must prove two situations concerning the aircraft: ownership and possession. Therefore, in strict sense, the owner of an aircraft must obtain the effective possession of the aircraft before working to de-register the aircraft.

As a final conclusion we must point that if a creditor intends to take any legal action in Mexican territory under the Cape Town Convention and its Protocol, the creditor should consider a list of implications that could emerge through the development of the procedure due to some practical problems of compatibility with the Mexican Aviation Law and others.

It's true that there are still reforms that need to take place in Mexico in order to offer an ideal environment for international investment. This ratification however represents a great breakthrough in the unbearable protectionism policy espoused by the Mexican Government in past years. Let's plead for this great change to become a national policy.



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