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Deregistration and Exportation from Mexico of
Repossessed Aircraft from Bankrupt Airlines.

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Bankruptcy Procedure.

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COELUM Pronunciation: 'che-l&m, is Latin for airspace or sky. The Romans began questioning the rights they had in the space above the land they owned and to how high above did that right extended to. Ad coelum et ad inferos, they discussed, meaning that their right of property would extend as high up to the heavens and down to hell.

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Deregistration and Exportation from Mexico of Repossessed Aircraft from Bankrupt Airlines.

by *Kendra Medina**.

Recent developments in the Aviation industry in Mexico have caused aircraft lessors to encounter challenges and questions not previously considered in depth, such as the steps they need to follow after successfully repossessing their aircraft in order to place the aircraft with a new operator within or outside of Mexico. These steps include the cancellation of the registration mark and any records related to the aircraft that are with the Mexican aviation authorities, concerning ferry flights, dispatch and exportation of the aircraft.

The purpose of this article is to explore the special circumstances that surround the exportation of an aircraft that has been repossessed from a bankrupt Mexican airline. Also the specific things which need to be taken care of under Mexican law in order prevent any potential liability to the lessor or owner of the aircraft or the imposition of any lien over the aircraft.

As discussed in previous COELUM editions, under Mexican customs law, aircraft operators holders of a concession title to provide air public transport services are exempted from paying the importation tax, provided the importation is made on a temporary basis. Under this regime the aircraft is permitted to be imported and to stay within the Mexico for up to ten years, provided it is exported by the end of this term.¹ This is a very attractive incentive for Mexican airlines to adhere to the temporary importation rule with respect leased aircraft, as opposed to definitively importing the aircraft, in which case the airline, as importer, would be required to pay the full importation tax rate.²

“The importer is the party responsible for completing the temporality cycle applicable to the importation of the aircraft by taken care of its exportation within the permitted ten year period”

In accordance with the applicable law,³ it is the importer who becomes the responsible party for complying with the requirements imposed by the temporary importation regime. Requirements such as not transferring the property rights of the aircraft (when the importer is the owner), or transfer its rights of possession over the aircraft, without previously having taken the aircraft out the temporary importation regime, either by exporting the aircraft out of Mexico or importing the aircraft on a definitive basis and paying the corresponding importation taxes prior to such transfer. In the same manner, it is the importer who is responsible for completing the temporary cycle applicable to the importation of the aircraft by taking care of its exportation within the permitted ten year period, if not exported by the deadline, or imported on a definitive basis, the aircraft would be considered to be illegally in Mexico.⁴ Failing exportation of the aircraft the importer would have to pay not only the corresponding import tax as required by the Mexican tax authorities, but any applicable fines and moratory interest on those charges, which can be very significant.

* IN COLABORATION WITH SAMANTHA GARNICA

1.- Customs act, article 106 f. V.

2.- General Importation and Exportation Tax Law, chapter 88.

3.- Customs act, Articles 59, 105, 106.

4.- Mexican Customs Law, Article 106.

When an aircraft lease agreement has expired or is terminated by mutual agreement, either previously agreed or not, the Mexican airline or operator usually cooperates in a timely fashion with the aircraft lessor to effect the deregistration of the aircraft and to obtain all records from the Mexican aviation authority, when applicable, as well as to obtain any permits from the Mexican authorities to ferry and export the aircraft out of Mexico. Unfortunately, when an event of default arises and repossession of the aircraft is not made on an amicable basis and furthermore, needs to be completed by judicial means within a bankruptcy proceeding of the Mexican airline in possession of the aircraft, the expectation of good cooperation is very low or sometimes nonexistent. The question is worth analyzing as to who should be legally entitled to and/or obliged to complete the de-registration of the aircraft and to close the importation/exportation cycle.

Once an aircraft is successfully repossessed from a Mexican airline (either as a result of the enforcement of a judicial resolution prior to the bankruptcy declaration of such airline or by means of a separate related procedure, such as the “*separation of goods*” proceeding,⁵ once the bankruptcy proceeding has begun), if the judicial resolution, on which the repossession was based on, ordered the airline not only to redeliver the aircraft to the complainant, but to complete all the necessary filings and acts, and deliver all the documentation, necessary to deregister (if applicable) and export the aircraft out of Mexico as well; or alternatively, order the relevant Mexican authorities to authorize the reposessor to complete such acts and/or filings itself, then the reposessor (either as owner, lessor or in any other capacity) has more than half of the problem solved because any further actions required from either the airline or the relevant authorities can be judicially enforced.

On behalf of the bankrupt airline, it is the individual appointed by the bankruptcy court (*síndico*), the officer in charge of taking over the administration of all the assets owned or possessed by the bankrupt airline, who has the responsibility to abide by any orders issued by the bankruptcy court on behalf of the airline. The relevant Mexican authorities that should be ordered to complete the proceedings filed by the reposessor, as the case may be, are the Mexican Aviation Authority (*Dirección General de Aviación Civil*) and its registry, the Mexican Aeronautics Registry (*Registro Aeronáutico Mexicano*), along with the Mexican customs authority (*Secretaría de Hacienda y Crédito Público, and Servicio de Administración Tributaria*). If however the aircraft is repossessed prior to the declaration of bankruptcy and no judicial resolution ordering these measures is available, the reposessor of the aircraft can encounter several practical problems.

The most significant are a) The ability to demonstrate that the aircraft is legally within the Mexican territory if it does not have the appropriate evidence (*pedimento or permiso de importación*)⁶ and b) The ability to guarantee the aircraft is free and clear from any lien if it intends to transfer the possession or ownership of the aircraft to a new operator who wants to have the aircraft operated in Mexico (i.e. if cancellation of the Mexican registration mark is not completed and certain security interests are thereto registered, or if the aircraft is subject to be attached by the Mexican customs authorities if the aircraft has not been properly imported definitively and the corresponding importation taxes have not been paid, or the aircraft has not been re-exported, prior to such transfer).⁷

5.- Mexican Insolvency Proceedings Law, Articles 70 thru 73 (Procedimiento de Separación de Bienes).

6.- Mexican Customs Law, Article 36.

7.- Mexican Customs Law, Article 155.

“The aircraft is subject to be attached by the Mexican customs authorities if the aircraft has not been properly imported on a definitive basis and the corresponding importation taxes have not been paid, or the aircraft has not been re-exported, prior to such transfer.”

In accordance with Article 35 of the Mexican Customs Law, importation and exportation of goods from Mexico shall be performed by the depositaries, owners, possessors, importers or customs agents with the customs authorities, hence, any person that can demonstrate ownership title over the aircraft, or is in legal possession of it, is entitled to complete the exportation process. However, it is required to present the relevant documentation.⁸ Consequently, it is of great importance to repossess, along the aircraft and the aircraft records, the evidence of proper importation into Mexico. Ideally, the reposessor should have obtained the original or a certified copy of this evidence as of the date the airline imported the aircraft into Mexico.

As for the deregistration of the aircraft and registration of security interests thereto, in accordance with Article 46 of the General Civil Aviation Law, the cancellation of the Mexican registration mark can be requested by the owner or the person in legal possession of the aircraft, and the cancellation of any other registrations, such as security interests, by the express consent of the beneficiary. However the common practice that has been followed up today by the Mexican aviation authority is to authorize these cancellation requests provided they are supported either by the operator’s consent or a judicial order. The foregoing criteria has been applied because although Article 46 of the General Civil Aviation Law expressly permits the person in possession of the aircraft to complete the cancellation of the registration mark, deregistering the aircraft without acknowledgement of the holder of such registration mark (the operator) may be in violation of the operator’s constitutional rights under Article 16 of the Constitution of the United Mexican States, considering that the Mexican aviation authority may not be considered as the competent authority to determine if the aircraft has been legally repossessed from the operator. Nevertheless, this criteria should be subject to further interpretation and analysis under the legal principle of “any accessory right shall follow the main right”, which means in the context of aviation, that the right to hold a registration mark is accessory to the right to hold the legitimate possession of the aircraft for which such registration mark has been obtained from the aviation authority and therefore, should not be a right that survives if the possession of the aircraft by the operator is not legitimate.

In any case, ideally, the repossessing party should be granted by the airline from the beginning of the contractual relationship with sufficient capacity to act on behalf of the airline, without need of any judicial resolution, nor the demonstration of the existence of an event of default, and to produce any necessary documentation requested by the Mexican aviation authority to cancel the registration mark of the repossessed aircraft.

8.- In accordance with Article 36 of the Mexican Customs Law this documentation

Separatory of Assets Claims within a Bankruptcy Procedure.

by Svein Azcué

Over the last few years and during this current world recession, Mexico has seen various companies, including airlines, go bankrupt and most of them have been involved in long and tedious bankruptcy proceedings or *concurso mercantil* (“Concurso”). The whole Concurso proceeding has been explained thoroughly in previous versions of Coelum, but there is a particular matter that hasn’t been addressed specifically and one that is of great importance due to its logical and necessary nature, therefore we will start this edition of Coelum with a simple question: What happens when a company undergoing a bankruptcy proceeding holds assets that are not their property?

The answer to our starting question sounds reasonably simple: if I hold possession of an asset that does not belong to me, then the rightful owner is entitled to claim its return, and I would be obliged to return such asset. Our logic is correct, but when put into practice within a Concurso, the law deems itself far more complicated.

“What happens when a company undergoing a bankruptcy proceeding holds assets that are not their property?”

Under the Bankruptcy Proceedings Law, the separatory claim is the action for separation of assets in possession or under the control of the bankrupt company which are readily identifiable and such asset’s property has not been subject to a legal and irrevocable transfer. Therefore the law provides a procedure in order to recover any such assets that are in possession or control of the bankrupt company. The judge will grant the separation with no further investigation if the separatory claim is not opposed or objected to by the bankrupt company, the conciliator or the creditors’ representatives. If any of the above mentioned parties oppose; it will be resolved as an ancillary proceeding to the Concurso. Hence if the separatory claim goes uncontested, the judge will order for the redelivery of assets to its rightful owner. If objected, the following ancillary proceeding initiates:

- Once the separatory claim is filed and notified, the involved parties will have a 5 working day period to file their response and offer evidence, stating the points to be proven.
- Within the next 10 days after the response period is over, the judge will settle a date for the evidentiary hearing to take place.

- Once the evidentiary hearing takes place, the judge has a 3 day term to issue the interlocutory judgment regarding the separation of assets.¹

Not all assets are subject to separation. Only the assets in the following classes or any other of a similar nature may be separated from the bankruptcy's estate:²

- I. Those who can be repossessed in accordance to law.
- II. Real estate property sold to the bankrupt company but not paid for by it, when the sale agreement was not duly registered with the corresponding public registry.
- III. Real estate property paid for in cash if the bankrupt company wouldn't have paid the total amount of the price by the time of the declaration of bankruptcy.
- IV. Real estate and personal property purchased on credit, if the resolution clause for non-payment was registered with the corresponding public registry.
- V. Securities of any kind issued in favor of the bankrupt company or endorsed in its favor as payment for sales made by a third party, as long as it is proven that the obligations come from those sales.
- VI. Taxes withheld, collected or transported by the bankrupt company on behalf of the tax authorities, and
- VII. Those assets that are in possession of the bankrupt company under any of the following cases:
 - a. Deposit, legal right to use another's property, trust, or received in administration or consignment. If such is the case and the bankruptcy was declared before the buyer expressed his desire to acquire the goods or if the period to do so hasn't expired;
 - b. Commission, sale, transit, delivery or collection;
 - c. To be delivered to a certain person for and on behalf of another party or to fulfill obligations which have to be met at the Company's address; When the result of the referral credit has affected the payment of a bill of exchange, its rightful owner may obtain the separation; or
 - d. The amounts payable to the Company for sales made by third parties. The separatist may also obtain the assignment of the corresponding right to collect a debt.

Regarding the existence and identity of the assets requested to be separated the following characteristics must be taken into consideration:

- I. The separation of property actions will only proceed when the goods are in possession of the Company since the declaration of bankruptcy.

1.- The above mentioned time periods are established within the Bankruptcy Proceeding Law, but these periods are often extended and not always observed by the courts.

2.- Article 71st, of the Law of Bankruptcy Proceedings.

- II. If the goods perish after the declaration of bankruptcy and were insured, the separatist shall be entitled to compensation or to be subrogated in the rights to claim.
- III. If the goods had been transferred before the declaration of bankruptcy, there will be no separation of the price received by them, but if the price hadn't been paid yet, the separatist would separate the amount of his credit and return any exceeding amount. In this case, the separatist cannot be considered as a creditor.
- IV. Goods will be separable if they have been remitted, received in payment or changed for any legal title, if equivalent to those that were separable.
- V. The identification of the goods may be performed even if the assets have been deprived of their packaging, unwrapped or partially sold, and
- VI. If the separated goods have been pledged to third parties in good faith, the pledgee may refuse to redeliver the goods until the secured obligation and its accessories are paid.

“The separation of property actions will only proceed when the goods are in possession of the Company since the declaration of bankruptcy.”

In order to better understand the mentioned scenarios and characteristics, let's for example consider the procedure as if we needed to recover a leased aircraft or airport space such as check in counters, kiosks, slots, etc. (collectively referred to as the “Assets”) from the Mexican airline *Mexicana de Aviación* (“MXA”) which is currently undergoing a *Concurso*. Taking into consideration that both the aircraft and the airports can be repossessed in accordance to law, and that MXA has been in possession of the assets before and since the declaration of bankruptcy, therefore the separatory claim would be admissible. First we would need to ground our right as owner to request for the separation of such assets through a property title and evidence of the company's possession of the assets since the date of actual control. Therefore the judge would have no alternative but to order for the separation and repossession of the assets, but as we mentioned before, the actual execution of such claim is itself more complicated than we might logically expect.

Within MXA's actual *Concurso*, different companies have filed for separatory claims such as *Nacional Financiera (NAFIN)* and various airports such as MEX, GDL, PVR, PZY, SJD, TIJ, MLM. Regardless that the *Concurso* is still within the conciliatory stage, only two of all separatory claims have been resolved so far and the District Civil Court's conclusions have been as follow: Regarding NAFIN's separatory claim, they requested the separation of 9 aircraft, which was granted; and second, for the separation of a real estate lot, which was denied. MXA objected both separation requests stating that the judge had ordered certain precautionary measures in order to avoid any risk to the viability of the Company to restart operations, but the judge

resolved that regardless of the fact that he has the authority to deny the separation claim if such assets are considered essential for the continuance of the Company's operations, there is no evidence that MXA continues or has restarted any operations whatsoever and therefore he granted the separation requested. Regarding the Airports, they have requested the separation of the leased assets to MXA in order to regain possession of this space so as to be able to lease them to someone else. MXA has again objected to this request with the same argument, stating that these are fundamental assets for MXA's operations and therefore the redelivery of such assets back to their rightful owner may constitute an action that would risk the viability of the Company to restart operations hence affecting the bankrupt mass. These airport separatory claims are still to be resolved, but taking the District Judge's prior logic, if MXA restarts operations, the airports may be denied of the separation of assets and even worse, be obliged to continue rendering the airports services and allow the use of the leased goods to MXA under a court order to do so.

“...the separation of assets may only be granted if it goes uncontested...”

Taking the above into consideration we can conclude this article with an interesting hypothesis that the separation of assets may only be granted if it goes uncontested and if the bankrupt company is not currently operating or close to restarting operations. Therefore, what happens when a company undergoing a bankruptcy proceeding holds possession of assets that are not of their property? They may or may not be returned to their rightful owner due to the risk of being considered as assets fundamental to the operation of the company's business or that may affect the bankrupt company's mass hence giving the bankrupt company all the benefits and leaving the creditors with no real legal protection against the defaults or lack of payment of the Company. Taking a second point of view, if the company is ever going to pay back their creditors, this needs to be done by operating the business and creating profit, ironically this would also mean that some creditors would be obliged to render more services and maybe even lose more money to a company that may not survive its own re-launch under the possible pretence of preserving a company that didn't pay their bills.

Bankruptcy – “best road for Mexicana”.

Truth to be told, Mexicana has never had sufficient resources to get out of the crisis they are facing, so the best road to take is for the company to formally declare definitive bankruptcy. Even though Mexicana has always been in serious financial trouble, these problems are now unbearable and it is up to the conciliator, Gerardo Badin, to request the judge to declare Mexicana bankrupt. *Milenio*. 03/March/11.

Nacional Financiera – about to sell nine Mexicana de Aviación aircraft.

Nacional Financiera is about to sell nine A320 aircraft that Mexicana de Aviación gave them as security for a \$789 million pesos loan. These aircraft have a much greater value than the \$780 million pesos, but, Nacional Financiera needs to recover the loan granted to Mexicana. The excess money resulting from the sale will be returned to the company. As the aeronautical industry is slowly recovering, it will now be easier to sell the aircraft. *Excélsior*. 03/March/11.

“Pay to See” – new requirement in Mexicana de Aviación case.

Authorities have requested a warranty of one million dollars from the parties interested in Mexicana’s rescue. This after PC Capital did not have enough resources to rescue Mexicana. This warranty will be returned to the interested parties if they are not the winners. They are also obliged to provide the necessary documentation to show the financial solvency requested. The amount needed as of today is about 230 million dollars, although a new variable in the operation is the fuel prices increase and interest rates. *El Financiero*. 09/March/11.

Wasn’t me!

Due the failure of the rescue of Mexicana Airlines by PC Capital, Mexicana did not paid fees to the company. Given these circumstances, there is no reason to sue for damages, or to take 20 million pesos from the Mexicana to pay fees to PC Capital. The responsibility for not having checked on PC Capital’s solvency is that of Gerardo Badin. *El Universal*. 09/March/11.

Airlines on their way to the Mexican Stock Exchange.

AeroMéxico, Volaris and Interjet are looking forward to listing on the Mexican Stock Exchange in order to obtain increased funding so as to expand operations. AeroMéxico is holding meetings with Banamex, who is their lead underwriter, and Interjet is holding meetings with IXE. This adventure will not be exempt from risk, as investors might punish their stock prices on entering the stock market, because these firms are in a sector that has been in crisis in recent years and have had falling profits. *Excélsior*. 14/March/11.

Texcoco airport remains as an option.

Because Mexico City Airport is at the operational limit, the Federal Government insists on the need to build an alternate airport for the Mexico City Airport in Tizayuca or Texcoco. *El Universal*. 15/March/11.

In this month extract was prepared by Jessi Saba, Vera Garcia and Samantha Garnica.

Mexicana's union wants to sue PC Capital because of the Mexicana case.

Mexicana's union will lodge criminal and civil complaints against those who, including PC Capital, caused the airline's financial crisis. The Union considered that it acted illegally in the bankruptcy (concurso mercantile) process. *El Universal*. 16/March/11.

Representatives will ask for information for Mexicana.

The Monitoring Committee in the House of Representatives considering the case of Mexicana Airlines, will call the Ministry of Communications and Transport, Dionisio Perez Jacome, the Ministry of Labour and Social Welfare, Javier Lozano Alarcón, the conciliator and administrator of Mexicana, Gerardo Badin, and the union leaders, in order to give information related to the process of buying and selling of the airline. The model, is supposed to be very similar to the PC Capital one, including only Airbus aircraft. There is no consideration of a resumption of operations by Mexicana Click and Mexicana Link.

CNN Expansion. 18/March/11.

GAP reviews investment security.

Pacific Airport Group (GAP) is conducting a review of its investment plan for this year, which includes \$420 million pesos (mp) for the implementation of new technology at its twelve airports. The new General Director of GAP plans to implement two innovative schemes, which are expected to be set up this year. The first one is to implement an X-ray security system to replace the manual checking of luggage and the second one is to remove the exclusive zones for airlines so that all the counter monitoring desks are used by any company in order to expedite the documentation process. *El Universal*. 22/March/11.

Mexicana de Aviación loses slots in Cuba and U.S.

From the process which started seven months ago, Mexicana de Aviación has lost Cuban and Los Angeles slots (landing and takeoff times) that they had at those airports. On February 28, the last day for the decision on whether they stay with the slots or not, no resolution was made. *El Financiero* 24/March/11.

Airlines held back by rising jet fuel costs.

The increase in the price of oil has begun to shake the world's airlines and Mexico is no exception as jet fuel rose from 12% of the operating cost structure to almost 40%. The price of jet fuel rose 68.06% over a period of five years. The price at the Mexico City International Airport went from 5.98 pesos to 10.05 pesos per liter. *El Universal*. 28/March/11.

In this month extract was prepared by Jessi Saba, Vera Garcia and Samantha Garnica.

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