

México Business Guide



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The information contained here is of a general nature guide to increase business efficiency. Although our purpose is to provide accurate and updated information, there can be no guarantee that such information is accurate as of the date it is read or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice.
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Introduction

Mexico is divided by 31 States and a Federal District. The States are free and sovereign, divided both administratively and territorially into local governments having their own set of powers. Mexico's principal trading partners include the United States, Canada, Japan, Germany, the United Kingdom and France. Mexico has also signed treaties for the avoidance of double taxation with such countries as the United States, Germany, the Netherlands, Spain, Sweden, Switzerland and South Korea.

I. Business Entities

There are different structures that investor's may use for investment vehicles in Mexico. They range from setting up a corporation or a branch to forming a joint venture or a trust. The General Corporations Law recognizes the existence of six types of entities; however in daily corporate practice in Mexico, the types of companies more used are the: (a) limited liability stock corporation or Sociedad Anónima and (b) the limited liability company or Sociedad de Responsabilidad Limitada. Any of these types of companies may be organized with variable capital which allows the business to alter its capital (the variable portion) with a minimum of formalities.

The Limited Liability Stock Corporation or "Sociedad Anónima"

The Sociedad Anónima or S.A. is the most used and accepted business structure in Mexico. It operates under a company name and ownership is in the form of shares in the capital of the company. Shareholders' liability is limited to making capital contributions to the company for the purchase of shares. The creation of an S.A. requires a minimum of two stockholders and a minimum share capital of not less than Pesos \$50,000.00 The authorized capital must be fully subscribed within one year of the establishment of the company. The management of the corporation is entrusted to a sole administrator or a board of directors.

Limited Liability Company or "Sociedad de Responsabilidad Limitada"

The limited liability company is one formed by members whose obligations are limited to the payment of their contributions to the capital of the company, but in which ownership interests cannot be represented by negotiable certificates, either in registered or bearer form. Such contributions are transferable only in the specific cases provided by the General Corporation Law. After the limited liability stock corporation, the Sociedad de Responsabilidad Limitada or S. de R.L. is the most commonly used business structure in Mexico, and may be considered for United States tax purposes as a partnership. A limited liability company may not have more than 50 members. The capital of the company may never be less than Pesos \$3,000.00 which must be divided into "parts" or "interests" which may be unequal in value and rights but must always represent one peso or a multiple of such amount. To incorporate any of the types of business organizations, the charter and articles of incorporation require formalization by a notary public and thereafter, registration with the Public Registry of Commerce thereby constituting notice to the world of the incorporation.

The Branch of a Foreign Corporation

The General Corporations Law provides that a foreign company has legal existence and is entitled to set up branches in Mexico when it is recorded in the Public Registry of Commerce in the location where it intends to set up the branch. It must obtain the prior authorization of the Ministry of Foreign Affairs and of the Economy. In order to obtain such authorizations, among other requirements, the foreign company must prove that it has been incorporated in accordance with the laws of its country and that its charter and by-laws contain no provisions that are contrary to Mexican law. In order to obtain authorization from the Ministry of Foreign Affairs to open a branch office, it is necessary to file a notice in which the company waives its right to invoke the protection of its government in matters related to the acquisition of ownership of property within Mexico.

Trust or "Fideicomiso"

In accordance with Mexican law, a trust is a contract whereby a person, known as the settler, makes use of certain property for a specific lawful purpose, entrusting the achievement of the purpose to a trustee. The person benefiting from the trust is the beneficiary. Business may be carried out through a trust. In Mexico, only banks and certain other financial institutions may act as trustees. Individuals or legal entities other than such banks or the specified financial institutions are prohibited by law from acting as trustees with the exception of stockbrokers in connection with the investment of trust funds in securities.

II. Currency Exchange

Since 1991, there have been no exchange control regulations. Therefore, there are no controls or limitations on the repatriation of profits or the remittances of funds outside of Mexico.

III. Foreign Investment

Pursuant to the Foreign Investment Law, any Mexican corporation or partnership with foreign shareholders or partners may engage in any business or participate in new fields of economic activity or manufacture new product lines, open and operate establishments and enlarge or relocate already existing establishments, provided the corporation or partnership does not engage in economic activities reserved for the Government or Mexicans, whether individuals or corporations, or is subject to other specific restrictions. The only requirement is that other applicable laws and regulations be observed.

IV. Mergers, Acquisitions and Business Combinations

Mergers

There are two different kinds of mergers provided for in the General Corporations Law: (i) a merger in which simultaneously a new company is created and one or more merging companies lose their separate legal existence, and (ii) a merger in which one or more companies are absorbed into the surviving company. Any merger of Mexican companies must be approved by the shareholders in an extraordinary shareholders meeting of each of the companies involved which must then be notarized and recorded with the Public Registry of Commerce in order to have legal effect.

Acquisitions

Under Mexican law, it is possible to acquire a business by: (i) the purchase of or subscription for shares of stock in a company or (ii) the purchase of the assets of the business.

Business Combinations

The current regulatory framework relating to business combinations in Mexico consists of the following laws: (i) The Federal Antitrust Law; (ii) The Foreign Investment Law; (iii) The General Corporations Law; (iv) NAFTA and other treaties to which Mexico is a party. Prior notice to the Federal Antitrust Commission of combinations, joint ventures, mergers and acquisitions may be required, depending upon the amount involved, in order to comply with the Federal Antitrust Law.

Antitrust / Anti-Competition Law in Mexico

The Federal Antitrust Law is intended to promote free competition and regulates concentrations, as well as absolute and relative monopolistic practices, in a similar way to antitrust law in the United States upon which Mexico's antitrust law is based. The Federal Antitrust Commission may impose fines to concentrations and monopolistic practices as follows: (i) order the suspension, alteration or ending of a concentration or monopolistic practice; (ii) order the reverse, partially or totally of a concentration and (iii) levy fines on those engaging in prohibited activities.

V. Real Estate

Basically any sale of real estate needs to be formalized in writing before a notary public. Furthermore, the notarial deed transferring title to real property requires registration with the Public Registry of Property of the place where the real property is located or the sale will not be effective with respect to third parties. It is important to point out that federal law also provides that the offices of the Public Registry of Property are to be located in the seats of the judicial districts of each Mexican State. There is therefore no single Federal Public Registry of Property, but rather numerous offices around the country where real property and related matters are recorded. In view of the above, before purchasing any real estate property, a search in the Public Registry of Property should be carried out as part of the due diligence review.

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Foreign Investment Considerations

With respect to title to and use and enjoyment of real estate, the Mexican Foreign Investment Law provides for a special legal framework to allow foreign investors to acquire and enjoy real estate in the so-called "Restricted Zone" (100 kilometers along land borders and 50 kilometers along the coastline), as follows:

1.- The acquisition of real estate by Mexican business entities with foreign shareholders:

Outside the Restricted Zone: Real estate may be acquired without any restriction.

Within the Restricted Zone: For residential purposes: title to and enjoyment of real estate may be acquired only through a trust, where the trustee holds direct title but the foreigner has the right to use and enjoy the property. For non-residential purposes: real estate may be directly acquired, provided such acquisition is registered with the Department of Foreign Affairs ("SRE").

2.- Foreign individuals and foreign business entities.

Outside the Restricted Zone: Real estate may be directly acquired, with the SRE's prior authorization.

Within the Restricted Zone: For residential purposes and non-residential purposes: real estate may only be acquired and enjoyed through a trust. The duration of a trust for the purpose set out above is 50 years but may be extended. As can be seen, real estate in the Restricted Zone to be used for industrial and tourist purposes may be held directly by Mexican entities with foreign shareholders without the need for a trust. Existing trusts may be canceled in order for such entities to own real estate directly.

Real Estate Transfer Taxes

In many states, the acquisition of real estate is taxed. The scope of this tax usually encompasses all transfers of real estate and rights thereto. Transfer taxes are borne by the entity that becomes the owner of the property, whether by virtue of purchase, donation, inheritance, in-kind capital contribution, merger, spin off, liquidation, etc. The tax rates range between 2% and 4.8% of the appraised value of the property or the transaction price, whichever is higher.

VI. Tax Issues

Income Tax

Mexican corporations (according to Mexican tax law, other legal structures such as *asociaciones en participación* are also considered as corporations for tax purposes) are under an obligation to pay income tax at the rate of 28% of net profits. Net profits are obtained by deducting from all taxable income earned in the fiscal year, the deductions authorized by law. The law authorizes, among other things, the deduction of the cost of the sale of goods and expenses as well as investments. Should the amount of the authorized deductions exceed the amount of gross income, a tax loss is incurred which may be carried forward up to ten years and set off against profits in those years. Mexican taxpayers are required to file annual tax returns which must be filed within the three months following the closing date of the fiscal year. In Mexico, the fiscal year runs from January 1 to December 31. During the fiscal year, corporations must calculate monthly estimated tax returns which are credited against annual income tax. No provisional payments have to be made during the fiscal year of incorporation.

Value Added Tax

In general terms, value added tax is paid at a rate of 15% by those buying goods, receiving services, having the temporary use of goods, or importing goods or services into Mexico. Value added tax must be passed on to the person who in turn acquires the goods or receives the services until it is finally paid by the ultimate consumer. In the zone along Mexico's land borders, value added tax is payable at a 10% rate.

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Taxation of a Branch or Permanent Establishment

A branch operating in Mexico usually constitutes a permanent establishment in Mexico. In general terms, tax treatment applicable to a permanent establishment is basically the same as for a Mexican corporation and it must comply with various tax requirements arising from its operations in the country, such as filing income tax returns and issuing invoices and meeting tax requirements, among others. Profits obtained by the establishment will be subject to a 28% corporate tax rate. Profit is calculated by deducting from all taxable income earned in the fiscal year attributable to the permanent establishment, the deductions applicable to the operations of the permanent establishment, whether amounts have been paid in Mexico or abroad. Only income earned from business carried out by the permanent establishment is deemed income attributable to the permanent establishment and subject to corporate tax in Mexico. Foreign tax residents having no permanent establishment in the country are under an obligation to pay taxes in Mexico only on income earned from Mexican sources.

Taxation of Dividends

If dividends are paid out of profits on which the company has already paid corporate income tax, such dividends are tax-free in Mexico. For this purpose, companies are entitled to create an “aftertax profits account” or “*Cuenta de Utilidad Fiscal Neta*” (“CUFIN”). Once the applicable corporate tax has been paid, any dividend or profit distribution made from this account is not subject to further taxation regardless of the nationality or residence of the recipient. If corporate income tax has been not paid on the profits used for the dividends, then the corporation must pay a dividend tax, on a gross up basis, and then apply the 28% corporate rate. No tax withholding is applicable regardless of the tax residence or nationality of the recipient.

VII. Intellectual and Industrial Property

Trademarks

Mexican Industrial Property Law (IPL) recognizes the following types of trademarks: (i) nominative (standard character format); (ii) non-nominative; (iii) three-dimensional forms; and (iv) stylized. In order to obtain the registration of a trademark, a written application must be filed with the Mexican Institute of Industrial Property (IMPI). If the application is properly completed, it is examined from both a formal and novelty standpoint to verify whether the trademark is eligible for registration in terms of the applicable Law. IMPI issues a certificate of registration for each accepted application as evidence of having granted a trademark registration. Registration of a mark is valid for 10 years as of the filing date. The owner of a trademark must request a renewal of a trademark registration within the six months prior to its expiration date although without having to demonstrate its continuous and uninterrupted use. However, an affidavit must be filed as well, stating that the use of the name has not been interrupted for a period of more than three years. Registration will lapse when the trademark is not renewed or when it is not used for a period of more than 3 consecutive years, unless there are justified reasons for the lapse in use.

Licensing of Industrial Property Rights

The trademark owner or its recorded licensee is entitled to use a trademark. A license agreement must be recorded with IMPI to protect trademarks against improper use by third parties.

Patents

Among points of particular interest, the IPL introduces the concept of “industrial model” which is defined as “objects, items, apparatuses, or tools which, as a result of a change in formation, configuration, structure or form, have a function or usefulness different from their constituent parts.” Protection of usable models and industrial designs is achieved by registration with IMPI, which grants the right to use a model for 10 years and a design for 15 years from the date of application. Protection will not be extended at the end of such periods. The IPL defines non-patentable items specifically only with respect to “living materials.”

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Copyright

The Federal Copyright Law protects the rights of the copyright owners of any intellectual or artistic work. Once registered in the General Copyright Bureau, a copyright is effective during the copyright owner's life plus 50 years after his death. Editors of intellectual or artistic works, newspapers and magazines and the producers of movies or similar publications may reserve the right to the exclusive use of the original graphic characteristics of such works, provided they are different from the work or collection itself. Computer software may be registered at the General Copyright Bureau and provides full protection for the author.

Franchising

The IPL provides that a franchise exists when a trademark license includes know-how and technical assistance to enable the franchisee to deliver goods and services in a manner consistent and uniform and in accordance with the operating, commercial and administrative methods (policies and procedures) established by the trademark owner (franchisor), all for the purpose of maintaining quality, good will and the image of the products/services. The franchise agreements must be recorded at the Institute for purposes of giving notice of the existence of the franchise to third parties.

Enforcement

The IPL contains broad protection of intellectual property rights and makes enforceability of these rights more efficient. Under the IPL, patents and trademarks are protected for periods of 20 and 10 years, respectively. In addition, protection is given to trade secrets, infringement of which is considered a criminal offense which may result in imprisonment of two to six years. Seizure of goods is now available as a means of immediately stopping an infringement without having to obtain a prior decision from the Institute or an investigation by the public prosecutor. This seizure is carried out by the IMPI.

VIII. Labor issues and Employment

The Federal Labor Law ("FLL") recognizes and protects the basic rights of employees, regulates employer-employee relationships and provides the working conditions for employees.

Employment Relationship

The FLL defines an employment relationship as a subordinated personal service by one individual to another in exchange for payment of compensation and in accordance with an employment agreement. The employment agreement should set forth the conditions under which it is to be performed. The employment agreement must state: (1) the employee's and the employer's name, nationality, gender, civil status and address; (2) whether the employment agreement is executed for a specific job or term, or for an indefinite term; (3) a description of the services to be provided; (4) the place where the work is to be performed; (5) the length of the work day; (6) the wage specifying the day and place of payment; (7) the training program for the employee pursuant to the programs established by the employer as required by the FLL and (8) other terms and conditions of employment, such as days off and vacations agreed upon by the employee and the employer. The employer is responsible for the execution of the agreement; nevertheless, not having a signed agreement does not limit the employee to the rights under the FLL.

Duration of Employment

The FLL assumes, as a general principle, that employment is for an indefinite period of time, unless the nature or the particular type of service to be provided calls for an employment agreement for a specific job or term. An employment agreement for a specific period of time may be made only if the work to be performed so requires it or if the worker is hired to temporarily replace another employee.

Dismissals

There is no concept of employment-at-will in Mexico and an employer may dismiss an employee without liability only if there is a cause for the dismissal, as provided in the FLL.

The Social Security Law and Workers' Housing Fund Law

In addition to the FLL, there are other general laws that regulate employment relationships in Mexico, such as the Social Security Law and National Workers' Housing Fund ("INFONAVIT") Law.

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Collective Bargaining Agreements

Employees and employers may also enter into collective bargaining agreements executed by one or more unions with one or more employers or one or more employer associations. Either party may request an annual review of the wage scale and every 2 years, a review of all other provisions of the collective bargaining agreement.

Right to Strike

The Constitution guarantees the employee the right to strike. The FLL, however, makes strikes relatively undesirable for both management and employees by providing limitations on the right to strike and by prohibiting employers from hiring permanent replacements, from operating during strikes (except for essential safety services), or from locking out employees. A strike must have one of the following objectives: (1) to attain a balance between worker and the employer rights; (2) to pressure the employer to execute or comply with a collective bargaining agreement; (3) to force compliance with the employer's obligation to pay profit sharing to the employees; (4) to claim higher wages; or (5) to support a strike at another business aimed at achieving any of the above-mentioned purposes. The union is required to file with the Conciliation and Arbitration Board a strike notice prior to the planned strike and which the Board must forward to the employer within 24 hours of receipt. The notice should state the union's demands, its intention to strike, and the strike purpose. The strike may not begin until the employer has been given at least 6 days' notice prior to the date of the planned strike (10 days if public utilities are involved). The employer must file a written response within 48 hours of receipt of the notice. The Conciliation and Arbitration Board then holds a hearing to try to seek a settlement. The parties may agree to postpone the strike in an attempt to reach an agreement. Within 72 hours after the strike begins, the employer may request that the Conciliation and Arbitration Board declare the strike illegal. The Board will do so if the strike has an unlawful purpose or lacks majority support. Both parties are given an opportunity to be heard. If the Board determines the strike to be illegal, employees must return to work within 24 hours.

Profit Sharing

Employees (except blue collar workers), whether or not they are Mexicans, are statutorily entitled to a portion of the employer's profits. The rate of profit sharing is determined every 10 years by a National Profit Sharing Commission integrated by workers' representatives, employers and the government. The rate for profit sharing is currently 10% of the employer's taxable income as defined by the Mexican Income Tax Law. It is important to point out that newly incorporated companies are exempt from the profit sharing payment during the first year of operations.

XI. Immigration Law

Compliance with Mexican immigration laws is the starting point for doing business in Mexico, since it is not possible for a non-Mexican to do business of any kind in Mexico without having a work visa. Foreigners may enter Mexico either temporarily to conduct business or to live and work, provided they are in possession of the appropriate work visa authorizing the activities that will be carried out by them while in Mexico. It is also important to bear in mind the substantial discretion that Mexican immigration authorities have with respect to immigration law and regulations. Mexican immigration policy classifies foreign nationalities into three groups: unrestricted, regulated and restricted, with different rules applying to each category. FMT, The Short-Term Non-Immigrant Visa are intended for visitors to Mexico on short term (6 months or less) visits; usually tourists and short-term business trips. For trips of longer than 6 months, a non-immigrant or immigrant visa should be considered. FMT visas are issued by airlines and are also available at ports of entry. FM3, The Long-Term Non-Immigrant Visa is a renewable (every year) long term visa which gives non-immigrant temporary residency status. This means that it gives a person the right to live in Mexico (under the terms set out in the visa) but it does not lead to, and cannot be converted to, a visa leading to permanent residency. FM2, The Immigrant Visa is intended for people seeking permanent residency status in Mexico or those seeking Mexican Citizenship. There are various categories under which FM2 visas are granted, and these relate to the activities you intend to undertake while in Mexico. Under the terms of the FM2, you are authorized to only undertake certain, specific activities which may be lucrative or non-lucrative.

X. Security Interests

The types of security interests that may exist in property under Mexican law are:

Pledge

A pledge agreement provides a personal property right to secure (a) the payment of an obligation as well as (b) the preferential right to such payment. In case of a breach by the debtor of the obligations secured by the pledge, the creditor may sell, following the proceedings established by law, the pledged assets and apply the proceeds to the payment of the secured obligations.

Mortgage

A mortgage is generally established over real estate but can also be granted over personal property attached to real property and over corporations' assets.

Surety Bond

A surety bond is an agreement by which a guarantor agrees to pay the obligations of a debtor in the event the debtor does not do so.

Guarantee Trust

This type of trust is a contract whereby a settlor transfers to a trustee the ownership of certain property in order to secure compliance with an obligation owing to the creditor or beneficiary. In Mexico, only banks and certain other financial institutions may act as trustees.

Equipment or Operating Loan

By virtue of this kind of contract, the debtor is obligated to use the exact amount of the loan for the acquisition of raw materials and equipment as well as for the payment of salaries and direct expenses of operations needed for the corporation. This type of loan is secured by the raw materials or equipment purchased with the loan proceeds or the manufactured goods.

Financing Loan

There are multiple uses for this type of loan. These loans are secured, simultaneously and separately, with the assets and the products and proceeds, whether future, pending or already obtained, of the business for which the loan was obtained.

Creating and Perfecting Security Interests

A security interest is perfected when all of the applicable steps required by law have been taken, generally, when the security agreement is signed. Registration in the appropriate Public Registry of Commerce and/or Property is required in order to ensure and preserve the priority of the interest being granted.

XI. Environmental Law

Mexican regulations applicable to environmental protection represent a complex system that may be difficult to comply with and may give rise to the imposition of penalties on individuals or companies for failure to comply. The Department of Environment and Natural Resources ("SEMARNAT") is principally responsible for environmental protection in Mexico. There are two agencies of SEMARNAT having environmental responsibility, the Environmental Regulations and Promotion Office, in broad terms having responsibility for permitting, and the Federal Environmental Enforcement Agency ("PROFEPA,"), as the name implies, having responsibility for enforcement. There are a number of permits, approvals and reports, federal or state, concerning environmental matters which must be obtained to operate an industrial plant in Mexico and/or filed during the course of such operations. PROFEPA's main activity is to deal with complaints, conduct inspections and, in general, verify compliance with all federal environmental laws and regulations. It also imposes penalties for violations of environmental laws and regulations and monitors compliance with any preventive and mitigating measures issued by it. PROFEPA also conducts environmental audits. With respect to industrial facilities currently in operation, the conduct of periodic environmental audits, both of a legal and technical nature is highly recommended in order to avoid potential penalties resulting from inspections by PROFEPA and/or state and local environmental authorities.

XII. Foreign Trade

The Foreign Trade Law deals with tariff and non-tariff regulations and restrictions (such as quotas, import permits and Mexican Official Standards or NOM's) as well as rules on unfair foreign trade practices (antidumping) and the administrative process held in accordance with internationally accepted practices and mechanisms. These regulations vary depending on the specific imported product and the country of origin, for this reason, it is imperative to review requirements before deciding to initiate the import/export operations of a company in our country.

The North American Free Trade Agreement

NAFTA provides a free trade zone that includes Canada, the United States and Mexico. The objectives of NAFTA consist generally of eliminating tariffs, obstacles to foreign trade and facilitating the circulation of goods and services between the three signatory countries; promoting competitive conditions as well as capital investment; adequately protecting intellectual property rights; creating efficient procedures for the resolution of commercial disputes between the parties, as well as between their nationals; and establishing policies for trilateral and multilateral regional cooperation as well as seeking to broaden the benefits and scope of NAFTA. With respect to tariff elimination, the three countries accepted diverse "speed of tariff phase outs" concerning goods entering their markets and originating in the NAFTA region. As of today, almost every single product that qualifies as having NAFTA origin is now free from the payment of customs duties. The provision of rules allowing importers to certify goods originating in the free trade zone is considered another beneficial aspect of NAFTA due to the application of the preferential treatment granted by Mexico as a NAFTA country.

The IMMEX Program

A decree issued in late 2006 has streamlined and expanded the two separate programs Mexico had maintained to promote manufacture-for-export operations by foreign-invested and domestic companies. The Nov. 1 Decree of the Manufacture, Maquiladora and Services for Exportation Industry (IMMEX) unifies the operation of the maquiladora and PITEX programs and centralizes control over those programs by Mexican authorities. The maquiladora program was established to encourage foreign investment in Mexico by allowing manufacturers to import materials, machinery and equipment free of duties and value-added taxes as long as the finished products were exported. The PITEX program expanded many of the benefits of the maquiladora program to domestic manufacturers. The publication of the IMMEX decree has combined these two initiatives into one program that will continue to focus on promoting Mexican exports while simplifying government controls and participation requirements. There are five categories of companies that can qualify for IMMEX participation: (1) industrial or manufacturing companies that produce goods for exportation (in which case exports must account for at least 10 percent of the company's annual sales or \$500,000, down from the previous threshold of 30 percent); (2) companies that provide services with respect to goods to be exported; (3) shelters, or a foreign company or companies that provide technology and materials to Mexican companies that do the actual manufacturing; (4) holdings, where one IMMEX-certified company is incorporated within the manufacturing operations of a holding company or one or more subsidiaries; and (5) trusted companies that have outsourced their manufacturing operations to a third party in Mexico because they do not have facilities of their own.

Highlights of the IMMEX program are as follows.

- The duty-free benefits of the maquiladora and PITEX programs remain in place.
- IMMEX authorization is only available to corporations and can no longer be obtained by individuals.
- All IMMEX-certified companies are exempt from paying income taxes as long as they comply with Mexico's transfer pricing legislation (e.g., they provide documentation showing that transactions between themselves and the foreign company with which they are involved were at arm's length) and there is a double taxation treaty between Mexico and the home country of the foreign company. However, it is expected that Article 2 of Mexico's Income Tax Law will have to be amended to clarify that this exemption is available for all IMMEX-certified companies, not just maquiladoras.

- When requesting an IMMEX authorization, corporations no longer have to provide either the HTS classification or a description for goods such as subassemblies, intermediate goods, materials consumed in the manufacture of the exported goods, etc.

PROSEC Program

PROSECs are instruments aimed at corporations that manufacture certain goods that allow them to import under preferential ad-valorem tariff (General Tariff on Imports) several items in order to be used for the manufacture of specific products regardless the final destination of these goods, whether for domestic or foreign markets. PROSEC beneficiaries are those organizations which manufacture goods detailed within "Section 4 of the Decree", using the mentioned goods. Companies which manufacture goods detailed in the PROSEC Decree will be allowed to import under preferential ad-valorem tariff several items in order to be employed in the manufacture process of the already mentioned goods.

Special Importation Requirements

In addition to the foregoing, with respect to some types of goods intended to be imported or exported, the importer must be registered as such with the Treasury Department not only on a general importers register but also on the register applicable to the particular product being imported. This additional registration is commonly required for sensitive products that may affect the Mexican market and production. Finally it is important to mention that, depending in the tariff item classification of the imported product, the importer must comply with the specific tariff (duties) and non-tariff regulations (import permits, Mexican Official Standards, etc.) mentioned before.

XIII. Telecommunications Law

Telecommunications in Mexico has changed to allow limited private or foreign investment. This increase in private investment has both driven and reflected rapid growth in the sector. The Foreign Investment Law restricts foreign investment in telecommunications to 49% of the capital of Mexican companies operating in the telecommunications sector. Activities to which this restriction applies are the use of radio / electromagnetic spectrum in Mexico, the installation and operation of public telecommunications networks, the occupation of positions in space by satellites, and the emission and reception of signals from foreign satellites. The restriction on foreign investment does not apply to cellular telephone operations. Foreign investors may invest in the capital of Mexican companies engaged in the restricted businesses referred to above provided they do so as minority shareholders or hold shares with limited voting rights, and in either case, agree to consider themselves as Mexican nationals with respect to their interest in the company and not to invoke the protection of their own government in the event of a dispute, under penalty of forfeiting their interest to the state for violation of the agreement. The Federal Telecommunications Law is the governing law in Mexico that regulates the use of the radio-electric band, telecommunications networks, and satellite communications. Subject to the restrictions mentioned above, any individual or company may obtain a concession to provide among others: (i) public local and long distance telephone service; (ii) data transmission; and (iii) restricted television.

XIV. Energy and Natural Resources

According to the Mexican Constitution, the state has direct ownership of the subsoil and thus ownership of natural resources belongs to the state and may not be transferred to private individuals or entities. The state has the exclusive right to exploit and develop oil and gas and may not grant oil exploration and exploitation rights to private entities or individuals. In addition, the generation, transmission, distribution and supply of electricity for public consumption are also reserved for the state. Currently there are discussions in Congress to allow private entities to do exploration and transportation of oil.

Mining

The mining industry in Mexico is under exclusive federal jurisdiction and while, as mentioned above, the state has direct ownership over mineral resources, Mexican individuals and companies may obtain concessions for their exploration and exploitation, granted by the Department of Economy.

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Electricity

As provided in the Constitution, the federal government exclusively carries out the generation, transmission, distribution and marketing of electricity that is supplied for public consumption. However, cogeneration; self-supply; independent power production; small power production; power for exportation; and importation of power are not considered as “public consumption” and, therefore, are open to the private sector with no foreign investment restrictions. Public, local and municipal institutions are also allowed to generate electricity for use in public lighting, pumping water, and other public services. The Energy Regulatory Commission (“ERC”) is the agency responsible for regulating the energy industry in general and specifically for granting permits as well as supervising compliance with permit terms.

Oil and Gas

As previously mentioned, the state has direct ownership of the subsoil, as well as the exclusive right to exploit and develop petroleum, including natural gas. As a result, the state may not grant oil exploration and exploitation rights to either private entities or individuals. The agency used by the federal government to exercise its rights in this area is the state oil company, Petroleos Mexicanos (“Pemex”). Pemex may carry out those activities within its responsibility directly or by hiring third parties. With respect to the construction of pipelines for transportation of petroleum and petroleum byproducts as well as oil and gas drilling, approval from the Foreign Investment Commission is required in order for a company having foreign investment exceeding 49% of its capital to carry out the same. The retail sale of gasoline is exclusively reserved for Mexicans and Mexican corporations that exclude foreign shareholders.

Natural Gas

While natural gas production is exclusively reserved for the state, private investment, including foreign, is allowed in the transportation, storage, distribution and marketing of natural gas in Mexico, subject to obtaining a permit from the ERC.

Liquefied Petroleum Gas

Private investment is allowed in the storage, transportation and distribution of liquefied petroleum gas, subject to obtaining a permit. Permits for transportation and distribution by pipeline are granted by the ERC, while permits for transportation and distribution not by pipeline are granted by the Department of Energy. Transportation and distribution of liquefied petroleum gas, however, is exclusively reserved for Mexicans and Mexican corporations that exclude foreign shareholders.

XV. Reorganization-Bankruptcy Proceedings

Reorganization and bankruptcy have become interesting subjects in Mexico as a consequence of the economic and commercial changes that the country has passed through in the last five years. In order to adapt the reorganization and bankruptcy legal framework to deal with the economic problems faced by businesses, on May 12, 2000, the Commercial Bankruptcy and Insolvency Law (“CBIL”) was published on the Federal Official Gazette. The CBIL only applies to businesses. According to CBIL, there are two successive stages or phases in insolvency proceedings: (i) reorganization or conciliation and (ii) bankruptcy. The reorganization stage is aimed at the preservation of the company or of the business (the “Debtor”) through the execution of a reorganization agreement between the Debtor and its creditors. The bankruptcy proceeding is aimed at selling the assets of the Debtor in order to pay its creditors.

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Reorganization Phase

A Debtor which is insolvent and does not comply with its payment obligations, may be declared to be insolvent and thus in the reorganization phase of the proceedings, at the request of the Debtor, its creditors, or the public prosecutor. The CBIL considers that general non-compliance with payment obligations occurs when the Debtor: i) has debts past due for 30 days, representing 35% or more of the total of the Debtor's obligations on the date the petition for the declaration of insolvency is filed and ii) the Debtor does not have assets to meet at least 80% of its past due obligations. The reorganization stage (as well as any subsequent bankruptcy) is dealt with by a District Court judge of the domicile of the Debtor. Once an application for a declaration of insolvency is made, the Federal Institute of Insolvency Experts (the "FIIP") must then appoint an examiner that will determine whether the Debtor is actually insolvent and then submit a report to the Court that will then decide whether to issue a declaration of insolvency. Once such a declaration is issued, the FIIP then appoints a conciliator, whose principal task is to seek an agreement between the Debtor and its creditors. The reorganization stage is supposed to take no more than 185 calendar days to be concluded, calculated from the date of the last publication in the Federal Official Gazette of the declaration of insolvency. The reorganization stage may be extended up to two consecutive times, for ninety calendar days each, on the understanding that this stage and its extensions may never exceed one year.

Effects of the Insolvency Declaration

The most important effects of the insolvency declaration are: (i) the suspension of creditor debt enforcement proceedings during the reorganization stage; (ii) the separation of third party property from that of the Debtor; (iii) the maintenance of the management of the business by the Debtor (however the conciliator may request the removal of the Debtor and appointment of a receiver in order to protect the assets of the Debtor; (iv) the creation of a special regime for the treatment of the Debtor's obligations; (v) the requirement that creditors prove amounts owing to them; and (vi) the dealing with fraud to the detriment of the Debtor's creditors.

Reorganization Agreement

The reorganization agreement must contain a schedule of payments of the amounts owing to proven creditors and must be signed by all proven creditors, except for tax and employment creditors, representing more than 50% of: (i) the amount of all general creditors and (ii) the amount of all secured creditors. The reorganization proceeding are terminated when the Court approves the reorganization agreement filed by the conciliator.

Bankruptcy

A Debtor is considered bankrupt, when: (i) the Debtor so requests it; ii) the reorganization period and any extensions have elapsed without the approval of a reorganization agreement by the Court; or (iii) the conciliator requests a bankruptcy declaration and the Court grants it.

Bankruptcy Declaration

The decision containing the bankruptcy declaration, among others: (i) suspends the legal capacity of the bankrupt to exercise its rights over its property; (ii) requires the Debtor and those who have in their possession property of the bankrupt, to deliver to the trustee in bankruptcy, such possession and the administration of the estate in bankruptcy; (iii) prohibits the Debtor from making payments or delivering its assets to others; and (iv) orders the FIIP to appoint the conciliator as trustee.

Effects of Bankruptcy Declaration

The main effect of the bankruptcy declaration is to transfer the administration of the property of the Debtor from it to the trustee, the latter having the same powers and obligations as the conciliator had. Once bankruptcy is declared, the trustee sells the property of the Debtor, trying to obtain the best price for it.

Payment to Proven Creditors and Conclusion of the Proceedings

Payment to creditors are to be made in the following priority: (i) creditors holding a special privilege (funeral expenses of a deceased Debtor); (ii) creditors holding a pledge or mortgage; (iii) creditors holding a special privilege (as defined in the CBIL); and (iv) general creditors (without security or privilege). The proceedings conclude when: i) the reorganization agreement made between the Debtor and its creditors is approved by the Court; ii) total payment is made to proven creditors; (iii) while payment is made to proven creditors, no other assets are left to be transferred and the estate of the bankruptcy is not enough to make a total payment of proven indebtedness; or (iv) if the Debtor and all proven creditors so request.

XVI. Legal Protection for Foreign Investors

Mexico's Federal Constitution makes no distinction between foreigners and nationals with respect to the protection of individual rights set out in it, any individual or company is entitled to enjoy such guaranties, regardless of nationality or place of incorporation, in the case of a company. One of the guaranties established in the Constitution is that no one can be deprived of life, freedom, property, possessions or rights without due process of law. Such due process must be carried out before courts of competent jurisdiction and pursuant to applicable law. The Commercial Code ("CC") is a federal statute that generally regulates commercial transactions and provides that, provided the subject matter is lawful, the parties to a contract may freely agree upon the terms and conditions of their choice. The CC also provides that the provisions of the Federal Civil Code apply to all commercial transactions when the CC and other commercial laws are silent on a particular issue. The parties to a contract are also free to agree upon the court or courts having jurisdiction in the event of a dispute under their agreement. They may also agree to submit to arbitration. Notwithstanding the latter, there are certain basic situations over which Mexican courts will always have exclusive jurisdiction, including: (i) land and waters located within Mexican territory, including sub-surface, air space, territorial seas and continental platforms (rights *in rem*, rights arising from concessions to use, explore or exploit the same or leases thereon); (ii) natural resources located in Mexico's exclusive economic zone; and (iii) actions of an internal nature by Mexican authorities, acting as such, and those of Mexican embassies and consulates abroad. The decision to submit to foreign jurisdiction must also be "reasonable" and such choice should be made based on practical considerations, such as the address of the parties, the location of assets and applicable law, etc.

Arbitration

Practically any private dispute may be arbitrated in Mexico and, consistent with the foregoing, Mexican legislation has produced its own domestic rules, as well as adopted rules of an international nature. The codes of civil procedures for each of the states, as well as the CC, contain provisions on arbitration as a means of settlement as do other laws with respect to banking, insurance, bonding and consumer protection. Some of the relevant provisions are: (i) proceedings may be conducted in Spanish or in a foreign language and take place in the location chosen by the parties; (ii) the procedural rules may also be freely determined by the parties, including the applicability of those issued by an institution engaged in the resolution of disputes, such as the International Chamber of Commerce and the American Arbitration Association; and (iii) the parties are also entitled to decide the applicable substantive law and if they do not address this question, the arbitrators must do so, considering the circumstances of the parties and their legal relationship.

Additionally, it is important to mention that arbitration awards are recognized in Mexico, regardless of the country in which they are issued and will be enforced in Mexico by Mexican courts unless: (i) one of the parties did not have the legal capacity to submit to arbitration; (ii) the agreement to arbitrate was not valid; (iii) an interested party was not properly notified of the arbitration or of the appointment of the arbitrators or was otherwise not able to present its case; (iv) the appointment of arbitrators or other proceedings did not follow the rules approved by the parties or in the absence of rules, the arbitration was not conducted in accordance with the applicable law of the jurisdiction in which the arbitration took place; (v) the award refers to matters different from those contemplated in the arbitration agreement; (vi) the award is not yet obligatory or has been annulled or suspended by a court in the country where the arbitration took place; or (vii) the Mexican court decides that the subject matter of the arbitration may not be arbitrated pursuant to Mexican law or its enforcement would violate public policy.

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[The Mexican Court System](#)

The Mexican federal judicial system consists of the Federal Supreme Court of Justice, the Federal Elections Tribunal, the Collegiate Circuit Courts, the Unitary Circuit Courts and the District Courts. As required by the Constitution, there are 11 Federal Supreme Court Justices, who hold office for a maximum period of 15 years. The Chief Justice is elected by the other justices every four years.