MILLER CANFIELD

DOING BUSINESS IN NORTH AMERICA

VOLUME TWO: **Mexico**

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The information in this booklet provides an overview of the fundamental legal considerations to be addressed when acquiring or establishing a business in Mexico.

The content is intended to summarize some of the pertinent provisions which apply and is not intended as specific legal advice. Readers are well advised to seek the counsel of specialist professionals in Mexico to advise on compliance with the laws and identify the many planning opportunities.

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Table of Contents

1. Overview

Introduction

Unlike the U.S., Mexico has a civil legal system, in which the vast majority of its laws are codified. The legal system is based on Roman law and similar to European legal systems. Although many practices and legal concepts are similar to the U.S., foreigners doing business in Mexico need to be aware of some significant differences. Most of the laws that govern business and commerce are set forth in the Commercial Code and the Civil Code, and are national in scope. Certain local differences may apply in some areas of the law, but, in general, Mexican laws apply across the entire country.

Similar to the U.S., Mexico's governmental framework has an executive, a legislative and a judicial branch of government. It is also a federal system, with the federal government and the various states responsible for different aspects of public and private life. However, because of its unique history, Mexico's federal government is much more centralized and controls and regulates more legal and economic activity than in the U.S. In addition, state and municipal authorities must complete certain legal formalities.

Legal practices are quite formalistic. For example, the form of contracts can be quite important. Certain types of documents must be prepared by a Mexican notary and executed in person, and then formally filed with public registries. Notary publics are licensed attorneys and appointed officials that serve an important function in Mexico than notaries in the U.S., have stringent legal requirements with which they must comply, and in certain cases must be used in order to effectuate documents or transactions. Many forms and permits must be filed with various agencies in Mexico City, which can sometime lead to delays. The parties and persons executing a legal document must have a valid power of attorney to do so, and this can also be a cause for delay. Foreign business people doing business in Mexico for the first time are often unprepared for the level of formality required both in normal commercial affairs and in dealing with government agencies. An understanding of this aspect of doing business in Mexico will help in planning business activities there.

The central government and its agencies are empowered with enforcing laws. Compared to the U.S., lawsuits are relatively rare, slow and expensive. With very few exceptions, there are no juries in Mexico for either criminal or civil cases. Judges are both fact-finders and decision makers in a legal dispute, and the American tradition of public trials applies rarely and under different rules in Mexico. The new National Criminal Procedure Law, which provides for public trials in addition to other similarities to the U.S. procedural criminal system, is in the process of enforcement and is expected to be fully enforceable by June 18, 2016, repealing all of the state criminal procedural laws currently enforced.

Although considered historically stable when it comes to legal framework, Mexico is in the process of "rebooting" many of its laws and legal structures and restructuring key industries within the country. In addition to the aforementioned changes to the criminal system, major recent reforms include the labor reform approved in 2012 and the following reforms that stem from the 2013-2018 National Development Plan (encompassing amendments to current laws or the constitution, repeals and new bills):

- Tax Reform
- Energy Reform
- Financial Reform
- Telecommunications Reform
- Education Reform
- Antitrust Reform

2. Types of Businesses and Operations

a. Overview

When conducting business in Mexico, foreigners should bear in mind that business entities are formed in accordance with the General Law of Commercial Enterprises, which is national in scope. The choice of the type of legal structure depends on many factors discussed below. Legal and financial advisors should be consulted in making this decision. Some key issues to consider in arriving at an appropriate arrangement include:

- Limited liability protection and risk management
- Funding and financing
- Public image
- Income and other taxes
- Repatriation of profits and capital

b. Forms of Entity

The two most common forms of entities in Mexico are:

1. *Sociedad anónima* (S.A.) or *Sociedad anónima de capital variable* (S.A. de C.V.): stock corporations with either fixed or variable capital

2. *Sociedad de Responsabilidad Limitada* (S. de R.L.) or *Sociedad de Responsabilidad Limitada de capital variable* (S. de R.L. de C.V.): limited liability company

Other forms of business entities include: *Sociedad en Nombre Colectivo* (general partnership), *Sociedad en Comandita Simple* (partnership with limited and unlimited liability partners), *Sociedad civil* (civil partnership, for professional practitioners), *Asociación en participación* (joint venture contract), *Sucursal de sociedad extranjera* (branch of a foreign corporation), *Comerciante - Empresa de persona física* (sole proprietorship), and *Asociación civil* (civil association, for charitable and other nonprofit corporations).

Foreign companies and individuals may own any portion or all of the equity of a Mexican company, with the exception of companies engaged in activities or acquisitions reserved or subject to specific regulation, such as banks, credit unions, oil and gas, electricity, postal services, and other governmental functions.

c. *Sociedad anónima*

The legal amount of capital for a S.A. (stock corporation) is fixed by the charter documents of the entity and any changes to the fixed capital require amendments to the charter documents and filings with the government, which is a relatively involved process. If there is a variable capital component, the capital can be changed without the requirement of formally amending the articles, which simplifies the process of issuing more equity. For this reason, a variable form of a stock corporation (S.A. de C.V.) is favored. Shares represent ownership interests. Shares have equal rights unless the charter documents authorize the issuance of different classes of shares.

Each S.A. must have at least two shareholders, which may be individuals or other companies, and may have an unlimited number of shareholders. The liability of shareholders for the debts and obligations of the corporation is limited to the amount of their equity investment. Under Mexican law, all shareholders must have the right to participate in receiving profits and the right to vote on amendments to the charter documents.

Every S.A. is managed by either a sole administrator or a board of directors, elected by the shareholders. Shareholders must have at least one general meeting on an annual basis within 4 months of the end of the year. Each share may have only one vote.

Each S.A. must set aside 5 percent of its annual net profits in a statutory reserve until its balance equals 20 percent of the capital stock.

Foreigners may serve as board members; however, foreigners must have the appropriate immigration status to represent the corporation in Mexico. In performing their duties, members of the Mexican company's board of directors have similar duties and liabilities as in an American company. Board members must act within the limits of their authority and can be held personally liable for exceeding their authority unless the shareholders subsequently ratify such actions. They can be held jointly and severally liable if they were aware of illegal or irregular acts of the corporation and failed to report these to the company's auditor. This joint and several liability can extend to illegal acts taken by other board members or the board as a whole, but there is no such liability for a board member who objected to the illegal conduct. Directors also have a duty to avoid conflicts of interest.

Each S.A. is also overseen by one or more statutory auditors (*Comisario*) whose appointment is revocable. The statutory auditor may, but need not be, a shareholder of the corporation; certain limitations apply regarding who may serve as statutory auditor. The oversight includes all aspects of the corporation's governance.

d. *Sociedad de Responsabilidad Limitada*

The S. de R.L. is often compared to an American limited liability company. Similar to the S.A., the S. de R.L. may also have a variable capital component, in which case it is designated an

"S. de R.L. de C.V."

The S. de R.L. must have at least two and at most fifty partners who may be individuals or other entities. Like corporations, liability of the partners for debts and obligations of the company is limited to the amount of capital they have subscribed. A change in the fixed capital requires similar procedures as for a corporation, while a change in the variable capital is accomplished via partners' resolutions. Ownership interests are called "equity participations" or "equity interests" and represent a percentage of the capital; they are not certificated and are not transferable except as permitted by law. Current partners have a right-of-first-refusal over any new equity participations to be issued to third parties. The company keeps a register of capital accounts.

Partners are the highest authority in an S. de R.L. and the company is governed according to a partnership agreement, similar to an operating agreement for an American limited liability company. There is no requirement that the company have a centralized management, although it may have a board of managers if the partners so determine. Annual meetings are required, as for corporations. Importantly, an S. de R.L. is generally considered a "check the box" entity for American tax purposes.

e. Tax Liability on Partners and Shareholders

One of the changes introduced by the Tax Reform is a new tax liability over partners and shareholders. For both an S.A. and an S. de R.L., partners or shareholders shall be jointly liable for tax liabilities caused in connection with the activities of the company when the partner or shareholder, as such, had "effective control" of the company. Such liabilities will only be triggered when the assets of the company are not enough to cover such contributions and shall be limited to the percentage of interest owned when the tax liability was caused. The aforementioned will only apply when either of the following applies:

i. Lack of registration in the Federal Taxpayers' Registry,
ii. Change of address or vacating the facility without providing adequate notice to the government, or
iii. Lack of bookkeeping, or hiding or destroying the books.

"Effective control," referred to above, means the ability to carry out any of the following acts:

i. Impose decisions at general meetings of members, shareholders or partners or appoint or remove a majority of the directors, managers or their equivalent.
ii. Maintain more than 50 percent voting ownership rights.
iii. Direct the management, strategy and major policies of an entity, whether through ownership of securities, by contract or otherwise.

f. Dividends

At least five percent of the company's profits must be set aside annually until the amount so retained reaches 20 percent of the value of the outstanding capital stock. Additional matters regarding taxes on dividends are provided for below.

g. Others

1. Joint Venture

The joint venture is an agreement by which one or more partners provide goods or services to their counterpart, managing partner, in exchange for the right to participate in the earnings of a commercial operation under the control of the latter. The joint venture is not a separate legal entity, per se, under Mexican law, but rather the purpose of the parties coming together. Joint ventures may be materialized into an entity, such as an. S.A., S. de R.L. or other legal structure, or may be solely in the form of a contract, such as an *Asociación en Participación*. The managing joint venturer has liability to third parties, while the silent partner has no liability.

2. Branch Office

A foreign corporation may register as a branch office in Mexico by complying with certain formalization and public registry requirements and obtaining approval of the Ministries of Foreign Affairs and Economy.

3. SAPI

A SAPI or *Sociedad Anónima Promotora de Inversión*, is a limited liability corporation that is very flexible in structure. It is a non-listed company, which, if compliant with the requirements established by the Mexican Stock Exchange Law, can be a formal and more trusted target for equity coming from sources independent to its founders and or controlling groups. It is a Mexican vehicle for attracting private equity investments.

4. *Maquiladora/IMMEX*

A *Maquiladora* is simply a Mexican corporation or company which operates under an IMMEX program approved for it by the Ministry of Economy (SE). See further details below.

3. Establishing a Business

a. Incorporation

After selecting the form of entity, the process of forming the company begins. Depending on the type of entity and the owners, it can take up to four to six weeks to form a new company.

The first step to begin with the incorporation process is the entity's name request and approval. The request is made to the SE. Once the name is approved and reserved, the company's charter documents must be drafted. As in the U.S., if the new company is a wholly owned subsidiary, the charter document is typically quite simple and formulaic. If the company's owners are two unrelated parties, the negotiations of what is included can take time. The charter document is the equivalent of a combined articles of incorporation and bylaws in the U.S. It must include the amount of share capital, both fixed and variable (if variable capital is included), how much capital must be paid in at the time of formation, the list of shareholders, the company's purpose (which must be specific and detailed), any limitations on transfers of shares, the names of the board of directors or managers, and whether meetings may be held by written consent, granting necessary powers of attorney to the legal representatives of the company, etc.

Once drafted, the charter documents must be formalized before a Mexican notary, which requires a personal appearance by the owners to sign the necessary documents and will add time to the formation process. Nevertheless, personal appearance may be replaced with a proxy holding the necessary documentation.

Once the deed is notarized, the charter is registered in the commercial registry of the state where the company is located. The corporate existence is deemed to begin as of the date of the notarized deed of formation.

If the company has foreign shareholders, it must also register with the Foreign Investment Registry within 40 business days from the date of formation; annual renewals and any subsequent changes to the charter documents must also be notified to the Foreign Investment Registry.

Depending on the industry in which the company operates, it may be required to file with a branch specific registry, e.g. the Register of Technological Industries. We advise consulting legal counsel prior to organizing a company in order to ensure that all necessary formalities are properly observed.

b. Taxes and Related Matters

After formation, the company must apply for its RFC (tax ID number) with the Finance Ministry, which will also issue other required electronic IDs (FIEL and CIEC). No business should be conducted until all authorizations are obtained and the company is duly authorized and registered. All companies operating in Mexico pay Value Added Tax (VAT, known by its Spanish acronym "*IVA*") at 16 percent on goods sold in Mexico. Proper administration of VAT records and payments is important. Companies also need to obtain their formal *facturas*, which is a receipt that includes the tax ID number, the VAT amount, the official company name, etc. The *factura* lists expenses that are tax deductible and subject to VAT. There are several requirements regulating how the *facturas* are to be printed – only certain paper is allowed, only certain print shops may print them, the numbering must be consecutive and printed on a prescribed form, etc. Bear in mind that it is not unusual among smaller Mexican companies or sole proprietorships to ask for a receipt (*recibo)* instead of a *factura*, if acceptable; this will remove the transaction from the tax rolls but may be illegal.

c. Bank Accounts, Permits and Other Filings

Once the RFC and other electronic ID numbers have been obtained, the company can proceed to open a bank account (a sometimes lengthy process), enter into contracts with utility companies and property owners, and complete the rest of the administrative requirements for operating a business. Before it can hire employees, once it has received its RFC number, the company must also apply for all necessary permits and make all necessary filings with the various social security agencies for employees (discussed below).

Foreign companies may lease properties and purchase real estate directly, except in a restricted area along the coast and borders. If a foreign company wishes to purchase real estate in the restricted area, a form of Mexican trust is generally used for this purpose. This process is relatively cumbersome and the assistance of effective legal counsel is very important.

d. Coming Soon: www.gob.mx

In September 2014, the Mexican government published the website www.gob.mx with the purpose of digitally integrating online filings and procedures (originally www.tuempresa.gob.mx). Although the website is expected to digitize around 6,000 federal processes, it is expected to begin offering digitalized and simplified versions of the incorporation processes soon. The website is currently only advertised as beta version but is expected to be fully up and running by 2015.

4. IMMEX and Shelter Operations

a. Maquila/IMMEX Companies

Maquila operations date back to the 1950s and have gradually changed over the years with the advent of NAFTA and the opening of the Mexican market. The Mexican government changed the program in 2006 to combine it with a similar one that applied only within Mexico— the current program is commonly referred to as IMMEX for its Spanish acronym of *Decreto para el Fomento de la Industria Manufacturera, Maquiladora y de Servicios de Exportación*. In its simplest form, a Maquila (or IMMEX) operation is a Mexican subsidiary wholly-owned by a foreign parent for the purposes of contract manufacturing in Mexico. The program allows companies to import equipment, machinery, raw materials and semi-finished goods into Mexico duty-free, perform value-added operations on them, and export the goods back abroad and, if desired, sell a percentage of the goods in Mexico. The equipment and machinery may be held in Mexico on a bailment basis while the Maquila/IMMEX program is in effect, after which it has to be re-exported or sold for its then-current value. Although such operation were initially restricted to only border areas, IMMEX operations can now be conducted and established anywhere in Mexico. The relationship between the foreign parent and the Mexican subsidiary is memorialized in a “*Maquila* agreement”, which must be filed with the government as part of the approval process. An IMMEX company may further sub-contract parts of its operation to other IMMEX companies in Mexico, which helps broaden its manufacturing base. The IMMEX application is filed with and approved by the SE, and many of the formalities of forming the Mexican IMMEX company that will contract manufacture are similar to formation of any other enterprise (see above).

The IMMEX application process is somewhat bureaucratic and, while not difficult, the application must be prepared properly to avoid delays. A great deal of operational data is required (e.g., list of goods to be imported, materials used, length of time equipment will be used, copies of purchase orders, etc.) as well as the formation documents of the Mexican entity, the intercompany *Maquila* agreement and other intercompany agreements such as management services. The involvement of a good American and Mexican customs broker is helpful to ensure that all import-export paperwork is completed properly on both sides of the border.

Operating properly pursuant to an IMMEX program also requires diligence from both the foreign and Mexican affiliate. Each item imported into Mexico receives a *pedimento*, an instrument which documents the import. Upon export of the good or its transfer to another company, the *pedimento*, as well as the certificate of origin and the invoice (*factura*) must accompany the item being transferred. Companies with IMMEX programs may transfer the temporarily imported goods to other companies with IMMEX programs, which will carry out processes of transformation, processing or repair, or will return the goods, provided that they process an export *pedimento* on behalf of the person making the transfer, to be filed together with a temporary import *pedimento* on behalf of the company receiving the goods.

Mexican tax authorities regularly audit IMMEX companies to determine whether all their paperwork is in order, that all the *pedimentos* match, and any duty owed has been properly paid. A company that is lax in its procedures and documentation may face, in addition to hefty tax fines for unpaid duty, an administrative process by Mexican tax authorities that will audit and investigate the company's customs filings, and may even impound machinery or equipment until the company can demonstrate that it was properly imported under an approved IMMEX program.

Among a company's main obligations with respect to its IMMEX program are the following:

a. The company must conduct annual foreign sales worth more than $500,000 or invoice exports for at least 10 percent of its total turnover.

b. The company must submit an annual report electronically to the SE including total sales and exports for the preceding fiscal year, no later than the last working day of May.

b. 2013 Tax Reforms and IMMEX Implications

In October 2013, the Mexican Congress approved a number of amendments and new laws relating to Mexican taxes ("Tax Reforms"). Most of these amendments and new laws were made effective January 1, 2014, and detailed rules and regulations have begun being published to follow the major Tax Reforms accordingly. Among the major Tax Reforms are those affecting IMMEX programs.

Under the Tax Reforms, reduction of Income tax for companies with IMMEX Programs is no longer available; such companies will therefore be subject to pay the same 30 percent as other companies.

Additionally, a foreign resident will be considered to have a Permanent Establishment (PE) within Mexico, for purposes of income tax, when carrying out business activities in Mexico through another entity, even if the foreign resident does not have an actual place of business in Mexico. In order for a foreign resident with a Maquila operation to avoid being considered to have a PE, the following must apply:

1. The foreign resident must:

    a. Be a resident of a country with a double taxation treaty with Mexico.

b. Own at least 30 percent of all equipment and machinery used by the Maquila. Any current Maquila must satisfy the 30 percent requirement by January 2016.

2. The Maquila must:

    a. Regularly perform transformation-of-goods operations in Mexico with goods owned by the foreign resident that have been imported temporarily (Maquila Operations).
    b. Export all imported goods, whether physically or virtually (transfer through virtual exchange of *pedimentos* to another Maquila, which will later physically export the goods). Note that no benefits will apply for transformation or repair activities on goods sold in Mexico (other than virtual exports).
    c. Only have income from Maquila Operations, which include certain personnel services, leasing of real estate and personal property to unrelated parties for up to three years, sale of fixed assets used for Maquila Operations, sale of scrap and interests.

These entities also will have to comply with the latest transfer pricing rules, which have been reduced to the following:

1. Safe Harbor – the greater of:

    a. 6.9 percent of the total value of the Maquila Operation's assets, including assets owned by the foreign resident, or
    b. 6.5 percent of the total amount of Maquila Operation's costs and expenses; or

2. Obtain an Advanced Pricing Agreement with the Mexican Tax Authorities.

With respect to Value Added Tax (VAT), as opposed to recent years, a 16 percent VAT for temporary imports, which may be reimbursed at the time of exporting the goods whether physically or virtually, will apply. Nonetheless, the Mexican tax authorities have published forms to request IMMEX certification (under A, AA, or AAA modalities) with which companies may avoid having to disburse such VAT payments. Although VAT will still be imposed, Maquilas that are additionally certified as A, AA or AAA will have a full tax credit for their temporary imports and will avoid having to make VAT cash disbursements. If an entity cannot obtain certification, it will have to disburse VAT payments – which will be reimbursed at the time of the products' export – or to provide security by obtaining a bond from an authorized Mexican bond company. The 100 largest exporters will be exempted from actual VAT payments. The certification dates for current IMMEX programs ranges through October 2014. IMMEX certifications will be valid for 1, 2 and 3 years for A, AA, and AAA certifications, respectively.

c. Shelters

Shelter companies offer a range of services, including HR services and employee leasing, facilities leasing or sub-leasing, customs brokerage, contract manufacturing, and general administrative services. Shelter operations also offer "instant Maquilas" that permit new companies to operate under their umbrella, thus offering a "soft landing" to foreign companies new to Mexico. Nonetheless, under the latest Tax Reforms, a foreign resident using these instant Maquilas will only be considered as "not having a PE in Mexico" (see PE rules in section 4.b.), for up to four years.

The advantages for a new entrant into the Mexican market to using a shelter company are that the company can set up quickly, without having to deal with real estate, employment and administrative formalities that may be difficult or time consuming at the outset. The shelter company will serve as the legal employer of the employees, the tenant on the lease, and responsible for the taxes and other administrative burdens related to the shelter company.

The IMSS (social security) regulations and laws have a tight control over the practice of labor outsourcing and have increased obligations over companies providing outsourcing services and those receiving the benefits of such services. Such regulations make the companies receiving the services directly liable for all IMSS contributions not paid by the outsourcing companies. In addition, both service providers and receivers must provide quarterly notices of their outsourcing relationships and agreements. Companies using these outsourcing services will have to improve control over their outsourcing providers to avoid unnecessary disruptions in their work process.

Shelter and any other labor outsourcing companies must comply with IMSS contributions, as well as with all other statutory employee benefits (see Section 5), and companies receiving the services are liable for any benefits not provided by the outsourcing company.

A recent development that may affect shelter companies is the 2012 Labor Reform that has tightened control over the practice of labor outsourcing (see Section 5).

5. Labor And Employment

a. Employment Regulation Overview

The federal government has exclusive power to issue special labor regulations. The Federal Labor Law (FLL) governs labor and employment, and is based on the principles of Art. 123 of the Mexican Constitution. State authorities apply the FLL within their jurisdictions, but certain industries, including regulated industries and those operating in multiple states, are subject to the exclusive jurisdiction of federal labor authorities and courts. The legal framework consists of formally adopted rules (e.g. laws and treaties) and supplementary standards. Labor laws are implemented by various government agencies and tripartite commissions, and enforced by various judicial tribunals.

Once a "work relationship" is established between an employer and employee, the laws governing the rights of workers apply automatically, with a presumption that a contract exists until proved otherwise, and the burden of proof is on the employer. While a labor contract can be modified after its creation, the changes cannot lead to a permanent reduction in the worker's rights guaranteed by law, e.g. lower salary or work conditions. An employment contract is presumed to be of an indefinite term unless it was entered into for a fixed term. While an employer is not required to have a written employment contract with each worker, many companies do so in order to satisfy their burden of proof.

b. Pre-Hire Issues

A standard practice among many Mexican companies is to conduct pre-employment screening, including drug testing and a medical exam. It is advisable to ensure that HR personnel and legal counsel experienced in employment law are involved in setting up pre-employment screening for new Mexican operations.

c. Mandatory Employee Benefits

Mexico has two statutory minimum wages based on the cost of living in certain cities, which are increased every January based on the inflation rate. Mexico City and other "Zone A" cities are classified for the highest rate, where the applicable minimum wage at the time of this writing is MXN $64.76 per day (approximately US $5 per day). There are also "professional" minimum wages depending on the professional/technical capabilities.

In addition to the statutory minimum wage, employers in Mexico are obligated to pay a variety of statutorily mandated employee benefits. However, employers do not pay certain benefits that are common in the U.S., e.g., there is no generalized system of unemployment insurance as in the U.S.; workers who lose their jobs have no expectation of receiving unemployment benefits from the state. Employees are also not paid for sick days or for short or long-term disability, these benefits are covered by the IMSS. Not all companies offer private health insurance; there is a system of public health clinics and hospitals that provide healthcare. Benefits and payroll taxes that are required by law include:

- PTU (profit sharing) of 10 percent of company profit annually (certain exceptions apply; payable no later than May 30)
- IMSS (social security) of approximately 17 percent of wages but varies depending on various factors for each employee. This also covers disability pay and government health clinics
- SAR (pension) of approximately 2 percent of wages
- INFONAVIT (housing fund, which provides low-cost loans to workers to purchase a home) of 5 percent
- Paid vacation, which varies by seniority. After one year of service, six days is mandatory
- Overtime – double time for regular overtime and more on Sundays
- Seven paid legal holidays (although many companies offer other paid holidays)
- *Aguinaldo* (Christmas bonus, payable no later than December 20 each year) of a minimum of two weeks' pay.
- Severance pay (see subparagraph g. Just Cause termination)

d. Compensation and Fringe Benefits

In addition to the statutory requirements, in very rural areas and in areas where it is difficult to find suitable workers, employers may also offer such benefits as transportation to and from work, free or reduced price lunches on site, medical care on site, or a monthly basket of household necessities. Obviously, in wealthier or urban areas such as large cities, benefits tend to be mostly financial; manufacturing companies outside of large population centers need to offer different incentives to find a good workforce. Note that many foreign companies set up separate companies that hold their employees and lease them back to the operating companies in an effort to restrict the amount of profit sharing that must be paid to Mexican employees. The regulations regarding this practice have recently changed, however, and care must be taken in structuring such dual companies to ensure they comply with applicable law.

e. 2012 Labor Reforms

On December 1, 2013, the long-awaited reform to the FLL took effect, including amendments and additions such as:

- No discrimination based on origin, gender, age, disability, social conditions, health, religion, immigration status, sexual preferences, marriage status, pregnancy, etc.
- Protection of expatriates' rights
- Outsourcing regulation
- New employment testing and training periods (temporary employment)
- Protection against sexual harassment
- New limit to payment of salaries due (only during litigation) of 12 months
- 5 days of paternity leave
- Additional weeks of maternity leave in case of birth defects or extensive need for hospital care
- Greater protection for minors
- Access of union contracts to the public

Amongst the most important amendments to take into consideration when doing business in Mexico, are the following:

(i) New employment testing and training periods. Before the Labor Reforms, any new employment relationship entitled the employee to certain rights, such as no termination without just cause. Employment testing periods, or temporary employment, are now provided under the FLL for up to 30 days, which can be extended to 180 days for managerial positions, upon which such employees may be terminated by the employer. Employment training periods are also possible for up to 3 months (6 months for managerial positions), after which employees may be terminated without employer responsibility. Both the testing and training periods are for new employees and neither apply to promotions or job changes.

(ii) Outsourcing Regulation. Prior to the 2012 Amendments, companies could subcontract their employees from third parties, which would provide the employee benefits and the company would not be considered the employer. As of December 2012, the subcontracting regime is modified and limited to work covering all of the activities in the workplace, being specialized in nature and not covering similar tasks to those rendered by the rest of the company's employees. If the three aforementioned factors are not fulfilled, the company may be subject to employer obligations, including mandatory benefits such as the PTU described above, in addition to fines. To avoid falling under this scenario, a careful review of subcontracting or outsourcing agreements should take place by legal counsel.

f. Unionization

Art. 123 of the Constitution provide both workers and employers with the right to associate. Accordingly, workers or employers may form a union ("sindicato"). The FLL provides that groups of 20 or more employees may form or join a labor union, and requires the company to negotiate to enter in a collective bargaining agreement with such a union. It is permitted, and commonly practiced, to enter into a contract with a union prior to reaching the 20-employee threshold, as this permits the company to select the union, rather than leaving it at the mercy of an organizing drive. Labor unions may be:

- Trade unions: workers of the same profession or skill
- Enterprise unions: workers of the same enterprise
- Industrial unions: workers who work in two or more enterprises in the same industry
- National unions: workers in the same industry and located in different states
- Multi-craft unions

Different classes of workers ("positions of trust" or white collar and blue-collar workers) may not be in the same union, but may form separate unions in the same enterprise if the white collar workers so choose. However, employees in "positions of trust" rarely form unions.

Collective agreements are between a union and an employer and if requested by a union, the employer must enter into one. The general terms (e.g. paid holidays, overtime) are subject to review every two years, while salaries are reviewed annually. To be effective, the collective agreement must be filed with the Federal or State Conciliation and Arbitration Board, which has jurisdiction in that area. The collective agreement may be for an indefinite or a definite time period.

Unions may:

- Challenge the annual tax declaration (significant for the mandatory profit sharing requirement) and determine participation of individual workers in profit sharing
- Initiate a collective dispute on economic issues
- Negotiate and sign collective agreements on behalf of workers
- Facilitate training, establish seniority and work rules, and monitor health and safety

Employer unions may be:

- Formed by numerous employers in a locality
- National associations comprised of numerous employers in multiple states

g. "Just Cause" Termination

Under Mexican Labor Law, there is no such thing as "at will" employment, as understood in the U.S. Therefore, the process of terminating employees is not as simple and in many cases subjects the employer to severance payment obligations. Dismissal ("*rescisión*") of individuals must be for "just cause", and the causes for such dismissal are listed in Art. 47 of the FLL. The intent of the law is to protect workers and society against unemployment. If the employer terminates a worker without just cause, the worker has a right to demand either mandatory reinstatement or indemnification. However, workers in "positions of trust" and certain other categories of workers may not demand mandatory reinstatement because of the nature of their work. In case of just cause termination, the employer must notify the worker in writing of the termination date and the cause. Failure to do this means the termination is deemed "without cause" thus triggering the indemnification provisions. Termination without just cause does not require prior notice, but does trigger the indemnification provisions.

Indemnification for workers dismissed "without just cause" includes:

- three months' salary, plus
- 20 days' actual salary for each complete year of service, plus
- if applicable, "seniority premium" of 12 days' pay for each year of service rendered, which is set at twice the minimum daily wage (minimum is currently MXN $64.76, so approximately MXN $1,500 per year of service would be owed), plus
- accrued salary, bonuses or extra statutory benefits, if applicable.

Higher indemnification amounts are required for those hired for a fixed term and terminated without cause: one-half the amount owed for the term if terminated in the first year, and 20 days' salary per year for those agreements exceeding a one-year term.

If workers are covered by a collective bargaining agreement, the termination process may differ. The FLL governs the suspension or termination of a collective agreement, both of which require a procedure before the appropriate Conciliation and Arbitration Board. Consultation with the union during the entire process is required, as it serves as the attorney in fact for the affected workers. Termination of a collective agreement may be made for a number of reasons, including *force majeure*, unprofitability, or bankruptcy of the company. Prior approval of the Conciliation and Arbitration Board is required to terminate a union contract, which can be obtained by filing a written request. The union must be involved with all aspects of the planned termination, as the representative of the workers.

Despite the statutory requirements, terminations and severance in Mexico are often negotiated and, the employee upon payment of the agreed-upon amount may sign a release of all claims. However, due to the statutory protections, care must be taken to ensure that any terminations are properly documented and able to withstand scrutiny of the Conciliation and Arbitration Board.

h. Recent Trend

A recent phenomenon is that of American citizens claiming both U.S. severance and protection under the Mexican labor laws if their employer terminates them. These are employees who are hired and paid by the parent company in the U.S. but work across the border in Mexico at the foreign operation. As a matter of public policy, any employee who works in Mexico is deemed to fall under Mexican employment law and is subject to its protection. To avoid "double-dipping" severance payments to U.S. employees, both a carefully drafted employment agreement with indemnification provisions, and a services agreement between the U.S. parent and Mexican subsidiary, is strongly recommended.

i. Workplace Safety

Mexican law requires all employers to meet minimum health and safety requirements within their establishments. Because of these requirements, the FLL allows for the creation of health and security committees. These committees are composed of management-level employees and the workforce they oversee. The committees, along with the labor authorities, have the duty of investigating work-related incidences and illnesses, determining their causes and developing safer procedures which they in turn implement and then oversee compliance.

The labor authorities and IMSS have the power to establish safety regulations and to inspect workplace premises to determine compliance with minimum safety standards and other industry specific standards. Employers may be sanctioned for noncompliance.

j. Record-Keeping Requirements

Employers are legally responsible for maintaining accurate records regarding all social security benefits paid to workers, for making all required payments to the relevant government agencies, and withholding all taxes required by law. There may be personal or criminal liability if the withholding is not done or is done incorrectly. In addition, employers must keep copies of employment contracts.

k. Discrimination, Harassment and Retaliation

The Federal Law to Prevent and Eradicate Discrimination, enacted in 2003, provides that no person may be discriminated against or denied access, maintenance or promotions in the workplace based on sex, race or religion. The National Board for the Prevention of Discrimination and the Ministry of Labor are two agencies tasked with enforcing the anti-discrimination statute. Recent amendments in the FLL provide for stronger and more effective means of enforcement.

l. Agency Agreements

Under the FLL, agents are considered employees of a company or companies to which they provide services to if their services are permanent, unless one of the following two exceptions takes place:

1. the agents do not provide the services personally, or
2. the agents are only involved in isolated instances or transactions.

The company would have the burden of proving that the agents were not employees under the FLL, meaning they were not subordinated and permanent laborers for the company in accordance with the two exceptions listed above. If an agent is deemed an employee, the benefit and severance rules mentioned above would apply. In order to avoid an agent being considered an employee, legal counsel should carefully review any agreement prior to signing.

6. Immigration

a. Overview

The continuing liberalization of the Mexican market, combined with NAFTA membership, has facilitated immigration clearance for work purposes for citizens of the U.S. and Canada. Immigration matters are governed by the federal Mexican Immigration Code. The Ministry of Interior (*Secretaría de Gobernación*) administers and enforces the Immigration Code. In addition to the Immigration Code, administrative regulations and internal policies also apply to immigration issues. Internal policies are set by the Ministry of Interior, the General Bureau of Population (*Dirección General de Población*) and the National Institute of Immigration (*Instituto Nacional de Migración*).

U.S. and Canadian citizens and other nationalities do not require a visa to enter Mexico when traveling as tourists, business visitors or in transit, as long as their stay does not exceed 180 consecutive days. In addition, foreigners that hold a valid current visa for entry into the U.S., or those who are permanent legal residents of the U.S., Canada, Japan, U.K. and the countries that comprise the Schengen area, do not require a visa to enter Mexico if traveling as tourists, business visitors or in transit if their stay does not exceed 180 consecutive days. A fee is applicable if entering by land. If travelling by air, the fee is included in the price of the plane ticket. In every case, a valid passport and a completed “Multiple Migratory Form” (FMM) must be filled out and be stamped at the first port of entry to enter Mexico,. The form must be returned when leaving Mexico. Note, not all nationalities are eligible for an FMM. Eligible nationalities include the U.S., Canada, China, amongst many others. Any individual that is a national for a country not eligible for an FMM must apply for a visa with the nearest Mexican Consulate.

Mexico offers various types of visas depending on the circumstances of each applicant. Generally speaking, Mexico distinguishes between short-term stays, long-term stays, permanent residency and naturalization. The discussion below focuses on the types of visas most frequently required by business people.

b. Business Trip for Fewer Than 180 Days

If the individual’s visit to Mexico is exclusively for business purposes (such as business meetings, marketing, participation in trade exhibits, consulting and staff support), and he or she does not intend to enter the local job market, the stay in Mexico will be for a maximum of 180 days, and generally, no visa is required. The FMM must be filled and stamped at the first port of entry and approve the legal entry and stay in Mexico.

c. Business Trip for More Than 180 Days

If the individual is travelling to Mexico exclusively for business purposes (as above), but his or her stay will be longer than 180 days, a visa must be obtained from the Mexican Consulate office nearest the individual’s place of residence. The visa allows the individual to remain in Mexico for a maximum period of one year with multiple entries and can be renewed for an additional four years, granted in one-year increments. Once the visa is obtained, it must be used within the validity term stamped on the visa and the FMM must be filled and stamped at the first port of entry. Additionally, within 30 days of arrival in Mexico, the applicant must go to the nearest office of the National Institute of Immigration to exchange the FMM for a Non-Immigrant Card.

d. Working in Mexico

Foreign nationals who have been offered a position in a Mexican company or who are intra-company transferees may enter Mexico with a FMM and exchange it for a Non-Immigrant Card. The foreign national is not authorized to work until his or her Non-Immigrant Card and work status is granted. As an alternative, the individual may obtain a visa through a Mexican Consulate if the Mexican company or branch files for a pre-approval of the work permit from the National Institute of Immigration prior to the employee entering Mexico, and asks that the visa be issued abroad through a Mexican Consulate. Within 30 days of arrival in Mexico, the applicant must undergo a shorter exchange process for the Non-Immigrant Card (since Consulates are not authorized to issue the cards) and may not work until the Non-Immigrant Card and work status is granted. However, this second option may allow the Mexican Consulate to issue the permit for importing household goods.

This process allows the applicant to remain in Mexico with multiple entries for a maximum period of one year, renewable in increments of one-year.

e. Board Member

In the case of foreigners who only wish to attend shareholder or board of director meetings in Mexico, or hold a position at or have authority to act on behalf of the Mexican entity, such individuals are required to fill out and FMM and present it at the first port of entry. The form must be returned when leaving Mexico. With the FMM, individuals may legally act in Mexico on behalf of the Mexican company, including opening bank accounts, signing contracts and/or obtaining loans.

7. Customs

a. Overview

Mexico is an aggressive proponent of cross-border free trade. In addition to NAFTA, it currently has trade treaties with more than 40 countries. As a result of the full implementation of NAFTA, there are now very few tariff barriers for U.S. exports to Mexico. However, the importing process is subject to numerous regulations administered by many ministries and agencies, and failure to complete forms correctly or inadvertent oversight of customs requirements can have serious consequences, including fines and confiscation of products.

The agency with primary responsibility for the administration of foreign trade in Mexico is SE. In addition, the Ministry of Finance and Public Credit (*Hacienda*) imposes requirements, as does the Health Ministry, the Agricultural Ministry and the Transportation Ministry. The Mexican customs regime changes with some regularity, and the information below is general in nature. Although no longer legally required, we recommend consulting a customs broker prior to beginning imports into Mexico to ensure that both the application process and the on-going paperwork are completed and filed properly.

b. Imports

For tax purposes, all Mexican importers must apply to and be listed on *Hacienda's* list of importers (*Padron de Importadores*). Prior to June 2013, the Administración General de Aduanas controlled such list but this has since been replaced by the *Administración General de Servicios al Contribuyente*. In addition, *Hacienda* has supplemental sector registries for such items as textiles, chemicals, electronics and auto parts. Mexican importers of items in these sectors must make separate application to be included in these registries. Mexico's import tariffs are assessed against goods classified according to the Harmonized Commodity Description and Coding System.

c. Duties

Under NAFTA, duties are calculated based on the U.S. plant value of products, as evidenced by the invoice, plus the inland freight charges and any other charges listed separately, such as packing. NAFTA compliant products imported into Mexico are not subject to the customs processing fee (CPF) unless they are only temporarily imported, in which case it may be levied. A certificate of origin must accompany NAFTA products. Goods imported under an IMMEX program are exempt from duty. U.S. companies do face certain non-tariff barriers, including the requirement to post a bond or guarantee the importation of certain goods, which are subject to under-valuation. Mexico has established a list of such products, and set a minimum estimated price for the goods on which duty is calculated. The guarantee is often in the form of a cash deposit or a line of credit, which must be held by a Mexican bank; the fees for opening and administering such accounts are relatively high. Mexico has implemented what are called "Sector Promotion Programs" (PROSEC) which reduce MFN tariffs to between 0-5 percent on a range of products considered necessary for the Mexican economy.

d. Value Added Tax (VAT)

In addition to customs duty, VAT is levied on goods imported into Mexico, unless they are imported on a temporary basis under an IMMEX program. Although VAT used to be 11 percent on goods that remain within the designated border region and 16 percent on those imported into the interior of Mexico, the new Tax Reform has modified the border regions goods to 16 percent as well. Certain goods, such as food and drugs, are exempt from VAT. Alcohol and tobacco products are subject to tax at the border in addition to VAT of between 20 percent and 110 percent, depending on the product.

e. Import Licenses

Certain sensitive items are subject to qualified import licenses issued by various governmental agencies, and the difficulty of obtaining such licenses varies with the product involved. Examples include weapons, some leather and fur products, medical products and equipment and diagnostic equipment, and toxic and hazardous products. Penalties for importing without a required license are fines plus penalties calculated as a multiple of the value of the imported goods.

f. Import Documents

The basic Mexican import document is the *pedimento*, which must be accompanied by a commercial invoice in Spanish, a bill of lading, certificate of origin, documents demonstrating guarantee of additional duties for undervalued goods (see above), and documents demonstrating compliance with Mexican product safety and performance regulations. The *pedimento* must be retained and accompany any goods that are re-exported, for instance via the IMMEX program. If *pedimentos* are not properly filled out, or the importing company cannot demonstrate that the goods were properly imported, the tax authorities may impose hefty fines or impound the goods or equipment involved.

All products intended for retail sale in Mexico must bear a label in Spanish prior to importation into Mexico. Products must also comply with all commercial and sanitary Mexican mandatory technical standards (NOM) which are government-imposed standards of quality and safety. A company importing products subject to such standards must obtain a NOM compliance certificate prior to import, which must be presented with the products at the time of entry into Mexico. The NOM standards are frequently updated and revised, and the importing company should regularly check with SE regarding import of categories of items, which are usually subject to NOM standards. NOM standards frequently require certain labels be affixed to imported goods, e.g. electronic products, toys and apparel.

8. Federal Income Tax and Other Taxes

a. Overview

The Mexican tax system is comprised of separate federal, state and local taxes. Federal taxes support the national government, and in many cases are shared with the state governments pro rata. This booklet only discusses the Mexican federal tax system, including the 2013 Tax Reforms. In addition to income taxes, the Mexican federal tax system contains specific excise taxes and the VAT. The Mexican Congress enacts federal income tax legislation, and annually approves the federal revenue law (*Ley de Ingresos*) which principally lists the amendments to the federal tax laws and specific federal taxes to be imposed during the year. *Hacienda* is empowered to issue regulations for implementation of the tax laws, which interpret the legislation.

b. Mexican Corporate Income Tax

Mexican corporations and all other Mexican entities other than non-profit organizations are taxed on their worldwide income. Nonresident corporations, including branches of foreign corporations registered to operate in Mexico, whose principal administration or management is established in Mexico, may be considered to have a permanent establishment in Mexico and taxed on their worldwide income as well. Nonresident corporations, which are not considered to have a permanent establishment in Mexico, are taxed only on their Mexican-sourced income at a flat rate applied on a withholding basis. All Mexican entities other than non-profits are taxed in accordance with the rules applying to corporations.

Among the 2013 Tax Reforms is the New Income Tax Law, pursuant to which Mexican corporations pay a 30 percent federal income tax on their corporate profits. Corporations may be able to reduce their corporate income tax burden by re-investing profits. The corporation must pay a deferred tax upon distribution of the profits. Any income tax paid to foreign countries on income received from foreign sources will usually qualify for tax credits against a Mexican corporation's Mexican income tax liability. Mexico has tax treaties with a number of countries, including the U.S. and Canada, to address and avoid double taxation.

Corporate profits are calculated by deducting certain allowed expenses from gross income. Income is considered accrued when the first of the following occurs: an invoice (*factura)* is issued, goods are delivered to the buyer or services are rendered, or partial amounts of the transaction are collected or payable, including advance payments.

Dividends received from a Mexican corporation are not included in gross income nor are they deductible by the distributing company, while dividends received from foreign corporations are taxable. Dividends paid by a Mexican company to its nonresident shareholders, or by a foreign company considered to have a Permanent Establishment in Mexico to its nonresident shareholders, are subject to 10 percent withholding tax. Such tax rate on dividends paid to a nonresident may be reduced under an applicable tax treaty by crediting the withheld tax against an individual's tax liability. Notable rates for dividends in tax treaties with Mexico include:

Country	**Substantial Participation**		**All other cases**
	If shareholder owns at least 10% of the voting stock of the company paying the dividends	**If shareholder owns at least 25% of the voting stock of the company paying the dividends**	
Canada	5%		15%
China	5%		5%
Germany	5%		15%
Japan		5%	15%
U.K.*	15%		15%
U.S.	5%		10%

*Exception in treaty.

c. Filing Dates for Returns and Payments

Taxpayers must use the calendar year as their fiscal year. Annual income tax returns must be filed by March of the following year. Most corporate taxpayers are required to file income taxes through monthly provisional payments, calculated based on 1/12th of the previous year's annual taxable income, which will be credited against the annual income tax return. An independent public accountant must audit most company financial statements. The shareholders or partners must approve the annual accounts and the disposition of any profit each year at an annual meeting called for that purpose. Companies that are listed on the Mexican stock exchange are required to publish their accounts in the newspaper; privately held companies are not.

Additionally, amongst the regulations published in relation to the 2013 Tax Reforms was the Regulation for the Federal Tax Code, which provides for instructions regarding the new requirement for monthly online submissions, which includes submitting information regarding journal entries, tax returns, bank statements, share ownership, IMSS documentation, and import and export documentation, amongst others.

d. Accounting Standards and Practices

Mexican accounting standards and practices are similar in many respects to the U.S., with a few key differences. As a result of historical periods of high inflation, the value of non-monetary assets must be adjusted annually. A company that has operations in both the U.S. and Mexico should select accountants that have experience on both sides of the border.

e. Withholding Taxes

In many cases, a company making payments to third parties is required to withhold and pay to the tax authorities the income tax owed by the third party. This is the case in general for all payments to individuals (e.g. payroll, dividends). In all cases, the company is jointly liable for the tax that should be withheld. Failure to make the appropriate withholding is subject to interest and fines.

f. Enforcement

In recent years, general rules to avoid abuse through transfer pricing have been broadened. Payments to related parties should be on an arm's length basis and properly documented in order to be deductible. There are strict rules regarding documentation, withholding taxes, and prior authorization for certain deductions, which if not complied with may result in denial of deductibility of costs and expenses. All items to be deducted must be set forth in a proper *factura* or the deduction can be denied. Tax authorities generally base their analysis on the documentation and not the purpose of a transaction, giving rise to the statement that form may rule over substance. They can be aggressive about pursuing delinquent taxes, taxes not properly withheld and improper returns.

g. Clearance Procedures

Under the rules of the Federal Tax Code, taxpayers may request advance rulings from *Hacienda* on specific transactions before carrying them out. Advance rulings can help provide legal certainty as to the effects prior to completion; however, these have been curtailed by recent changes in the tax law. Such rulings are more difficult to obtain and the process can be lengthy and time consuming. If the ruling adversely affects the taxpayer's interests, this can be overcome by obtaining annulment in the tax court or federal appeals courts.

h. Tax Audits and Appeals

Income tax returns are considered accepted by the tax authorities as filed, although they are empowered to review or audit in detail any return. The audit may include a detailed review of accounting records to determine compliance with tax duties. Any type of federal tax is subject to audit, including foreign trade taxes, import duties (and the corresponding *pedimentos*), payroll taxes and income tax. Keeping meticulous records is important with respect to all tax matters, as the form of the documents filed is very important. Generally speaking, audit rights and the ability of the authorities to collect additional taxes expire after five years. However, in cases where the taxpayer failed to conform to certain form requirements, such as maintaining tax records for ten years, the statute of limitations is ten years.

i. Other Taxes

1. Value Added Tax

A company doing business in Mexico will also be obligated to pay VAT at a general rate of 16 percent on sales, rents, and imports of goods and services. VAT is paid at each stage of a commercial transaction to the "upstream" operation, and is reimbursed from the "downstream" operation. The ultimate consumer pays the VAT in the end. Companies must file their VAT reports and make monthly payments to the tax authorities. Additionally, in accordance with the 2013 Tax Reforms, in order to obtain a VAT refund, the operation must have taken place with documentation that includes the particular tax receipt. States and municipalities are prohibited from taxing transactions subject to VAT, as they receive a portion of the federal VAT receipts.

2. Employment Taxes

Mexican corporations are subject to a local state payroll tax and federal social security and labor contributions, which may equal up to 35 percent of the payroll (for details see above). Payroll fees are deductible for income tax purposes. However, deductions for contributions to pension plans, retirement contributions and medical benefits will be limited to 47 percent of amounts paid. If such fringe benefits are equal to or greater than those of the previous year, the deduction will be 53 percent of the amount paid. All salary payments for workers residing in Mexico will be subject to a withholding tax of up to 30 percent, while salary payments for workers residing abroad are subject to various tax rates.

3. State and Local Taxes

Although the federal income tax is the main tax levied on Mexican companies, states and municipalities may also impose certain taxes. These normally take the form of property taxes, taxes on the transfer of real property, and payroll taxes.

4. Other Indirect Taxes

In addition to the taxes discussed above, there are federal excise taxes on alcohol, cigarettes and gasoline. There are also federal taxes levied on the ownership of automobiles and on the purchase of new vehicles.

j. 2013 Tax Reforms

In addition to the changes provided for in the 2013 Tax Reform mentioned above, the following are changes that should be noted:

1. ISR – Federal Income Tax

a. The Tax Consolidation regime is modified as follows:
   i. Groups that decided to consolidate as of 2010 may still continue to do so.
   ii. Groups that have consolidated for more than five years may no longer consolidate and are given three options on how to de-consolidate.
   iii. Replaced with new regimen whereby entities may defer taxing for up to three fiscal years (the entity must be a Mexican resident).
   iv. Maquila entities may not be included within consolidated entities.

b. Deductions
   i. Fixed asset investment and machinery and special equipment deductions are no longer immediate.
   ii. Pension and retirement contributions are now deductible up to 53 percent.
   iii. Social security contributions are not deductible.
   iv. Exploration costs for the location and quantification of new mining deposits are deductible up to 10 percent.

c. Dividends
   i. Foreign residents and Mexican individuals are now subject to a 10 percent dividend tax on income by means of retention by a Mexican (or in the case of Mexican individuals, by a Mexican or foreign) entity.

d. Other
   i. Investment income in the Mexican stock market is now taxed at 10 percent.
   ii. The general withholding tax for payments to foreign residents is now 35 percent.
   iii. Installment sale income may no longer be accumulated and shall be paid over two years.
   iv. Additionally, there are changes to personal income tax (for individuals).

3. IETU – Flat Tax

The IETU tax (*Impuesto Empresarial a Tasa Única,* tax on EBIT plus investments) used to serve as a minimum tax. A Mexican taxpayer corporation would be obliged to pay a IETU tax of 17.5 percent on net income only to the extent such amount exceeded the company's regular income tax for the year. Nonetheless, this law was repealed by Congress as part of the Tax Reforms.

4. Cash Deposit Tax Law

Prior to the Tax Reforms, accumulated tax deposits more than $25,000 a month were taxed at a rate of two percent. Although this law has been repealed, financial institutions are still obliged to make a report once a year on taxpayers' cash deposits exceeding $15,000 MXN a month per the VAT tax law.

5. Federal Tax Code

The amendments to the Federal Tax Code include the following:

i. New electronic tax income whereby tax authorities notify taxpayers of any act or resolution.
ii. Online digital tax receipts will now replace any other means of proof of operation.

9. Payments To Foreign Persons

a. Dividends

Dividends of a Mexican subsidiary to its foreign parent are subject to a 10 percent withholding obligation, as discussed below.

b. Management Fees and Administrative Support Reimbursements

In order to be deductible, expenses for management fees and administrative support must meet the test of being "strictly indispensable" for the conduct of the business. Charges from a foreign affiliate for a pro rata share of general and administrative expenses or research and development costs are not deductible, except in the case of branches or other permanent establishment of foreign corporations.

c. Executive Compensation

Fees paid by a company domiciled in Mexico to a non-resident for services performed in Mexico, including director's fees, are subject to a 30 percent income tax withholding. There are no specific limits on amounts paid, as long as all normal payroll taxes and income tax withholdings are paid. After the withholding is made, the amount withheld can be credited toward the payment of taxes in the country of tax residence pursuant to the tax treaty.

Depending on how long the individual stays in Mexico and the amount of compensation involved, tax obligations and withholding in Mexico may be required even if the fees are paid outside of Mexico by the foreign entity. Consult with legal counsel if this may apply to you.

d. Interest Payments, Royalties, and Technical Services Fees

Payments for interest, royalties and technical services made to a foreign-related party that controls or is controlled by the taxpayer are not deductible when the foreign party is considered transparent, the payment is considered nonexistent for tax purposes in the foreign country, or when such foreign party does not consider the payment as taxable income.

e. Transfer Pricing

Residents entering into transactions with related nonresidents, are obligated, for income tax purposes, to determine their taxable revenues and authorized deductions by considering the prices and amounts of compensation that would have been used with or between independent parties in comparable transactions. With a few exceptions, such residents are required to obtain and keep supporting documentation demonstrating that the amount of their revenues and deductions were determined in accordance with the prices or amounts that would have been used by independent parties in comparable transactions. Residents may submit to the Mexican Tax Authorities consultations related to the transfer pricing methodology used in their transactions in order to reach an Advanced Pricing Agreement, as long as resident provides the necessary documentation.

10. Financing a Mexican Operation

a. Owner Loans and Capitalization

If a form of entity with variable capital is selected (see above), increasing capital when needed is a relatively simple matter. Companies in Mexico are not taxed on their capital or the number or value of shares outstanding. Generally speaking, domestic intercompany loans are treated the same as third-party loans with respect to deductibility of interest. However, if certain criteria are met, the interest paid may be characterized as a non-deductible dividend. These criteria include a payment on demand clause and if the interest is based on obtaining certain profit levels.

As previously mentioned, interest is non-deductible when a foreign related party controls or is controlled by the taxpayer and the foreign party is considered transparent, the payment is considered nonexistent for tax purposes in the foreign country, or when such foreign party does not consider the payment as taxable income. Additionally, interest payments made by a Mexican resident on a loan from a related nonresident is non-deductible in excess of a 3:1 debt-to-equity ratio.

b. Bank Loans

A local bank has the ability to make loans either in Mexican pesos or in foreign currencies. If the entity is a Mexican subsidiary of a foreign company, the bank may be willing to negotiate a line of credit with the parent company for the subsidiary so long as the parent company guarantees the loan. Financing tends to be expensive in Mexico and the application process can be cumbersome.

With respect to foreign banks, tax on interest paid to foreign bank loans remains at a 4.9 percent income tax withholding rate for payment by a Mexican resident or foreign resident with a Mexican PE (as long as the foreign country has a tax treaty with Mexico). Additionally, as of the 2013 Tax Reforms, foreign financial institutions are no longer required to be registered with the Mexican Tax authorities in order to obtain an income tax preferential rate on interest payments by Mexican residents to these financial institutions.

c. Other Financing Sources

Bancomext (the Mexican export-import bank) and Nafinsa (a public financing agency) also have financing available, but their rates are usually higher than foreign financing options. Details can be obtained from the Mexican federal government or incentive agencies.

d. Venture Capital

Venture capital in Mexico is still in its infancy and largely foreign-based. However, there is growing interest from the private sector, universities and governmental bodies. Venture capital as a means of financing is expected to grow in the next few years.

11. Securing Assets in Mexico

a. Means of Securing Assets

The following are the main vehicles to secure assets in Mexico:

1. Pledge

A pledge under Mexican law is a security interest over tangible movable property. The pledge requires the pledgee or a third party to take actual possession of the property. The following may be pledged under Mexican law:

- Bank Accounts
- Equipment
- Animals
- Crops
- Timber
- Inventory
- Leases
- Receivables
- Contractual Rights
- Vehicles
- Cash

The formalities for the pledge include delivery of the bearer instruments to the pledgee, delivery of the pledged assets to the pledgee (or third party), and registration with the public registry of commerce.

2. Non-Possessory Pledge

A non-possessory pledge is a security interest over tangible movable property or over present and future movable assets that the pledger has identified generically, where the pledger remains in possession of such property. Similar to the pledge, in order for a non-possessor pledge agreement to be enforceable against third parties, the agreement should be registered with the public registry of commerce.

3. Pledge on Listed Securities

A pledge on listed securities requires an authorized broker or financial institution named as administrator and executor of the pledge in order to be perfected. Additionally, the listed securities can either be held in a special account held by the administrator under a securities depositary or may be directly transferred to the pledgee who will then return the equal amount of securities once the underlying obligation has been covered. The formalities for the pledge on listed securities when held in the special account mentioned above is to have the pledge executed in writing and a request must be made to a securities depositary authorized under the Securities Exchange Act to balance the accounts in which securities are held. Otherwise, when directly transferred to the pledgee, formalities include the delivery or endorsement (where applicable) of the securities.

4. (Civil) Mortgage

A mortgage is a security interest on specific real estate. The real estate will remain in the mortgagor's possession. A creditor can foreclose on a civil mortgage once an event of default occurs. Real estate, for these purposes includes:

- Land
- Constructed Works/Improvements
- Fixtures

A mortgage can be created by an agreement between mortgagor and mortgagee or unilaterally through a unilateral declaration of intention from the mortgagor. Similar to the pledge and non-possessory pledge, a mortgage agreement should be notarized and registered with the public registry of commerce in the state where the real estate is located.

5. Security Trust

A security trust provides for title to any type of assets to be transferred to a trustee who will hold it for the benefit of the creditors, and in case of an event of default, foreclose on it. The trustee must be a financial entity authorized to act as such. A security trust is created by an agreement between a settlor (usually borrower, debtor or guarantor), creditor and trustee institution. For third party recognition purposes, and in case of real estate being part of the assets, the security trust agreement must be notarized and registered with the public registry of commerce.

6. Other

Security over specific types of assets, such as aircraft, requires a special mortgage regulated under the Civil Aviation Laws of Mexico. In order to perfect such a mortgage, it must be notarized and registered under the Aeronautic Registry. Similarly, vessels require a special mortgage regulated under Mexican Maritime Law, and notarization and registration under the

Maritime Public Registry. Depending on the type of security instrument used, formalities for security over intellectual property may require registration before the Public Copyright Registry. Additionally, collateral assignment of rights under Mexican law can be used as a form of quasi-security. Debtors can assign their rights under commercial agreements to creditors as a repayment mechanism.

b. Release

Releasing security interests, where the creation formalities included the need to execute before a notary public and/or register with a government registry, require execution of the same formalities to effectuate their release. Otherwise, a release letter would suffice. Where assets were transferred to be held under a security trust or to be held by the creditor must be immediately returned to the debtor upon release.

C. Enforcement

Enforcement of loans varies depending on the type of security interest, the type of secured asset and the nature of the creditor. Most enforcement measures require court intervention in order to obtain the payment of a secured obligation. If agreed to by the parties, private agreements over security may be enforced by non-judicial means. In the case of enforcement through insolvency procedures, creditors are ranked in accordance with Mexican law (usually starting with employee wages, followed by funeral expenses, secured creditors, employee claims and unsecured creditors).

12. Economic Development Incentives

Historically, Mexico provided few investment incentives. Of those provided, many were repealed in an effort to reduce national debt and those that remained were mainly industry-specific. Tax incentives were marginal. In more recent years, as part of the general liberalization of the Mexican economy, the federal and various state governments of Mexico, through the utilization of Executive Decrees, have modified laws and tax rules to make Mexico an appealing location for development. ProMexico is the agency responsible for attracting investment to Mexico. It has offices in a number of U.S. cities.

a. Federal Tax Incentives

Seeking to encourage industrial movement outside of Mexico City, Guadalajara and Monterrey (areas already enjoying significant industrial development), Mexico provides certain federal tax incentives for industrial operations outside of these zones. Further, if a company upgrades to more modern equipment it may be able to take advantage of accelerated depreciation of the new equipment.

Given the changing landscape in Mexican economic development, the programs sponsored by the Mexican government vary over time. Among the list of incentives offered are the following programs:

- Drawback: tax return to import for exporters
- IMMEX Program
- PROSEC
- PROLOGYCA: competitiveness program for logistics and supply markets
- PRODIAT: program for the development of high level technological industries
- PYMES Fund: support fund for medium and small-sized companies
- PROSOFT: program for the development of the software industry

Additionally, companies that purchase pollution control equipment may be eligible for accelerated depreciation of such equipment at a rate of up to 35 percent per year. Finally, the Federal Government, through the National Commission of Science and Technology (CONACYT) provides support for funding research and development projects, which may be granted to taxpayers who invested in research and development projects during the fiscal year. It is advisable to seek the advice of experienced legal counsel to work with local and federal authorities to complete incentive applications.

b. State Tax Incentives

In order to encourage industry in various regions, many Mexican state governments have established active economic development programs to provide incentives to new business, or to grow or retain current business. These include offering incentive packages of reduced property taxes. Additionally, states are encouraging development through the use of exemptions in areas such as payroll taxes, construction licensing fees, real estate tax and utility connection fees. Exemptions are also being utilized to encourage environmentally friendly investment projects. Depending on the state in which the foreign company is located, the level of technology or the specific industry involved, the incentives can be quite generous. Applying for such incentives is fact intensive and requires the assistance of experienced legal counsel experience.

c. Tourism

The main non-tax incentives that Mexico offers are in the area of tourism. The Mexican government has traditionally sought to encourage the development of hotels, condominiums, shopping centers and other such types of establishments. Rights to established tourist locations can be purchased at subsidized rates from FONATUR, Mexico's tourism agency. The agency develops these locations and provides consultation regarding development plans and projects. Foreigners are authorized to purchase these properties and are permitted to own all of the rights, except legal title to land in the coastal areas or along Mexico's borders. There are no restrictions on ownership of nonresidential property in these locations. FONATUR has made a substantial investment to develop the necessary infrastructure to support numerous resort developments.

d. Industrial Parks

Industrial parks have been developed in many areas in order to provide the necessary infrastructure required by the development of industry. Land is generally available in these locations and can often be obtained on investor friendly terms. The terms of the investment package may be included in other incentive arrangements offered by the state or municipality.

e. Free Trade Zones

There are a number of duty-free zones in border areas that were traditionally the site of *Maquila* operations. These tend to be industrial parks close to the U.S. border and details vary from state to state. They can be important for non-NAFTA countries, but with the full implementation of NAFTA are less relevant for the U.S. and Canada now than in the past.

13. Product Liability

All Mexican entities and individuals that produce, distribute or sell goods are subject to the Federal Consumer Protection Law, which is administered by the Federal Consumer Protection Agency (PROFECO), which has power to levy fines and shut down businesses violating the law. The Federal Consumer Protection Law was passed to protect consumers against merchants and manufacturers who do not comply with minimum standards or specifications for products and services. In addition, SE is empowered to impose fines and use other enforcement measures to protect consumers. There are minimum standards for sanitation and safety and availability of spare parts. Food products and medicine are subject to special regulations and control.

The Mexican Civil Code does not have specific provisions governing the liability of manufacturers for damages caused in Mexico by defective products. Lawsuits for defective products are extremely rare in Mexico, because courts are reluctant to recognize liability of manufacturers for such products. Any such action would be based on Art. 1910 of Federal Civil Code, which governs liability generally for “wrongful acts.” A plaintiff would need to prove negligence or misconduct on the part of the manufacturer; while not impossible, it is not part of the Mexican legal or commercial culture to sue for product liability.

Damage awards are also generally limited, covering only compensatory and not punitive damages. Compensation for medical and other expenses and lost wages are standard in the event a claim of damages resulting from defective products is proved. Any further damages, such as disability, are limited by statute to an amount set in the FLL, a maximum of four times the amount of the highest minimum daily wage in effect in the region.

14. Litigation

a. Overview

Although at first glance, the judicial system in Mexico appears quite similar that of the U.S., a closer analysis reveals fundamental differences. As a federal state, like the U.S., Mexico has federal and state courts, which dispense justice based on jurisdiction over certain subject matters. However, certain unique features of Mexican law, in particular the process of *amparo* permit citizens to appeal many state court decisions to federal courts, lawsuits that begin in state courts may continue in federal court. Other key differences to the U.S. are the following: the absence of juries, the central role of judges, and the lack of public trials. Except for certain limited offenses, all cases are tried to either one judge or a panel of three judges. In certain appeals cases, an *en banc* panel of judges will hear a case. As is customary in civil law countries, judges serve as both the finder of fact and the interpreter of the law. Most trials are conducted primarily on the basis of written submissions of complaints and evidence filed by the lawyers for either side; oral examination of witnesses, if any, is usually conducted by the judge, and the judge and his or her clerks are responsible for collecting and organizing the evidence on which to decide the case. All evidence in support of a claim must be attached to the complaint. The "trial" is not as one would see in the U.S. Generally, there is no public hearing and the judgment is handed down based on the documents and evidence provided to the judge.

b. Commercial Disputes

Overall, Mexico is considered generally less litigious than the U.S. and most business people attempt to resolve their differences outside of court. As in the U.S., litigation is costly and time-consuming. Although injunctive relief exists in concept in Mexico, it is not easily or quickly obtainable.

Commercial matters in Mexico are governed by the Commercial Code, which also includes procedural rules. Commercial disputes are normally brought before the state civil courts, with the statute determining where the lawsuit must be filed. An unsuccessful party in a lawsuit may have to pay for both parties' attorney fees if the parties agreed to do so, or if the plaintiff filed a lawsuit without merit or in some way abused the litigation process. Lower court decisions can be appealed, and during the appeal, the lower court judgment may or may not be stayed. Mexico has procedures for summary enforcement of judgments, including attachment and sale of a debtor's property.

c. Overview of Commercial Litigation

Commercial lawsuits are initiated in the local courts with a first instance litigation, which is heard by a single judge. The ruling of the local state court may be appealed before the State Court of Appeals (*Tribunal Superior de Justicia*). The ruling of the State Court of Appeals may be appealed by the *amparo* proceeding to the Federal Courts of Appeals. Secondary court rulings that do not end a trial may be appealed to the federal District Courts. There are no jury trials in Mexico except for treason cases. Trials can be lengthy as there are opportunities for delay on the part of the defendant and the proceedings are largely written.

d. Stages of a Civil Lawsuit in Civil Court

Prior to filing a complaint, there are three possible types of preliminary discovery or pre-filing motions.

1. Pre-filing stage (Etapa Preliminar)

a. *Preparatorios del proceso* – a party tries to clarify a doubt, remove an obstacle or cure a defect before a complaint is filed, for example to obtain an admission or denial regarding facts, production of property or evidence or prior examination of witnesses

b. Filing motions for interim equitable relief (*medidas cautelares*)

2. Opening or introductory phase (Etapa Expositiva): Statement of claim or response

a. This stage is also called *etapa postulatoria* or *etapa introductoria.* The parties state their claims to the court, including the facts and the law on which they rely. These are made by written submissions of a complaint by the plaintiff and a written response by the defendant.

b. The judge rules on admissibility of the complaint. If the complaint is admissible, then the Court serves the defendant who has nine days to respond for normal civil suits. Failure by the defendant to respond can lead to a default judgment

c. The defendant's response may be:

i. Acquiescence to demand (*allanamiemto a la demanda*),

ii. An affirmative defense (*opisición de excepciones),* or

iii. A counterclaim (*contrademanda*)

d. A pre-trial conference is held within 10 days of the defendant's response (*audencia previa y de conciliación*)

3. Evidentiary Stage (Etapa probatoria)

The parties prepare and present evidence to the court. The judge conducts this stage without any intermediaries. Only facts may be introduced into evidence and these may include evidence of usage or custom. The rules of evidence are less stringent than in the U.S., since a judge is collecting and weighing the evidence, rather than a jury of laypersons. There are relatively few hearings; witness testimony is similar to a deposition in the U.S. and conducted by the judge and the lawyers.

4. Closing stage (Etapa conclusiva)

The parties make their closing arguments, reciting the facts and law that they find relevant. The judge issues a judgment (*sentencia*) which must include a discussion of the issues and the evidence and the basis in law for the decision. The judge's decision binds only the parties, and is not precedent for later cases between other parties, except in the case of jurisprudence (see subparagraph g. Jurisprudence). This is a key difference to the U.S. legal system.

e. Appeals Court

Appeal courts in Mexico may review the legal conclusions reached by the lower court and also its factual findings. The appeals court may reject the lower court's factual findings if it is clear that the lower court misinterpreted the facts. Appeals are classified as ordinary, special or exceptional.

Ordinary appeals (*medios de impugnación ordinarios*) include a motion to appeal and a motion for reconsideration of an interlocutory order of a trial judge.

Special appeals are only for challenges to certain types of decisions set forth in the Civil Procedure Code (CPCDF) Art. 723, and a civil action filed against a judge for violating the law either negligently or through inexcusable ignorance.

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Exceptional appeals can be filed even after a case has been finally decided.

f. Ordinary appeals

These must be filed with the judge who issued the judgment, within 6 days of an interlocutory decision and nine days of a final decision. The lower court judge forwards the appeal to the appeals court, which agrees to hear if it meets the statutory requirements. A stay of execution of the lower court's judgment may or may not be granted. No new evidence may be introduced other than evidence of an event that took place after the trial began and was cause for a dismissal.

There are five phases to an appeal:

1. Receipt of the appeal, consideration of admissibility of the appeal and determination of the effects of the motion
2. Statement of causes for the appeal
3. Review of the evidence
4. Arguments
5. Final decision by the appellate court

The appeals process is largely written, with closing oral arguments made by the parties. The final ruling may uphold the lower court's decision, partially modify the lower court decision, or completely overturn the lower court decision. In the latter two instances, the case will be returned to the lower court for action in keeping with the appellate decision.

g. Jurisprudence

As stated previously, the general rule under Mexican law is that a judge's opinion binds only the parties and is not precedent for future cases. Nonetheless, Mexican law provides for a concept similar to case law, *jurisprudencia*, which reflect a courts' interpretation of a law and must be applied by lower courts. Jurisprudencia, or jurisprudence, may be created by any of the following means:

1. *Reiteration:* Jurisprudence by reiteration takes place when the Supreme Court or a Federal Court of Appeals (*Tribunales Colegiados de Circuito*) has the same opinion five uninterrupted

times in a row (majority opinion for the Supreme Court opinions and unanimous for the Federal Court of Appeals opinions).

2. *Contradictory opinions:* Jurisprudence by contradiction takes place when the Supreme Court or the Circuit Boards (*Pleno de Circuito*) determine the correct rule of law for discrepancies in between opinions.

3. *Substitution:* A substituted jurisprudence may only take place when a magistrate or justice so requires to the Supreme Court or the Circuit Boards.

Jurisprudences are suspended when an opinion is held opposing the jurisprudence and which includes the motives to doing so.

h. Enforcing Foreign Judgments

Judgments and other judicial decisions from foreign courts have the force in Mexico that its treaties may provide. In the absence of a treaty, they have the same force as is given to Mexican judgments and decrees in the country of origin. Foreign judgments and decrees will be enforced only if:

- They comply with regulations relating to rogatory letters;
- They were rendered in a personal action;
- The obligation on which they are based is legal in Mexico;
- The defendant was personally served in the action;
- They are final judgments according to the law of the country of origin; and
- They are properly authenticated.

Foreign judgments are enforced by the Mexican court that would have had jurisdiction if the judgment had been rendered in Mexico. The Mexican court does not inquire into the merits of the judgment, but merely determines its authenticity and whether it is enforceable under Mexican law.

From a procedural standpoint, the foreign judgment must be duly translated and both parties and a government attorney must be heard in the matter. The Mexican judge’s decision to enforce the foreign judgment may be appealed.

Mexico is a signatory to the UN Convention on Recognition and Enforcement of Foreign Arbitral Awards. For this reason, including an arbitration clause in a contract between a foreign and a Mexican company should be considered, as an arbitration award may be more easily enforced.

15. Antitrust

a. Overview

Mexico has both constitutional (Art. 28) and statutory prohibitions on monopolies and other practices that restrict competition. Part of the new legal reforms, the New Federal Law of Economic Competition and constitutional amendments, published may 2014, regulate competition and anti-trust matters in Mexico. The new law resembles U.S. anti-trust legislation. Regulations to the New Law of Economic Competition remain pending. Monopolies, monopolistic activities, and unlawful business concentrations are prohibited, as is price-fixing.

The Antitrust Reform seeks to ensure fair competition and the prevention, investigation and combating of monopolies, monopolistic practices and other restrictions on the efficient functioning of markets.

This new legal framework focuses on three major changes: credibility, effectiveness and legal certainty and enforceability. With respect to credibility, the Antitrust Reform created a new Federal Competition Commission (COFECE), separated the entities in charge of investigation and resolution of anticompetitive practice within the COFECE, and created mechanisms to make public the meetings, agreements and resolutions of the COFECE.

Generally, the Executive branch of the Federal Government will be responsible for determining the goods and services that may be subjected to maximum prices, the COFECE will determine if there is a lack of effective competition while the SE will determine the prices for the goods and services previously referred to and the Federal Consumer Protection Agency (PROFECO) will be responsible for inspections and monitoring.

As for effectiveness, the new powers of COFECE include the ability to order the removal of competition barriers, to regulate essential supplies and goods, and to order the divestiture of assets in concentrated markets as a measure of last resort. The new law preserves the key concepts of the previous law relating to absolute and relative monopolistic practices, relevant market and concentrations. Additionally, it strengthens COFECE's internal processes, including audits and verification visits, sets new sanctions and strengthens criminal penalties.

Finally, with respect to legal certainty and enforceability, the Antitrust Reform provides for new specialized courts related to antitrust matters.

While the law contemplates that individual citizens, the SE or the PROFECO may initiate antitrust complaints, only the COFECE may prosecute cases, judge the violations and carry out any penalties.

Fines and sanctions vary by the severity of the violation, ranging from warnings to detention and fines imposed for "absolute" monopolistic practices, similar to *per se* violations in the U.S. These include price-fixing, limiting distribution of goods, dividing market share and colluding in public bidding, auctions or other competitive proceedings. Lower fines are levied for "relative" monopolistic practices, which include actions that have the effect of improperly displacing others in or preventing them access to the market, anti-competitive distribution agreements, tying agreements and the like. Fines are expressed as either a multiple of the Federal District minimum wage (GMW), with the highest being 180,000 times the daily minimum wage, or ten percent of an entity's income for an absolute monopolistic practice.

b. Mergers and Acquisitions

A foreign company planning to purchase an existing Mexican company should first confirm that no competition filing is required. The COFECE is the agency responsible for approving such applications. In addition to mandatory filings (discussed below), a company contemplating a merger or acquisition in Mexico may make a voluntary filing for approval. If cleared, the transaction may not be later challenged or investigated in Mexico.

A filing with the COFECE for clearance must be made prior to the execution of a purchase agreement if the underlying transaction:

- involves in Mexico, through one or more steps, directly or indirectly, regardless of its place of execution, an amount greater than 18 million times GMW (approximately US $90 million);
- through one or more originating actions, implies the accumulation of 35 percent or more of the assets or shares of an economic agent, whose annual assets or sales in Mexico are greater than 18 million times the GMW (approximately US $90 million); or
- through a single or subsequent originating actions, implies an accumulation of assets or stock in Mexico greater than 8.4 million times the GMW (approximately US $42 million), and the transaction involves at least two or more economic agents with worldwide annual sales or assets greater than 48 million times the GMW (approximately US $240 million) whether individually or combined.

As amounts are determined by reference to the GMW and the applicable exchange rates, the exact thresholds for clearance filings should be determined on a case-by-case basis. Transactions between foreign entities must be filed if they are in any way legally or de facto effective in Mexico. Thus, notice of a transaction must be filed even if any of the parties has a presence in Mexico such as a branch, subsidiary, any distribution, sale or other commercial agreement or owns any real or personal property located in Mexico. The parties' identities, charter documents, financial statements, market involvement, real estate, main operations and competitors, as well as a description of the potential transactions, must be disclosed with the COFECE in order to obtain clearance.

The amount of time permitted the COFECE to issue a clearance depends on the likelihood that the filed transaction has anti-competitive effects. Within the first 15 business days following the filing, the COFECE is entitled to request additional information, which must be delivered by the parties within the following ten business days. Filed transactions not raising any obvious competition concerns, eliciting additional requests or once all of the additional requests have been responded to, must be resolved within 60 business days. As a consequence, the 60-day period for issuing the clearance is not deemed to have commenced until the COFECE has received all of the information it requires. In cases involving competition concerns, the COFECE may communicate such concerns at least ten days prior to the conclusion of the review, in which case, the parties may provide for changes to correct or modify the concerning issues. In justified cases, the original 15-day period (for requesting additional information) and/or the 60-day period (to issue a resolution) may be extended by the COFECE for an additional 40-day term.

16. Environmental Laws

a. Overview

Over the past few decades, in part due to NAFTA, Mexico has increased its regulation of environmental hazards and its administration of the environmental programs. It can no longer be viewed as a country tolerant of pollution or environmental hazards.

A comprehensive package of laws, the General Law of Ecological Equilibrium and the Protection of the Environment, or "Ecology Law," serves as the umbrella federal legislation. It contains numerous laws, regulations and standards modeled principally on U.S. environmental laws and regulations.

In addition to passage of the Ecology Law, Mexico also updated and re-issued its environmental standards and issued dozens of new ones. The administration of the federal environmental legislation has changed over the years and currently resides with the *Secretaría del Medio Ambiente y Recursos Naturales* (SEMARNAT).

A Federal Attorney General for the Environment was created to assist in enforcement. The criminal code was also amended to include environmental crimes. Enforcement of environmental norms, traditionally weak in Mexico, was boosted by Mexico's conclusion of the NAFTA treaty, by funds from the World Bank and by rising economic conditions.

Environmental law is an area of concurrent jurisdiction, so state and municipal governments may also legislate in this area. As a result, in addition to federal laws many states and municipalities also have environmental standards and regulations with which companies must comply. Coastal areas have additional requirements regarding ocean and estuary quality.

Although many laws and rules were on the books for years, enforcement is increasingly rigorous in Mexico and foreign companies operating there should be aware of this change. Companies beginning operations in Mexico should carefully examine the environmental laws applicable to their industry, and consult with counsel and industry experts early in the process.

b. New Facilities

Any company desiring to establish a new facility that may have a negative impact on the environment or exceed the limits set in the Ecology Law must seek prior approval of federal and state officials by filing an environmental impact statement. If the facility will also generate, store or dispose of hazardous waste, it must also comply with numerous other regulations and reporting requirements.

c. Existing Facilities

Companies purchasing an existing facility should be especially wary of old environmental problems dating from the days of lax enforcement and poor infrastructure. Many smaller facilities operated without proper permits, and many stored or buried hazardous waste on-site, resulting in later contamination of the surrounding area. SEMARNAT has a voluntary audit program that can be helpful to potential purchasers of existing Mexican facilities. It permits the company to conduct its own environmental audit and notify SEMARNAT of the results. Once the audit is completed and the remediation plan is negotiated with SEMARNAT, and becomes legally binding. Remediation is then done in cooperation with SEMARNAT to avoid future surprise inspections, shutdowns or fines. Careful diligence is required prior to purchasing any existing facility and the involvement of experienced legal counsel is advised.

d. Toxic or Hazardous Waste

The Mexican standards for regulating the generation, treatment, storage, disposal and transportation of hazardous waste are based on those in the U.S. and are nearly identical. Mexican's water laws were based on the U.S. Clean Water Act, although in many respects the Mexican law is broader. Mexico's air quality standards are likewise modeled on the U.S. Clean Air Act. In the border areas, there is close cooperation between the U.S. Environmental Protection Agency and Mexican authorities regarding environmental issues. However, air quality remains an issue in Mexico, both along the border and in Mexico City, due in large part to lax enforcement.

e. Enforcement

Lack of infrastructure and enforcement remains a problem in Mexico, as the central government has had difficulty finding resources to enforce the laws with respect in particular to existing business. Another factor affecting enforcement is the centralized nature of administration in Mexico. Environmental issues are rarely addressed by means of citizen lawsuits, as they are in the U.S. In Mexico, only the federal and state government agencies have the authority to enforce environmental laws and have struggled to field enough inspectors.

SEMARNAT's inspection program is divided into four programs:

- Targeted inspection (mostly for highly-polluting industries such as petroleum, petrochemicals and the like);
- Public complaints;
- Aerial surveillance for air quality violations, and
- Vehicle emissions.

Environmental enforcement in Mexico can be draconian, and generally involves one or more of the following: plant closure (permanent or temporary), negotiation of compliance agreements and posting of a compliance bond, and steep fines. It is not uncommon for the authorities to begin with a plant closure, which facilitates the negotiations.

F. Transfer of Liability

When acquiring an equity interest in a Mexican entity, the buyer acquires a share of the environmental liabilities as well (limited to the contribution). Nonetheless, the parties may agree to have the seller retain environmental liability.

With respect to asset sales, a buyer may inherit environmental liability specially when purchasing land. Similar to a stock sale, the parties can agree that the seller retain environmental liability. Keep in mind, however, that if an environmental issue, such as contamination, is detected prior to the transaction, the SEMARNAT must authorize the transaction.

In the case of a lease agreement, the party causing the actual contamination is ultimately liable for it. Nonetheless, both the owner and lessee may be jointly and severally liable for the remedial measures unless it can be proved who actually caused the contamination: whether the owner, lessee or any previous possessor. Hold harmless provisions can be included in sale and lease agreements to limit a party's environmental liability. Negotiating such agreements with the support of legal counsel is key to limiting your potential liability

17. Dissolving a Business

a. Overview

The term "dissolution" refers to the true ending of a company's legal existence for purposes of conducting business. Below is a general outline of procedures involved in dissolving corporations and limited liability partnerships. The Commercial Code governs dissolution of all entities.

b. Corporations

A Mexican corporation may be dissolved in several ways. It can be dissolved by a vote of the shareholders or by judicial action filed by a third party having an interest in the corporation. There are five possible causes for dissolution:

- Expiration of the company's legal term;
- The impossibility of carrying on the principal object of the company, or when the object has been achieved;
- Resolution of the shareholders or partners, in accordance with the articles and the law;
- When the number of shareholders or partners is reduced below the minimum required by law or when all the shares are owned by one person;
- Upon the loss of two-thirds of the capital stock (i.e. when the assets are worth less than one third of the stock issued).

c. Liquidation

Upon dissolution, the company must be liquidated by one or more liquidators who are appointed by the shareholders who approved the dissolution. The liquidation process is similar to that in the U.S. The liquidators must complete any pending transactions, collect any outstanding payments owed to the company, and sell the assets of the corporation to calculate the final liquidation balance. This is deposited with the Public Registry of Commerce where the request for cancellation of the registration of the corporation must also be filed. The final liquidation balance must be published three times prior to completing the liquidation process. If any assets remain, they are distributed among the shareholders. Once the Public Registry has registered the cancellation of the corporate registration, the company is officially dissolved. The dissolution process is the same for an S. de R.L. and an S.A. corporation.

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