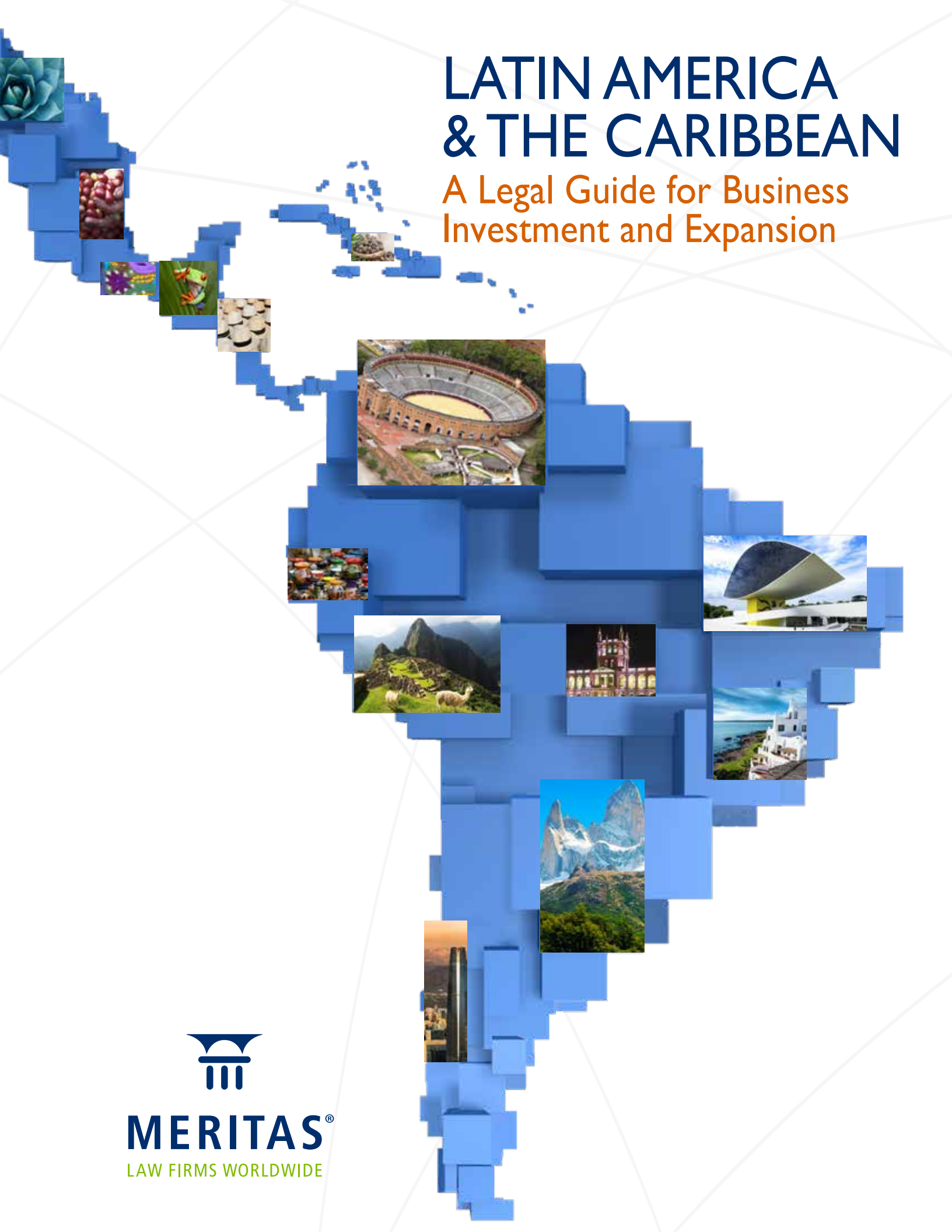


# LATIN AMERICA & THE CARIBBEAN

A Legal Guide for Business  
Investment and Expansion



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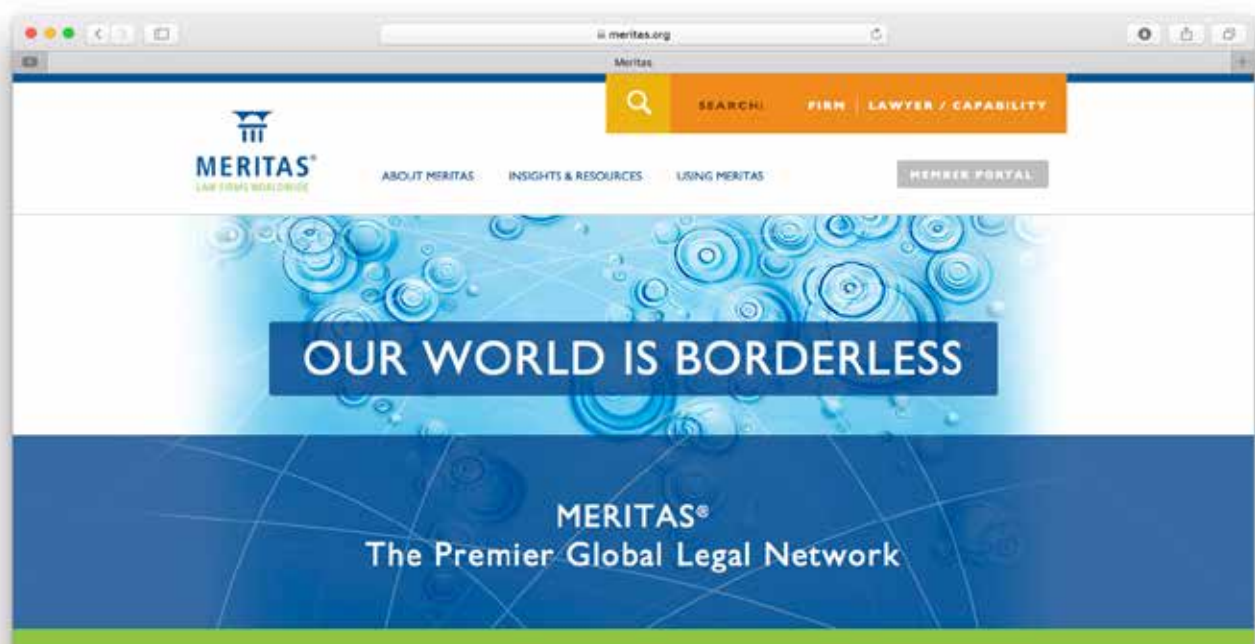
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# MEXICO

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## 1. What role does the government of Mexico play in approving and regulating foreign direct investment?

In Mexico, the regulation of foreign investment is entrusted to the National Congress, which is the only authority legally empowered to issue laws on that matter. The Ministry of Economy is responsible for their implementation and execution, as well as for the coordination of mechanisms to comply with any regulations on this matter.

Despite the fact that Mexico is a Federal Republic, composed of states with their own state government; foreign investment is a topic within the exclusive authority of the Federation. The states do not have any legislative authorities to regulate foreign investment, being exclusively allowed to participate in its promotion, fostering and execution.

The Foreign Investment Law establishes the rules to receive foreign direct investment and to make sure that such investment contributes to national development.

The following activities are considered as foreign investment:

- Participation of foreign investors in the capital stock of Mexican entities (in any percentage);
- Investments made by Mexican entities in which foreign investors have a majority interest (percentage in the capital stock); and

- Participation by foreign investors in activities and acts described in the Foreign Investment Law.

The Foreign Investment Law contemplates categories of activities that are:

- Exclusively reserved to the Mexican state (government);
- Exclusively reserved to Mexican nationals and to Mexican companies, in which foreign investment cannot participate;
- Activities in which foreign investment is limited to specified percentages, ranging from 10% to 49%; and
- Activities requiring permission from the National Commission of Foreign Investment to have more than 49% of foreign participation.

The National Commission of Foreign Investment has the following authorities:

- To dictate the guidelines of the policies to promote investment in Mexico;
- To determine the terms and conditions of participation of foreign investors in activities with specific regulations;
- To issue opinions when requested by other agencies of the Federal Government relating to foreign investment; and
- To establish the criteria for the application of laws and regulations in connection with foreign investment.

## 2. Can foreign investors conduct business in Mexico without a local partner? If so, how does the Mexican government regulate commercial joint ventures between foreign investors and local firms?

As a general rule, foreign investors are allowed to conduct business in Mexico without a local partner, either through a branch (foreign entity doing business in Mexico) or a subsidiary (a Mexican entity), being the latter the most commonly used under the following corporate forms:

- *Sociedad Anónima (S.A.)*: Comparable to U.S. corporations and incorporated by shareholders whose liability is limited to their contributions in capital stock.
- *Sociedad de Responsabilidad Limitada (S. de R.L.)*: Comparable to the limited liability company in the U.S., and organized by partners also with limited liability.

Depending on the specific features of the project, foreign investors can choose more specialized and targeted corporate structures, such as:

- *Sociedad Anónima Promotora de Inversión (SAPI)*: Similar to Sociedad Anónima, regulated by the *Ley del Mercado de Valores*.
- *Sociedad Anónima Bursátil*: When shares are offered in the Mexican stock exchange.

- *Sociedad Financiera de Objeto Múltiple (SOFOM)*: To conduct activities related to granting of credit, leasing or factoring.

Regarding joint venture agreements between foreign and local investors, even though there is no specific legislation in Mexico, there are several regulations that should be considered in specific cases, for example: public participation partnerships with the government for infrastructure projects. In addition to the already mentioned limitations to foreign investment, it is also important to consider antitrust law provisions to evaluate the need of a merger control filing to obtain clearance prior to closing.

In conclusion, Mexican law allows foreign investors to conduct business in Mexico without a local partner but with some limitations over specific activities.

### 3. What laws influence the relationship between local agents and distributors and foreign companies?

The relationships of agents, distributors and foreign companies must be analyzed considering the following legal aspects:

- Commercial: To define the contractual and business structure in regard to territory, exclusivity, business and sales goals, prices, market, delivery terms, guaranties, among other business terms.
- Labor: Special provisions are needed so that the parties are considered as independent contractors. Also, it is important to avoid assumption of labor and social security risks or liabilities of another party (derived from employees, agents or subcontractors).
- Intellectual Property: Will there be any licenses on trademarks, secrets or brands? How much access to know-how or good-will should the distributor or agent have? How will the marketing be conducted? What is the understanding in connection to the development of new brands, products or designs?
- Foreign trade: In case of imports or exports, it is important to define: who will be responsible for the import/export clearance? Who will be importer/exporter of records? Who is responsible to obtain all the necessary permits and licenses, and to pay the applicable taxes? What INCOTERM to use? Among other topics.
- Administrative: What permits and licenses apply to the products? The agreement must state which party will be responsible to obtain and maintain each of them valid.
- Foreign investment: As mentioned before, there are statutory limitations to foreign investment in certain economic activities. It is advisable to review whether any of such limitations are applicable.
- Tax: Several types of taxes at federal, state and municipal level may apply. It is advisable that the payment flow is supported by an appropriate tax analysis. Tax requirements must be considered.
- Anti-corruption: Agreements must contain proper regulations to avoid anti-corruption liabilities under Mexican and international laws.
- Consumers Protection: Depending on the market, consumers protection regulations can be applicable. Parties should address these in their warranty policy.

### 4. How does the Mexican government regulate proposed merger and acquisition activities by foreign investors and are there any areas of the economy where they are prohibited (e.g., natural resources, energy or telecommunications)?

The main legal orders related to M&A activities by foreign investors in Mexico to take into consideration are the Foreign Investment Law, Mexican Economic Competition Law, Securities Market Law, and General Corporations Law. The Federal Economic Competition Commission (“COFECE”), and the Federal Telecommunications Institute (“IFT”), are constitutionally autonomous agencies independent from the executive branch that regulates economic competition and prevents monopolistic and anticompetitive practices.

Certain activities are reserved exclusively for Mexican government, such as the control of the national electricity system, generation of nuclear energy, radioactive minerals, telegraphs, radiotelegraphy, mail, emission of currency, control of ports, airports and heliports. There are some economic activities reserved exclusively for Mexicans, such as domestic ground transportation of passengers, tourism and cargo, development banking institutions and the provision of professional and technical services that expressly indicate the applicable laws. Foreign investors may not participate in these activities directly or through agreements, pyramid schemes or any other mechanism.

It is also relevant to identify whether the type of industry of the target entity is subject to special regulations (aeronautic, banking, maritime, energy, transportation, among others).

There are some restrictions to certain industries provided by the Foreign Investment Law that are to be analyzed as a first step to evaluate the feasibility of the transaction. In case a foreign investor intends to invest more than 49% of the equity of a Mexican entity, when the aggregate value of the assets of such companies at the date of acquisition exceeds the amount determined annually by the National Commission of Foreign Investment (approximately USD 192.8 million, subject to exchange rate variations), they will require prior authorization from the National Commission of Foreign Investment.

In case the transaction exceeds certain thresholds, an antitrust test must be performed to determine if the M&A transaction requires approval from the Mexican Competition Commission or by the Federal Telecommunications Institute.

Applicable competition compliance regulations in Mexico (and in the jurisdictions involved in the transaction) must be considered, especially regarding the information exchanges during the negotiation of the transaction. In case the closing is subject to pre-merger clearance, it is important to be careful on covenants and commitments that could be considered as “gun-jumping”, typically situations in which the acquirer takes certain control, decision-making on the business of the target entity/assets or closing activities prior to antitrust clearance; and noncompete provisions, in which their validity and scope will depend on the type of transaction.

## 5. How do labor statutes regulate the treatment of local employees and expatriate workers?

The Federal Labor Law (FLL) governs all labor and employment relationships for services provided in Mexico, whether the employer is a foreign or Mexican national. Foreign investors must consider that Mexican labor and employment regulations are of public order and aimed to protect employees' rights that may not be waived. Foreign investors should also evaluate salary

levels, labor and employment conditions offered in the industry and the location where they are to be established in order to be competitive.

The most relevant statutory benefits provided by the FLL that must be included in employment agreements are:

- Salary (must not be lower than the minimum wage);
- Christmas Bonus (at least of 15 days of salary);
- 6 days of vacations increasing with seniority;
- Vacation premium equivalent to at least 25% of the employee's salary;
- 10% profit sharing benefit, calculated with the taxable income (also calculated and distributed based on certain rules and formulas);
- Official holidays such as Labor Day, Independence Day, Christmas and New Year's;
- A maximum 48-hour weekly shift and overtime system compensation, among others benefits.

The employer can grant to the employee other benefits and labor conditions in addition of the above.

All employers must register their employees with the Mexican Social Security System.

Regarding expatriates to be relocated in Mexico, the FLL and the Immigration Law provide certain requirements to be considered by employers:

- No employer may have more than 10% foreign employees (general managers, directors and managing level officers are exempted from this rule);
- Must be registered and receive an employer certification from the National Immigration Institute;
- Expatriates should have an appropriate working visa; and
- The employer and the foreign employee must closely keep control of due renewal of the worker visas and of filing of notices to the National Immigration Institute.

A second agreement has to be settled between the host Mexican entity and the foreign entity in case of hiring of expatriates. This agreement includes, among other provisions:

- Expatriate's conditions;
- Nomination of entity that will assume tax costs;
- Benefits that the expatriate will maintain with the original employer.

Tax effects applicable to the salaries and benefits paid to the expatriates must be analyzed on a case by case basis; considering international tax treaties and the employee's tax residency.

## 6. How do local banks and government regulators deal with the treatment and conversion of local currency, repatriation of funds overseas, letters of credit, and other basic financial transactions?

The Mexican Central Bank (Banco de Mexico) regulates the Mexican banking system and is responsible for implementing monetary policies to ensure the effective payment system. Mexican banking institutions are privately owned, and foreign investment is allowed.

The National Banking and Securities Commission (CNBV) is a government agency that reports to the Ministry of Finance (SHCP, for its acronym in Spanish) in charge of supervising and regulating banks and financial institutions, and their legal performance in accordance to the financial regulations.

The Mexican Central Bank sets and publishes the official exchange rate for the payment of the legal obligations specified in foreign currency but payable within Mexico.

The Mexican local currency (*Peso*) is freely convertible into all other currencies with no restrictions on remittance of profits or the repatriation of capital abroad.

All currencies may be freely transported or traded. However, certain reporting requirements apply for travelers and financial transactions.

## REPATRIATION OF FUNDS OVERSEAS

Mexico does not have any exchange control or limitations on remittances in foreign currency when a repatriation of funds is made overseas, including repatriation of capital investments, payments of intercompany loans or payment of dividends.

It should be borne in mind, however, that the Mexican General Act for Commercial Entities state, that commercial entities must form a legal reserve fund setting aside at least 5% of yearly profits until an amount equal to 20% of the capital stock of the entity is reached.

## BASIC FINANCIAL TRANSACTIONS

Mexican banks offer different types of credit oriented toward consumption and productive activities. The basic financial transactions offered by the banking institutions for households are credit cards, mortgage loans, credits for the purchase of durable consumer goods and automobile loans. Meanwhile, companies apply for credits, working capital loans (*crédito de habilitación o avío*), fixed asset loans (*crédito refaccionario*), revolving credits, asset-based lending facilities, among others.

The common securities requested for the banking institutions can be constituted through mortgages, pledges (including the modality of non-possessory or floating lien pledge), corporate guaranties or guaranty trusts.



## LETTERS OF CREDIT

Letters of Credit are commonly used in Mexico. Its purpose is to facilitate foreign and domestic trade, eliminating mistrust and risk between the buyer and the seller.

The most common Letters of Credit are:

- **Import:** a typical payment instrument in foreign trade.
- **Domestic:** a payment instrument in commercial transactions.
- **Export:** payment instrument received by the exporter / seller / beneficiary through a confirming bank with the commitment to honor the payment in its favor, against the presentation of documents related to the sale of goods or services.
- **Stand-by:** to guarantee different obligations (commercial, financial or services obligations), in which the applicant might not fulfill the commitments acquired.
- **Contractual Guarantees (bonds):** the bank guarantees and supports the participation of companies in international public tenders, or tenders for the award of contracts, sale of goods or provision of services.

Demand Guaranties and other financial figures under the International Chamber of Commerce (ICC) rules are also implemented in sophisticated transactions.

## 7. What types of taxes, duties, and levies should a foreign investor in Mexico expect to encounter?

Mexico has proven great openness to foreign investors through several mechanisms and incentives established to attract foreign direct investment. However, when investing in Mexico, investors must take into account some aspects and regulations, in order to have a successful landing.

Mexico has three levels of laws and authorities, therefore applicable local taxes, local policies and criteria, incentives and legal framework shall be considered when choosing a location in Mexico. The majority of taxes are levied at the federal level. Most states may offer different types of incentives to attract foreign investment.

Every taxpayer (corporation or individual) shall be registered before the Tax Administration Service in order to obtain a Taxpayer Identification Number. This number is required for all tax records of the company and must be included in all electronic invoices for the taxpayer's deductible expenses.

The most relevant federal taxes are income tax, value added tax, and special tax on products and services.

Regarding the income tax, a 30% tax rate is applicable on all taxable income of Mexican corporations. An annual tax return must be filed by the end of

the third month following the end of the fiscal year. In addition, the law requires that business entities file monthly estimated tax returns reports.

Until 2013, profits in Mexico were only taxed at the corporate level, not at the shareholder level. Since 2014, profits obtained and distributed shall be levied with an additional tax of 10% at the shareholder level when such profits are distributed to nonresidents or individual residents in Mexico.

The value-added tax (VAT) is levied on the alienation of goods, rendering of independent services, granting of temporary use or enjoyment of goods, and on the importation of goods and services. The general VAT rate is 16%. Exports and some other specified items are subject to the 0% rate.

The VAT collected by taxpayers from their suppliers must be remitted to the tax authority, and may usually be credited or reduced against the tax paid by the taxpayers. Excess credits may be reimbursed. This tax is computed for each calendar month and the monthly returns must be filed no later than the 17th day of the following month.

The Special Tax on Products and Services is applicable to entities and individuals that sell and import certain goods in a definitive manner or render certain services.

## 8. How comprehensive are the intellectual property laws of Mexico, and do the local courts and tribunals enforce these laws regardless of the nationality of the parties?

Intellectual Property Laws in Mexico strictly follow and cover all principles and figures contemplated by international treaties, such as the Paris Convention for the Protection of Industrial Property, the Berne Convention for the Protection of Literary and Artistic Works, the Madrid Protocol, the Nice Agreement, the Patent Cooperation Treaty, Trade-Related Aspects of Intellectual Property Rights, etc.

The main intellectual property laws in Mexico are:

**Industrial Property Law.** Which establishes the proceedings for obtaining protection over patents, designs, utility models, trademarks, tradenames, trade secrets.

**Federal Copyright Law.** Which establishes the proceedings for obtaining registration certificates for copyrights and “*reservas de derechos*”.

**Plant Varieties Act.** Which regulates the procedures and requirements for obtaining protection over plant varieties.

There are several other laws that indirectly impact and rule secondary aspects of intellectual property rights, such as health, consumers, economic competition, customs (import and export of products), criminal, etc.

The Mexican legislation covers all intellectual property aspects, including litigation, such as cancellation and annulment proceedings.

As to the enforceability of intellectual property in Mexico, administrative authorities, District Courts and Circuit Courts (which are the authorities in charge of all litigation proceedings regarding intellectual property), study, prosecute and decide on matters without the nationality of the parties being a deciding factor.

A very high percentage of intellectual property rights in Mexico are property of foreign entities, and Mexican authorities have proven over time, that their main focus is to protect intellectual property rights regardless of the nationality of the titleholder.

## 9. If a commercial dispute arises, will local courts or will international arbitration offer a more beneficial forum for dispute resolution to foreign investors?

For international M&A and sophisticated commercial or multijurisdictional transactions it is usually advisable to elect arbitration as the dispute resolution process. It is important to verify that all parties involved are located or do business in countries that recognize the validity and enforcement of arbitral awards. For other types of commercial disputes, several topics must be analyzed to determine if an arbitration provision is the best choice, and if the type of dispute can be subject to arbitration (in Mexico, for example, trademark and patent disputes must be resolved by governmental authorities). Contracts involving credit instruments or securities on financial transactions will generally requires the use local laws and courts for enforcement.

Mexico is a party to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, also known as the “New York Convention” and the Inter-American Convention on International Commercial Arbitration.

Based on the above, the parties on a commercial agreement can validly introduce an arbitration clause either following the rules of an arbitral institution (such as ICDR, ICC, among others) or electing an *ad hoc* procedure.

Some advantages of electing arbitration for the resolution of potential disputes arising or relating to an international commercial transaction are:

- flexibility and broader alternatives for interim measures that may be required during the arbitration procedure;
- possibility to elect arbitrators with reputation, expertise and knowledge on the type of dispute, who must fulfill independency, impartiality and ethical principles;
- confidentiality of the arbitration procedure;
- less formalities for the enforcement of an arbitral award compared to the formalities required for the enforcement of a foreign court resolution;
- rich experience of international and national arbitral institutions and arbitrators on M&A disputes;
- Mexico recognizes the enforceability of national and foreign arbitral awards.

The arbitration experience has become more sophisticated with time. It is not necessarily true that arbitration procedures will be highly expeditious and inexpensive, but the advantages and the usual complexity of M&A or certain commercial disputes make the election for arbitration worthwhile.

### **10. What advice can you provide for how best to negotiate or conduct business in Mexico?**

It is always important to understand the customs, cultural traits and particular economic and social conditions of the location where a business is intended to be carried out. In this sense, having references or the intermediation of a reliable firm or consultant that knows and has experience on how to do business in Mexico and its different regions, could be decisive to get a soft-landing or the best of a negotiation, especially in joint ventures with other partners.

A reputable brokerage firm will be of high relevance for searching real estate for acquisition or lease.

It should also be taken into account that the timeframe to accomplish certain objectives, such as incorporation of Mexican entities, registration for tax purposes, opening of bank accounts, obtaining governmental permits and clearances, anti-money laundering regulatory requirements, among other procedures, do not always occur with the same speed as in other countries. This circumstance must be taken into account when establishing the terms of a business plan. Nevertheless, Mexico makes continuous efforts to speed up processes.

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