

DOING BUSINESS IN MEXICO

A general overview

1. Introduction to Mexico. Mexico is one of the main economies in Latin America and has a diversified economy. In turn, its strategic position as a bridge between North and South America gives it a crucial role in international trade. The signing of trade agreements such as the Agreement between Mexico, the United States and Canada (T-MEC) reinforces the economic integration of the region and has strengthened Mexico's position as an attractive destination for foreign investments. The country has experienced constant growth in the manufacturing, technology, tourism and financial services sectors, offering businesses a unique combination of strong economic factors, a broad cultural heritage and a strategic geographic location, making it an attractive destination for investment and business expansion.

Additionally, in light of the economic clash between China and the United States, Mexico is emerging as the key gateway to North America, thanks to its more conducive business environment for Chinese investments.

2. Legal and Regulatory Framework. In Mexico, foreign companies are subject to various laws and regulations that govern their establishment, operation and business relationships. Mexican laws related to foreign companies are governed mainly by the Foreign Investment Law and its Regulations, as well as by additional provisions contained in other laws and international treaties, as referred to below:

- i) **International Treaties:** Mexico has signed various international treaties that address matters related to foreign investment, such as the North American Free Trade Agreement (NAFTA, now USMCA) and other bilateral agreements. These treaties typically provide additional protection and benefits to foreign companies for investment in the region;
- ii) **Foreign Investment Law:** This law regulates foreign investment in Mexico and establishes the conditions under which foreign companies can participate in different economic sectors. It defines the limits of foreign participation in certain activities and establishes the procedures for the authorization of investments. The LIE allows foreign investment in most economic activities, but there are restrictions in some strategic sectors;

- iii) National Registry of Foreign Investments (RNIE): Foreign companies that wish to invest in Mexico must register with the RNIE, which is administered by the Ministry of Economy. This registration is mandatory and provides information on foreign investment in the country;
- iv) General Law of Commercial Companies: This law regulates the constitution, organization and operation of commercial companies in Mexico. Contains provisions applicable to foreign companies that wish to establish themselves in the country, including the procedure for forming and establishing their branches;
- v) Commercial Code: Contains provisions related to commercial contracts, obligations and rights of the parties involved in commercial transactions;
- vi) Federal Labor Law: Regulates labor relations in Mexico, including issues such as hiring, salaries, working hours and workers' rights. Foreign companies must comply with these provisions when employing workers in Mexico;
- vii) Social Security Law: Establishes the rights and obligations of workers with respect to social security, as well as those that correspond to employers, referring to affiliation with the Mexican Social Security Institute (IMSS) and in general guaranteeing the right to health and medical assistance.

3. Incorporation of Companies. Setting up a company in Mexico involves following several steps and complying with certain legal requirements. Therefore, it is important to take into account the following:

- i) Definition of the type of commercial entity: In Mexico, the most common forms of commercial entities are the Sociedad Anónima (SA), Limited Liability Company (S. de RL), Sociedad de Anónima de Capital Variable (SA de CV), among other;
- ii) Name reservation: It is important to verify the availability of the name or company name of the company;
- iii) Preparation of the articles of incorporation: This document establishes the fundamental rules of the company, such as the name, corporate purpose, address, duration, and distribution of shares or participations;

- iv) Share Capital: Determines the amount of the company's share capital in accordance with the purposes of the entity;
- v) Signature of the articles of incorporation before a notary: The articles of incorporation must be signed before a notary public in Mexico;
- vi) Registration at the Public Registry of Commerce: Submission of the documentation to the Public Registry of Commerce for the purpose of registering the company, obtaining the Federal Taxpayer Registry (RFC) and subsequently obtaining the Electronic Signature (e.firma) for tax procedures;
- vii) Registration at the Mexican Social Security Institute (IMSS): Registering the company and employees at the IMSS to access social security services;
- viii) Registration with the Ministry of Economy: Some companies require registration with the Ministry of Economy, depending on their line of business and specific activities.

4. Commercial Companies Law. Types of business organizations regulated by the General Law of Commercial Companies and the Securities Market Law:

- i) Corporations (SA and SA de CV): These entities, whether as a Sociedad Anónima (SA) or Sociedad Anónima de Capital Variable (SA de CV), are common forms of business organization that offer flexibility in the structuring of ownership and operations;
- ii) Limited Liability Companies (S. de RL and S. de RL de CV): Limited Liability Companies allow the participation of several partners with limited liability, providing an intermediate structure between the public limited company and the partnership;
- iii) Investment Promotion Corporations (SAPI): Investment Promotion Companies are characterized by their focus on facilitating and promoting investments, allowing the participation of different investors in specific projects;
- iv) Public Limited Companies (SAB): Public Limited Companies are entities that are listed on the stock exchange and are subject to specific securities market regulations. They allow the participation of public shareholders and can be financed by issuing shares on the stock markets.

5. Foreign Investment Law. The Foreign Investment Law (FIL) in Mexico allows foreign investors to have a total participation within Mexican companies and participate in various activities without the need for prior approval. However, there are exceptions for those activities reserved for the Mexican State and some specific sectors, such as the financial sector, which are restricted. These activities reserved for the State are exclusive for Mexican nationals and are subject to limitations or prior approval. Examples of such sectors include petroleum, nuclear energy, land transportation, port services, education, legal services, and railways.

6. Competition Law. The Competition Law in Mexico introduced substantial changes and established the Federal Economic Competition Commission (COFECE) and the Federal Telecommunications Institute (IFT) as autonomous entities. These bodies play a crucial role in enforcing the law in various sectors, regulating monopolistic practices and abuses of dominant position.

7. IMMEX or Maquiladora Program. The Mexican government implemented the Maquiladora Decree and the Income Tax Law three decades ago. These measures are aimed at promoting employment. Under the IMMEX regime, foreign investors can operate with a corporate presence, allowing maquiladoras to have up to 100% foreign ownership. This legal framework facilitates the temporary importation of goods intended for manufacturing and export, exempting them from non-tariff regulations. In addition, varied deadlines are established for different types of goods, with operating options that include purchase-sale models or consignment manufacturing. Maquiladoras also enjoy tax exemptions and are granted the possibility of marketing up to 90% of their production in the domestic market.

8. Taxes. Mexico has established treaties to prevent double taxation with various nations, applicable to both Mexican residents and foreigners who generate income from a Mexican source. In this context, allowable deductions and formal restrictions have been outlined. For foreign residents, a 10% withholding on dividends applies, although there is the possibility of reduction under the terms of international treaties. In addition, withholdings at source are implemented for interest and royalty payments, with variable rates depending on the beneficiary and their country of residence.

Regarding the Value Added Tax (VAT), the general rate is 16%, but there are specific cases, such as exports and certain goods, that enjoy a rate of 0%. The VAT Law establishes requirements to credit VAT on pre-operational expenses and investments, with the

possibility of crediting VAT generated before starting commercial operations subject to VAT. In addition, additional deductions are contemplated for the maquiladora industry, as well as tax benefits for employees with disabilities and real estate trusts. From 2014 onwards, the sale and import of sugar-flavored beverages as well as fossil fuels, are taxed with the Special Tax on Production and Services (IEPS).

9. International Trade and Rules of Origin under the T-MEC. In Mexico, the Treaty between Mexico, the United States and Canada (formerly NAFTA) was replaced by the T-MEC in July 2020.

Mexico may impose non-tariff regulations to protect health, safety, the environment and other public interests. These regulations may affect certain products and require compliance by importers.

T-MEC establishes specific rules for the following:

- i) **Change in Tariff Classification:** Specific rules are established to determine when a product complies with the change in tariff classification;
- ii) **Regional Value Content:** Products must have a certain percentage of regional content to qualify for T-MEC benefits; and
- iii) **Transformation during the Production Process:** Specific transformation processes are defined so products can qualify as originating in North America.

10. Labor Law. The Federal Labor Law (LFT) regulates labor relations in Mexico, applying to anyone who performs subordinate services in the country, regardless of their nationality or place of employment. The last relevant modification came into force on January 1, 2023, impacting the calculation of workers' vacations. Companies have the power to grant benefits that exceed the minimums established by law. The outsourcing of personnel services, a measure recently implemented, is prohibited. However, its use is allowed for specialized services, as long as specific regulations are met.

11. Environment. Mexico has an extensive legal framework made up of numerous laws, regulations and standards aimed at environmental protection:

- i) The Ministry of Environment and Natural Resources (SEMARNAT) plays a crucial role in establishing environmental policies at the federal level;

- ii) The Federal Environmental Protection Agency (PROFEPA) is responsible for applying current environmental legislation;
- iii) The National Water Commission (CONAGUA) plays a fundamental role in the supervision and management of water in the country;
- iv) Since the 2014 reform, the Security, Energy and Environment Agency (ASEA) regulates activities in the hydrocarbon sector.

The Mexican government establishes a series of procedures with the purpose of protecting, safeguarding and conserving the environment, for which it established a series of measures that it is imperative to obtain, such as the case of the Environmental Impact Authorization, which must be issued before operating an industrial facility, as established by regulations. Mexico is aware of the environmental situation worldwide, which has been exposed in various international forums and meetings, which is why it has committed to achieving a 35% reduction in emissions by 2024, as part of its efforts in the fight against climate change. Currently, a pilot program is being developed for the creation of a carbon market, demonstrating the country's commitment to finding innovative solutions to address environmental challenges.

12. Intellectual Property. The Mexican government has established a set of regulations dedicated to the monitoring and protection of intellectual property, which implementation corresponds to the Mexican Institute of Industrial Property (IMPI) and the Federal Copyright Law (LFDA), which implement various measures to guarantee the protection of rights associated with trademarks, patents, industrial designs, inventions, compositions, among others.

13. Real Estate. Mexican legislation on real estate for foreign investors covers the regulation of foreign investment, the transfer of titles and financing. Property categories, such as private property, are governed by rights of use and transfer established in specific contracts. Ejido property, granted by the government for agricultural purposes, has certain restrictions, while communal property, similar to ejidal property, lacks exclusive plots.

It is important to note that foreigners must obtain special permits and accept the "Calvo Clause" in their acquisitions. In addition, the regulation addresses concessions for the exploitation of mineral and water rights. Common collateral includes mortgages and pledges, with the ability to retain title until agreed-upon contingencies or payments are met.

The formalization of ownership involves the signing of instruments before notaries, which the are registered after meeting the established conditions. In the Restricted Zone along the borders and coasts), financial institutions act as trustees and irrevocable trusts, with a duration of 50 years and an option for renewal, allowing foreign beneficiaries to hold and transfer their rights.